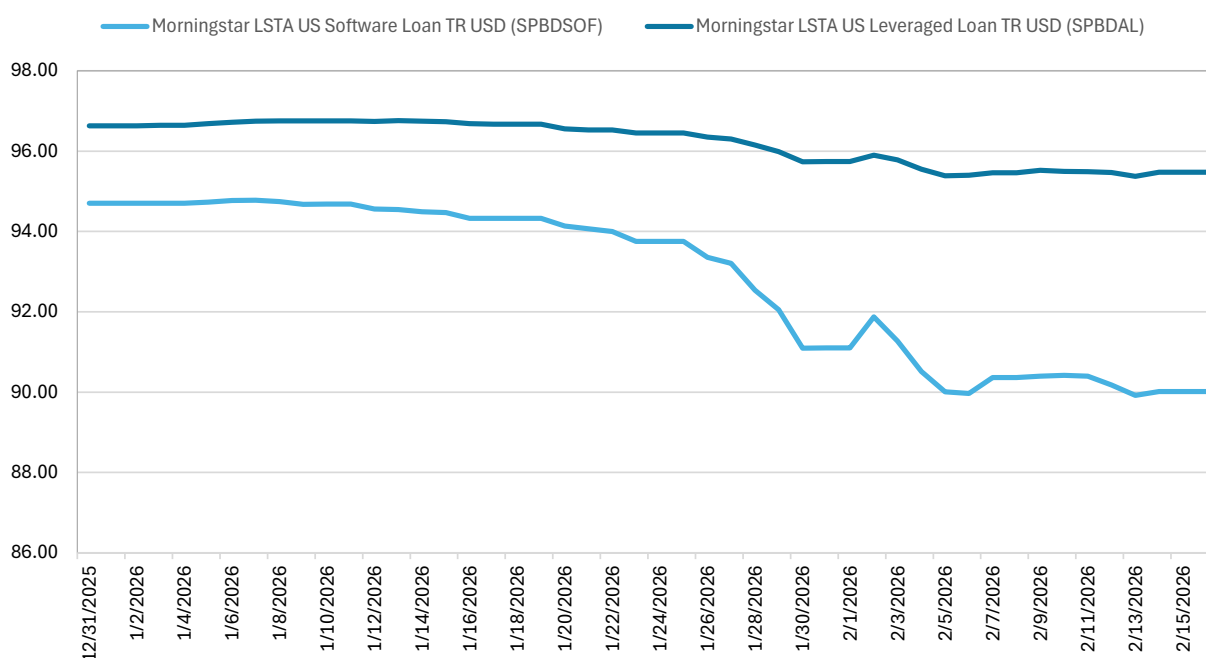


Attack of the Bots

Across both equity and credit markets, the software sector has experienced a broad-based sell-off beginning in mid-January and extending through February. The market sell-off has been largely attributable to growing fears that AI—once viewed as a tailwind for software companies—could ultimately displace these businesses, their products, and their processes.

The impact has been particularly felt in the loan market. Year-to-date, the average price of software issuers in the LSTA U.S. Leveraged Loan Index has declined by nearly 5 percentage points of par, materially underperforming the broader loan index, which is down about 1 percentage point of par.¹

Software Loans Have Underperformed the Broader Loan Index¹

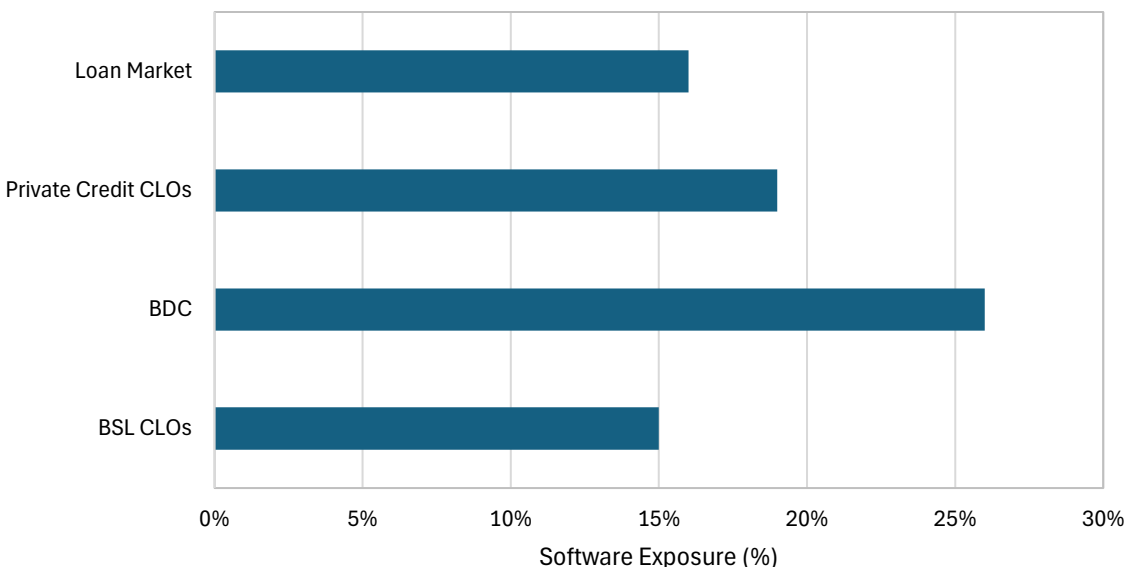


While software exposure in U.S. broadly syndicated loan (BSL) CLOs is meaningful (on average roughly 15% of total CLO held loan portfolios), it remains well below software concentrations observed in BDCs and private credit CLOs, which stand at approximately 26% and 19%, respectively.² Moreover, BSL CLOs benefit from structural diversification constraints (for example, single borrower concentration limit typically set at 1%) and active management by CLO managers, which have allowed portfolios to maintain lower software exposure than the broader loan market.³

¹ Pitchbook LCD, as of February 16, 2026.

² Morgan Stanley Research, as of February 9, 2026.

³ Morgan Stanley Research, as of February 9, 2026.

Software Exposure is Lower in BSL CLOs²

Notably, the sell-off in software borrowers has been largely indiscriminate. Even software companies that delivered robust earnings were not spared, as market attention shifted away from near-term performance and toward longer-term uncertainty. For example, Ultimate Software (UKG) and CSC—both viewed as AI-exposed names—were upgraded in recent weeks following rating agency commentary highlighting strong fundamentals.⁴ However, after an initial post-upgrade price rebound, both loans traded down and remained down year-to-date. We believe this underscores what appears to be an overreaction driven by sentiment rather than credit fundamentals. More broadly, AI-exposed software loans are now trading at lower prices than the chemicals sector—*despite software having fewer CCC-rated borrowers.*⁵ We believe this suggests a temporary dislocation rather than a deterioration in underlying credit quality. Additionally, most software companies have low loan-to-value ratios which points to the sell-off being primarily an equity repricing driven by growth and AI-disruption concerns rather than a more fundamental and dramatic debt service deterioration.⁶

However, long-term AI concerns are not unfounded across a broad swath of business models and industry sectors. We would have greater near-term concerns about outsourced call center business models (and loans thereto), to name just one example. Based on discussions with our CLO managers, horizontally-integrated software companies—particularly enterprise SaaS and general-purpose software providers—face the greatest long-term risk from AI, as their products and workflows are more easily replicated or substituted by AI-enabled solutions. In contrast, vertically-integrated software companies appear relatively more insulated due to deeply embedded workflows, proprietary data, and regulatory constraints which add more frictional costs for customers looking to replace those companies for AI-based solutions. In addition, these businesses are actively working to implement their own suite of AI-based products and processes that may complement their existing products and solutions.⁷ However, regardless of whether

⁴ Bank of America Global Research, as of February 6, 2026.

⁵ Bank of America Global Research, as of February 6, 2026.

⁶ Clarion Capital Partners, as of February 12, 2026.

⁷ Clarion Capital Partners, as of February 12, 2026.

software companies are horizontally or vertically integrated, AI-related risk should be assessed in the context of incumbent displacement risk and the degree to which the software is embedded within customers' systems, workflows, and operating processes. Furthermore, we believe AI risk should not be viewed as unique to the software sector, but rather as a potential source of disruption across all industries.

Looking ahead, loan prices are likely to remain volatile in the near term. This volatility could create buying and par building opportunities for certain loans that sold off as part of the broader AI-related sell-off, but are still fundamentally stable and attractive. One of our CLO managers indicated they passed on several credits for insurance brokers as too pricey at new issue, however, they can now buy them cheaper and at much improved relative value in the secondary market. Fears that AI bots will become the prevailing way to sell commercial insurance seem overblown at the moment. While the path forward may be uneven and highly dependent on company-specific vulnerabilities, we view the current sell-off as a pause and reset rather than a sector decline. We, of course, welcome the sell-off where managers can buy secondary loans at better entry prices and implicitly wider yields.

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