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INSIGHTS

AI Ambitions. Pension Obligations.

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Artificial intelligence (AI) seems to be everywhere. It writes emails, answers questions, builds software, and if you believe every earnings call, will soon transform just about every industry. For investors, the story has largely played out in equities, where a small group of companies has driven a meaningful share of market returns. But AI's influence is no longer limited to equity markets.

Building AI requires data centers, chips, power, and networking equipment—basically, a great deal of capital. Increasingly, the companies funding that buildout are doing so through investment-grade corporate debt. For US-defined benefit plans, many of the same bonds are held in liability-hedging portfolios and are used to set the discount rate to value pension obligations.

So, what happens if the AI trade disappoints? A reversal could affect pension funded status through familiar channels such as credit deterioration and equity declines, but also through a less obvious one: the composition and yield of the AA-rated corporate bond universe used in liability measurement. This piece examines AI risk from multiple angles and the potential steps plan sponsors can take to manage them.

Why AI concentration matters in the AA-rated corporate universe

Under accounting guidance, pension discount rates are generally based on high-quality fixed income investments. In practice, many actuaries and plan sponsors rely on AA-rated corporate bond universes or AA yield curves to estimate those rates. Given the relatively small size of this subset relative to the broader credit universe, concentration within that market can have a material impact on pension liabilities.

Concentration in the index has been a concern for quite some time, as fewer corporate issuers have had AA ratings. However, this concentration has become much greater recently, predominantly as more AI-related firms have come to rely on debt markets to build out the infrastructure needed for AI compute.

Figure 1 illustrates the growing share of AI-related debt in the relevant AA-rated corporate bond universe. Given the longer duration nature of pension liabilities, the Bloomberg US Corporate Long AA Index was used for reference, but the general trend applies to all maturities. While the precise exposure depends on how "AI-related" is defined,[1] issuance linked to AI has become a larger portion of the opportunity set. For sponsors using AA-based discount rate methodologies,



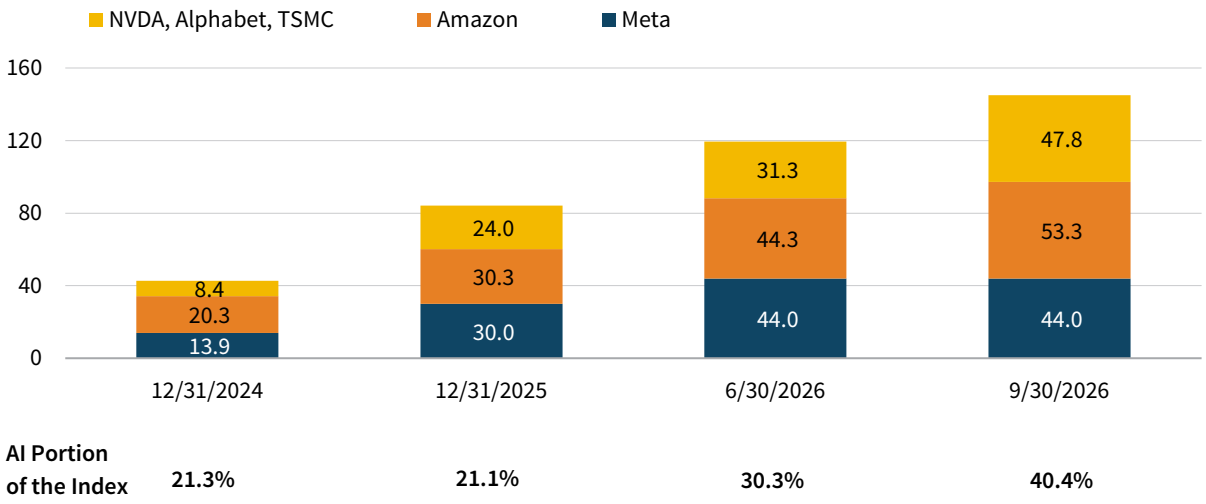
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1 In the Bloomberg US Corporate Long AA index, AI issuers are composed of Alphabet, Amazon, Meta, Nvidia, and TSMC.

this creates greater sensitivity to the credit profile of a relatively small set of issuers. The concentration of AI-related names in the index has nearly doubled since December 31, 2024, increasing from 21% to 40% as of September 30, 2026. With the amount of capital needed to continue expanding the AI buildout, this concentration is likely to grow over time.

Figure 1 Amount of AI debt has tripled over the past 2 years

AI issuance in Bloomberg US Corporate Long AA Index • USD billions • Par value



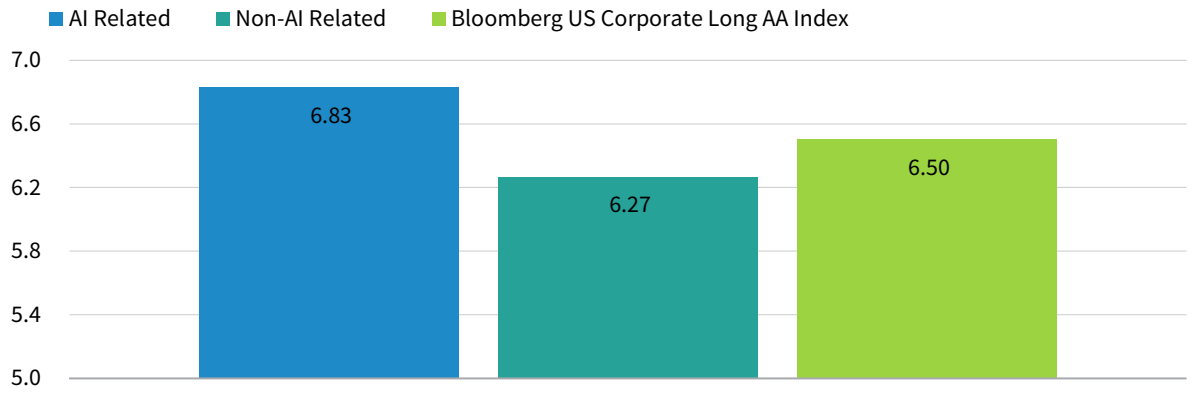
AI Portion of the Index	21.3%	21.1%	30.3%	40.4%

Source: Bloomberg L.P.

So far, this has been a positive development for US pension plans as AI firms have come to market with higher yields to incentivize investors for increased debt supply and uncertain investment returns. Using the Blomberg US Corporate Long AA Index as a proxy, the average yield on the index is 6.50%. However, the average yield for AI-related names is 6.83%, while the yield on non-AI names is 6.27%, indicating a 56-basis point (bp) gap between AI-related and non-AI related firms (Figure 2). This has increased the discount rate, meaning that pension liabilities have declined during this period.

Figure 2 Yields for AI-related names are 56 bps higher than the rest of the index

As of September 30, 2026 • Yield-to-Maturity • Percent (%)



Source: Bloomberg L.P.

Note: "AI-related" represents debt issued by Meta, Amazon, NVIDIA, TSMC, and Alphabet included in the Bloomberg US Corporate Long AA Index.

The current higher yields benefit investors and reduce pension liabilities. However, if a meaningful share of higher-yielding issuers were downgraded out of the AA-only universe, their removal could lower the discount rate and increase reported liabilities, all else equal. Depending on the duration profile of the liability and the type of yield curve methodology used, the increase in liability could range from 0.5% to more than 2.0%, assuming only AI names get downgraded.

Plans using a bond matching approach to determine the discount rate are especially vulnerable as this methodology tends to pick out the highest yielding names. Although these methodologies generally impose issuer concentration limits, they do not impose sector-level limits or caps on aggregate exposure to hyperscalers. As such, downgrades of these issuers could therefore exclude a substantial share of bonds from the discount rate calculation, amplifying the liability impact noted above.

What about total portfolio impact?

The balance sheet effect may extend beyond the liability calculation into the asset component. Many plans hold public equities, high-yield credit, REITs, infrastructure, and other risk assets with direct or indirect exposure to the same underlying AI theme. An adverse repricing of AI-related sectors could weaken funded status through multiple channels simultaneously: declines in growth-sensitive assets such as equities, wider spreads in credit holdings, and lower liability discount rates if downgrades alter the composition of an AA-based liability benchmark.

Most pension plans hold some allocation to investment-grade credit. Typically, these mandates are broad and cover the entire investment-grade universe, not just the AA-rated names. Even in this case, 13% of the Bloomberg Long US Corporate Index is directly tied to hyperscalers or AI names.[2] While it would take a major event for AI names to fall out of the investment-grade index, a downgrade in these names would reduce the value of the fixed income portfolio.

Portfolio implications

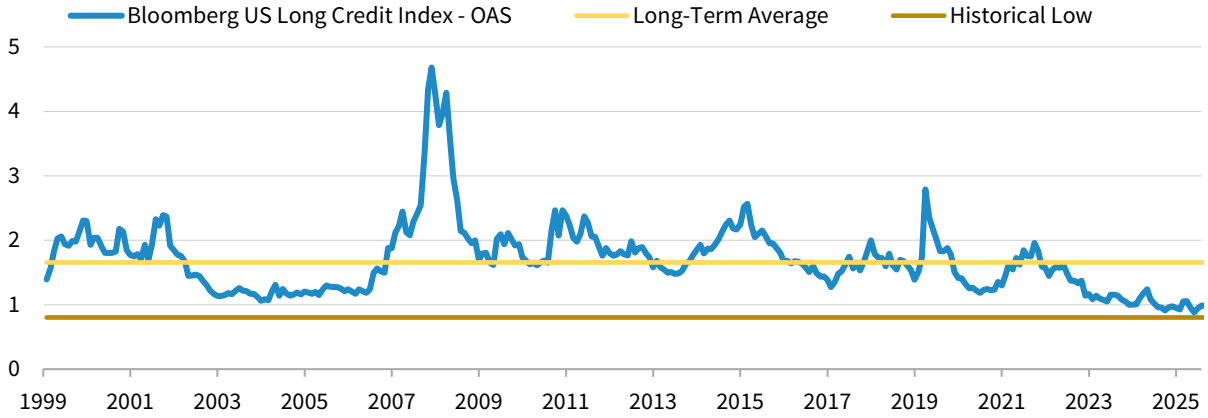
From a pure liability management perspective, there are limited options available as the use of AA-rated bonds for discount rate determination is generally required by US accounting guidance. Reducing reliance on a bond matching approach and migrating to using a larger portion of the universe could mitigate any future volatility and reduce the risk, although certainly not eliminate it. Measuring the liability on a broader index, such as bonds rated A or better can help smooth out the impact of the AI-issuance risk. While this methodology cannot be used for accounting purposes, it can create a more holistic view of the liability, which plan sponsors can use to design investment strategies, such as glide paths or any other aspects relying on a mark-to-market funded status.

Perhaps more options exist on the asset side of pension plan management. A common theme has been to underweight credit risk in general, especially as spreads have remained near all-time lows (Figure 3). As of September 30, 2026, the average option-adjusted spread on the Bloomberg US Long Credit Index was just under 100 bps, compared to the long-run average of 166 bps.

2 The broader list of AI and Hyperscaler names include: Alphabet, Amazon, AMD, Applied Materials, Broadcom, Dell, HP, IBM, Intel, Lam Research, Meta, Micron, Microsoft, Nvidia, Oracle, Qualcomm, Salesforce, SpaceX, and TSMC.

Figure 3 Spreads have remained near all-time lows

December 31, 1999 – September 30, 2026 • Long credit option-adjusted spreads (OAS) • Percent (%)



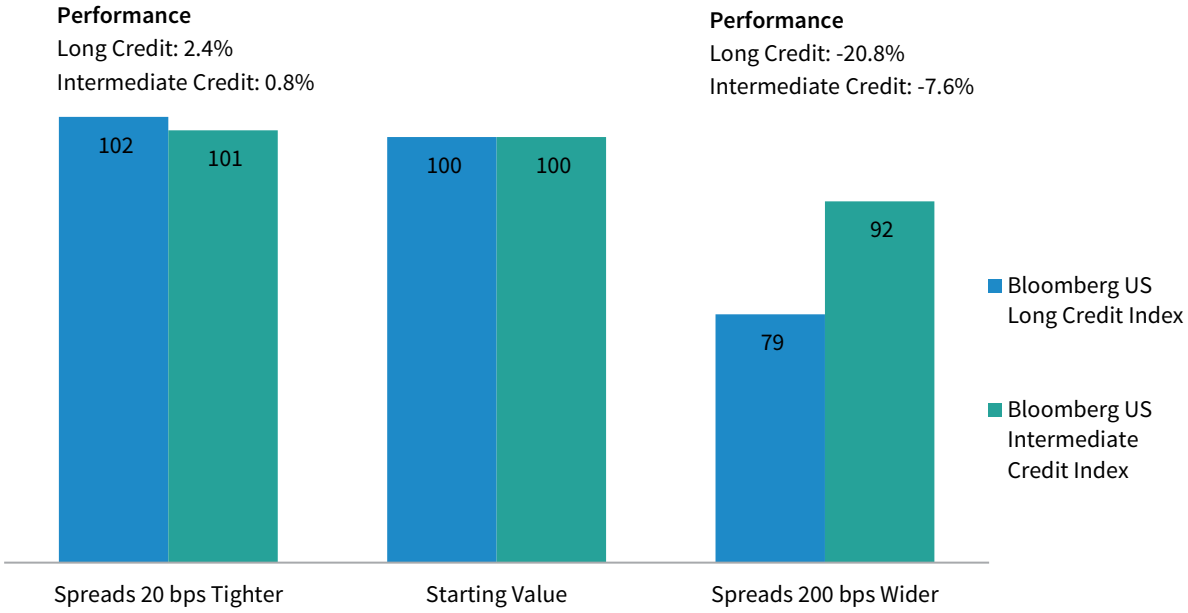
Source: Bloomberg L.P.

Note: Long-term average and historical low reflect month-end OAS data since January 1998.

At current levels, taking credit risk is not ideal as it creates an asymmetric risk profile. Credit spreads may stay at these levels or even continue to grind lower by 10 bps–20 bps and break through all-time low levels not seen since 1998, but they can also widen by 200+ bps from a severe market downturn. Reducing this risk may be most prudent now and with the right approach, can help protect funded status from the AI concentration. Figure 4 estimates the return expectations from these credit events on both the Bloomberg US Long Credit Index and Bloomberg US Intermediate Credit Index.

Figure 4 Credit's downside risk far outweighs its upside potential

As of September 30, 2026 • Long credit performance from spread changes (instantaneous change)



Source: Bloomberg L.P.

Note: Performance figures based on duration of 11.7 years as of September 30, 2026.

It's worth noting this phenomenon is different than equity-related risk, as equities can continue outperforming even as credit spreads remain range bound. Due to this, it may be more prudent to take AI exposure to equities than relying on credit markets.

There are two options to consider when plan sponsors wish to reduce credit risk.

1. REDUCE LONG CREDIT EXPOSURE FOR INTERMEDIATE CREDIT EXPOSURE. As foreshadowed in Figure 4, this is a pragmatic approach to reduce duration times spread (DTS), helping reduce funded status deterioration from widening credit spreads. In essence, if the credit spread duration of the fixed income portfolio is lower than the credit spread duration of the liability, funded status should improve from a widening event. However, it is important to note that the full impact of the liability decrease may not be realized due to the AI-issuance downgrade discussed in this paper. Nonetheless, shifting the portfolio toward intermediate-duration bonds can reduce the impact of spread widening on fixed income holdings and help protect funded status. This shift does not eliminate that risk, however, because the Bloomberg US Intermediate Credit Index is also exposed to AI-related issuance. There are also a few other considerations for this trade:

- This approach is effective only if the duration loss can be managed elsewhere in the portfolio
- It is helpful to consider the correlation between credit spreads and equities. Portfolios with substantially higher equity allocations can shift further away from long-duration credit.

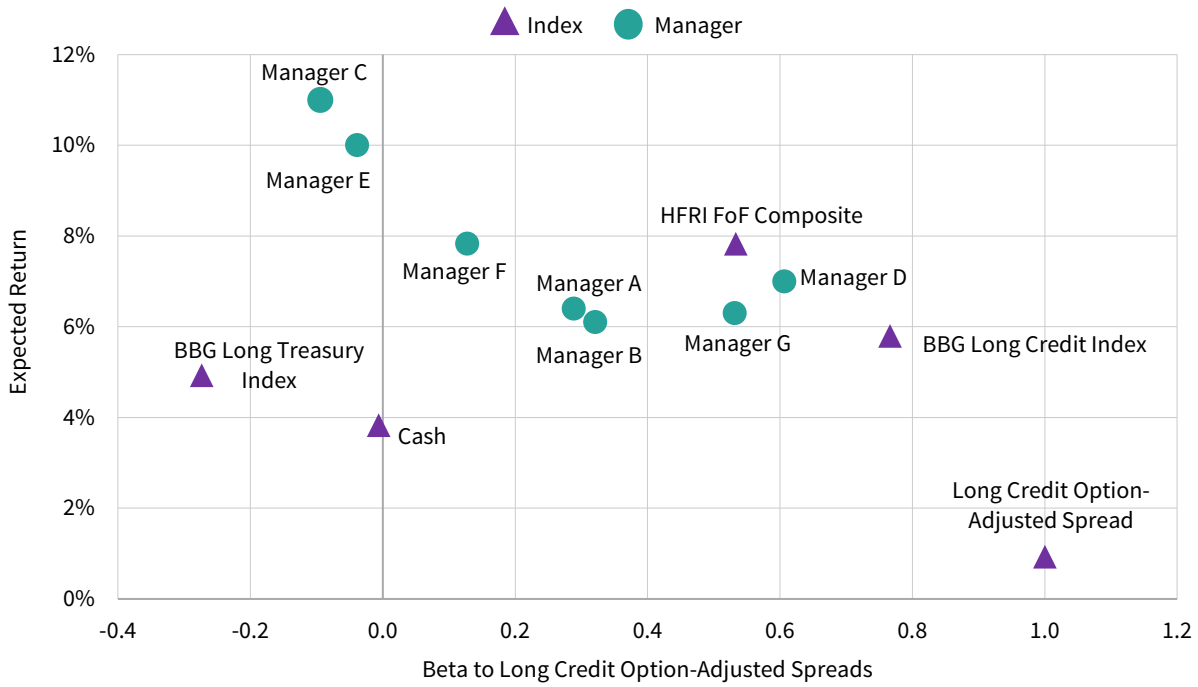
2. DIVEST FROM CORPORATE CREDIT ENTIRELY. A more refined approach may be needed at this time by moving away from pure corporate issuance into more differentiated assets:

- Securitized credit, such as asset-backed securities (ABS), encompassing auto loans, credit card receivables, student loans, and many other sectors. These assets would likely still have high correlation to credit as performance for both is still tied to underlying economic factors. However, if structured properly on tranche quality and sector concentration, this allocation could behave meaningfully different than corporate credit.
- Other securitized assets such as asset-backed finance (ABF), including inventory receivable, machinery or equipment, transportation assets, or litigation finance. These assets benefit from longer lease times, that are sometimes more immune from short-term economic contractions. They focus on economic infrastructure outside hyperscaler- and AI-related areas, such as data centers.
- Other esoteric, income based, or hedge fund strategies. These may include lower risk/lower beta assets to effectively transition the liability-hedging portfolio away from credit and reduce the risk of downgrades. Some hedge funds can take advantage of this dynamic since they have the option of shorting securities. Other multi-strategy hedge funds can generate returns in varied avenues. The objective being to include lower risk strategies with low correlation to credit spreads.

ABF strategies may offer lower correlation with corporate credit, but their liquidity and economic exposures vary. Some strategies do exist that provide monthly or quarterly liquidity in this space and could be great additions to a liability-hedging portfolio, assuming the rating quality is investment grade or closer.

Hedge fund strategies that have low correlation with credit spreads and equity markets exist, with ample liquidity as well. If duration and credit risks are managed, this allows for a reduction in liability-hedging allocations in favor of these diversifying asset classes. Figure 5 describes a few of these strategies, along with their return and beta relative to long credit spreads. Overall, positive yield pickup can be achieved with meaningful risk reduction. In many cases, the trade-off is continuously positive. A higher yielding manager can have the lowest credit beta. Liquidity considerations are important as described earlier so not every strategy may be applicable to each plan sponsor.

Figure 5 Manager options to diversify from long credit spreads
As of June 30, 2026



Sources: Bloomberg Index Services Limited, Cambridge Associates LLC, and Hedge Fund Research, Inc.
Notes: Expected returns reflect yield to maturity where available; otherwise, they are based on manager-provided information. Credit spread betas are estimated using 10 years of return history where available; Manager C's estimate uses only 50 months due to limited data availability.

Important considerations

Long credit has been a staple of liability-hedging portfolio due to its longer duration and great liability-hedging ability. However, modern hedging programs can achieve this duration in multiple ways, with the most effective being Treasury completion management. Under this approach, a specialized manager employs physical and synthetic Treasury securities (most notably Treasury futures) to maintain a target hedge ratio. The same amount of capital that is typically provided

to physical Treasury managers can be more effectively used to replace the lost duration from divesting long-term credit. The approach is extremely helpful to enable the changes discussed in this paper, as it means the overall duration or hedge ratio will not be impacted by the reallocation. In essence, the benefits include:

— Keeping interest rate hedging consistent

— Reducing corporate and AI-related exposure for less correlated strategies

— Increasing the overall yield and return of the portfolio

Another consideration, especially if selecting hedge funds, is manager selection. Hedge funds are a dynamic asset class with high manager turnover and niche strategies. Selecting, monitoring, and adjusting these managers to fit the right objectives is crucial to long-term success.

If done properly, the adjustments may result in a win-win-win combination and something all plan sponsors should be considering at this point in their pension plan management framework.

Conclusion

AI-related debt issuance has introduced a new concentration consideration for liability-driven investing (LDI) investors. The risk is not limited to credit spread widening or a decline in AI-related equities. For plans whose accounting discount rates are informed by AA-rated corporate bond universes, a broad deterioration in the credit quality of a concentrated group of issuers could also alter the discount rate reference set and increase reported liabilities.

Plan sponsors should therefore evaluate this exposure through both an asset and liability lens. The appropriate response will vary by plan, but should include a review of discount rate methodology, concentration within credit allocations, the relationship between asset and liability spread exposure, and the ability to maintain duration through Treasury completion or other tools. The goal is not to eliminate credit risk indiscriminately, but to ensure that the sources of funded status risk are intentional, diversified, and aligned with the plan's objectives. ■

Graham Landrith also contributed to this publication.

Index Disclosures

Bloomberg Long US Corporate Index
The Bloomberg Long US Corporate Index measures the performance of investment-grade, USD-denominated, fixed-rate, taxable corporate bonds with remaining maturities of at least ten years. It includes eligible securities publicly issued by US and non-US industrial, utility, and financial issuers.

Bloomberg US Corporate Long AA Index
The Bloomberg US Corporate Long AA Index measures the performance of USD-denominated, fixed-rate, taxable corporate bonds in the AA rating category with remaining maturities of at least ten years. It includes eligible securities issued by US and non-US industrial, utility, and financial issuers.

Bloomberg US Intermediate Credit Index
The Bloomberg US Intermediate Credit Index measures the performance of investment-grade, USD-denominated, fixed-rate, taxable corporate, and government-related debt with remaining maturities of at least one year and less than ten years. The index includes corporate securities and a non-corporate component comprising non-US agencies, sovereigns, supranationals, and local authorities.

Bloomberg US Long Credit Index
The Bloomberg US Long Credit Index measures the performance of investment-grade, USD-denominated, fixed-rate, taxable corporate, and government-related debt with remaining maturities of at least ten years. The index includes corporate securities and a non-corporate component comprising non-US agencies, sovereigns, supranationals, and local authorities.

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