Strategic: Invest in transformational innovation

Invest in transformational innovation

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- **Why?** 1) Innovation remains a key driver of long-term equity performance and an important feature of enduring market leaders. 2) Structural shifts in AI, energy infrastructure, and health care are expanding global profit pools and reshaping industries. 3) We expect our TRIO themes to offer durable, structural growth that we believe can persist well beyond short-term market volatility.

Position at the forefront of change and seek long-term growth in transformational innovations. Source: Anna Evans_Unsplash

Historically, the stock market has mirrored transformational structural changes. In the US, the Dow Jones Industrial Average has been variously dominated by steel, automobile, internet, and pharma companies as technological innovations have blossomed. Our analysis also shows that between 1990 and 2020, a mere 2.4% of US companies and 1.4% of non-US firms account for 100% of stock market returns.

Picking the right themes and the right companies at the forefront of those themes is therefore crucial for long-term equity returns. So, we identify three enduring market drivers, exposure to which should be investors' first task when building long-term stock allocations as part of a well-diversified portfolio.

These Transformational Innovation Opportunities (TRIOs) are *AI*, *Power and resources*, and *Longevity*.

AI

The AI rally is in its fourth year, but the narrative is evolving. We project the total AI addressable market to reach USD 3.1tr by 2030, growing at a 30% CAGR from 2026. The sharp rise then rebound in many semiconductor companies and other AI-linked parts of the market this year has heightened the risk of single-stock concentration.

Looking ahead, we expect AI capex to rise further, with supply bottlenecks in key segments requiring significant time and investment to resolve. While higher spending and strong earnings are a tailwind, any reversal in this momentum could quickly shift investor attention back to monetization. Gains thus far have been led by semiconductors, though we think the value-creation story is broadening beyond US technology, with opportunities emerging across the enabling (semiconductors, cloud), intelligence (software, algorithms), and application layers. Within semis and hardware, our top three areas of focus are currently semiconductor capital equipment, foundries, and compute names, particularly CPU-related.

Power and resources

The intersection of AI-driven demand, energy market disruption, and geopolitical risk is sharpening the focus on energy security and infrastructure resilience. Elevated energy prices reinforce the importance of resolving grid bottlenecks and accessing essential materials. We expect capital allocation to remain directed toward power, grid, and critical resources, with the current investment cycle shaped by structural growth drivers and tactical risk mitigation considerations.

Ballooning data center demand is continuing to accelerate investment in power and grid infrastructure, with global grid investment projected at USD 500bn in 2026 and annual sector investment reaching USD 3tr by 2030. Opportunities span grid resilience, renewables, nuclear, industrial automation, and critical minerals, with companies at the core of this transition reporting record order backlogs and robust demand.

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Longevity
While ongoing geopolitical uncertainty in the Middle East has weighed on investor sentiment in more economically sensitive sectors, health care companies' revenues tend to be less affected by these developments. We think that the diversified supply chains and strict cost controls of health care companies should allow them to protect profit margins, even in adverse scenarios where energy prices remain high.

How the TRIOs can complement a diversified portfolio
Structurally, we think the Longevity market is set to expand from USD 5.3tr in 2023 to USD 8.0tr by 2030. In our view, the current period stands out for its concentration of clinical milestones and regulatory events, offering potential for outsized returns in select segments. We expect 2026 to be a catalyst-rich year, with multiple late-stage pipeline readouts in obesity, oncology, and medical devices, and potentially more strategic M&A as large-cap pharma companies seek to expand their pipelines. While the risk of AI-driven disruption is present, we believe that the threat to core health care activities remains manageable and that biopharma and medtech are positioned to benefit from productivity gains.

We believe the most direct way to access CIO's Transformational Innovation Opportunities is to follow our portfolios. Investors can consider tools that provide access to the CIO selection of global stocks in each of our TRIO themes. This approach spares investors the need to make dynamic adjustments and rebalancing when we adjust our selections to account for evolving value chains, while also helping to tailor and hedge FX exposures to the investor's reference currency. Last, it may provide the convenience of single, flexible trading in and out of the "AI," "Power and resources," and "Longevity" portfolios, subject to normal secondary market conditions.

For investors with existing exposure to CIO's "AI" and "Power and resources" portfolios, we believe investing in "Longevity" may provide potential growth and diversification benefits. Our analysis suggests "Longevity" has demonstrated negative relative return correlations to our "AI" stock list and low positive correlations to our "Power and resources" selection. In simpler terms, the "Longevity" selection would have generally outperformed on days when our "AI" portfolios would have underperformed global stocks (MSCI AC World.)

Investors who construct their own portfolios may also consider using building block modules that follow CIO's TRIO portfolios, dedicated single-equity approaches as part of a well-diversified portfolio, and diversified investment funds whose current constituents overlap with the principal holdings in CIO's portfolios. Additionally, we see scope to use structured strategies to take advantage of pockets of volatility on single stocks. Thematic private equity and private infrastructure (especially for *Power and resources*) may also offer access to our TRIOs for long-term-oriented investors with the willingness and ability to bear private markets' unique risks, including but not limited to illiquidity.

Global asset class preferences definitions
The asset class preferences provide high-level guidance to make investment decisions. The preferences reflect the collective judgement of the members of the House View meeting, primarily based on assessments of expected total returns on liquid and commonly known indices, House View scenarios, and analyst convictions over the next 12 months. Note that the tactical asset allocation (TAA) positioning of our different investment strategies may differ from these views due to factors including portfolio construction, concentration, and borrowing constraints.
Attractive: We consider this asset class to be attractive. Consider opportunities in this asset class.
Neutral: We do not expect outsized returns or losses. Hold longer-term exposure.
Unattractive: We consider this asset class to be unattractive. Consider alternative opportunities
Note: For equities, we have a five-tier rating system with two additional preferences
Most Attractive: We consider this asset class to be among the most attractive. Investors should seek opportunities to add exposure.
Least Attractive: We consider this asset class to be among the least attractive. Seek more favorable alternatives opportunities.
When equities are included with the other asset classes in the three-tier rating system, we collapse “Most Attractive” with “Attractive” and “Least Attractive” with “Unattractive.”

Appendix

Risk information
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