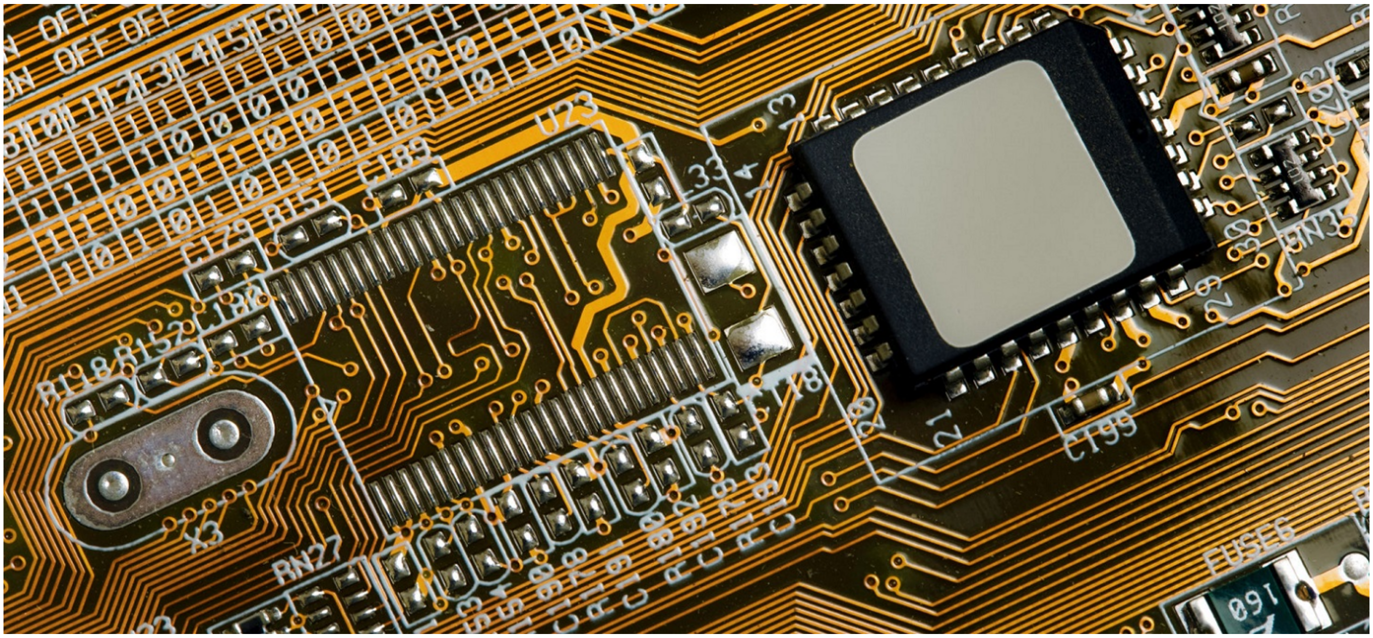

CIO maintains their positive view on AI and believes the technology will continue to drive growth in the years ahead. (UBS)

Tech volatility may increase as US export controls take shape

11 November 2024, 2:01 pm CET, written by UBS Editorial Team US Editorial Team

The US has reportedly ordered Taiwan Semiconductor Manufacturing Co to halt shipments of advanced chips used in artificial intelligence (AI) applications to mainland Chinese customers starting Monday. According to a Reuters report, the restrictions detailed in a Department of Commerce letter apply to chips of 7 nanometers or more advanced designs. TSMC shares traded 0.5% lower in Taipei on Monday.

The US order came just days after the conclusion of the US presidential election, with markets having anticipated some form of chip-related export controls in the fourth quarter. The US Department of Commerce introduced such restrictions in October 2022, with plans to review them at least every 12 months. Back then, similar letters were sent to NVIDIA, AMD, and equipment makers to restrict their ability to export top AI-related chips to mainland China, and the restrictions in those letters were later turned into rules that apply to companies beyond them.

Volatility in the broader semiconductor sector is likely to pick up as more details on the latest round of export controls emerge, while potential tariffs during President-elect Donald Trump's second term could create additional headwinds. But, without taking any single-stock views, we continue to believe solid fundamentals should provide support for quality semi names with exposure to the AI growth story.

Investors are likely to refocus on fundamentals once uncertainty is removed. In both 2022 and 2023, semiconductor-related names experienced sharp corrections in October due to uncertainty around export controls, with the Philadelphia Semiconductor Index falling around 15-20%from peak to trough. However, chip stocks rebounded over the next few months as the impact appeared manageable. While the broader implications of the latest restrictions remain unclear at this stage, we believe investors will look beyond the headlines and assess the company-specific impact when details become available.

Big tech's commitment to AI spending should continue to support semi names exposed to the secular AI trend. Recent earnings from big tech companies continue to underscore their willingness to invest in the technology. We now expect their combined spending to grow 50% this year to USD 222bn and another 20% to USD 267bn in 2025. Assuming peak capital intensity (capex divided by sales) for each company, the combined capex could potentially reach USD 280bn, highlighting further upside to our estimates. The biggest beneficiaries of big tech's robust AI spending, in our view, are companies exposed to AI semis, especially in areas like graphics processing units (GPUs), custom chips, and high bandwidth memory.

AI demand remains robust as adoption and monetization pick up. In addition to continued investment in AI infrastructure, recent tech earnings also showed accelerating cloud revenue growth that points to an uptick in AI monetization. Management comments also suggested increasing AI adoption and efficiency gains across industries. We maintain our positive view on AI and believe the technology will continue to drive growth in the years ahead.

So, investors should be prepared for heightened volatility. Those with low AI exposure may utilize structured strategies to build up long-term allocations, while investors with high exposure may consider capital preservation strategies.

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