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Market Update
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Potential for Rapid AI Adoption Triggers Selloff

Over the past few weeks, investors likely noticed another pullback in technology stocks, particularly companies involved in artificial intelligence. What is interesting about this selloff is that it is happening for almost the opposite reason as the one we saw late last year.

The previous correction (which we mentioned in our fourth quarter letter) was driven by "bubble" concerns—investors questioning whether the massive investments in AI infrastructure would actually generate sufficient returns. The worry was that adoption would be slower, benefits smaller, and expectations too high relative to reality.

The concerns triggering the current selloff are inverted: investors are worried that AI is advancing *too quickly* and that widespread adoption will disrupt entire industries faster than anticipated. Instead of questioning whether AI will work, the market is grappling with the implications of it working very well. For example, Anthropic's product Claude recently introduced specialized AI capabilities for legal work, finance functions, and sales operations that triggered significant selloffs in established software companies.

The implications of this change are significant. When markets worry about a bubble, they are questioning the underlying technology's capability and value creation potential. When markets worry about disruption, they are validating that the technology works—the concern has moved to which companies benefit and which face headwinds.

This creates a more complicated investment environment, and the potential for more differentiated returns among AI companies. For example, infrastructure providers—semiconductor companies, cloud platforms, data centers, and related power infrastructure—are positioned to benefit from rapid adoption regardless of which specific applications succeed. The faster AI gets deployed, the more infrastructure is needed.

Software companies on the other hand face a more mixed picture. Those with defensible competitive moats, proprietary data assets, or businesses that become more valuable with AI integration will continue to thrive. But companies whose value proposition rests on functionality that AI can replicate face legitimate questions about pricing power and margins going forward.

AI represents a genuine technological shift with significant economic implications. With any rapidly evolving industry, there will be winners and losers along the way. For investors, it is better to see a transition resulting from too much adoption of a new technology than too little. That said, it is still necessary to understand the impact of rapid change, both positive and negative, on different industry participants. This will become increasingly important as AI transitions from a concept in most investors' minds into a real industry.

Thank you as always for being a client, and please feel free to call Roger or me should you wish to discuss your portfolio.

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