AI: Temporary trend or enduring opportunity?—Part II

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In **part 1** of our series on artificial intelligence (AI), we examined its transformative potential and the influence of short-term dynamics on its long-term promise. This overview laid the groundwork for a deeper exploration of specific investment opportunities in part 2. We believe we are in the early stages of a significant growth opportunity, as AI continues to reshape industries. Investors now have the chance to identify potential winners and underperformers within key sectors that are leveraging AI to drive innovation and efficiency today while paving the way for future advancements. By analyzing these sectors and the characteristics of successful companies integrating AI, we can uncover compelling investment opportunities, keeping in mind this is a dynamic space so being agile and willing to pivot when necessary is essential.

Leaders and Losers

When considering potential net share gainers in the AI landscape, a few key success factors have emerged: scale, efficiency, a history of innovation and robust data infrastructure. Larger companies have an inherent advantage due to their ability to invest significantly in research and development or acquire venture-backed startups. This "buy vs. build" strategy enables them to enhance their capabilities more effectively. For example, companies such as Microsoft, Google, Meta or Nvidia are well-positioned to capitalize on AI advancements due to their substantial resources and established market presence. Their financial strength also enables them to weather economic downturns while continuing to invest in AI, furthering their leadership positions.

Focusing on established players with a strong track record in innovation is also important. One sub-sector within software exemplifying this is observability. Observability software includes the tools and platforms that provide insights into the health and performance of complex systems, allowing organizations to monitor, collect and analyze data from various sources. In theory, observability acts as a second derivative AI beneficiary; the more workload that is created, the more need there is to monitor them. Companies like Datadog and Dynatrace demonstrate this approach with their robust product pipelines and historical commitment to advancing technology. Organizations with a strong culture of internal innovation are more likely to emerge as leaders in this rapidly evolving market, making these factors essential considerations for identifying future champions in AI. This is not to suggest that new winners will not emerge along the way that may be worthy of consideration.

Additionally, companies that build and maintain robust data infrastructure are crucial for effectively leveraging AI technologies. Investors would be wise to seek firms committed to data management and integration, as the ability to harness quality data will be a key differentiator in the success of AI initiatives. Organizations lacking the necessary systems for collecting, managing, and analyzing data are likely to struggle with AI implementation, yielding generic results that limit overall value. For instance, HubSpot excels with its comprehensive customer relationship management (CRM) data, while Meta leverages its Facebook data to improve the effectiveness of its ad targeting. This vertical-specific data is critical; without it, organizations cannot effectively leverage insights to drive decision-making and strategy. Therefore, companies that fail to establish a strong data foundation risk losing their competitive edge in an increasingly data-centric world.

Sectors to watch

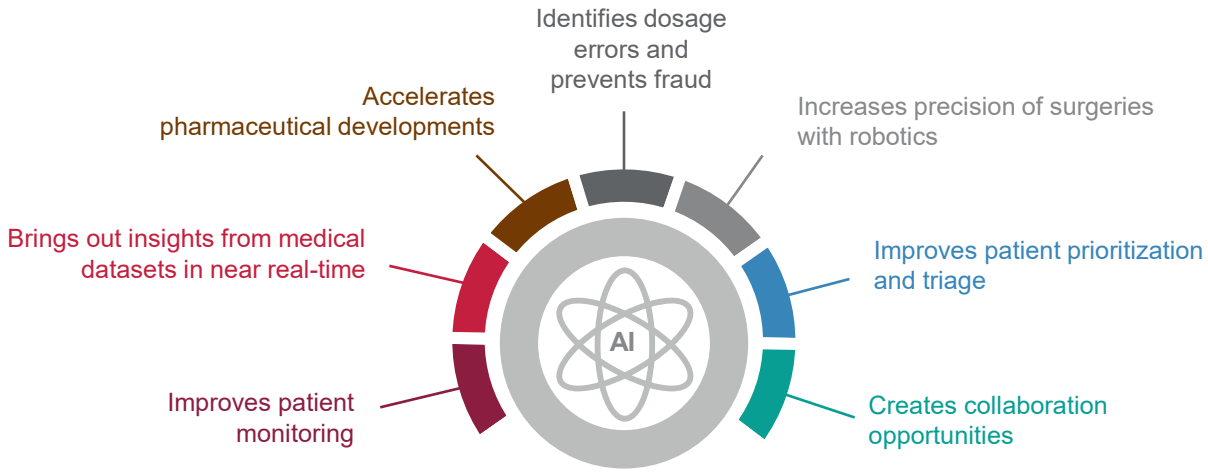
The examples below showcase diverse AI applications across various industries—highlighting both the profitability potential and the transformative impact on traditional practices.

Healthcare

AI is significantly enhancing drug discovery, personalized care, and diagnostics within the healthcare space. AI technologies are used to identify novel drug targets, design medications with specific properties, and match existing drugs to new indications. This accelerates the development timeline and reduces costs. Additionally, we see AI-driven systems optimizing hospital operations by predicting patient admissions and managing staff allocation, which results in improved resource utilization and reduced wait times. Furthermore, AI is being used for ambient listening, which allows the technology to identify key information during doctor-patient conversations and assist accordingly. It is also being explored in generating tailored treatment plans based on individual patient data.

In radiology and pathology, companies like GE Healthcare are utilizing AI technologies to analyze medical images and detect anomalies that may be missed by the human eye. This not only improves patient outcomes and leads to faster and more accurate diagnoses but also streamlines workflows, allowing radiologists to focus on more complex cases. Despite significant advancements, there is still a need for large, high-quality datasets to train deep learning models, which can be a challenge to obtain, particularly for rare diagnoses.

Figure 1: How AI benefits healthcare operations



Finance

Financial institutions are leveraging machine learning algorithms to detect fraudulent transactions in real-time, providing enhanced security for consumers. Firms are developing AI solutions that not only protect against fraud but also build customer trust. Furthermore, AI tools are revolutionizing risk assessment processes by analyzing vast amounts of data to evaluate creditworthiness and investment risks, enabling financial institutions to make more informed lending decisions. Companies that have a history of innovation in AI are likely to emerge as leaders in this space, gaining market share from competitors that lag behind.

Agriculture

Another sector to watch is agriculture, where companies like John Deere are leveraging AI to improve yields and reduce waste through precision agriculture. This data-driven approach allows farmers to optimize their crop and livestock management by analyzing soil data, weather predictions, and other relevant factors. AI technologies can assist in making informed decisions about when and what to plant, ensuring that resources are used efficiently. Productivity is greatly enhanced through the use of AI software, as drones can pinpoint areas requiring water or fertilizer, and new self-driving tractors are designed to address labor shortages. The integration of AI in agriculture presents numerous opportunities for growth and innovation, making this area of the industrials sector one to monitor for potential investment.

Sales and Marketing

The advertising industry is increasingly leveraging large data sets and AI technologies to enhance targeting and campaign effectiveness. Companies like Meta utilize rich data and proprietary AI models to create detailed profile graphs, enabling advertisers to better reach their audiences. Public advertisers are adopting AI-infused products that refine these profiles, while AI also facilitates automated content creation, allowing for the easy replication of successful campaigns. Platforms like GoDaddy and Wix generate multiple variants of previous campaigns, catering particularly to small and medium-sized businesses that may lack in-house resources.

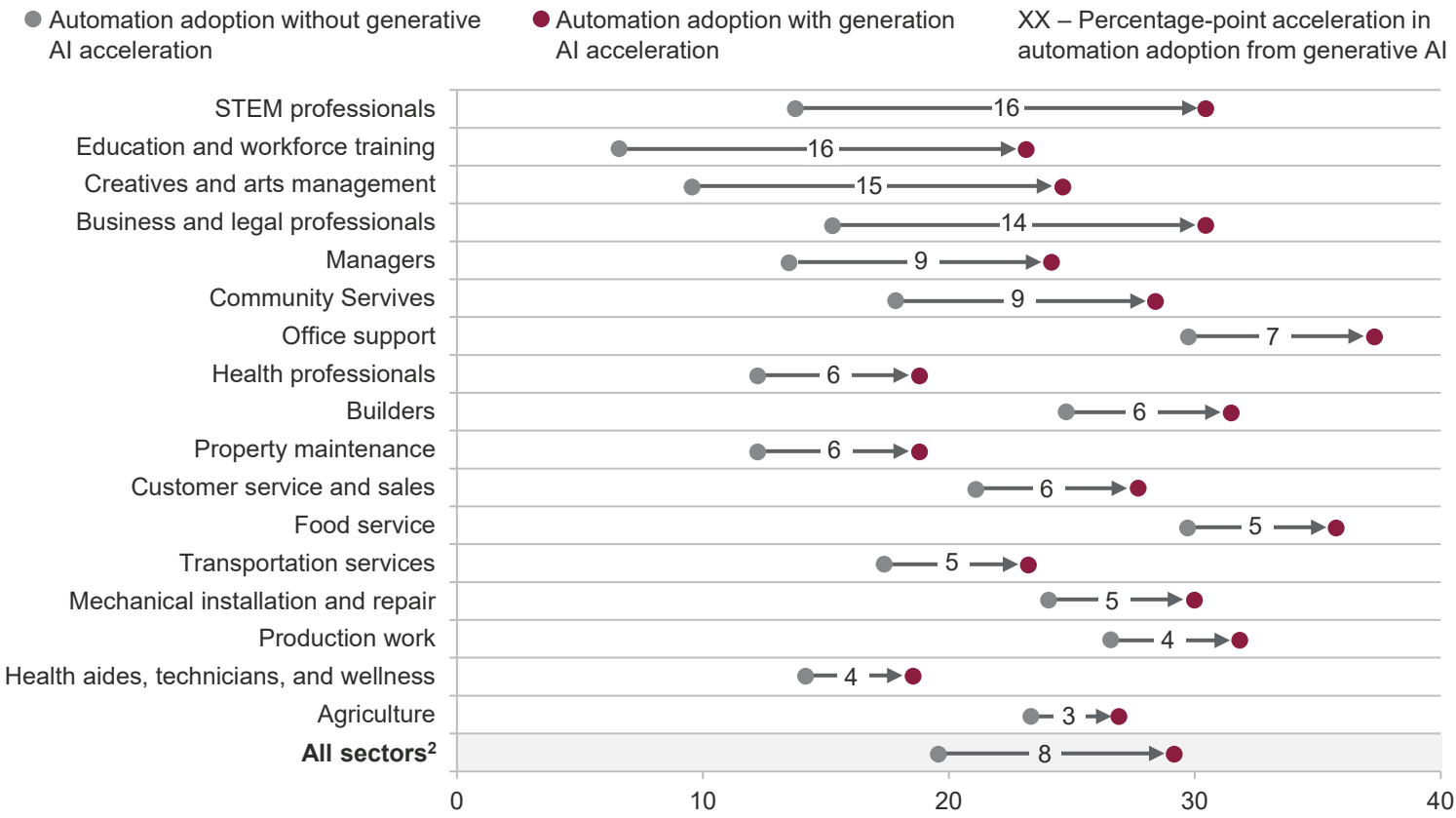
In sales and marketing, tools like Salesforce and HubSpot are transforming how companies engage with their enterprise customers. AI enhances the productivity of inside sales teams by automating personalized email creation tailored to prospects and existing customers. By integrating with a company's CRM database, AI generates relevant communications based on customer history and specific needs, allowing sales representatives to focus on refining content rather than starting from scratch. Overall, AI integration in advertising and sales is driving significant advancements in efficiency and effectiveness across these sectors.

Conclusion

As we navigate the complexities of AI, we must keep in mind that we are only scratching the surface of the full potential of this transformative technology. While short-term disruptions may introduce volatility, the promise of AI innovation remains compelling. By focusing on established players, prioritizing data infrastructure, and monitoring market dynamics, investors can position themselves to take advantage of the opportunities presented by this evolving landscape.

Figure 2: With generative AI, 30% of hours worked today could be automated by 2030[1]

Midpoint automation adoption by 2030 as a share of time spent on work activities, US, %



Staying informed about regulatory changes and industry trends is vital for making informed investment decisions along the way. However, we advise against a “try this at home” approach; the intricacies of emerging technologies require expert guidance. After all, in a world where technology is rapidly reshaping industries, the right insights can make all the difference in your investment journey.

For more information on investment opportunities and challenges within the artificial intelligence space, please contact a member of your CIBC Private Wealth team.

While many companies stand to benefit from AI tailwinds, not all are suitable investments for a given strategy. We take into account valuation, business composition and factors such as size and quality metrics when making investment decisions.

1 Source: O*NET; US Bureau of Labor Statistics; McKinsey Global Institute analysis. Midpoint automation adoption is the average of early and late automation adoption scenarios as referenced in *The economic potential of generative AI: The next productivity frontier*, McKinsey & Company, June 2023.
2. Totals are weighted by 2022 employment in each occupation.