AlixPartners

MARCH 2025

THE END OF A SOFTWARE ERA

Big tech and AI are poised to erase mid-size software companies. How can they fight back?

In the ever-evolving landscape of enterprise software, mid-size companies face unprecedented challenges driven by AI disruption, intense competition, slowing growth, and shifting investor demands.

These companies are caught in a "big squeeze"—pressured on one side by nimble, AI-native entrants that can replicate applications at a fraction of the cost and on the other side by tech behemoths, such as Microsoft, Salesforce, and Oracle, that are pouring billions into the AI arms race.

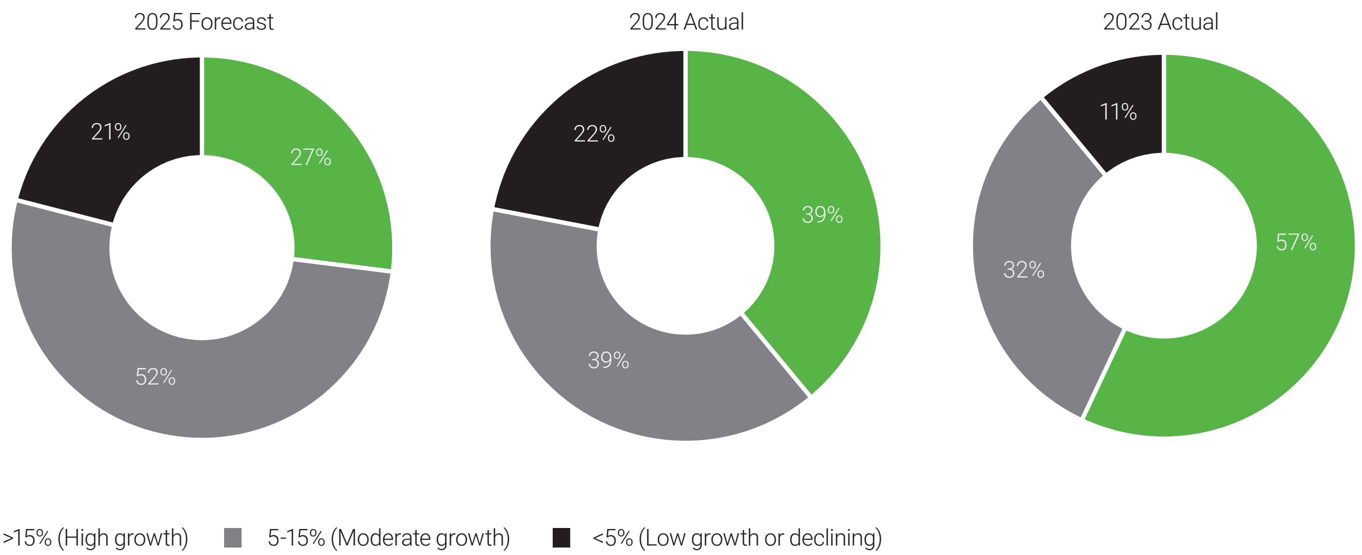
While AI holds immense future promise, it is no panacea; companies with outdated technology and operations will struggle to realize its benefits. The future lies in their ability to adapt their operations and business models at speed, or risk being disrupted by more agile competitors.

As a result of this "big squeeze," we believe many mid-size enterprise software companies will face threats to their survival over the next 24 months.

ENTERPRISE SOFTWARE GROWTH CONTINUES TO DECLINE

Across the enterprise software industry, top-line growth has slowed considerably. Our analysis of 122 publicly listed enterprise software companies below $10B in revenue shows that the percentage of high-growth companies decreased from 57% in 2023 to 39% in 2024. In 2025, industry analysts are expecting further declines, indicating that only 27% of companies will be in the high-growth category. While AI-native players have attracted significant recent investment (more than $100B in 2024 alone) and growth rates remain high, we believe this represents only a small portion of the broader enterprise software market. Additionally, enterprise customers are facing their own cost pressures, leading to lower expansion rates and higher customer churn. Per Bank of America's 2024 year-end review, the median net dollar retention rate (NRR%) of enterprise software companies has dropped from 120% in 2021 to 108% in Q3 2024, suggesting customer stickiness has declined.

FIGURE 1: LESS THAN HALF AS MANY COMPANIES ARE EXPECTING HIGH GROWTH IN 2025 COMPARED TO 2023



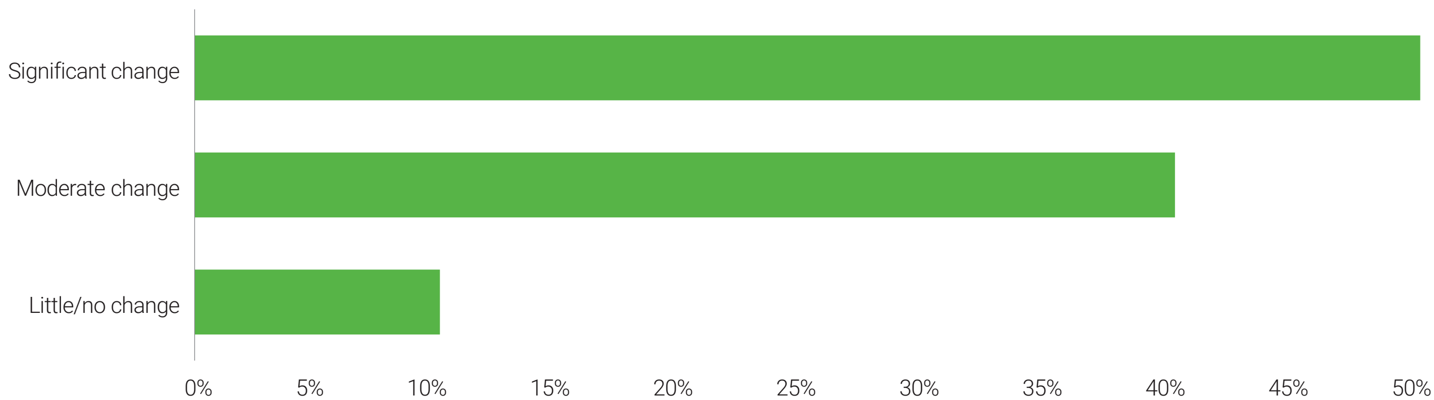
Source: CapIQ, AlixPartners analysis of 122 publicly traded enterprise software companies below $10B in revenue

COMPETITION IS MOUNTING FOR ENTERPRISE SOFTWARE COMPANIES

As customer demand for tailored solutions continues to rise, the enterprise software industry has seen a surge in smaller, more agile players offering specialized services, often at a lower cost and enabled by AI (e.g., Freshdesk from Freshworks, Zoho One from Zoho Corporation, and Agent OS from Sierra).

Meanwhile, tech behemoths are driving consolidation through acquisitions, developing platforms and aggressively pursuing cross-selling opportunities. These large players can deliver a wide range of capabilities at lower prices through economies of scale. With competition building from both sides, many mid-size enterprise software companies are forced to reassess their strategy and business model.

FIGURE 2: HALF OF SOFTWARE COMPANIES EXPECT SIGNIFICANT BUSINESS MODEL CHANGES IN THE NEXT YEAR



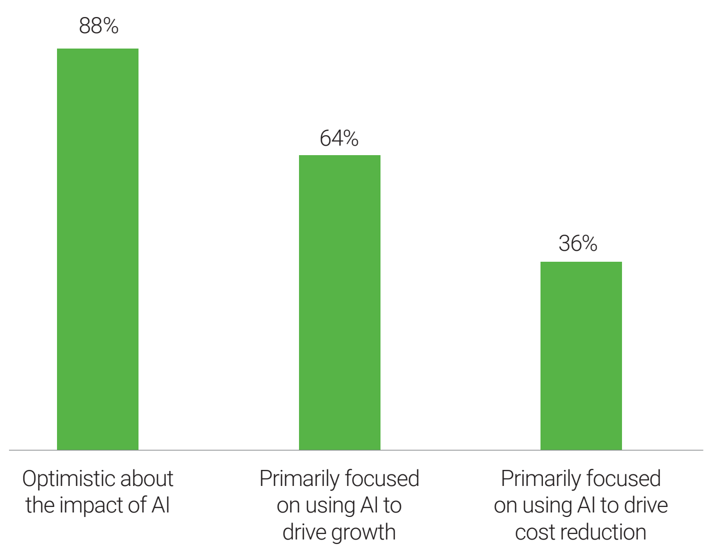
Source: 2025 AlixPartners Disruption Index

AI DISRUPTION IS ENTERING PRIME TIME

AI-driven solutions have started to make a significant impact in enterprise software. While the most mature applications today are in AI-driven coding and customer support (e.g. GitHub's Copilot for coding and Zendesk's Answer Bot for customer support), we are approaching a tipping point where AI will dramatically improve efficiency across other critical business functions as well. Companies that successfully integrate AI into their products will be well-positioned to meet the rising customer demand for efficient solutions. As a result, almost two thirds of the software company executives in our survey are focused on using AI as a growth driver.

On the other hand, AI agents are set to disrupt the logic and presentation layer of SaaS applications. Practical examples are already appearing, such as Klarna's well-publicized decision to terminate its relationships with both Salesforce and Workday in favor of a suite of in-house developed AI apps and smaller agile vendors. The recent unveiling of DeepSeek suggests a further acceleration by bringing the possibility of "budget" AI to almost all levels. This shift could eliminate the need for many enterprise software companies that thrived in the traditional SaaS architecture.

FIGURE 3: MORE THAN 60% OF SOFTWARE EXECUTIVES ARE FOCUSED ON AI AS A GROWTH DRIVER



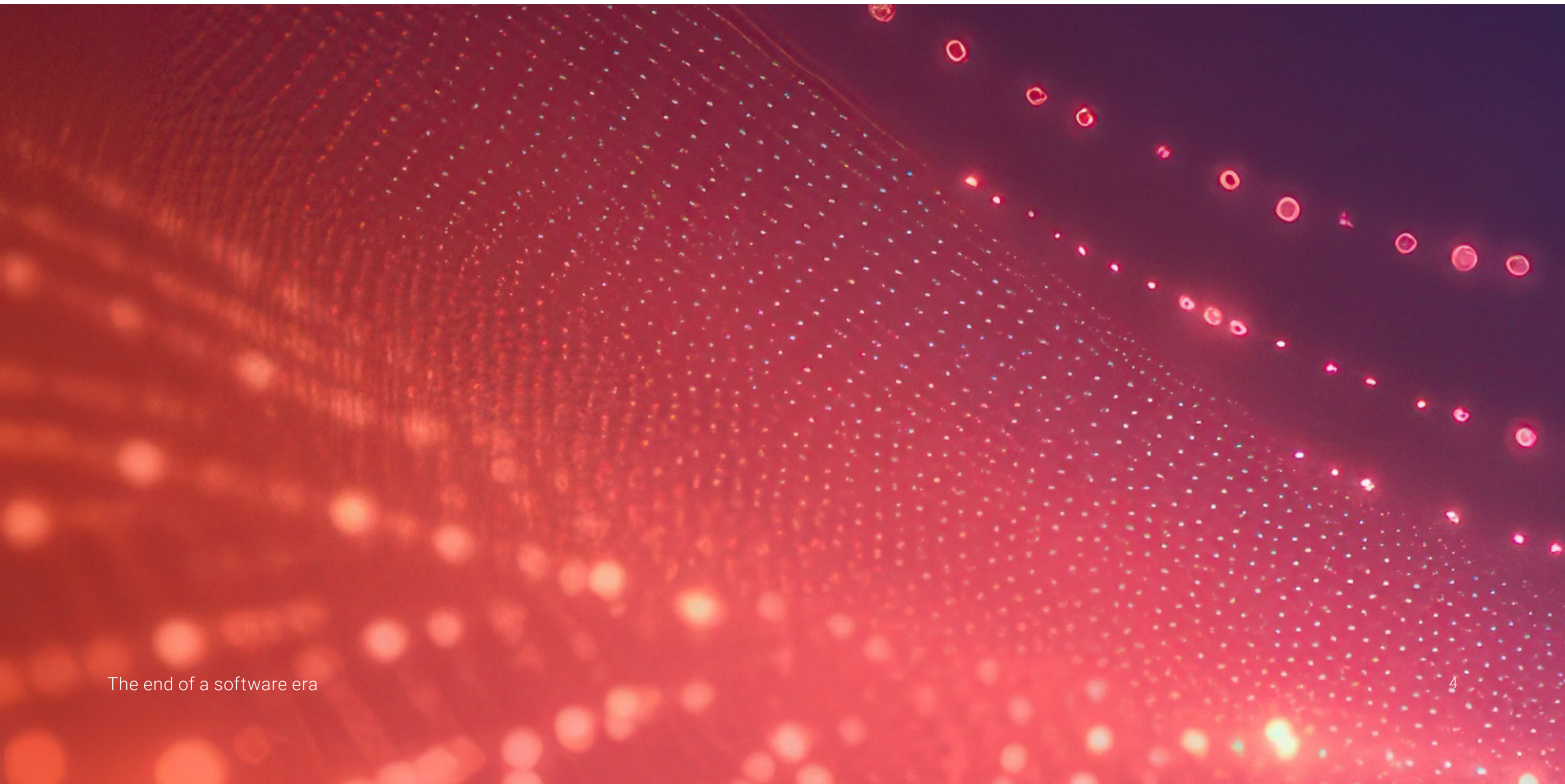
Source: 2025 AlixPartners Disruption Index

INVESTOR DEMANDS ARE SHIFTING

As growth continues to slow across both public and private markets, investors are placing a greater emphasis on profitability. Higher interest rates are partially to blame, raising return on investment (ROI) targets. It is becoming more expensive to pay off debts, which is driving the importance of positive and predictable cash flows. In response, we have seen a significant pivot within the mid-sized software companies toward active cost controls and selective capital deployment. We believe the emphasis on efficiency will intensify in this uncertain macroeconomic environment.

FIGURE 4: OPERATIONAL EFFICIENCY IS A TOP PRIORITY FOR SOFTWARE COMPANIES WHEN FACED WITH DISRUPTION

Source: 2025 AlixPartners Disruption Index



HOW CAN ENTERPRISE SOFTWARE COMPANIES NAVIGATE AND OVERCOME THESE CHALLENGES?

Enterprise software executives face a difficult task of deciding when and how to focus on running vs. growing the business. In these disruptive times, we believe the best leaders need to do both, finding a path towards predictable growth while driving operational rigor to unlock funds to invest in AI.

1

TRANSFORMATION FROM TRADITIONAL SAAS TO AI AGENTS

Traditionally, logic and presentation layers have been central to many SaaS offerings. However, with powerful AI agents that do not require structured data, customers no longer need these intermediary layers. This shift reduces the relevance of conventional SaaS models, prompting many companies to quickly develop their own AI agents.

Developing an AI agent requires significant R&D investment as well as a fundamentally new product strategy. But this transition goes beyond simply launching a product—it requires a comprehensive business model transformation across pricing, sales, marketing, operations, and revenue recognition. For example, companies like Salesforce and ServiceNow have started adopting outcome-based pricing for AI agents where revenue scales with customer outcomes, introducing significant volatility to revenue performance. Additionally, elevated compute costs for AI agents may drive a higher cost of revenue compared to traditional SaaS offerings, forcing companies to rethink their cost management strategies.

2

A GROWTH FLYWHEEL TO GENERATE PREDICTABILITY IN A DISRUPTIVE MARKET

Over the past decade, enterprise software growth has been centered around new customer acquisition driven by expanding product portfolios and sales teams. But in the current environment, customer acquisition is increasingly challenging and expensive. To successfully navigate this shifting landscape, enterprise software companies must implement bold changes to their go-to-market strategies with an emphasis on customer retention and targeted acquisition. This should be reinforced by a well-defined product portfolio strategy, value-additive AI use cases, and innovative pricing models. We call this the “growth flywheel” approach.

3

CREATING THE FUEL FOR GROWTH

By optimizing spend across operations, enterprise software companies can unlock the capital to invest in high-impact innovations (such as building AI agents) or traditional growth initiatives (such as strategic partnerships). This process involves streamlining product portfolios, cutting investments in low-growth products, and utilizing AI and other automation techniques to optimize front- and back-office functions. Additionally, leaders must drive cultural transformation by challenging complacency and structuring incentives to reward innovation and operational efficiency.

4

PURSUING INORGANIC GROWTH

Many enterprise software companies are pursuing acquisitions or positioning themselves to be acquired by larger players or investors. These strategies allow such companies to leverage the resources and scale of bigger competitors, ensuring they remain competitive in an evolving market. This trend is echoed by the 2025 AlixPartners Disruption Index survey, where growth and profitability leaders say they are twice as likely to execute a transaction in 2025 versus 2024. Proactive approaches, such as drawing clear operating-model lines around business units and cleaning up back-office operations, can make carving out or integrating targets much more attractive to potential partners.

AlixPartners

CONTACT THE AUTHORS

Eric Wobig
Partner
+1 773 668-8136
ewobig@alixpartners.com

Michelle Miller
Partner & Managing Director
+1 305 205-6095
mmmiller@alixpartners.com

Mario Ribera
Partner & Managing Director
+1 917 375-5400
mribera@alixpartners.com

Giacomo Cantu
Global Leader of Technology, Media, & Telecommunications, Partner & Managing Director
+1 312 450-4960
gcantu@alixpartners.com

Satchi Mishra
Director
+1 512-316-9089
smishra@alixpartners.com

Joe Wiles
Senior Vice President
+1 248 520-1678
jwiles@alixpartners.com

ABOUT US

For more than forty years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges—circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line—a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.

Tackling situations when time is of the essence is part of our DNA—so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.