CIO continues to recommend investors examine their tech exposure and ensure sufficient allocation to beneficiaries of AI chip demand and big tech. (UBS)

Commitments by AI supply chain companies suggest resilient AI demand

16 October 2024, 1:39 pm CEST, written by UBS Editorial Team

Semiconductor stocks fell on Tuesday after chip equipment maker ASML's lower-than-expected 2025 sales forecast sparked worries over global chip demand. The Philadelphia Semiconductor Index slid 5.3%, while ASML shares closed the day 16% lower in Amsterdam.

In its quarterly earnings published a day earlier than scheduled, the Dutch company significantly lowered China's contribution to its revenue in light of export controls, and said that non-AI parts of the semiconductor market had been weaker for longer than expected. As the softness "is expected to continue in 2025," the company now anticipates next year's total net sales growing in the lower half of the range it previously forecast.

But we note the growing division in the tech sector between strong AI demand and mixed trends in consumer electronics. A weak start to the tech earnings season is unlikely to be a reliable predictor of the industry outlook. Instead, we offer several observations based on our recent and historical analysis of the industry.

Volatility is likely to pick up in the near term amid uncertainty and potential risks. October has historically been the most volatile month for tech stocks. The monthly realized volatility for the Nasdaq 100 over the past 40 years has been 26% in October, compared to an average of 22% in other months. In addition to upcoming company financials, we expect still-elevated geopolitical uncertainty and the risks around export restrictions to also contribute to rising volatility. Earlier this week, Bloomberg reported that the Biden administration is mulling new sales caps on advanced AI chips to be applied on a country-specific basis, with US officials viewing semiconductor export licenses as diplomatic leverage.

Commitments by AI supply chain companies suggest resilient AI demand. Despite investor concerns about the sustainability of AI-related capex, AI supply chain companies' investment plans suggest a more constructive multi-year outlook—including TSMC's rapid expansion in advanced AI packaging facilities, Hon Hai's plan to build the world's largest facility for specific chips that are crucial to the development of advanced AI applications, and Oracle's ambition to develop sizable computing clusters that can handle large amounts of data and perform complex computations. Without taking views on any single names, we continue to see a strong growth outlook for AI semis, and are closely watching managements' guidance on future demand in the days and weeks ahead.

Consumer tech demand is mixed. Demand in traditional tech segments such as smartphones, PCs, and consumer electronics has been lackluster in recent quarters. The trend could continue into next year. For example, wait times for the latest iPhone series are shorter compared to previous models, while "rush orders," where vendors request expedited fulfillment amid higher-than-anticipated consumer demand, were limited in the PC market in the third quarter, a notable shift from previous quarters. Original design manufacturers are also guiding for flat to slightly declining shipments in the fourth quarter. Overall, we expect a low-single-digit rise in smartphone and PC volume in 2025, although new consumer-centric AI features could accelerate the replacement cycle.

So, we continue to recommend investors examine their tech exposure and ensure sufficient allocation to beneficiaries of AI chip demand and big tech. We forecast earnings growth of about 35% for our preferred AI companies this year. Investors should take advantage of tech volatility through structured strategies or a buy-the-dip approach for quality AI stocks.

Main contributors: Solita Marcelli, Mark Haefele, Sundeep Gantori, Delwin Kurnia Limas, Daisy Tseng

Original report: **Weak start to tech results does not derail AI growth story, 16 October 2024.**