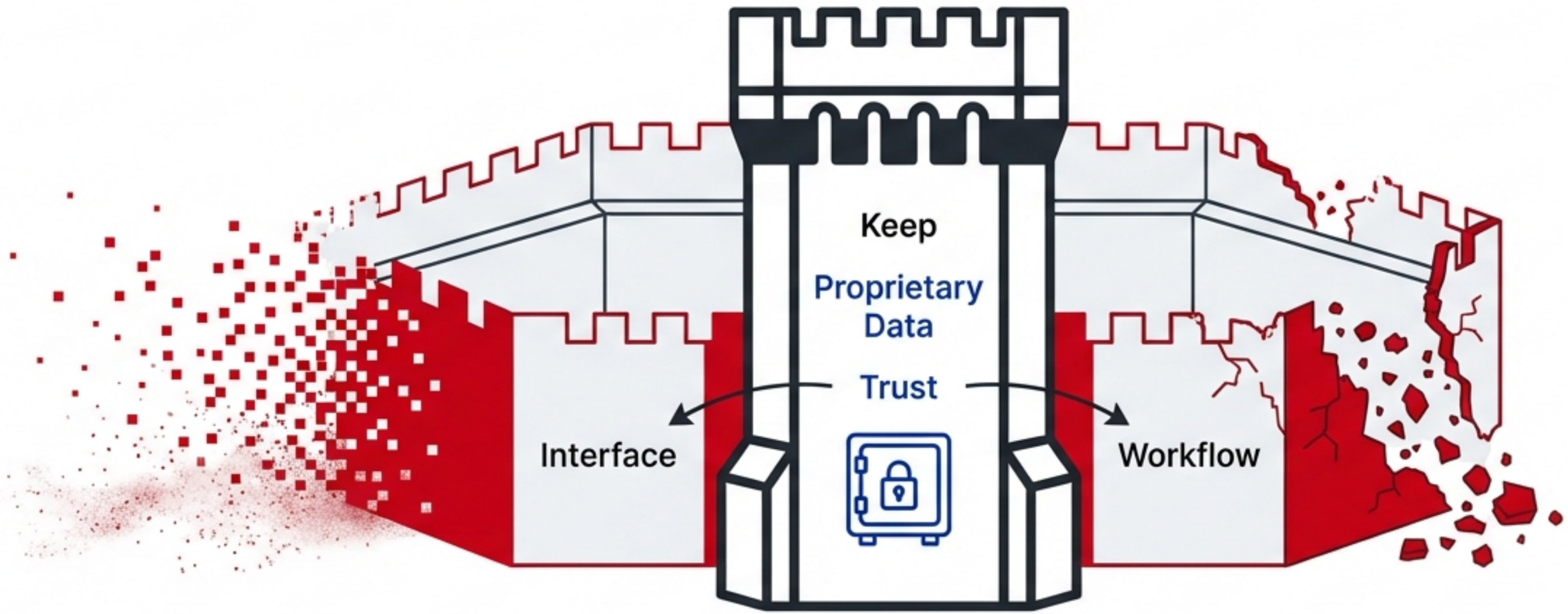
The Deconstruction of Vertical Software Moats

Why $1 Trillion was wiped from the sector, and which defensive barriers still hold.



Perspective from 10 years in Vertical SaaS: Building Doctrine (`Pre-LLM legal tech`) vs. Fintool (`AI-native financial analysis`).

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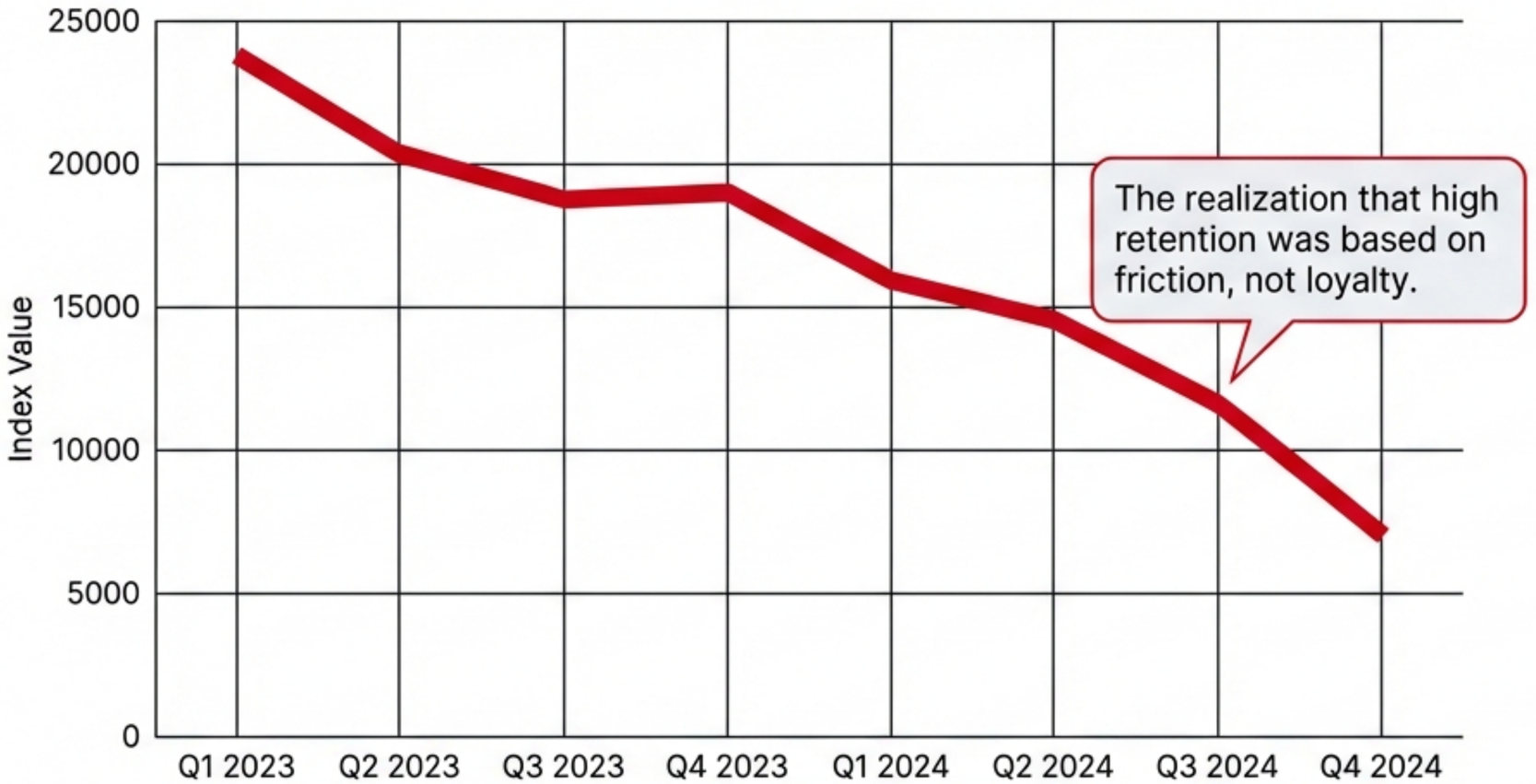
The Market is Pricing in the End of the Interface Premium

S&P 500 Software & Services Index Performance



$1 Trillion

Wiped from software & services stocks.

FactSet

Market cap dropped $20B -> $8B.

S&P Global

-30% valuation correction.

Thomson Reuters

Shed ~50% market cap.

Insight: The revenue cliff hasn't hit yet due to long contracts (12-24 months). This crash is multiple compression. Investors realized "Learned Interfaces" are liabilities, not assets.

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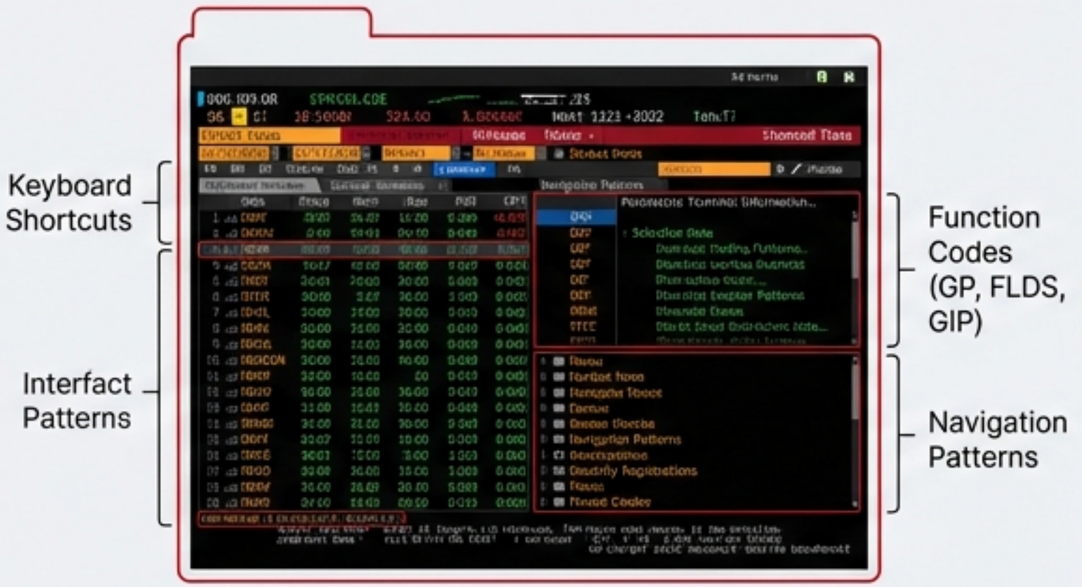
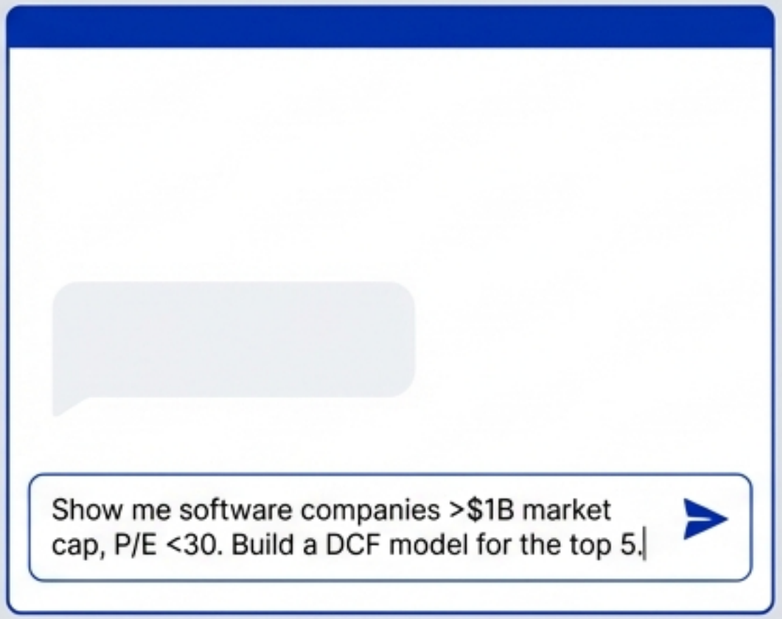
Muscle Memory is No Longer a Moat



10 Years to Master. High switching costs because leaving means becoming illiterate.



0 Minutes to Master. Switching costs drop to zero.

When the interface becomes natural language, the $25,000/seat premium for “workflow familiarity” dissolves.

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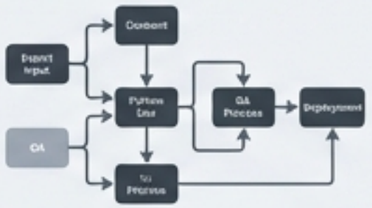
Business Logic Migrates from Code to Markdown

 **Doctrine (Traditional SaaS)**	**Fintool (AI-Native)**
Process: Legal experts teach engineers -> Engineers write Python -> QA -> Deploy	**Process:** Portfolio Manager writes a ‘Skill’ in a markdown file.
Cost: Thousands of lines of custom code, years of development.	**Cost:** One week of writing text. **0 lines of code**.
Constraint: Engineering Scarcity.	**Constraint:** **None**.

“The accumulated business logic that took vertical software companies a decade to build can now be replicated in weeks.”

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The Vaporized Moats (Sell These)

- **Learned Interfaces** - Destroyed by Chat. Users no longer pay to avoid relearning workflows.
- **Business Logic** - Converted to Markdown. Complex logic (DCF `models`, `legal citations`) is just a text file now.
- **Public Data Access** - Commoditized. LLMs are native parsers. They read SEC filings (10-Ks) without scrapers.
- **Talent Scarcity** - Inverted. Domain experts can now ‘code’ via prompts; you don’t need **200** engineers.
- **Bundling** - Weakened. Agents act as the new unbundlers, cherry-**picking data** sources via **APIs**.

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The Durable Moats (Buy These)

- **Proprietary Data** - Stronger. If you can’t scrape/buy/synthesize it, it is gold (e.g., Real-time trading pricing).
- **Regulatory Lock-in** - Structural. HIPAA, FDA, and Audit Trails do not care about GPT-5 (e.g., Epic Systems).
- **Network Effects** - Sticky. Communication layers remain valuable; the value is the other people (e.g., Bloomberg Chat).
- **Transaction Embedding** - Durable. If you sit in the money flow, AI sits *on top* of you, not *instead* of you (e.g., Stripe).
- **System of Record** - Safe (for now). The canonical source of truth is hard to move.

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The ‘Public vs. Proprietary’ Trap

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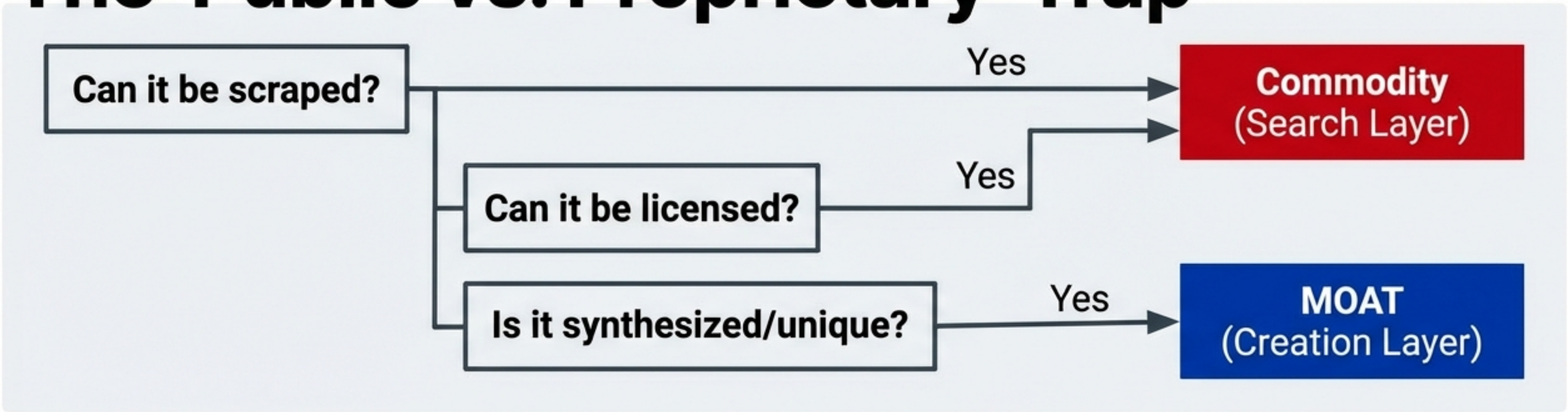

Vaporized Example	Durable Example 1	Durable Example 2
Making SEC filings searchable (FactSet). The model IS the parser.	Credit Ratings (S&P Global). LLMs cannot issue regulated opinions.	Proprietary Editorial (Doctrine’s pivot). Analysis that doesn’t exist elsewhere.

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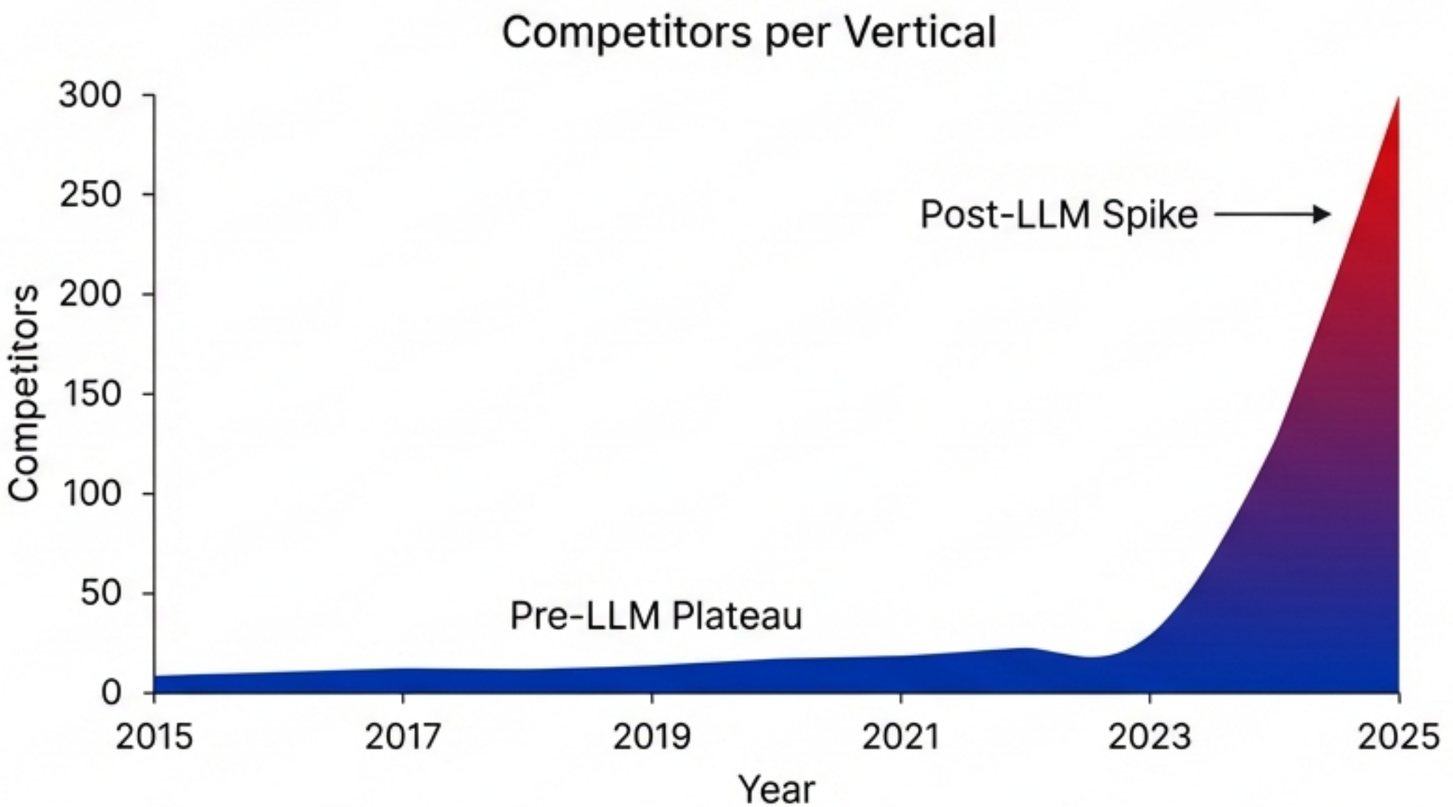
Competition Explodes Combinatorially

Pre-LLM:	200 Engineers	+	$50M Data License	=	1 Competitor
Post-LLM:	6 Engineers	+	Frontier Model API	=	1 Competitor

“We serve hedge funds that relied on Bloomberg. Not because we have better data, but because a team of 6 built a faster answer engine.”



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The Pincer Movement: Attacks from Above and Below

The Giants (Horizontal Platforms)

Microsoft Copilot / Anthropic.

Extending horizontally into vertical use cases (e.g., Excel doing DCF modeling).

Traditional Vertical SaaS
(The Incumbent)

Fintool / Startups.

Hundreds of headless startups offering 80% features at 20% price.

The Swarm (AI-Native Startups)

Key Concept

Software is becoming Headless. The interface disappears, and **horizontal** platforms win via plugins (MCP).

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The Risk Assessment Framework

The 3-Question Test for Vertical SaaS Survival

Questions	0 Yes	1 Yes	2-3 Yes
1. Is the data proprietary? (Cannot be scraped) 2. Is there regulatory lock-in? (HIPAA/FDA) 3. Is it embedded in the transaction? (Money flow)	**High Risk / Search Layer.** Expect multiple compression. (e.g., Legal research)	**Medium Risk.** (e.g., Mixed portfolios)	**Safe / Durable.** (e.g., Healthcare EHRs, Payment Processors)

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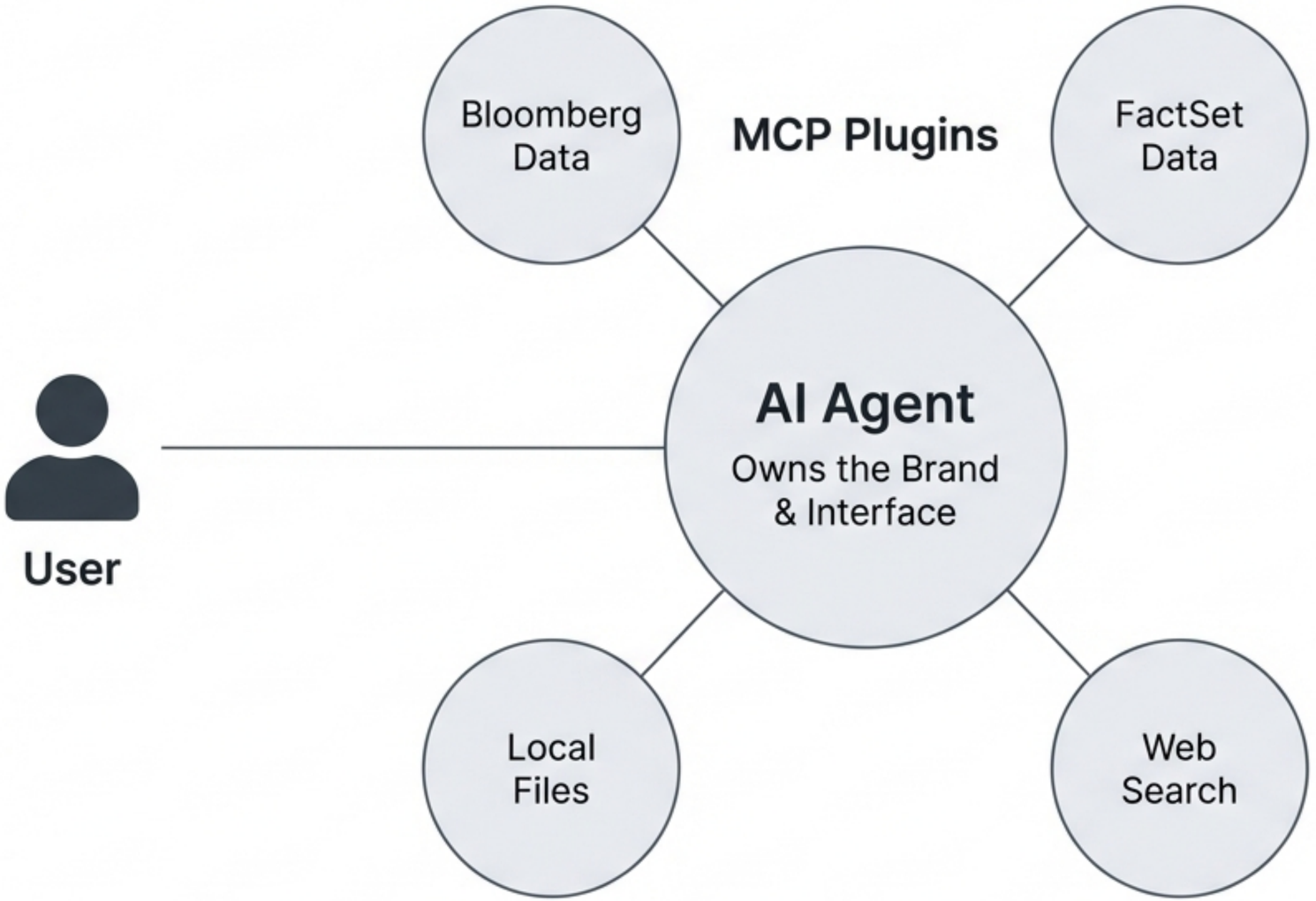
Future Outlook: The Agent as Aggregator



Aggregation Theory 2.0: The Agent captures the relationship. SaaS companies risk becoming “dumb pipes” competing on price to feed the Agent.

Technical Driver: Model Context Protocol (MCP).

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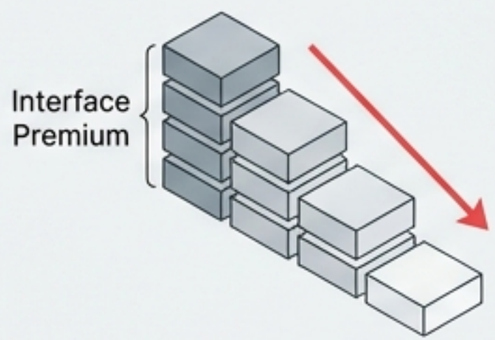
From Access to Authority

1. The Crash is Rational:

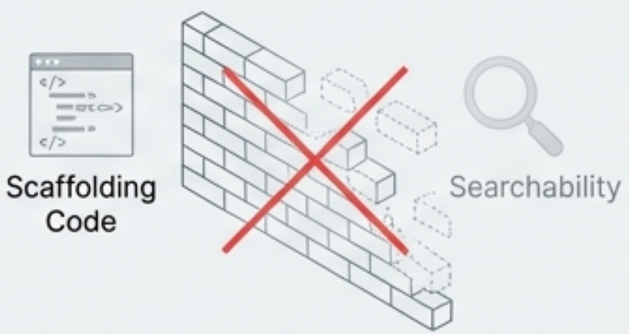
The market is correctly removing the “Interface Premium”.



`Market Correction: Value Compression`

2. The Moat is Gone:

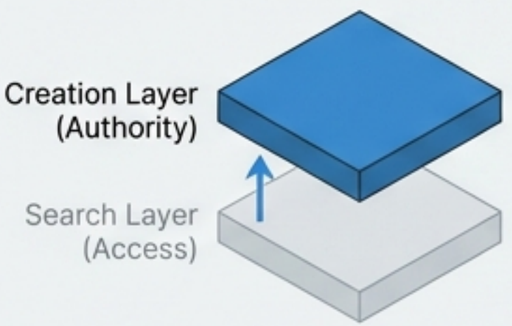
Scaffolding code and “searchability” are now commodities.



`No Proprietary Data = No Moat`

3. The Pivot:

Survival depends on moving from Search Layer (Access) to Creation Layer (Authority).



`Value Creation: Proprietary Ownership`

“The companies that survive... moved from ‘we organize public data better’ to ‘we own data you can’t get anywhere else.””

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