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AI Investing: Climbing the Wall of Worry

Author

Mark Baribeau, CFA
Head of Global Equity

Mark Baribeau, CFA, Head of Global Equity at Jennison, challenges common misconceptions and shares his views on today's AI investment landscape, from inflecting demand and valuations to emerging opportunities and key risks across the AI value chain.

Key Takeaways

- AI infrastructure valuations appear reasonable to us
- Current AI demand is robust and supported by trillions[1] of dollars in contracted cloud commitments
- AI compute build is in early stages
- Multiple supply chain choke points offer investment opportunities
- Software sector faces structural challenges
- Key risks to monitor include supply constraints and execution, but current trends support a durable multi-year investment cycle

Introduction

Far from being in a euphoric bubble about AI, looking at the fundamentals and the shrinking valuations of some of the AI infrastructure companies, we are climbing a "wall of worry" of epic proportions. When it comes to the AI investment opportunity set, many market participants have expressed concerns about valuations, soaring capex, choke points that will act as limiting factors for AI capacity rollouts, lack of funding/financing, and the impact of AI on other industries, with software in particular being in the crosshairs. While we are monitoring all these factors, we believe that the changing dynamic in software is the only valid concern at this time.

Is this a Re-Run of the 1990s "Dot-Com" Bubble?

The AI opportunity is being driven by accelerating, contracted enterprise revenue, and the dispersion between potential winners and losers has become the defining feature of the landscape. The comparison to the 1990s technology bubble is misleading on the most critical metrics that matter. I was investing through that period, and three differences stand out:

1. **Valuations.** If this period was anything like 1999, the major AI winners would likely be trading at multiples in the 60-70x range. Today, many AI beneficiaries trade in the 20-25x forward P/E

[1] Source: Company financial filings as of Q1 2026. Combined remaining performance obligations and backlog figures across Alphabet (Google Cloud), Microsoft, Amazon (AWS) and Oracle. Compiled by Cloud Wars, April 2026.

multiple, which in some cases, values them cheaper than widely held quality consumer names. Investors are not paying a premium today for an overly-optimistic view of the future.

2. **Adoption.** In 2000, I did not know anyone who had bought a book online. Today, AI use is broad-based across age groups and use cases. It is not unusual to find 70-year-olds running ChatGPT on their phones. The technology has crossed into mass adoption ahead of the capex peak, not after. Most companies we speak with are already using AI internally to improve productivity. That is the reverse of the 1999 dynamic, when spending ran ahead of demand that had not yet materialized.
3. **Funding model.** The vast majority of AI capex is being funded by the operating cash flows of the largest hyperscalers, supplemented by private credit to a new generation of cloud infrastructure providers. This is fundamentally different from the speculative IPOs that characterized the late 90s technology bubble. The companies driving today's cycle have, in our view, been able to raise capital on favorable terms. In the current environment, demand continues to outpace the most optimistic expectations. As a result, capex budgets continue to increase, with the additional funding requirements getting disproportionate attention.

The financial media has yet to fully grasp these dynamics, and the market remains doubtful. However, we see this skepticism as an opportunity.

"It's all Just Hype, the End-Demand Isn't There"

The empirical evidence does not support this critique. AI demand is no longer theoretical; it is no longer even generally contested. It is increasingly visible in contracted revenue. By the end of Q1 2026, the combined backlog of contracted cloud commitments across the major hyperscalers had exceeded $2 trillion[2], up materially from the prior quarter. Several hyperscalers have publicly stated they cannot keep pace with current demand. These companies are racing to fulfill contracts, not building speculatively.

A year ago, the demand bear case was more credible: meaningful capex was being deployed, and relatively little revenue was being generated. We believe that bear case no longer holds. Anthropic became the fastest company in history to reach a $30 billion annualized revenue run rate[3], and recent reports estimate that figure has already climbed north of $43 billion in the months since.[4]

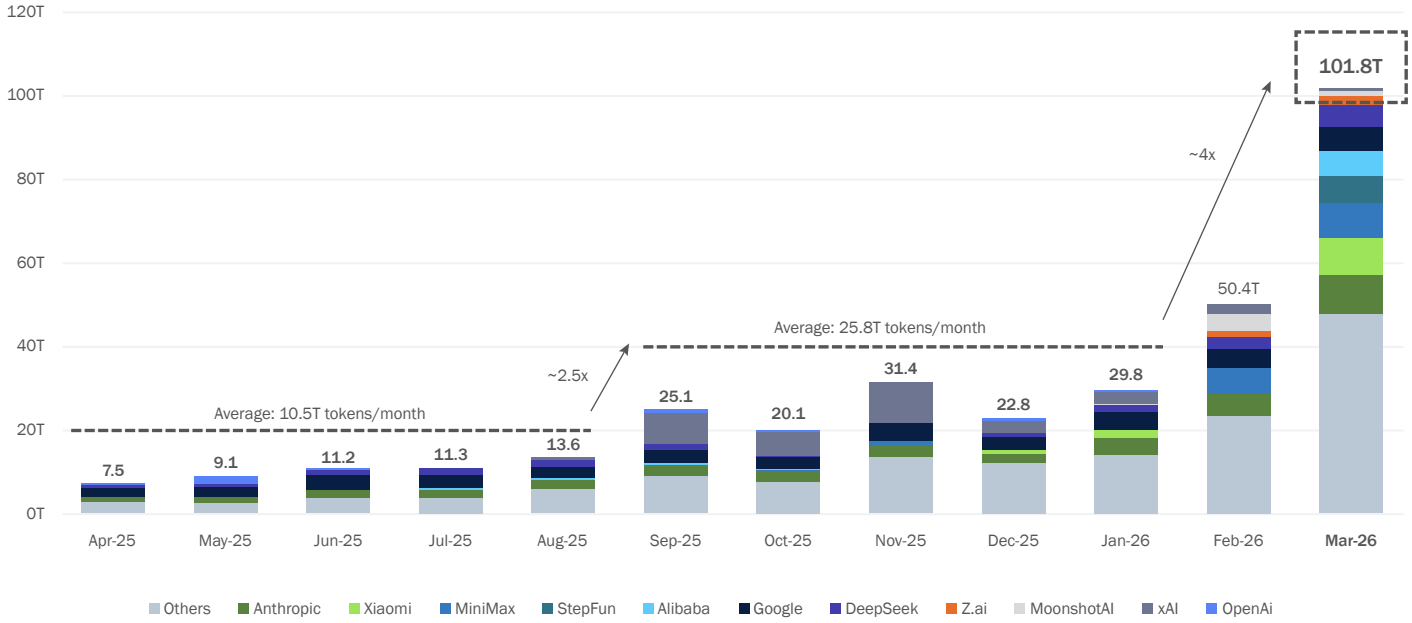
Token generation, which is the measure of compute output from an AI system, is another useful indicator. Per our estimates, token volumes have increased roughly tenfold over the past twelve months, running at approximately 100 trillion per month. This is what enterprise AI adoption looks like at scale, and it is exposing every choke point in the supply chain, from logic chips to memory to power. Within AI infrastructure, market reactions during the Q1 2026 earnings season have correlated closely with revenue inflection, not driven by multiple expansion.

[2] Source: Company financial filings as of Q1 2026. Combined remaining performance obligations and backlog figures across Alphabet (Google Cloud), Microsoft, Amazon (AWS) and Oracle. Compiled by Cloud Wars, April 2026.

[3] Source: Anthropic disclosure, April 2026.

[4] Source: Sacra Research estimate, April 2026 (figure based on third-party analysis; not disclosed by the company).

Token Consumption by AI Lab (OpenRouter Usage Data)



As of 4/13/26. Source: Truist Securities; used with permission. The examples above are for illustrative and educational purposes only and should not be considered investment advice.

"It's Too Late: We're Already at the Peak"

This is a legitimate concern, but we believe we are still in the early innings of the AI investment cycle. Hyperscaler capex is expected to exceed $700 billion this year and is on track to approach $1 trillion in 2027.[5] We anticipate that approximately 50% of next year's expenditure will be allocated to semiconductors, representing a significant shift in profit distribution towards AI computing at an unparalleled scale. Nvidia's upcoming Vera Rubin platform is scheduled to begin shipping later in 2026. It is engineered to provide significantly enhanced inference performance while achieving a tenfold decrease in inference cost per token.[6] That kind of step-change is what drives the next leg of demand: lower cost per token tends to encourage more usage, which in turn drives more revenue. If each new generation platform continues to deliver this kind of step-function improvement, we believe the addressable market continues to expand rather than saturate.

"The AI Investment Opportunity is too Narrow – It's All Nvidia GPUs and Mag 7 Hyperscalers"

The acceleration in AI demand has exposed multiple supply-chain choke points that were not on the consensus map twelve months ago. These represent substantial incremental investment opportunities in our view.

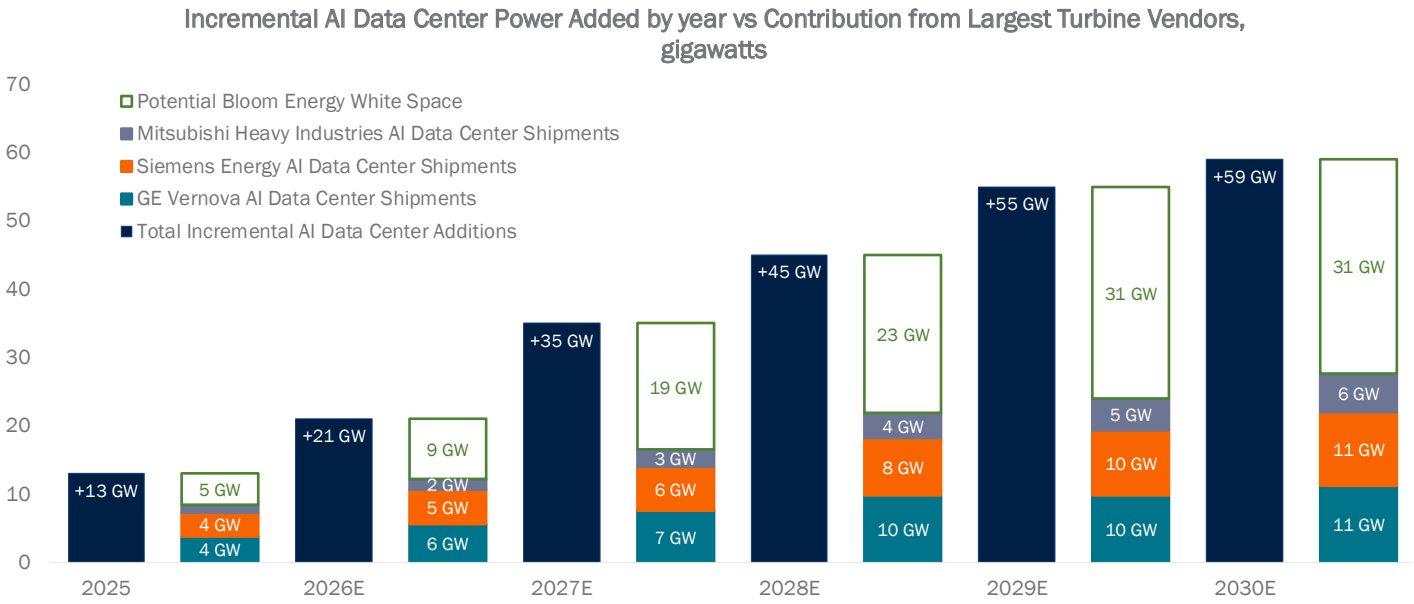
The first is CPUs. As we move from AI model training (which is GPU intensive) to inference and to Agentic AI, CPU chips have a bigger role to play in these AI workloads. The reasoning workloads that agents perform run partly on CPUs rather than entirely on GPUs. Companies delivering CPUs for AI workloads have guided materially higher revenue growth as inference demand scales. We believe this development has been under-appreciated by the market.

[5] Sources: Hyperscaler 2026 capex guidance, as compiled by Reuters and Futurum Research, May 2026; Moody's Investors Service estimate for 2027, May 2026.

[6] Source: Nvidia.

The second is memory. Currently, there is a shortage of memory, and producers are gaining pricing power through new long-term and take-or-pay contracts for the first time in years. This applies not only to DRAM and high-bandwidth memory commonly used with GPUs, but also to NAND flash memory needed for inference workloads, which store the model's context and prior outputs. The imbalance between demand and supply is also expected to benefit capital-equipment companies involved in the memory supply chain.

Finally, power is the most acute physical constraint on the AI infrastructure buildout. Data center demand requires a multifold increase in power generation over the next few years. Natural gas turbine manufacturers are largely sold out through the end of the decade. This creates room for innovative solutions, including off-grid, behind the meter, fuel-cell technologies which offer better time-to-power and improved environmental outcomes.



As of 4/29/26. Source: Jennison and company reports. GW = gigawatts. Based on capacity gas turbine OEM capacity and Jennison estimates. *Estimated. Forecasts may not be achieved and are not a guarantee or reliable indicator of future results. Although Jennison believes that the expectations reflected in such forward-looking statements are based on reasonable assumptions, actual results may differ materially from those projected. The examples above are for illustrative and educational purposes only and should not be considered investment advice.

"AI Monetization Will Never Meet Optimistic Expectations"

This push back is fascinating: coming despite monthly evidence that OpenAI and now Anthropic are the two fastest growing companies in corporate history.

Roughly half of agentic AI usage relates to software engineering. Coding has been the natural first use case: it is structured, well-defined, and AI can learn it faster than a human can. That has made the technology industry's own adoption frictionless. Technology companies are already using AI to drive down coding costs and increase output. Use cases are now expanding into other enterprise verticals, with companies re-engineering workflows around agentic AI. This is the reason behind Anthropic's exponential growth over the last two years.

Outside of technology, most users are unlikely to learn AI coding themselves. They will need packaged applications. There are, by our count, hundreds of AI-native venture funded private companies attacking individual verticals with agentic products, affecting financial services, healthcare, customer service, and supply chain. A few of them are likely to grow into very large businesses, and we believe the next leg of token growth comes from vertical adoption through these packages. Most businesses will reach for finished applications rather than train their staff on the underlying models.

"The SaaSpocolypse Shows Why It Is Dangerous to Invest in Tech Right Now"

Almost, but not quite. The "SaaSpocolypse" refers to the recent sell-off in software companies as the market began to worry about the sustainability of the software companies' investment moats, as AI allows companies to code their own software applications quickly, easily and cheaply. This is a reminder that it is dangerous to invest in companies on the wrong side of the growing reach of AI's transformative power, particularly as the tech and IT spending dollars are all moving in one direction.

The investment case for many traditional software companies is breaking down on several fronts simultaneously. Firstly, and importantly, we do not expect customers to remove their enterprise software systems in the near term. Those will likely remain in place as repositories of data. However, the value-add layer on top of that data is increasingly being delivered by agents rather than by the incumbent software, which creates downward pressure on renewal pricing over time.

Second, enterprises are reallocating their internal software-development budgets away from new installations and toward agentic AI products. We think it is unlikely that a typical large enterprise will evaluate a new CRM installation this year. They are far more likely to divert their spending toward agentic tools that can reach across their existing software stack.

Third, with modern AI models being used to write new applications, competitors may be able to replicate years of accumulated engineering work in a fraction of the time, eroding what were previously durable competitive moats.

The market is forward-looking and is already discounting these pressures. Most software companies are not missing earnings today, but the terminal value equation has changed, which we believe is driving the multiple compression in the industry. With more compelling opportunities elsewhere in the AI value chain, it is important to be decisive.

"Nothing is Ever All Plain Sailing"

Correct: we believe the key risks lie in supply and execution rather than in demand. There are constraints throughout the AI supply chain, which paradoxically makes this less of a gold-rush dynamic and more of a measured, multi-year buildout. That measured pace gives us confidence in the durability of this investment cycle.

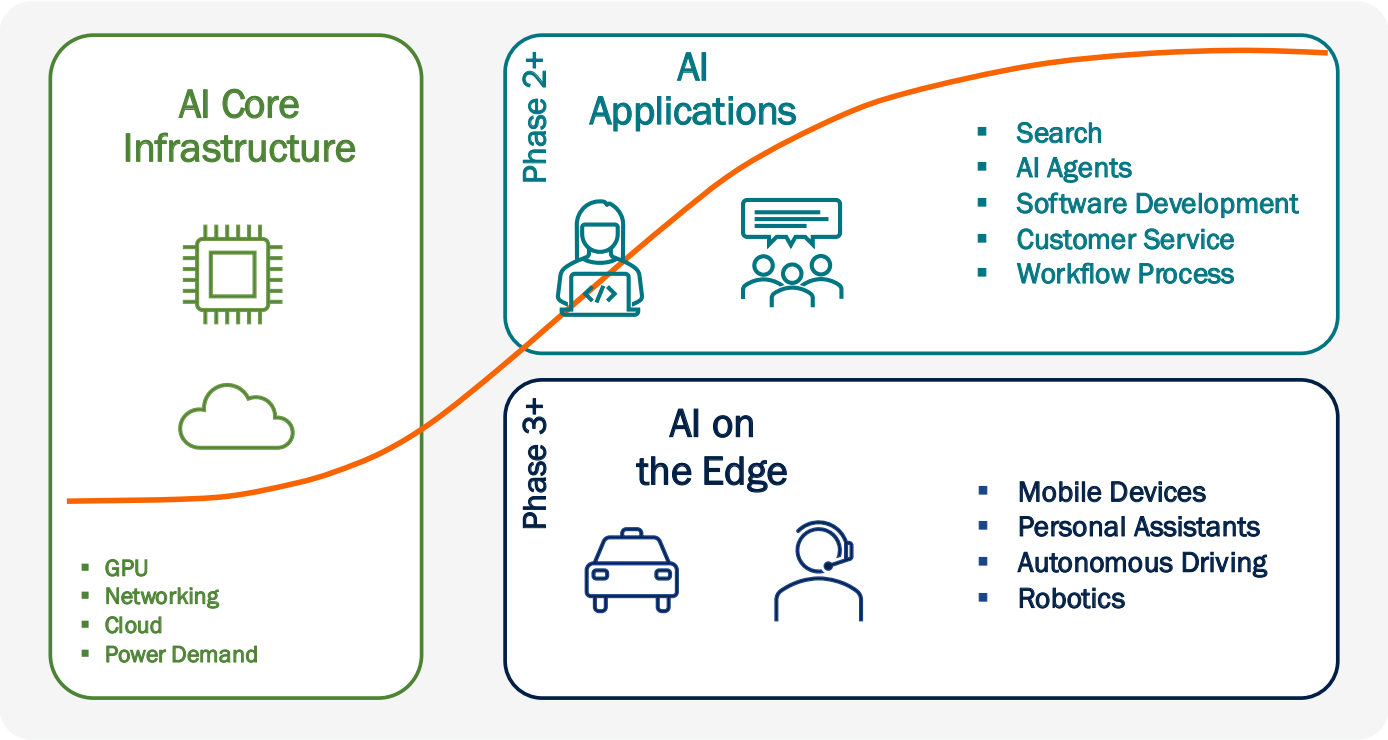
That said, there are specific risks worth monitoring closely. The first is the financial condition of the major AI labs. Many ecosystem partners are tied to their monetization trajectories, and if those paths falter, the broader ecosystem could become less healthy, even if other providers can absorb part of the slack. The second is political pushback on electricity prices and water consumption near data centers, a risk that off-grid power solutions may help to mitigate (but it remains a real near-term constraint). The third is the unit economics of tokens. If cost-per-token does not continue to decline on the trajectory that upcoming chip generations imply, demand could weaken. We have not seen evidence that this is occurring, but it remains a variable we watch.

Closing Thoughts

The most common error we see in client portfolios today is the assumption that AI is a single trade, fully priced, late-cycle, and analogous to the bubbles of the past. Our work suggests almost the opposite: we believe this is a multi-layered, multi-year cycle, funded by cash flows of some of the most profitable companies in history, and validated by contracted enterprise revenue. AI infrastructure companies are today trading at compelling forward earnings multiples. The opportunity set is wider than the market appreciates, and the dispersion between winners and losers is now the defining feature of the landscape. In our view, the AI investment opportunity is a transformational, multi-phased investment opportunity that we expect to remain fertile ground for active managers in the years to come.

The AI Monetization Cycle

Potential Sources of Alpha Along the S-Curve



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