From Seat-Based Growth to Systemic Intelligence: The AI Challenge for HY

As in private credit—where countless interventions and commentaries have attempted to defend or challenge the asset class, often without sufficient grounding in facts—I prefer to step away from commentary and noise that add volume rather than clarity. For the final time (after receiving many questions), I will address AI disruption without leaning on rating categories, rating migrations, spread dynamics and pricing, purchase price multiples, or the so-called maturity wall. These metrics remain relevant, but they are inherently case-specific and insufficient to capture the structural shifts now underway. Nevertheless, I will address in the future particular situations that merit careful scrutiny.

First, the actors.

Since 2025 AI-related bond issuance by leading technology companies has generated market concern regarding elevated leverage; however, the underlying reality is more nuanced. Most top AI corporates continue to exhibit robust balance sheets, characterized by low debt-to-enterprise value ratios and, in certain cases, positive net cash positions even after completing sizeable debt issues. Rather than indicating financial stress, this new debt represents capital efficiency optimization—providing long-term funding certainty for multi-year AI and hyperscale data-center investments, while preserving liquidity for operational flexibility and shareholder returns.

The more salient narrative in this first quarter of 2026 is not one of deteriorating credit quality, but of market dynamics: large, tech-concentrated issuance is materially increasing supply, exerting downward pressure on spreads and elevating sector concentration within investment-grade indices. Concurrently, AI-driven capex introduces extended-duration payoff profiles and execution risk, particularly in the high-yield market, which could amplify dispersion between structurally advantaged "winner issuers" and those more vulnerable to disruption.

Now, the other businesses.

As AI becomes a structural, multi-decade investment cycle, credit markets are recalibrating—not in response to weaker issuers, but to the expansion of a technology-dominated footprint that brings both higher volatility and selective

alpha opportunities for active credit managers. Entering 2026, high-yield spreads are compressed, leaving valuations sensitive to idiosyncratic and macro-driven risk. Nonetheless, relatively low portfolio durations and current all-in yields provide "on paper" a carry buffer capable of absorbing moderate spread widening, assuming no material deterioration in default rates or significant upward shifts in sovereign yields. Market conditions and managers' abilities will determine whether this "yield-duration buffer" can maintain portfolio stability without triggering mark-to-market drawdowns.

AI is accelerating sectoral dispersion, particularly within software and technology credits. Concerns over application-layer disruption, erosion of pricing power, and elevated capital intensity have triggered pronounced volatility, most acutely in the mispriced leverage loan market and levered credit segments. These conditions underscore the importance of granular, credit-specific positioning, emphasizing: cash-flow durability, leverage trajectories, refinancing capacity, and competitive advantages. In the CLO world while the portfolio managers of the vehicles retain the ability to conduct granular credit assessments, it remains an open question how effectively they can manage the risk exposure when the holdings are significant and when underlying collateral pools face already idiosyncratic pressures from credits without any connection to the AI. Observing and studying the par burn in trading activity and monitoring tests can offer valuable insight into portfolio dynamics, allowing CLO investors to assess the ability of the PM and whether the risk buffers are functioning as intended. In a previous analysis, I drew a comparison with the oil and energy crisis of 2015 and its impact on high-yield portfolios (bonds and loans); however, I maintain that the current environment is distinct and more complicated. While underlying stress in certain asset pools warrants close attention, this moment calls for active engagement and precise calibration, rather than assuming temporary or immediate disruption. The CLO market today is fundamentally different from 2015, and not necessarily for the better.

The broader software and tech landscape is experiencing structural repricing. This is not a collapse of the sector, but a dispersion event: credit and stock markets are actively "re-underwriting" business models, not merely "adjusting for cyclical growth deceleration". Corporate multiples are compressing as revenue durability, margin stability, net revenue retention, and long-term CAGR assumptions come under scrutiny. Value capture at the application layer is being renegotiated as intelligence becomes increasingly horizontal, favoring firms that control proprietary data, orchestration frameworks, and embedded distribution.

The cumulative effect is wider cross-sectional dispersion, longer-duration uncertainty, and a reevaluation of terminal value assumptions. Portfolio outcomes and tiering are therefore likely to diverge more meaningfully, rewarding active managers capable of distinguishing transient execution pressures from structural impairment. This represents a regime shift in software and technology credits, driven by AI as a structural catalyst rather than a cyclical headwind.

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