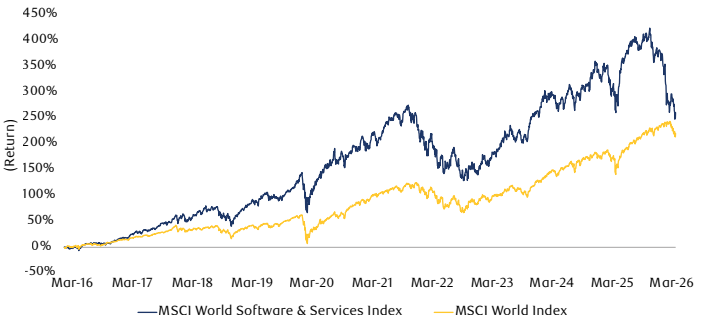
RBC Global Asset Management
PH&N Institutional

The RBC Global Equity team's perspective on navigating the challenges facing enterprise software today

The software industry has experienced a remarkable decade of growth and value creation, driven by the proliferation of cloud computing, the shift toward Software-as-a-Service (SaaS) models, and the increasing digitalization of enterprise operations. This growth was underpinned by a powerful investment thesis: software businesses possessed durable competitive moats through high switching costs, user lock-in, and integration complexity, enabling market leaders to compound revenue and earnings for years. The sector's expansion reflected a simple premise – that enterprises would pay predictable, recurring fees to avoid the costs and friction of replacing often mission-critical systems. This monetization model was particularly powerful at scale: per-seat pricing created natural revenue expansion as organizations grew, with each new hire or expanded department representing incremental margin that could be harvested for years to come. Yet this structural picture is now being disrupted at its foundation by artificial intelligence (AI), which is fundamentally challenging the assumptions that powered the industry's bull case for the past decade.

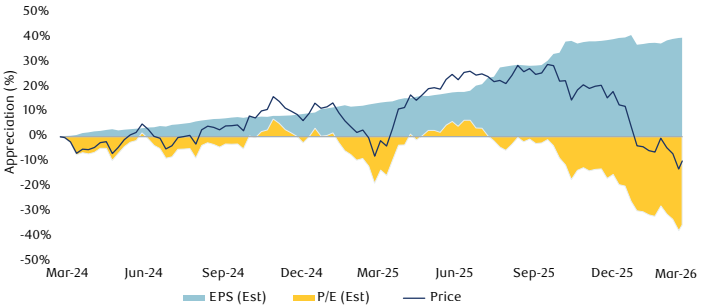
The bear thesis that has emerged and is now dominating market sentiment is that agentic AI will *eventually* collapse the SaaS stack, driving valuations toward zero. This argument functions as a "non-disprovable negative thesis" – in the short run, no single quarter of revenue beats, no round of margin expansion, and no improvement in net retention can refute a thesis that relies on the word "eventually." While this bear thesis cannot be disproven in the near term, it obscures a more nuanced reality: the structural challenges facing software are real, but they are not uniformly distributed. Rather than dismissing the industry as doomed, we aim to determine which specific aspects of the traditional software business model are under genuine pressure, and which may prove more resilient than skeptics assume.

Figure 1: 10 year performance of MSCI World Software and Services Index vs. MSCI World Index



Source: RBC GAM, Bloomberg‡. All Returns in U.S. Dollars. As of March 31, 2026. Performance over the past 10 years.

Figure 2: Software & Services earnings continue to rise while multiples compress



Source: RBC GAM, Bloomberg‡. All Returns in U.S. Dollars. As of March 31, 2026. Data pertaining to MSCI World Software & Services Index

Existential questions the software industry must answer

Beyond sentiment, there are legitimate structural issues that the industry must confront:

- **Seat-based pricing is under pressure.** If AI agents increasingly perform the work previously done by human users, the logic of seat-based pricing – that is, charging customers a recurring fee for every individual user accessing the software – begins to erode. The question of who pays, and for what, is becoming central to every enterprise software procurement conversation.
- **Traditional moats are weakening.** Historically, enterprise software companies benefitted from deep moats built on user interface familiarity, switching costs, and integration complexity. AI is lowering barriers to entry, enabling new entrants and adjacent competitors to build comparable functionality at a fraction of the historical cost and time.
- **Business lines are blurring.** If the cost of software development approaches zero as result of agentic AI, competitive boundaries collapse. We are already seeing this play out: Salesforce is building IT workflow capabilities, ServiceNow is building CRM, Microsoft is building everything. Every major vendor aspires to be the orchestration layer for enterprise AI agents, and the technology now makes it feasible to branch into adjacencies in months rather than years.

The software monetization model is in limbo

The industry is simultaneously experimenting with seats, consumption tokens, outcome-based pricing, and hybrid models – often within the same company. ServiceNow, for example, is currently running seat-based, consumption-based, and outcome-based pricing models concurrently, creating confusion among both customers and investors regarding revenue predictability and growth trajectory.

The lack of industry consensus on pricing architecture is a meaningful source of investor uncertainty. This ambiguity extends beyond near-term forecasting: traditional SaaS businesses commanded premium valuations precisely because their predictable, recurring revenue streams were easy to model and discount. As monetization models fragment and shift, investors face a fundamental valuation problem as the financial models that once provided confidence in long-term cash flows no longer apply. Until the market gains clarity on how AI-driven software will be monetized, we expect this to remain a headwind.

Our framework for identifying software winners

Not all software companies face the same degree of AI-related risk or opportunity; some will suffer while others create enormous value from AI. The following framework helps us assess where AI creates disproportionate value versus where it poses existential risk:

1. **AI spend-to-benefit ratio:** Who extracts the most value for the least AI investment?
2. **Competitive intensity shifts:** Does AI entrench incumbents or empower disruptors?
3. **Revenue creation vs. cost takeout:** Does AI unlock new revenue streams or merely drive efficiency?
4. **Total Addressable Market (TAM) expansion:** Does AI make previously uneconomic markets addressable?
5. **Value chain collapse:** Which intermediaries become redundant?
6. **Cognitive labour intensity:** Where is the highest ratio of knowledge work that AI can augment?
7. **Proprietary data moats:** Who possesses irreplaceable data that improves AI inference?
8. **Regulation as moat:** Where do compliance requirements protect incumbents?

The key insight from this framework: **The companies positioned to win are not necessarily those with the best AI features today, but those where AI expands the addressable market or deepens existing competitive moats.** The following two case studies exemplify such companies.

Case study 1: Twilio

Twilio is a cloud-based customer engagement platform that allows developers to embed voice, messaging, video, and email capabilities directly into software applications (for example, Uber uses Twilio to connect riders and drivers directly through the app without revealing their personal phone numbers, while Netflix uses Twilio to send one-time passwords for login security). The company exemplifies that AI can transform a business's competitive position and growth trajectory. Examples of this include:

- **Voice AI as a transformative opportunity.** The Voice AI market has reached a critical inflection point as sub-500ms latency – the threshold required for natural, human-like voice interactions – has been achieved. Costs per call have declined to levels that support scale deployment. Twilio is transitioning from a provider of communications "pipes" to the orchestration layer and operating system for Voice AI agents, moving meaningfully up the value chain.
- **Concrete evidence of inflection.** Q1 2026 confirmed a broad-based growth inflection across products, channels, and geographies as Twilio delivered $1.41 billion in revenue (+20% YoY reported, +16% organic), its fastest organic growth rate since 2022. Voice revenue accelerated to 20% YoY growth, the highest it's been in 19 quarters and its sixth consecutive quarter of acceleration, while Messaging accelerated to 25% YoY.[1] Importantly, Voice is no longer a standalone growth story – it is becoming the tip of the spear for broader platform adoption, as customers who land on Voice AI rapidly expand into Messaging, software add-ons, and adjacent channels.
- **Broad-based adoption across customer cohorts.** Adoption is not limited to AI startups, although they are a significant catalyst. Traditional independent software vendors are embedding Voice into SaaS products to modernize their offerings; for example, enterprise customers are rebuilding customer care and outbound marketing functions using Voice AI. AI-native leaders such as Sierra (a leading customer experience AI company) and Bland AI have signed deals leveraging Twilio's infrastructure.

Case study 2: Guidewire

Guidewire is a leading provider of cloud-based software platforms tailored for property & casualty insurers and represents a different but equally compelling application of our framework. The company is a "System of Record" in a regulated vertical where domain expertise, regulatory acceptance, and proprietary data form deep, durable moats. They stand to benefit from AI adoption in the following ways:

- **AI as a TAM multiplier.** Guidewire has articulated how AI-powered capabilities in pricing, underwriting, and claims – areas beyond the company's traditional core system footprint – could potentially triple its addressable market. This positions the company to capture value from a larger portion of the insurance industry value chain, moving beyond IT spend allocated to core systems.
- **Ability to adopt the compliance & regulatory burden.** Guidewire invests huge sums of money in global regulatory compliance, and manages most regulatory updates globally to ensure compliance and regulatory velocity. They bake these updates into their content packages so insurers don't have to manually update their rating tables or forms every time a state changes a rule. For clients, getting rid of Guidewire would mean getting rid of regulatory and liability shield and insourcing all the legal risk.
- **Providing a reliable audit trail.** For a large carrier (Tier 1), the audit trail is everything. Guidewire provides a deeper, non-repudiable audit log of every underwriting decision and claim adjustment, which is pre-mapped to common regulatory frameworks. This is critical, as regulators are demanding explainable AI – if a State Department of Insurance (DOI) audit asks, "Why did you charge a 65-year old widow 15% more than last year?" an insurer cannot point to an AI-generated codebase and say, "The agent wrote it."
- **Offering an extended ecosystem.** Guidewire Marketplace delivers significant value because most insurers won't build everything internally. AI-driven insurance applications built for Guidewire's cloud APIs offer "plug and play" integration, reducing costs and risk. Guidewire can quickly access real-time wildfire risk data, flood maps, and historical loss data without custom connectors. Conversely, using Claude code to build 100+ integrators with dynamic data sources and monitor their performance is a massive engineering effort, even if the AI writes code 10x faster than a human.
- **Software costs can compare favourably to the alternative.** In the absence of Guidewire, an insurer can get rid of license cost (1-2% of the total cost) but will need to hire staff for compliance, regulatory, development, and maintenance roles until the AI models are probabilistic and not deterministic.

[1] Twilio Q1 2026 Earnings Call, April 30, 2026.

In short – can an enterprise customer rip and replace Twilio or Guidewire and use Claude code instead? Technically maybe, but this amounts to a massive strategic gamble and can present significant business and regulatory risks.

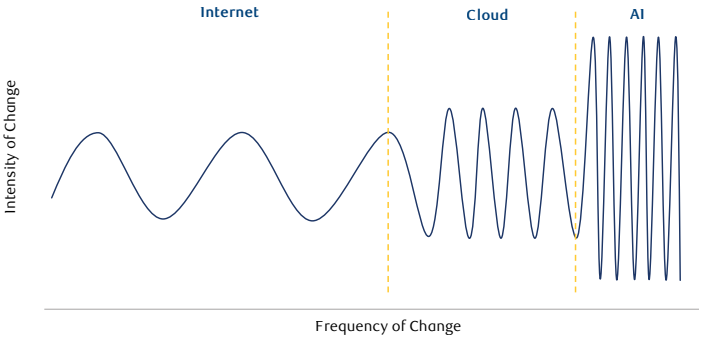
These two cases are not outliers; they reflect the broader pattern our framework identifies. Twilio and Guidewire succeed not because they have the most sophisticated AI features, but because AI fundamentally expands what their platforms can do and who can benefit from them. Twilio moves from a communications utility to the operating system for an entirely new category of agents. Guidewire moves from a system of record to a TAM multiplier across the insurance value chain. In both cases, AI is not a threat to the business model – it is a multiplier of existing competitive strength.

Conclusion

Enterprise software is navigating a difficult sentiment environment, but the fundamental picture does not support the "terminal value goes to zero" narrative for all software companies – though some will certainly struggle. The companies that thrive will be those where our framework applies: where AI expands addressable markets, deepens competitive moats, or creates entirely new revenue streams. Twilio and Guidewire exemplify this thesis, but they are not alone.

The pace of change, however, demands intellectual humility. Just two years ago, the debate centered on whether meaningful enterprise AI use cases even existed; today, models have improved by orders of magnitude, companies are exchanging leaderboard positions at a dizzying rate, and what was speculative is now production-ready. This velocity of transformation is unlike anything the technology sector has experienced, and rigid frameworks and fixed convictions will be liabilities in a world where the competitive landscape can shift very quickly. In this environment, the ability to continuously reassess assumptions, update priors, and remain genuinely adaptable has become more critical than ever.

Figure 3: AI rate of change has been dramatic with wide ranging implications



Source: RBC, MongoDB analyst day presentation.

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