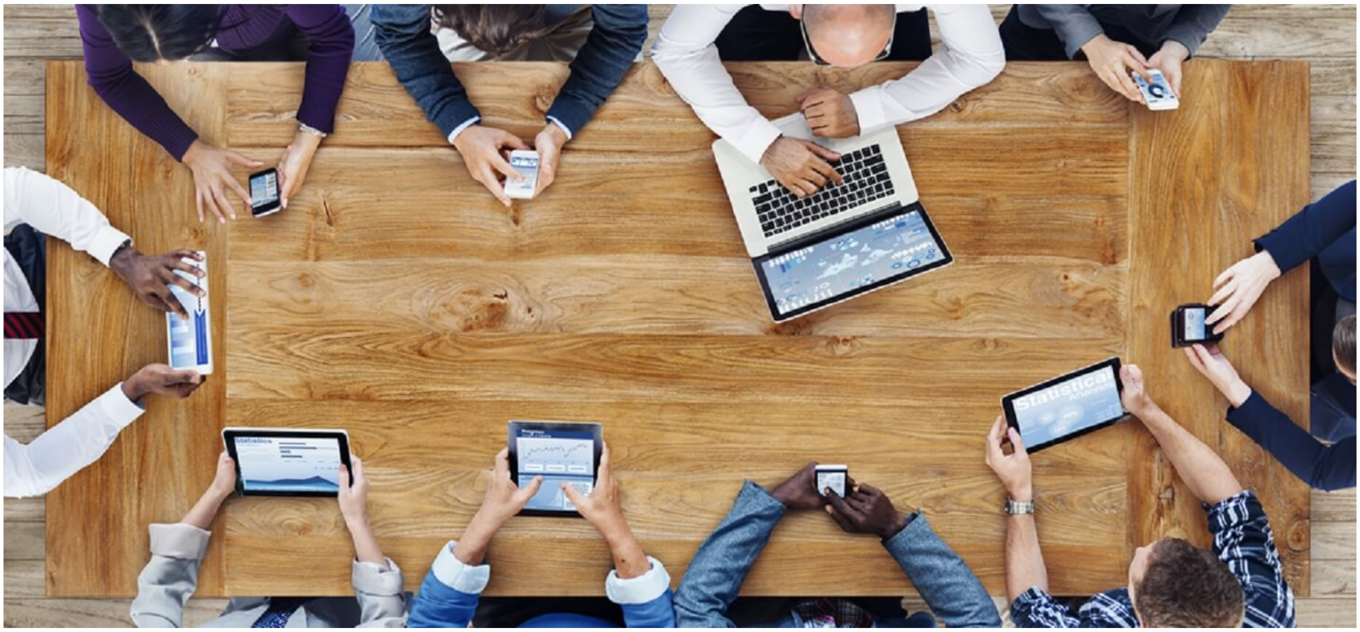

Software firms are less sensitive to global growth thanks to their strong recurring revenue bases, yet should gain from broadening AI demand trends for applications and models. (UBS)

US tech gains set to continue on stronger AI growth

03 January 2024, 10:02 pm CET, written by UBS Editorial Team

The largest US technology stocks ended 2023 as the shining stars of their domestic market. While the benchmark S&P 500 Index ended last year with a 24.2% price return, the so-called "Magnificent seven" stocks posted gains of between 48% and 249%.

Many of these companies are integral players in the development and dissemination of artificial intelligence. Investors may naturally worry that 2023's AI-fuelled gains could lose steam in 2024—whether due to slower practical implementation of AI to boost efficiency and profits, or as investors look to book potential gains and rebalance portfolios away from last year's leaders.

But we believe the investment case for AI and related companies will endure in 2024—and is indeed set to strengthen:

We upgrade our AI revenue forecasts to 15x growth between 2022 and 2027. When we launched our AI industry revenue estimates last year, we expected growth from USD 28bn in 2022 to USD 300bn by 2027. That translated into a compounded annual growth rate of 61%. But we now upgrade our estimate further, with the greatest risk being that we are too conservative. We now forecast industry revenues of USD 420bn by 2027—a 72% annual growth rate and a fifteenfold increase in just five years. The drivers will likely be stronger-than-foreseen demand for AI and greater clarity on company spending plans on AI infrastructure. While such figures may seem lofty, they are consistent with prior phases of the computing cycle, such as mainframe, PC, and smartphone shipments.

Clearer corporate spending plans can support expanded AI infrastructure spending. With more businesses offering greater transparency on their AI investment intentions, we think the markets for chips and GPUs will be the biggest 2024 beneficiaries. We also think AI chips spending will benefit from higher inferencing—the application of rules to analyze and draw conclusions from data—thanks to the increased use of generative AI and applications like copilots. Looking further ahead, we expect a broadening use of AI across more economies and markets to drive increased use of AI applications and models. We expect this market to grow from around USD 2.2bn in 2022 to USD 225bn by 2027, a near 152% compound annual growth rate.

Increased regulatory focus should provide more opportunity than threat in 2024. We expect debate and rule-setting around AI to gain pace this year, with numerous elections making the topic an increasingly politicized one. Our overall view is that clearer regulatory frameworks in the earlier stages of a new technology's development are preferable to retroactive regulation when a technology is well established. Recent investor experiences in the education technology and financial technology fields are instructive examples of the potential damage from later legislative changes. We think excessive corrections in major AI beneficiaries—due to geopolitics or regulations—could present a buying opportunity as underlying demand trends for AI should continue to be solid in the foreseeable future, in our view.

So, we think AI trends can continue to support technology stocks, especially US ones, in the year to come. We retain a most preferred stance on the US technology sector, as part of our equity sector strategy.

When it comes to expressing these views in portfolios, we believe the semiconductor and software industries (with a combined market cap of more than USD 10tr) are the best ways to ride the strong and improving visibility for AI. Semiconductors, while cyclical, are well positioned to benefit from solid near-term demand for AI infrastructure. Improved pricing could help deliver 25% revenue growth and more than 50% operating profit growth here, in our view.

Software firms are less sensitive to global growth thanks to their strong recurring revenue bases, yet should gain from broadening AI demand trends for applications and models. We expect mid- to high-teen percentage revenue growth in 2024, which would be a solid outcome, thanks to strong AI and cloud tailwinds as well as resilient margins of 36%, well above the global IT average of 22% and global average of 16% (based on MSCI AC World IT and MSCI AC World indexes, respectively).

Main contributors – Solita Marcelli, Mark Haefele, Kevin Dennean, Sundeep Gantori, Delwin Kurnia Limas, Bennett Chu, Matthew Carter, Christopher Swann

Read the original report : **US tech gains set to continue on stronger AI growth, 3 January 2024.**

For more details, please see **TechGPT: Raising AI revenue forecast by 40%(January 2, 2024).**

Watch: CIO Artificial Intelligence video series