



With the semiconductor industry trading at a 10% discount to the broader tech sector, the risk-reward profile remains attractive, and CIO sees it as a good way to ride the AI wave. (UBS)

# Outperformance of global semis should continue

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**The semiconductor industry, fueled by the rise of generative artificial intelligence (AI), has outperformed the broader tech sector, with the Philadelphia Semiconductor Index up around 19% year-to-date versus a 13% gain for the MSCI All Country World IT index.**

Despite the strength of the rally, we anticipate continued outperformance for global semis due to faster earnings growth, improving operating margins, and strengthening balance sheets.

We expect earnings growth of 50% for the global semiconductor industry this year and 25% in 2025—outpacing the estimated 20% and 16% for global tech—driven by increased capital expenditures from big tech firms, particularly in AI computing. This should offset mixed end-demand for other segments like smartphones and PCs. Google parent Alphabet last week announced a series of products that showcased the tech giant's AI efforts across its businesses, including a beefed-up Gemini chatbot and improvements in its search engine.

Operating margins in semiconductors are improving, potentially reaching around 35% this year and 37.5% in 2025, rivaling the traditionally high margins of the software industry. This is due to strong pricing power and operational efficiencies, with less impact from cyclical factors like inventories and capacity changes. Instead, structural drivers such as AI, cloud, and the increasing silicon content in chips are expected to sustain pricing strength.

Semiconductor companies are also seeing better free cash flow margins, which we expect to rise from 15% in 2023 to approximately 22% this year and 26% in 2025. This should enable higher cash distributions and investments in start-ups.

*Takeaway: With the semiconductor industry trading at a 10% discount to the broader tech sector, the risk-reward profile remains attractive, and we see it as a good way to ride the AI wave. We favor industry leaders in logic, foundries, and semiconductor equipment, viewing semiconductors as a top choice to capitalize on the AI trend, including tactical opportunities in memory.*

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