Within tech, CIO thinks investors should focus on companies with exposure to disruptive technologies and those with high growth potential. (UBS)

Within tech, focus on companies with exposure to disruptive technologies

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The AI race to build and harness new capabilities and tools has boosted related capital expenditure across industries. CIO thinks the adoption of AI will unlock value across a number of sectors.

Large-cap tech names have more room to run, and for us, US IT is most preferred. This aligns with our bias for quality, as the sector offers robust balance sheets and high earnings growth, in our view.

AI to continue to drive tech outperformance

- Tech stocks delivered strong returns in 1Q24, led by AI; semiconductors posted the best returns within tech globally.
- We expect the global tech sector's earnings to grow by 18% in 2024, with AI revenues rising 55% in 2024 and 35% in 2025.
- 1Q24 marked the first quarter where revolutionary AI products were introduced including more powerful GPUs and generative AI in both text-to-video and software engineering.

But the story doesn't end with AI; large tech names offer quality exposure

- US tech company balance sheets are strong, a positive driver in a period of high interest rates and slowing economic activity.
- Earnings revisions are improving, adding to confidence that key end-markets have reached a trough.

- Historically, quality growth stocks tend to perform well during the later stages of the business cycle, as market expectations of policy easing become cemented.

We favor a barbell approach to investing in AI: titans and unicorns

- Global tech stocks outperformed broader markets in 1Q; AI-sensitive industries like semiconductors outperformed most, rising 34%, while software rose 9%.
- Key indicators suggest that AI growth trends will stay robust in 2Q, with the semiconductor and software segments our most favored.
- We continue to recommend a barbell approach to AI investing: Big tech in the listed space (strong scale, margins, and execution advantages), and unlisted AI unicorns and startups (breakthrough innovations and strong long-term potential).

Did you know ?

- The IT segment is the most global of all S&P 500 sectors. More than 58% of its revenue comes from outside the US, versus 40% for the index as a whole.
- Disruptive innovation, a term coined by Harvard University professor Clayton Christensen, refers to processes in which a product or service takes initial root in simple applications at the bottom end of a market before moving up the value chain and eventually displacing established competitors.
- We expect AI industry revenues to grow from USD 28bn in 2022 to USD 420bn in 2027, with risks tilted to the upside.

Investment view

We raised the US information technology sector to most preferred in 4Q23. Within tech, we think investors should focus on companies with exposure to disruptive technologies and those with high growth potential. We like high-margin tech industries: Software, internet, and semis.

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