

Chris Lyons

Episode 228: Navigating Private Credit and Alts: Insights with Chris Lyons of Voya IM



GUEST Q & A

Stewart: Welcome to another edition of the Insurance AUM.com podcast. My name Stewart Foley, I'll be your host. We've got a terrific podcast for you today. We're joined today by Chris Lyons, who's the head of private fixed income and alternatives at Voya Investment Management. Chris, thanks for being on. Thanks for taking the time.

Chris: Hey, happy to be here. Thanks.

Stewart: So we're going to start this one off the way we always do, which is where did you grow up? What was your hometown and what was your first job? Not the fancy one.

Chris: Yep. I'm a Los Angeles native, but moved to Atlanta, Georgia when I was seven years old, spent my whole life there. I joke; I worked for SunTrust Bank and if I'd have worked for Delta and Coca-Cola, I'd be the most Atlanta guy on the face of the planet. That was not my first job. My first job was in an un-air-conditioned warehouse in Norcross, which is no fun in the summer, repairing patio furniture.

Stewart: Oh, wow. I can relate. I live outside of Austin and it's plenty warm down here, I can assure you. So I can only imagine-

Chris: Longest with boiling pots of water around you and hot plastic straps in your hands is not quite as much fun as what I do now.

Stewart: Absolutely. And speaking of which, give us a little bit on Voya and what led you to insurance asset management? I think people love to hear, particularly younger folks want to hear. People think that you get into this seat as the head of private fixed income or whatever, and people land in that seat. But you have an interesting background and I'd love to get that on before we start going into our questions.

Chris: Yeah, yeah, sure. With respect to Voya Financial, retirement service company, health company and investment manager, it's taking people on the voyage to and through retirement. So, our insurance products help do that. But then you have the asset management products obviously because that's a key part of people's retirement journey. And I've actually been with the company for over 30 years, and so I've seen the change. It was originally ING who most people recognized as the big Dutch company in the US forced to sell off during the crisis and went public. So, I joined what I'll call Voya, sometimes I actually say ING. I've been with them so long, so excuse me if I do.

But I joined Voya in the early 1990s. I had a banking background. I went to Georgia Tech, didn't know what I wanted to do. My dad told me to get into banking. I listened to him, learned how to analyze companies, and a couple of years I got a call and it was, what was Voya Investment Management at the time, the predecessor, sounded like a more interesting job than lending money to car dealers in suburban Atlanta.

So I came over and went down the path as we talked before, CFA and all that stuff, and started doing what are US private placements, so what I think of as investment grade, private credit for our own balance sheet for 20 years, built a portfolio that's about \$20 billion from scratch. And then Voya actually started selling off its fixed annuity, variable annuity in life businesses. So our GA went from almost a \$100 billion to about \$35 billion today. And at that point, we had established ourselves very strongly in a unique value-add market within private credit. And not a lot of people

commercialized that business because the insurance balance sheets wanted all of it because the ALM characteristics and the yield characteristics.

And so we were one of the first ones to take it out and commercialize it, and ran that business for 10 years, took it from... We do about \$5 billion a year in lending in that market. Took it from being all for our proprietary account to about 90% for, call it 6 dozen third party clients in a fund. Ultimately they said, "Hey, you did pretty good at that, maybe we'll put you over the other platforms that you don't know a whole lot about the assets, but we figure you'll figure it out."

That's a long way of saying it. I apologize. I tend to be long-winded. For me, it wasn't a, "Gee, I looked at this." It was really everybody in their life gets the intersection of preparation and opportunity. That's really the definition of luck and you have to take the opportunity. A lot of people don't. Took it and turned out to be a good decision.

Stewart: That's awesome. I love that story. So there's been a fair amount of negative press on the growing risks of private credit. I think that is mainly... It's interesting, we had a guest on that talked about how this'll be the greatest distress class ever because this is about interest rates levels as opposed to problems in these businesses. But can you talk a little bit about the environment that the private credit market is facing right now and how are you managing those risks?

Chris: Yeah, so whoever your prior guest was, I don't disagree that you'll go through a distress cycle and you'll probably come out the back with a lot of these companies. Well, because there's a combination; it's not just a lot of money was borrowed and people assume that they'd have 3% debt or whatever it was for the rest of their lives and they don't. And we joke in my shop that if your business model can't work with a 3% cost to debt, you probably need to get in another business, right? That's pretty low.

Stewart: Absolutely.

Chris: And then you have the rise in rates. And so really what you would see is strain on profits of the underlying portfolio companies, mostly because of higher rates and also inflation leaking in and them not able to necessarily pass that along to the consumer in some sectors as well. That's a double whammy. Also, where I might disagree a little bit is it's going to depend on the markets in which you accessed leveraged private credit.

If you did it through covenant light structures, those deals will end up in workout because there's no trigger to get you to the table to renegotiate before the company's un-savable. But if you stuck to structure to financial covenants and corporate lending to appropriate debt service coverage ratio triggers and infra to appropriate triggers and private ABS, and that was the core of what you did and who you are as a lender, then what'll happen is you will get to the table while whatever the entity you're lending to is still salvageable.

And I think that people will work through that problem. So for us, look, there's always cycles where you have more problems than others. The hallmark of what we've always done, whether it's the US private placement market, whether it's infrastructure, whether it's private ABS, whether it's below investment grade, direct lending, is our catch basin in our funnel, we will kick a lot more deals out over structure than price.

When you lend money for a living, the returns are not asymmetric, you don't have any upsides, you just have downside. So your job as the investment manager is to fight against that wall that's trying to collapse on you, and you do that with covenants. So, we've always stood on structure. We also are very willing to use the structure in a strong manner when there's a violation. Some people get a covenant violation and they're afraid to use it, right?

They're afraid to enforce or negotiate an economic result out of it because they're afraid the company will get worse. You have to be willing to use your covenants and enforce it and extract economic value. We're good at that. And then we don't just focus in corporate lending or in health and tech or... In fact, we avoid tech as a lender, right? Technological obsolescence is very hard to predict over 10 years. I'm not that smart, and I don't want anything to do with lending money to something where the government 5 years later can change their mind on my reimbursement rates and that kills my company.

So we avoid some sectors because of that, but we also do a lot of investing through our broad private credit platform. We do it specifically as well in infrastructure. First deal I did 30 years ago was a dual cycle combined natural gas plant in the Northeast. So I've been doing project finance, been doing infra since before infra was cool; that's maybe a good way to put it. And then also all the way back in the early 90's, did the first MRI receivables equipment deal in private ABS. And so we

managed it by diversifying across assets that aren't necessarily in the cross-hairs of everything and have different ways of getting home and act differently in different environments.

Stewart: One of the things that comes up frequently on our podcast is liquidity, and it's very important to insurance companies, particularly if they have a need to raise capital to pay claims as an example. How have you seen liquidity evolve in private placements and private credit?

Chris: Yeah, so if you look at private placements is what's actually rapidly developing to what people are calling private credit investment grade because you have more structured product coming in, that's investment grade and that's a good thing. The liquidity in that market, I'm a true believer that the level of illiquidity or the lack of liquidity is vastly overstated. So, in the private placement market, which is 85% syndicated and has more demand than supply, if you look at statistics from some of the leading agents or one of the leading agents, I won't name their name since I don't know if I can or not, the average private placement has 12 investors in it. It's also oversubscribed by two times. So what you have is people that do a lot of work on a deal and then only get half of what they want. So if you're an idiosyncratic seller of a piece of a loan that has 11 other investors 3 years down the road because you have a liquidity issue and nobody else does, if that credit's performing, there's literally 11 people sitting on the other side wanting to buy it because they're under allocated to the name and they've done a lot of work.

And we have experienced, we have the leading broker trader in private placements, mark our book every year into a one week, two week, three week type of liquidity issue. And his opinion is our book, 86% of it today in a normal market and environment, we could have a trade and be done in two weeks. And then we've also had situations where we've taken investors up to their strategic asset allocation, so we're not building a loan book anymore. Now, we get to a point where they wanted to have 12% of their assets in privates, now it's at 12%. We start to run it more like a public book and we'll sell tighter deals and buy wider deals to maximize their yield.

We went through an exercise after we sold our fixed annuity book where our general account ended up over allocated to privates in the RemainCo. And over a four quarter period we did, I think, 107 trades at like 99.9% of our prior months mark. So we've lived the liquidity of selling on that side.

I think that what happens is you still get what people call an illiquidity premium in the private placement market. It's really an opportunity cost premium because you don't hire a public manager to perform to the benchmark. You hire them to generate alpha and you generate alpha by sector trade, name trade, up and down the curve by trading. Private placements, even though you can trade them or a buy and hold mentality. And so for an allocator to say, "I want privates," they're giving up the opportunity for their public bond manager to generate alpha. And so you have to get something for that.

I believe that's why there's the consistent upfront spread. I do not believe, with the exception of club deals, where there's maybe two people and certainly directly originated bilateral loans between one insurance company and the borrower are completely illiquid because nobody has the information, but the syndicated market, you're getting paid for the opportunity cost, not for the illiquidity.

Stewart: And to go back, you said 85% of the market is syndicated?

Chris: Yes.

Stewart: Okay. So that is, I think, a really insightful review of liquidity. I've never heard it put in real concrete terms where you've got numbers on it and you can back it up. So thanks for that.

Chris: Yeah. We've lived it, Stewart. And now that's the US private placement market. When you get into direct middle market lending and the market that's developed over the last 15 years since the crisis, there's not as great liquidity, but it's improving significantly.

Look, a lot of these are put into funds and where the liquidity happens is really through LP trades. And so what you are seeing and what people would think of as direct middle market lending below investment grade private credit is you are having the private credit secondaries business ramp up. It's been growing at 18% a year. So if you think of private equity secondaries, which is an established business, you've had big growth in private credit funds and now you're seeing big growth in the trading of the LP units underneath.

So let's say you're XYZ Insurance Company, you get into a liquidity issue, you have 20 LP interests in various credit investments in your alts book, you might come and trade 8 of those out. They all have 30 underlying names and there are people setting up funds to buy those private credit secondaries. And so I think the liquidity is improving, but it's through a different channel. I haven't seen the real loan to loan trading in that area like you see in private placements, but you see it through the structured vehicles in which you own that type of level of private credit.

Stewart: But Chris, I mean to me what you're saying makes perfect sense because there's a lot of growth in private credit by insurance companies and it's been talked about, the regulators are looking at it, and blah, blah, blah. But the reality is that the more people in this market, the better liquidity gets, right? I mean it stands to reason and it's a one direction trade at the moment as folks are seeing real value in this market. Here's a knuckle ball for you. Do you think real estate has reached an inflection point?

Chris: That's a harder one for me because I'm over our real estate group, but it's not something I live every day. I'll recant the experience of our manager. And I actually think maybe you've talked to him, Greg Michaud, who's fantastic-

Stewart: We did.

Chris: ... been with Voya. Greg and I joke, not to go off column, that we were 24 in Atlanta running around having a good time. And here 30 years later, we're both bald and we put 7 kids through college. So we've been together a time, right?

Stewart: That's great. But that's how this business works, right?

Chris: That's how this business works.

Stewart: I mean, it's a community of people who've worked together for a long time and is often the case.

Chris: Yeah. Look, if you think about it by sector, I don't think there was ever really a bottoming in distribution because of everything going on. I think retail is a slower burn trade in the bottom because you have to have rent rolls that were signed before COVID and it's more of a slow bleed. It's the experience of your local strip center. The nail shop has been there because they signed a lease and now in 2025 the lease is up and they can go across the street for 40% less. You're not going to retain the same lease to keep them there.

So I think in retail you don't have the dramatic downside problem of office, but I think it's a slower burn. And look, COVID accelerated the away from bricks and mortar retail trade probably by 10 to 15 years. And so that's playing out. Apartment space has been good. Look, it got overheated, you're going to have problems in various sectors in various areas, and I think there's still a little bit of that to come, but some of that's flush through the system. The real problem's office.

And the real problem is it's all over the place, but gateway city trophy properties where you just paid too much per pound for the steak as one of the guys in our real estate like, "What'd you pay for pound?" You overpaid. And you just don't see the return to office like people had hoped it would be. I think that one's still got a ways to play.

Now, from a Voya perspective, Greg has and his predecessor, Maurice Moore, always shied away from office because if you ever get the keys back on an office property, you have to put a lot of CapEx into releasing it and TNI, whereas distribution or even apartment, just slap some new doors on the cabinets and granite countertops and new carpet and you're off charging more and releasing it.

So we are very light on office. If you look at all of the big insurance company managers, we have the lowest percentage of office in there. And I think partially due to our size, we never had the size to be a big investor in the huge property. So we focused on secondary and tertiary markets in terms of cities and stayed away from the gateway areas where it was really high price.

There's pain to come, people are going to get keys back, we've got some problem loans, a very low percentage relative to others, but I don't think it's quite over yet. I think you're starting to see the back of it. I do think it's the time and we're doing it at Voya. Greg's working through a process right now. I think we're going to be coming out with a CML with a commercial mortgage loan opportunity fund that's down the balance sheet from where we've been. And that's based off a lot of the relationships Greg has. But the performance that we've had through the cycle, we've done very well through the downside. And when you do that, you should come up. And I think if you're going to do that type of business, now is the time to be doing it. You don't want to wait another year or year and a half. People are going to be ahead of you in the fundraising cycle to pick the term.

Stewart: Just my professor radar popped up when you were talking about real estate CapEx and you used the term, I think you said TNI. Can you tell me what that means, what that is?

Chris: Tenant improvement. So the guy who had it before wanted this configuration because he used it this way. The guy that takes the space needs you to do a bunch of work to make his office work. Offices tend to be much more costly in that tenant improvement or re-tenanting work. Then think about a distribution facility where it's a warehouse with 20 foot ceilings. There's not a whole lot you're going to be doing there. Right?

Stewart: Right, exactly.

Chris: Look at the market price and put some money in.

Stewart: That's super helpful. So what's next on the horizon for your teams as you look out today?

Chris: Yeah, so one I've already mentioned we're looking very hard at starting a private credit secondaries business. We actually are starting it. We're in the market looking for trades now to kind of test it, to test out what we think our return thesis is. I personally love the asset class as a deep credit investor.

If you think about it, you'll buy, call it 15 to 20 LP interests or GP continuation funds, however you get the assets. On average, those are going to have, call it 30 names. So now you've got a credit portfolio with 600 names of diversification that looks a lot like a CLO, you've bought it at a discount to nav. We're looking at it across corporate credit, infra and real estate because we have the expertise to do all three. And so you're looking at 600 names of diversification and you're looking at what we believe will be returns that are probably 300 basis points above standard middle market returns.

So, you get enhanced middle market return with CLO level diversification, and then you slap what's called a rated note feeder over it where you make the senior tranches very attractive to insurance companies and the first loss piece goes to your unregulated investors at a 20 plus percent IRR. I think it's a great business. You need to be very, very good at managing credit portfolios and deep line item underwriting, re-underwriting loans in the portfolio. That's a big one.

We'll be in the market in about a month for fund number two with our infrastructure subordinated Mez fund, our REIT product is what we call it, that focuses on renewable energy and sustainable renewables outside of power and looks to come in and provide an equity dilution alternative to developers as they go from development to construction. Tend to be 2 to 5 year loans. Fund one has been doing fantastic.

Essentially it's net returns are where the gross we're promised, right? That's always a good thing for your investors the first time around. You've got a lot of tailwinds behind you there, right? At a state level you have pushes towards requirements around renewable energy, AI and everything happening in terms of data centers is going to be a big draw on power. So you're not just trying to convert from fossil fuels to renewables at some pace, but your need for power is growing at the same time. So, all sorts of opportunities there in the long term.

I mentioned the commercial mortgages. If you performed well and you're not going to get bogged down for the next two or three years by all your problems, you should be able to very much accelerate out in that manner. And then what we're seeing from what I'm seeing being in front of clients with a lot of insurance companies is the liability streams have been changing over the past few years for our clients and potential clients.

Where historically it was, "Hey, we want something that's 8, 9 years duration X, Y, Z," and you're seeing more business lines come in where more of our clients want short paper and yield. So our REIT product fits in there, private credit secondaries do fit in there. Our enhanced middle market product fits in there, our direct middle market lending. A lot of what we do and we've kind of grown up doing in this space, you have the insurance liability side of the balance sheet coming to you needing that product.

And so for us, it's being realistic about what our capabilities are and what we're able to do financially to stand up a business appropriately and responsibly as a firm so that we can serve the client and what we tell them we're going to give them and honestly make money for ourselves as well, right? We're not going to be everything to everybody, but we're definitely going to lever off the strengths that we've had in the past and look for those tangential opportunities.

Stewart: That's super helpful. And so on the way out the door here, I'm curious to know if you think there's one area that clients are overlooking, and to tack onto that question, is there a risk that you think is being missed or is being under-priced today?

Chris: Yeah, so on the opportunity side, one of the platforms that reports up to me, and we have a hedge fund product in it, so it makes sense, it's some public assets and some privates. It goes in as our mortgage derivatives strategy. We have the mortgage investment fund, which is a long short fund in the space. Those guys are fantastic. It's a small team, they're the smartest guys in the room. The guy that runs it was a math professor and there's two rocket physicists on the team. When I took over the team managing it, I had to go in and check their math on their prepayment models. And once I realized they were right, I got out of the way.

Stewart: I love it! I love it!

Chris: So where we see a lot of value there is in IOs and reverse IOs. So, any kind of mortgage product where the tranche of what you're buying, higher rates force it to stay out longer where you make more money. That's what an IO is. The market hasn't priced in rates and the stability of rates higher for longer. And so where you've seen spreads in corporate lending space, particularly in the public area, collapse in over the last two years to getting close to all-time tights. You haven't seen that in the IO trade on the mortgage side.

And that can run through mortgage servicing rights. And there's various ways to play that that are probably too deep for you and me to talk about. But there's variety of ways. And you're looking at... You probably have 300, 400 basis points of spread tightening still sitting there on what a lot of is a AAA asset class.

So from an insurance standpoint, it's great because it's non-correlated with other assets, with credit assets. It's highly rated from a wharf standpoint, risk adjusted ratings or risk adjusted credit quality for an insurance company. It helps there. What does make it difficult for an insurance company is accounting-wise, it's a little bit complex. And so it's something that we've done for the general account since I joined in 1990. We've been doing this forever for our own account. We do it for a couple of other insurance companies, but again, the accounting stuff's tough. It's been most sellable through that hedge fund product and then out to pension funds, but definitely and undervalued space.

The spot that I worry about that's really specific to us, and this is very specific to us, is on the infra side and the renewable side, not necessarily with our mezzanine fund because we don't have a whole lot of competitors there yet. People haven't figured out that stratification of the liability side of the project balance sheet yet. But the long-term, senior lending that's done, anytime you get outside governmental, whatever you want to call it, influence into a market that pushes against the natural economics of a market, you get overpriced assets.

And so what we've seen in call it solar, wind, traditional space, senior lending is we've seen the credit spreads relative to other infrastructure assets collapse on the lending side, probably to a point that you're really not a lot of times getting paid for the risk buying that asset, because they want to check the green box. And so anytime I see something like that happen, it concerns me.

Do I think it's something that 5 years down the road leads to an implosion in senior level loans to utility scale solar projects? It's not going to be a default issue. It's going to be a, you weigh under price the risk from a capital standpoint and for insurance companies that's not as bad as default and losing the first dollar, but nobody wants to buy an asset that's you priced at BBB for capital and ends up being a BB the whole time you own it. And you see the level of pricing relative to the debt service coverage ratios that are not going up, they're staying stable, but the price and the ratings staying the same and the price is coming down that I think you're getting the risk of frothiness there. And again, anytime you put outside influence into a purely economic situation, you run the risk of one side of that trade or the other.

Stewart: Well Chris, you have covered a lot of ground and you've done it very well and I really appreciate you being on. I've got a couple of fun ones for you out the door if you're interested.

Chris: All right, take a shout.

Stewart: You mentioned working with one of your colleagues for quite a while and the question goes like this, what advice would you give a 25-year-old Chris Lyons today? As you look out the financial markets, you look out at the traction that AI is getting, college students are coming out with degrees that haven't incorporated some of these changes as they look out into the world. And you've got younger people on your team I know as well. So what's a piece of advice that you'd pass along to somebody who's a little earlier in their career today?

Chris: Yeah, so I actually do this a lot because I've got kids that are entering the workforce. Voya is actually very active in a mentor/mentee type of program with senior folks. And then you manage a lot of people and it's one that you got to be serious about. I'm kind of a goober for Kenny Chesney, not like the old-old, but more the beach Kenny Chesney, but he has a song, I Didn't Get There Alone. So nobody gets there alone, so you got to give back. So we spend a lot of time doing that at Voya.

To me, that the quick punchy one is don't pick a career that a smart guy can write an algorithm and run you out of business. I gave that to my oldest kid who's now 26 and doing great, and that's what he did. He took his intellectual talent, but he picked an area where there was still the human touch that can't be replicated.

Maybe it can be, I'm not that smart about AI, but it's pretty tough. The more broad guidance I give to people in the firm is don't worry about what you're making or what's happening when you're 25 other than experience. You want to worry about the money that you're making when you're 40. It'd be great if we all made it when it's 25, don't get me wrong, I'd love that. But where are your part peak earning years? And then you had to do a realistic evaluation of your skillset and what you like to do.

Find that intersection and then within the context of a company, understand the company you work for, what they do, and what values, what you like to do, and what you're good at. And then find the part that you think in 15 years you can have a thesis that's going to be the big revenue generator and money maker within the firm.

Now, you can translate that outside of the firm, but my advice is you want to put yourself in a position where you're happy with what you're doing and put yourself in a position. My dad always said, if you're going to work for a company, you might as well work for the part that makes the money. So figure out if you have that skill set and that interest, and then go consciously target that area and try get into it and get a foothold and start your career there. You might get 15 years out and you were totally wrong and that area stinks and you don't make any money, but to me, that's the thought process that kids should have to go through. I got lucky. It was kind of left up to luck to me. I didn't plan my career that well, but looking back, it could have been better if I'd have had that thought process.

Stewart: It looks to me like it worked out pretty good for you.

Chris: Yeah, it's been good. But the advice I'm getting, it's the old joke, athletics, those who can't do coach. Right?

Stewart: Right. That's true. Yeah, I get it. So, okay, last one out the door. Lunch. A lunch table, you can invite up to three guests: one, two, or three, alive or dead. Who's going to lunch with you?

Chris: Oh, my God. Never thought about it. It's like the dream foursome, right? I take my dad.

Stewart: Your dad, all right.

Chris: Dream foursome. I probably take one of the guys that works for me now because I enjoy him so much. He's the person that took over the PCIG business for me, Justin Stach, he is a fun guy to be with and very interesting. It's not that I can't have lunch with him anymore, I can't have it with my dad anymore. And if I took somebody, gosh, from history, that's a hard one. I don't know. Somebody like Abe Lincoln. Ah, you know what? Actually, Teddy Roosevelt.

Stewart: Oh wow, we've had Teddy Roosevelt before.

Chris: I like the concept of the man in the arena.

Stewart: You know what? I do too. I love that quote. I really do. I've really enjoyed the conversation. Chris, thanks so much. Thanks for being on. Thanks for covering all the ground that you did, and thanks for some great advice along the way. So thank you.

Chris: Thank you. Appreciate it.

Stewart: We've been joined today by Chris Lyons, who's the head of private fixed income and alternatives at Voya Investment Management. Thanks for listening. If you have ideas for podcast, please shoot me a note. It's stewart@insuranceaum.com. Please rate us, like us, and review us at Apple Podcast, Spotify, Google Play, Amazon, Stitcher, or wherever you listen to your favorite shows. My name's Stewart Foley, and this is the InsuranceAUM.com podcast. We'll see you next time.