LSEG Yield Book
Analytics Research Report

Quantifying Software Risk in CLOs

March 2026

Executive Summary

- Sharp loan price selloff due to AI disruption fear rocked the CLO market with 16% software exposure. From early January to end of February, the software loans saw a steep drop of over 7pts, while market overall saw a modest 2pts decrease in the same period.
- We classified 633 software companies with material exposure across the CLO space by differentiating structural durability of their business models, resulting 33% of issuers in Category 1 (least vulnerable) and 57% in Category 2 (vulnerable), and 10% in Category 3 (most vulnerable to AI disruptions).
- Category 3 issuers clearly lag in credit metrics with the largest loan price drop. But Category 1 and Category 2 issuers are mixed in terms of loan characteristics and price movements.
- With empirical cross check using LSEG Yield Book CLO Credit Model outputs, our study found the market could be oversold for both Category 1 and Category 2 software issuers at current levels, while the pricing of Category 3 might be fair with the incremental default risk matching historical benchmark for low-moat software firms.
- We also examine CLO software exposure risk with top 20 CLO managers, recent vintages 2020-2026, reinvestment period status, and top 10 software issuers, and by applying rating downgrade scenarios.
- The underlying credit profile of the software sector remains healthy with lower CCC% and default% compared to other sectors, in contrast to what headlines may suggest. While the near-term software maturity wall is light, it rises steeply in 2028 and 2029, which can be a major concern for Category 2 and 3 issuers.
- Private Credit CLOs hold significantly higher software exposure than BSL deals, but downgrade risk is being offset by enhanced structural protection.

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LSEG DATA & ANALYTICS

Software selloff driven by AI fear

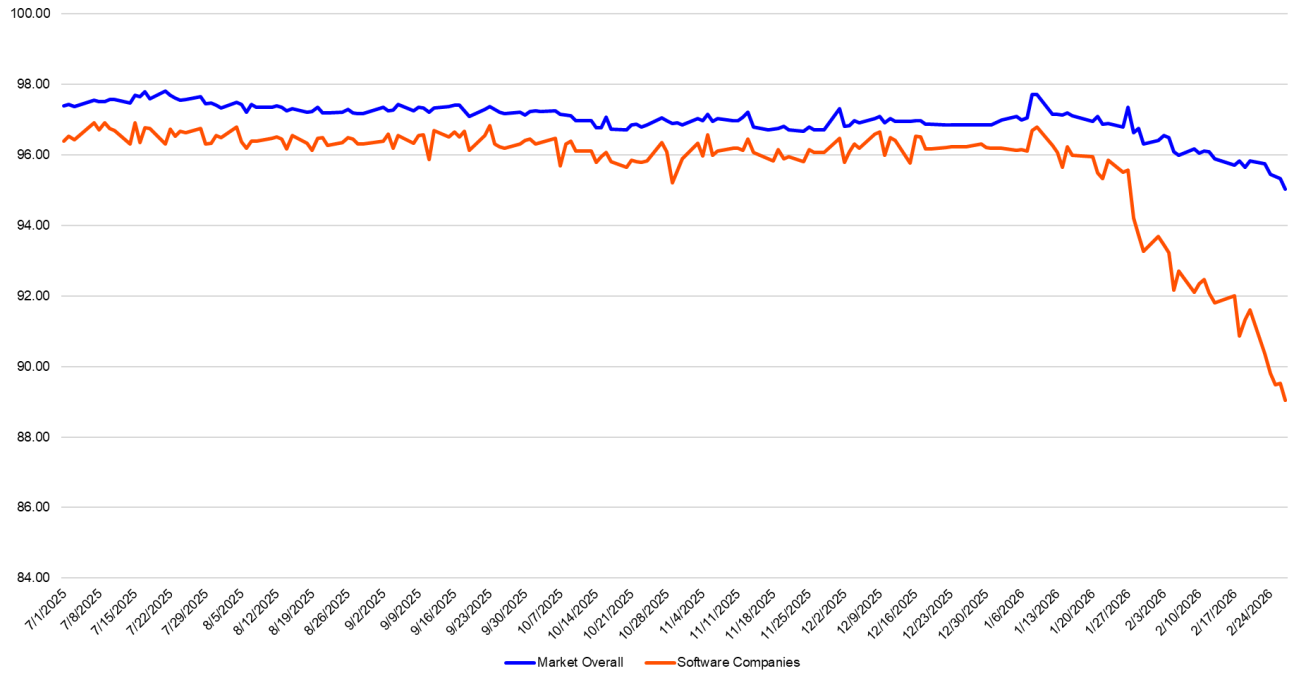
Entering 2026, the software sector has faced mounting pressure as equity markets reassess the long-term viability of traditional software business models. The shift was triggered by the rapid rise of advanced AI agents, especially new workflow-automation capabilities recently introduced by Anthropic. These innovations have fueled concerns that AI may displace or reduce demand for many established software offerings, particularly those dependent on manual processes or seat-based licensing structures.

As these worries grew, investor sentiment weakened across the broader software landscape. What began with concerns around professional services and data-centric platforms quickly broadened into a sector-wide selloff, as investors grew cautious about how quickly AI might reshape competitive dynamics and whether legacy monetization approaches can adapt. This uncertainty prompted a rotation out of software and into segments of the market perceived as less vulnerable to structural disruption.

The market pullback also extended into the CLO market, where software stands out as the one of the largest sector exposures in collateral portfolio. We identify roughly 16% of loans related to software sector in the CLO universe (based on S&P industry classifications for IT Services, Professional Services, and Software – we will use the same definition for "software sector" throughout this article). With fears rising around long-term business-model disruption, lenders and CLO managers have adopted a more conservative stance toward software loans with heightened scrutiny, and CLO credit investors become more selective while evaluating the implications of rising downgrade and default risk.

In Exhibit 1, we showed the daily weighted average price of the software-related companies versus the overall market since July 2025. After reaching session high in early January, the price of software sector started to fell, along with the softening of the broad market. The two lines diverged significantly from early January to end of February, where the software sector saw a steep drop of over 7pts, while market overall saw a modest 2pts decrease in the same period.

Exhibit 1: CLO loan price movement of software sector vs. market overall



Source: LSEG LPC, LSEG Yield Book (March 2026)

CLO loan issuer tiering: not all are the same

While almost all software companies are in distress, they are not necessarily subject to the same level of AI disruption impact. The logic is simple, the more entrenched a software is in user's system, the less likely it will be displaced by AI. In this study, we try to classify 633 software companies with material exposure across the CLO space by differentiating structural durability of their business models. Durability reflects switching costs, workflow embedding, data moat, and regulatory constraints. In below we attempt to define three distinct categories of software firms ranging from Category 1 (least vulnerable to AI disruption) to Category 3 (most vulnerable).

Category 1 — Core Infrastructure / Systems of Record
These issuers operate mission-critical systems with high switching costs and regulatory or operational dependencies. AI is predominantly additive (e.g., automation, analytics).

Example: Boxer Parent (BMC Software) — enterprise IT management (mainframe management, ITSM, AIOps) embedded deeply in customer operations, with very high switching costs and mission-critical workloads.

Category 2 — Operational Workflows & High Touch Services
Companies providing workflow platforms or relationship driven services where AI can streamline tasks but cannot fully replace human governance, integration depth, or physical operations.

Example: Polaris Newco (Solera / Omnitracs / DealerSocket) — automotive/fleet workflow software with ~85% recurring revenue and deep integration across insurers, repair shops, and dealers.

Category 3 — Commoditizable Tools & Easily Replicable Services
Issuers delivering standardized tools or content with lower moats and higher susceptibility to AI-enabled substitution, bundling, or price compression. Historical analogues show concentrated defaults and faster rating migration among low moat businesses.

Example: Gen Digital (Norton/Avast/LifeLock) — consumer cybersecurity and identity-protection tools operating in a competitive, low switching cost environment where AI can replicate core functionality.

Exhibit 2: CLO loan issuer classification results summary

Category	Count	% by Count	Avg. Facility Size	WAS	WARF	B3/B- %	Caa/CCC %	WAP	WA Px Change	Par ($bn)	% by Par
1	123	33%	980	327	3469	39%	9%	89	-6.75	54.07	5.34%
2	430	57%	610	349	3332	49%	7%	91	-6.30	93.08	9.20%
3	80	10%	475	366	3674	38%	18%	81	-11.24	16.26	1.61%
Total	633	100%	719	344	3411	100%	100%	89	-6.93	163.41	16.14%

Source: LSEG Yield Book, Trepp (March 2026)

We see most of the CLO loan issuers concentrating in Category 1 (33%) and Category 2 (57%), while Category 3 only has 10%, indicating a relatively small exposure in software issuers most vulnerable to AI disruptions. The classification is also consistent with average facility size and loan spreads with smallest facility size and widest spreads issuers classified as Category 3, and largest facility size and tightest spreads issuers classified as Category 3. On the other, Category 1 seems to have higher WARF, higher CCC%, and lower prices than Category 2, which is a little counter-intuitive, but that could mean Category 2 issuers might have stronger financials and better credit metrics than Category 1 issuers, before the AI disruption eventually takes effect.

Is the selloff overdone?

To test whether software market price actions align with historical disruption patterns, we applied the LSEG Yield Book CLO credit model to four representative "typical loans"—one for each AI-exposure bucket (software loan Categories 1–3 and market overall including both software and non-software loans). Each typical loan used average observed attributes (rating, spread, remaining maturity, etc.). We ran the model using two price points for each bucket: the beginning-of-year price and the current market price. The difference in model-generated cumulative default rate provides a measure of incremental default rate implied by loan price drop for each category. To screen out the macro distress which applies to all loans, we would compute the net incremental default rate (for category specific risk) by subtracting the incremental default rate from the "market overall loan". Finally, we try to compare the net incremental default results with historical benchmarks of default increase resulting from prior technological shifts (e.g., cloud migration, workflow automation, dot com displacement, etc).

Exhibit 3. Empirical cross check using LSEG Yield Book CLO Credit Model outputs

Category	Early January Price	Model-Implied Cum. Def. Rate	End of February Price	Model-Implied Cum. Def. Rate	Model-Implied Incremental Default Rate	Net Incremental Default Rate	Historical Benchmark of Default Increase
1	95.89	11%	89.14	13%	18%	8%	0%
2	97.39	9%	91.09	13%	44%	34%	20%
3	92.47	12%	81.24	21%	69%	59%	60%
Overall	96.99	9%	95.02	10%	10%		

Source: LSEG Yield Book (March 2026)

- Category 1: Market-implied default increase is 18%. After subtracting the 10% overall systemic increase, the category-specific effect is 8%, above the 0% historical benchmark for high-moat software systems.

- Category 2: The net increase of 34% post controlling systemic effect, is well above the 20% benchmark level observed in prior moderate-disruption cycles.

- Category 3: The net 59% category effect (after excluding the general market risk) is surprisingly close to the 60% default increase based on historical benchmark.

The study above suggests the market could be oversold for both Category 1 and Category 2 software issuers at current levels, potentially presenting opportunities for CLO managers to build par. Meanwhile the pricing of Category 3 might be fair with the incremental default risk matching historical benchmark for low-moat software firms.

That said, we would caution that market trading could be driven by technicals and investor sentiment, especially during heightened market volatilities, hence sell off can continue despite being oversold and we can't foresee when the rebound will happen.

CLO exposure to software

In the CLO market, investor attention has increasingly shifted toward managers' sector concentrations, with software exposure now central to portfolio-level risk discussions. As concerns about AI-driven disruption and business-model durability increase, investors are evaluating managers not only on issuer-level credit risk, but also on the extent of their software exposure and the vulnerability of those positions to broad-based rating pressure.

We present the top 20 BSL CLO managers by software par exposure in Exhibit 4, ranging from $9.6bn of Blackstone Credit to $1.9bn of CBAM. For managers with elevated software concentrations, the key question is no longer simply whether individual credits may experience volatility, but how a sector-wide downgrade cycle would interact with structural constraints, particularly the standard 7.5% Caa/CCC test threshold.

We consider two scenarios. In the moderate scenario, we assume that all category 3 software loans are downgraded by one notch. In the severe scenario, we assume that all category 2 software loans are downgraded by one notch and all category 3 software loans are downgraded by two notches. Under the moderate scenario, seven of the 20 managers would have their overall CLO loan portfolio breaching the 7.5% CCC trigger, of which five are already above 7.5% based on current holdings. Under the severe scenario, all 20 managers exceed the 7.5% CCC limit, indicating high potential downgrade risk they are facing.

Exhibit 4: Top 20 BSL CLO Managers by software par exposure

Manager	Software Par ($mm)	Software Exposure%	Category 1 Exposure	Category 2 Exposure	Category 3 Exposure	Current CCC %	CCC% in moderate scenario	CCC% in severe scenario
Blackstone Credit	9,575	22.74%	6.81%	13.01%	2.92%	7.06%	8.39%	17.11%
CSAM	6,374	19.34%	6.81%	11.13%	1.39%	10.92%	11.47%	18.14%
CIFC	5,770	19.21%	6.59%	10.42%	2.20%	4.22%	5.69%	12.82%
Ares	5,131	18.91%	6.38%	11.10%	1.42%	7.78%	8.08%	14.82%
Carlyle	4,589	16.28%	6.34%	9.04%	0.89%	5.69%	5.85%	10.66%
Oak Hill	4,323	22.85%	9.10%	12.42%	1.33%	5.95%	6.61%	13.15%
Elmwood	4,242	18.16%	6.87%	9.44%	1.84%	4.69%	4.82%	9.63%
Bain	3,898	16.99%	4.94%	10.08%	1.97%	5.93%	6.63%	12.28%
Palmer Square	3,841	18.17%	6.42%	9.70%	2.06%	5.80%	6.75%	13.47%
Neuberger Berman	3,460	14.78%	4.07%	9.42%	1.28%	8.54%	9.32%	15.44%
AGL	3,411	17.49%	5.20%	10.86%	1.44%	4.59%	5.18%	10.78%
Sound Point	3,354	15.68%	6.36%	7.20%	2.12%	11.10%	11.94%	16.50%
Onex	3,209	13.61%	4.91%	7.20%	1.50%	3.99%	4.23%	7.81%
Octagon	3,072	14.61%	5.15%	8.38%	1.08%	7.38%	7.88%	13.22%
CVC	3,066	12.51%	5.06%	6.39%	1.06%	7.13%	7.68%	11.20%
Barings	2,678	13.48%	4.69%	7.32%	1.47%	5.34%	5.82%	10.65%

Benefit Street	2,576	14.44%	5.28%	8.23%	0.93%	5.92%	6.46%	10.83%
RRAM	2,511	15.07%	6.53%	7.88%	0.66%	6.27%	6.89%	10.81%
Golub	2,367	27.60%	8.45%	16.43%	2.71%	5.76%	7.32%	17.54%
CBAM	1,940	17.40%	6.54%	9.99%	0.88%	6.04%	6.23%	11.26%
Market Overall	148,859	16.01%	5.53%	8.90%	1.57%	6.98%	7.60%	12.98%

Source: Trepp, LSEG Yield Book (March 2026)

We also examined the scenarios by deal vintage. Across deals issued over the past decade, software exposure appears relatively evenly distributed by vintage. However, more seasoned deals (2016-2019 vintage) start from higher CCC exposure levels and are therefore more sensitive to downgrade risk.

Exhibit 5: CLO exposure to software by vintages

Vintage	Software Par ($mm)	Software Exposure	Category 1 Exposure	Category 2 Exposure	Category 3 Exposure	Current CCC %	CCC% in moderate scenario	CCC% in severe scenario
2015	1,322	14.85%	5.17%	7.94%	1.75%	12.85%	13.41%	18.62%
2016	2,559	14.74%	5.17%	8.11%	1.46%	10.17%	10.72%	15.96%
2017	3,839	15.77%	5.50%	8.58%	1.69%	10.71%	11.33%	16.56%
2018	7,296	16.71%	5.64%	9.16%	1.92%	12.74%	13.54%	19.58%
2019	10,880	15.91%	5.52%	8.75%	1.63%	9.42%	10.02%	15.48%
2020	9,421	15.75%	5.55%	8.62%	1.58%	8.15%	8.75%	13.77%
2021	24,525	16.18%	5.55%	8.97%	1.66%	8.05%	8.72%	14.12%
2022	15,301	16.30%	5.54%	9.10%	1.67%	7.62%	8.28%	13.71%
2023	12,482	14.98%	5.26%	8.20%	1.51%	6.02%	6.59%	11.51%
2024	28,512	16.22%	5.55%	9.18%	1.49%	5.52%	6.13%	11.68%
2025	30,755	16.20%	5.63%	9.14%	1.43%	3.64%	4.20%	9.57%
Market Overall	148,859	16.01%	5.53%	8.90%	1.57%	6.98%	7.60%	12.98%

Source: Trepp, LSEG Yield Book (March 2026)

To evaluate the underlying downgrade risk for deals in different reinvestment period (RP) stages, we also sliced and diced the dataset into deals within RP and out of RP in Exhibit 6. Deals within reinvestment period show slightly higher software exposure and Category 2 exposure but a much cleaner overall credit profile, with substantially lower concentrations of CCC rated assets under both current and stressed conditions. On the other hand, out of RP deals hold less software exposure yet exhibit materially higher levels of downgrade risk, reflecting the reduced ability to rotate out of weaker names once the portfolios become static.

Exhibit 6: CLO exposure to software by reinvestment period (RP) status

Reinvestment Status	Software Par ($mm)	Software Exposure	Category 1 Exposure	Category 2 Exposure	Category 3 Exposure	Current CCC %	CCC% in moderate scenario	CCC% in severe scenario
Out of RP	13,891	15.01%	5.44%	7.68%	1.89%	14.39%	15.08%	20.41%
Within RP	134,968	16.12%	5.54%	9.04%	1.54%	6.16%	6.77%	12.15%
Market Overall	148,859	16.01%	5.53%	8.90%	1.57%	6.98%	7.60%	12.98%

Source: Trepp, LSEG Yield Book (March 2026)

At a more granular level, we reviewed the ten largest software issuers by CLO exposure and their key characteristics. All ten are rated B2/B or B3/B-, and their average facility size is $3.74 billion, significantly larger than the $664 million average across the broader software loan universe. Within this group, five issuers fall into Category 1 and the remaining five into Category 2. Their average price decline of 5.87 points is modestly lower than the 6.44-point decline for the full software loan universe, suggesting resilience among the largest loan issuers.

Exhibit 7: Top 10 software loan issuers by CLO exposure

Issuer Name	Exposure ($mm)	Category	YTD Price Change	Average Facility Size ($mm)	S&P Issuer Rating	Moody's Issuer Rating	Average Spread
Boxer Parent Company, Inc.	3,169	1	-7.41	2,991	B	B2	353
McAfee Corp.	3,152	2	-6.30	4,127	B-	B2	310
Cloud Software Group, Inc.	2,876	2	-7.62	2,687	B	B2	306
UKG Inc.	2,642	1	-5.78	6,335	B	B2	240
Sedgwick Claims Management Services Inc.	2,637	1	-3.68	5,564	B+	B2	252
Genesys Cloud Services Inc	2,404	2	-5.19	3,133	B	B2	265
Proofpoint, Inc.	2,154	2	-4.84	4,793	B-	B3	296
Rocket Software, Inc.	2,109	1	-7.46	2,167	B-	B3	371
CoreLogic Inc.	2,021	1	-3.28	3,233	B-	B3	387
RealPage, Inc.	1,977	2	-7.14	2,335	B-	B3	334

Source: Trepp, LSEG Yield Book (March 2026)

Credit fundamentals still solid for software sector

From a credit fundamental perspective, the software sector continued to outperform other sectors, despite recent market anxieties. In February, the Caa or CCC rated or below percentage as well as the default exposure for software sector remained below the levels observed across most other industries, underscoring the sector's structural resilience. This relative strength reflects the recurring-revenue models, high gross margins, and cash-flow visibility that characterize many software businesses, which provide cushion during periods of macro uncertainty or shifting technology narratives. As a result, even as sentiment has weakened, the underlying credit profile of the software sector remains healthy in contrast to what headlines may suggest.

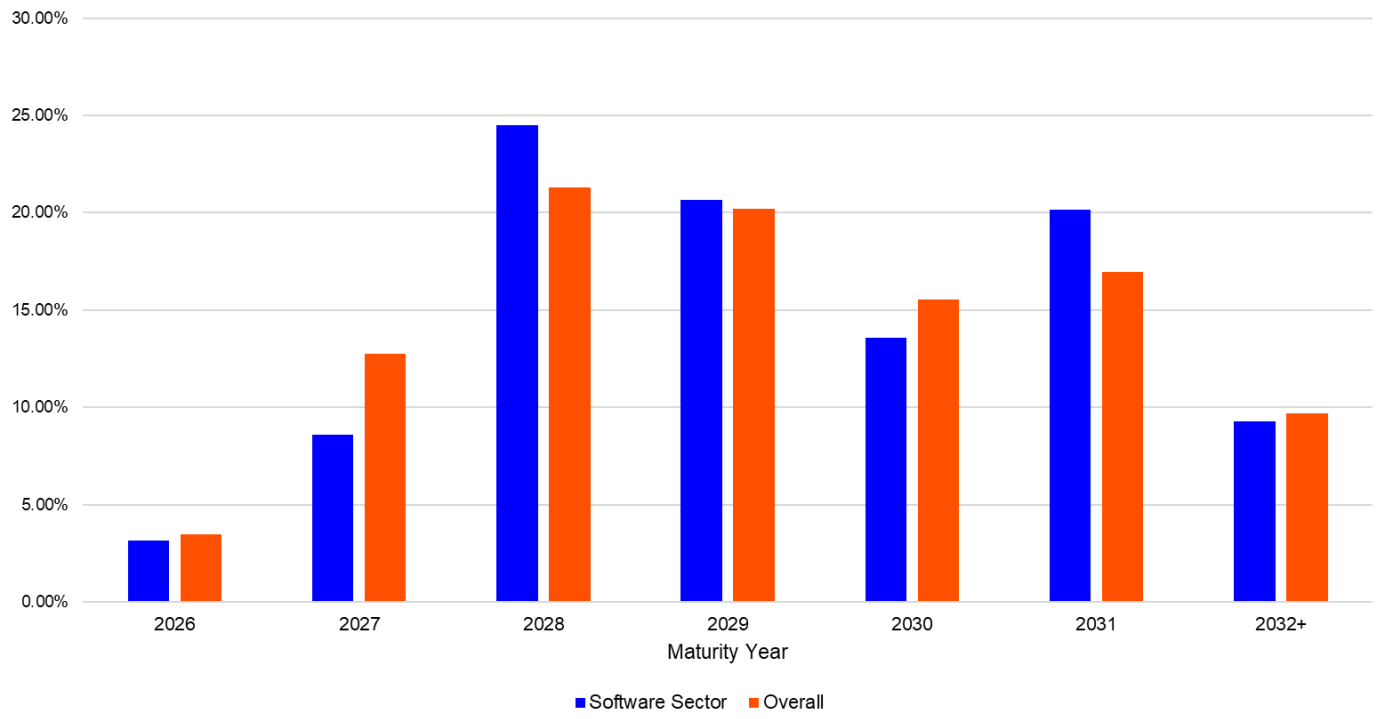
Exhibit 8: Credit risk metrics for software sector vs. others in the last 12 months

Date	Caa or below % Software	Caa or below % Others	CCC or below % Software	CCC or below % Others	Defaulted % Software	Defaulted % Others
Mar-2025	5.63%	5.00%	5.41%	5.00%	0.58%	0.38%
Apr-2025	5.50%	5.41%	6.33%	5.41%	0.61%	0.36%
May-2025	6.26%	5.63%	6.42%	5.63%	0.89%	0.39%
Jun-2025	6.44%	5.45%	5.67%	5.45%	0.86%	0.38%
Jul-2025	6.19%	5.70%	6.12%	5.70%	0.49%	0.41%
Aug-2025	5.84%	5.96%	5.99%	5.96%	0.38%	0.46%
Sep-2025	5.18%	5.47%	5.29%	5.47%	0.36%	0.41%
Oct-2025	5.41%	6.06%	5.33%	6.06%	0.37%	0.42%
Nov-2025	4.93%	6.16%	4.76%	6.16%	0.27%	0.42%
Dec-2025	4.75%	6.06%	4.57%	6.06%	0.30%	0.41%
Jan-2026	4.22%	5.36%	3.86%	5.36%	0.23%	0.29%
Feb-2026	4.67%	5.32%	4.37%	5.32%	0.25%	0.37%

Source: LSEG LPC, LSEG Yield Book (March 2026)

As lenders reevaluate the long-term growth outlook of software businesses, particularly in a market where AI adoption is accelerating, refinancing conditions are expected to become more challenging. Even though near-term credit profile remains steady, lower-quality software issuers could face pronounced refinancing stress once maturities begin clustering later in the decade. In Exhibit 9, we show the maturity wall distribution as of February for software loans and overall assets in CLO holdings.

Exhibit 9: Maturity Wall for software loans vs. overall in CLOs



Source: Trepp, LSEG Yield Book (March 2026)

The software maturity profile is relatively light in the near term, with only 3.18% of total software exposure coming due in 2026 and 8.62% in 2027, both below the overall CLO loan portfolio levels. The wall rose steeply in 2028, where software maturities reach a high of 24.50% compared with 21.32% for the overall, followed by another sizable block in 2029 at 20.68%, which is closely aligned with the broad market. Software remains elevated again in 2031 at 20.14%, above the overall portfolio's 16.97%, before tapering to 9.30% in 2032 and beyond. Overall, the software sector shows a more pronounced concentration in the 2028 to 2031 window but remains broadly consistent with the market's maturity distribution. Against the backdrop of AI-driven competitive realignment, uneven demand for software credits, and evolving underwriting discipline, the maturity bulges in 2028, 2029 and 2031 may pose refinancing challenges for weaker Category 2 and 3 issuers.

Private Credit CLO: more software exposure but better structural protection

The software-sector selloff carries particularly important implications for Private Credit CLOs (PC CLOs), given the rising investor concern on private credit market in the last six months. PC CLOs also see sizeable exposure to software borrowings underwritten during the low-rate, growth-oriented environment of recent years. Against this backdrop, tracking performance differentials between software credits and the broader market has become critical for PC CLOs in comparison to BSL CLOs (Exhibit 10).

PC CLOs hold significantly higher software exposure than BSL deals, with software accounting for 20.52% of their portfolios compared with 16.01% in BSL. Furthermore, PC CLOs have much higher Category 2 (12.28% vs. 8.90%) and Category 3 (3.34% vs. 1.57%) exposures than BSL CLOs. The software default rate of PC CLOs (0.42%) is also higher than BSL CLOs (0.18%).

On the OC front, PC CLOs begins with a higher CCC level at 11.78% versus 6.98% in BSL, rising to 12.29% in the moderate scenario and 15.02% in the severe scenario. Note that BSL deals typically set their CCC threshold around 7.5%, whereas PC CLOs commonly use a threshold closer to 17.5%, giving Private Credit portfolios considerably more room to absorb downgrades without pressuring their tests. As a result, we expect most Private Credit CLOs to be able to manage the software downgrade risk offset by enhanced structural protection.

Exhibit 10: Software exposure in Private Credit CLOs vs. BSL CLOs

Deal type	Software Par ($mm)	Software Exposure	Category 1 Exposure	Category 2 Exposure	Category 3 Exposure	Software Default %	Current Default %	Current CCC %	CCC% in moderate scenario	CCC% in severe scenario
BSL	148,859	16.01%	5.53%	8.90%	1.57%	0.18%	0.43%	6.98%	7.60%	12.98%
Private Credit	16,861	20.52%	4.90%	12.28%	3.34%	0.42%	0.52%	11.78%	12.29%	15.02%

Source: Trepp, LSEG Yield Book (March 2026)

About LSEG Yield Book

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