

Thinking Out Loud



The Village

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Investors are questioning the durability of software companies' cash flows and their long-term valuation assumptions. Concerns about potential obsolescence from AI-driven disruption are weighing on sentiment, compounded in some cases by balance sheet leverage — particularly where growth was supported by private credit financing. Since the end of 3Q25, the software-heavy stock indices have fallen close to 30%. Over the same period, the S&P 500 is higher by roughly 4.0%.

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In the 2004 film *The Village*, written and directed by M. Night Shyamalan, a group of elders traumatized by modern-day violence constructs an isolated 19th-century community inside a wildlife reserve, led and financed by Edward Walker (William Hurt), a history professor at the University of Pennsylvania. The elders invent monsters and even ban the color red to sustain the illusion of danger and justify remaining “safe.” Although the creatures are ultimately revealed to be fabricated, the fear they cultivate is deliberately engineered to prevent anyone from engaging with the modern world beyond the village walls — even to obtain basic medicines.

In our view, the parallel to today is less about organizations rebuking “red-cloaked” technology and software names, and more about markets reacting to another illusion of danger. Investors are rapidly repricing software companies, selling down stocks on fears that AI will compress margins, erode subscription moats, or disrupt legacy business models.

Like the villagers who manufacture monsters for existential threats, markets may be extrapolating short-term uncertainty into long-term impairment. Meanwhile, the world beyond the wildlife reserve (in our analogy, software companies) is already operating with AI embedded throughout workflows, research, coding, and capital allocation.

In the climactic scene of *The Village*, Edward Walker's blind daughter, aptly named Ivy, leaves the safety of her community to obtain life-saving medicine, illustrating that change is driven by necessity, not fear. Like the villagers who mistake staged threats for real danger, markets may be overstating the long-term impairment of software companies from AI. The recent selloff suggests investors are assuming AI will swiftly render legacy platforms obsolete or permanently erode margins. While disruption is inevitable, that leap may be premature. AI operates on top of the software, data, and enterprise platforms already in place — it does not replace them overnight. Those systems are more likely to serve as the foundation for AI's growth than its victims. The greater risk may be mispricing adaptation as extinction.

We believe selective value is beginning to emerge within segments of the software space — particularly among companies with strong balance sheets and business models positioned to integrate, rather than be displaced by, AI. In our view, the recent selloff risks becoming another instance of indiscriminate de-risking; in other words, throwing the baby out with the bathwater.

We'd love to hear your thoughts.

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