WEEKLY STRATEGY

Perspectives

BMO | Wealth Management

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The Muddy Middle

"Your perspective will become your prison or your passport. It will either confine you to the way things are or launch you into the way things are meant to be."

– Steven Furtick, evangelical pastor, author, Grammy-winning songwriter

The Through Line: Angsting over the viability and durability of the AI trade (Again. Still.) has dominated the narrative in recent weeks. Can it last? Will newly elected U.S. federal and state policymakers clamp down on growth prospects? Will the industry disrupt debt markets with too many capital demands? Is it a bubble about to pop, echoing 1999's dotcom episode? Who's making money? Who isn't? Who's protecting cash flow? What current business lines will become obsolete? So many questions. So few clear answers. There is no going back, yet the path forward remains shrouded in mystery. Thus, we're stuck in the dreaded muddy middle. We outline some key touchstones that we're probing for clues about the future.

Recombobulation required

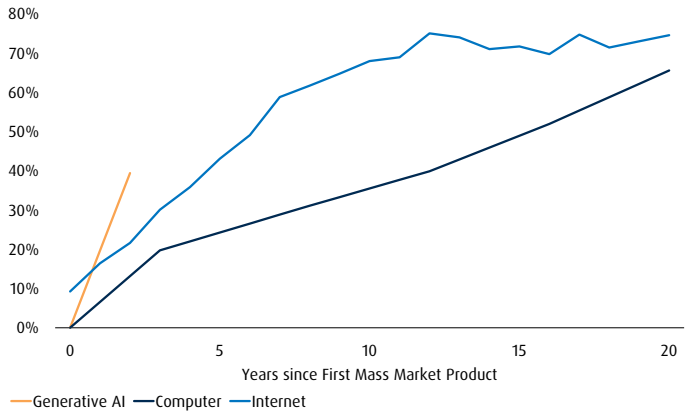
On a recent trip through Milwaukee's Mitchell International Airport, I was charmed to see a sign above the benches at the end of the TSA line reading "Recombobulation Area." It's a brilliantly simple idea: pause briefly, regroup and prepare for the next stage of the journey. On a more philosophical level, recombobulation – a playful word meaning to recover after a state of confusion –acknowledges the need to calmly put ourselves back together again. That's especially necessary after the fraught process of getting through a security checkpoint – shedding shoes, laptops, belts and the like. It can leave us frazzled and anxious. Reminds us of the emotions surrounding the AI trade at the moment. **A deep breath and a bit of perspective recombobulation would be helpful right about now.**

End-user demand is NOT an issue

So, let's level set *again*. **AI is here to stay – no matter what happens to the pace of data center buildout or how chip stocks trade this month.** End-user demand is definitely NOT a problem since it is ramping faster than any other technology in recent (perhaps human) history. Generative AI hit 40% penetration in barely a year, a feat that took PCs more than a decade to achieve (chart).

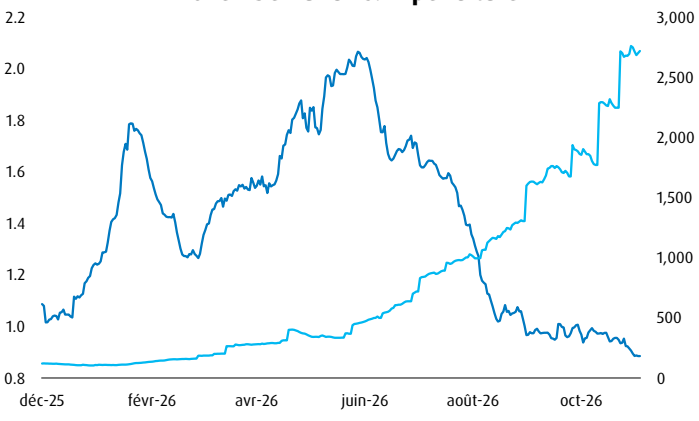
Similarly, the price of compute (measured in tokens) is declining quickly, helping propel (and/or fund) more use cases as companies and individuals become hooked on the ability to automate rote knowledge work and crunch through large, laborious data sets in a matter of minutes (chart). **Companies are simply NOT going to risk losing their competitive position to pause or withdraw their use of AI.**

Adoption Rate of Digital Technologies



Sources: St. Louis Federal Reserve (2024); 'Computer' introduction year assumes 1981 when IBM PC released, Current Population Survey (1984-2003); 'Internet' introduction year assumes 1995 when NSF decommissioned NSFNet and allowed the internet to carry commercial traffic, International Telecommunication Union (1995-2021); 'Generative AI' introduction year assumes 2022 when ChatGPT released, Real-Time Population Survey (2024).

Token Demand vs. Expenditure



Source: Bloomberg L.P. (2026), as of 11/3/2026

Satisfying demand IS an issue

While end-user demand isn't in question, many aspects of the ability to fulfill it are. For decades, electricity usage had been relatively stagnant, providing little reason to substantially upgrade or expand the electric grid's capacity. However, the nearly parabolic curve of demand that has erupted in the wake of agentic AI's introduction has changed that, necessitating rapid increases in the infrastructure required to support AI model training and use. Plant expansions, reshoring efforts and the shift to automated manufacturing (e.g., robots, autonomous pick-and-pack machines, forklifts) exacerbate the energy requirements.

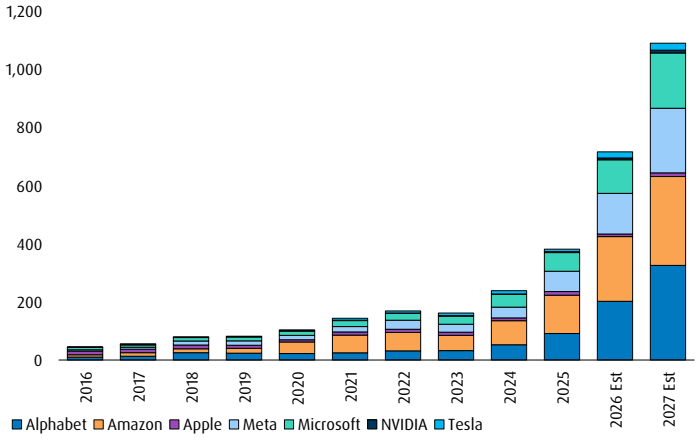
Data centers have been around for years (they're what powers the cloud after all). It has been a unique hurdle, however, to secure sufficient land and local regulatory approvals plus the materials, production machinery, components and memory/advanced processing chips required to build the type of facilities needed to train and operate complex AI models. Labor skilled enough to build them has also been in short supply.

The AI buildout is being primarily funded by the private sector (as were other innovations such as railroads and energy infrastructure). Industry players such as the large hyperscalers (Microsoft, Alphabet, Meta, Amazon, Oracle) and frontier model creators (e.g., OpenAI, Anthropic, xAI) are competing in an existential race to build relationships, market share and an ability to reliably service end markets.

Announced plans to build data centers have scaled quickly, though according to Bloomberg up to half may be delayed and/or have been rolled back.[i] While Wall/Bay Street often convert delays or issues into all-or-nothing thinking, it's more nuanced than that for the hyperscalers and model creators. **Not building compute capacity isn't an option,** so roadblocks in one area necessitate redirecting and rethinking and possibly moderating the pace. Despite obstacles, retrenchment is not likely.

Leveling of the torrid pace of data center build, particularly if it's an industry-wide issue, may actually help on several fronts. Shortages of core components like memory chips have spiked inflation that has spilled over to other parts of the economy. Intel, for example, saw its stock price decline nearly 30% on a single day last week when it announced its most recent quarter was negatively impacted by the high price of PCs that slowed consumer demand more than anticipated. A leveling of demand for such parts could lead to a decrease in upward price pressure and allow production of those components to catch up. An added benefit of reducing price pressure could filter through the broader economy, giving the U.S. Federal Reserve more wiggle room to watch and wait versus launching multiple rate hikes.

Mag7 Capital Expenditures ($B)



Data based on respective company's fiscal year. Source: Bloomberg L.P. (2026).

A few words on the midterms

When the first trickle of blue wave results from the U.S. midterm elections began surfacing Tuesday evening, futures markets turned sharply lower. The technology-laden E-Mini NASDAQ 100 (CME) Index,[ii] for example, showed declines of close to 2%. Traders were spooked by the building Democratic tide that was becoming evident – and most specifically in critical state races like Texas, New York and New Jersey where key data center initiatives were on the ballot. According to some reports, nearly half of the proposed data center projects are in states that flipped to politicians who campaigned on moratoriums or slowdowns in data center construction.[iii]

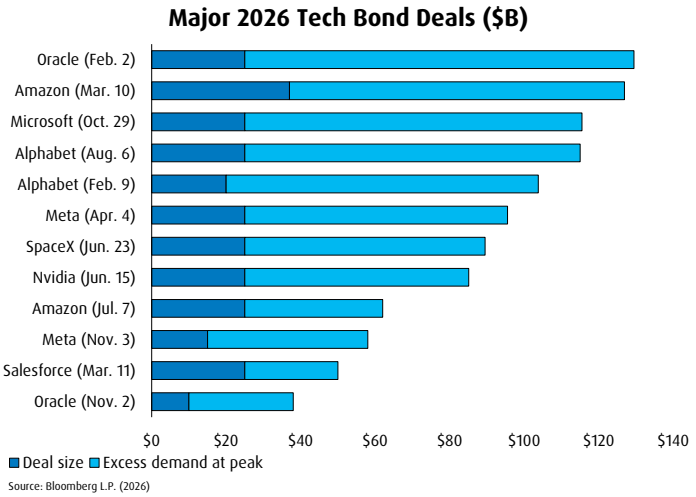
The Republican trifecta of the last two years has been quite favorable for equity markets. Investment and economic activity were supported by reduced regulation, relaxed oversight, encouragement of and tolerance for large-scale tie ups and favorable tax treatment for research and development, plus plant expansions hard coded into tax law. These attributes are readily apparent in recent strong GDP results, durable goods orders and productivity numbers. The labor market, too, has illustrated the health of the economy: the unemployment rate is lodged solidly in the low 4% range.

In classic fashion, markets had knee-jerk reactions to the initial election results, projecting that the Democrats would withdraw the equity punch bowl after their first week in office. However, any student of politics knows that **campaign promises and actual legislation are two very different things. While both the House and the Senate have flipped more decidedly blue than even the most optimistic projections, Washington's gears turn slowly**. It will undoubtedly take some time to select new leadership, form new affiliations/coalitions and take new actions. Then, too, any legislation will need to survive President Donald Trump's veto Sharpie. (Although Democrats won control of both the Senate and House, they are far short of the two-thirds majority of each chamber required to override a presidential veto.) **Realistically, a deliberative, well-crafted framework for both model oversight and data center issues at the federal level would be preferable to leaving a vacuum in which 50 states and hundreds of municipalities are free to craft their own.**

Capital markets are already tapping (not pumping) the breaks

How tech companies are funding the AI buildout has obviously become an investor obsession. In the beginning, the hyperscalers paid the compute/data center bills largely by using ample operating cash flows generated from existing businesses like cloud, search and advertising. Creators of frontier models (e.g., Anthropic PBC and OpenAI) were eagerly seeded by multiple rounds of venture capital funding.

As spend has increased, public and private debt and equity issuance has also been tapped. Interestingly, the debt offerings have been global, with bonds floated in Canadian dollars, euros, Swiss francs, British pounds sterling, and Japanese yen. Spreading the offerings into different currencies allows a broader pool of investors to absorb the large dollar amounts while providing companies the opportunity to secure the lower rates available in some non-U.S. markets. Initially, each offering was many times oversubscribed. Recent issues have still been oversubscribed, but at a lower level than earlier offerings – a hint that investors are becoming a bit more cautious and/or their investment allocations are nearing max limits (chart). In the later offerings, we've seen great differentiation in the yields investors are demanding, particularly for bonds with longer-dated maturities. To entice buyers, the more highly levered and/or cash-flow-negative issuers are having to pay higher yields.



Equity markets absorbed the largest initial public offering (IPO) on record for SpaceX earlier this year. They are prepping right now to handle another – Anthropic's, which is reportedly coming before the U.S. Thanksgiving holiday. The company's offering circular was out last week. It also released updated Q3 numbers this week. While the spend to secure compute capacity is large, the company continues to scale its revenues quickly and already sits on a cash pile of over $100 billion – surprising many.

On a related note, OpenAI initiated another pre-public funding round in the last couple weeks yet wound up reducing the size by more than half. Additionally, the funding occurred at a lower valuation that the prior round. This is a bit atypical, hinting that equity investors may also be nearing capacity to absorb more AI-centric investment, particularly given recent volatility. Several IPOs for chip, hyperscaler and AI-adjacent companies have been pulled recently. **In short, the signs of discriminating investor behavior are plentiful and healthy.**

This is NOT dotcom part II

We are frequently asked to explain how the current AI investment trade differs from the dotcom era that eventually morphed into the bubble that burst in 2001-2002. Having lived and worked through that period, we can readily point to the differences (and very few similarities):

- Today's infrastructure is largely in place (at least in part, even if not large enough to satisfy rapidly scaling demand). In 1995 – 2000, the routers, switches, fiber and other wiring to facilitate internet communication had to be laid, while companies had to convert the dumb terminals prevalent from prior years to PCs. Keep in mind this period happened nearly a decade before the first iPhone was released.
- Companies then had few (or more likely no) revenues and definitely no earnings. Valuations were based on clicks and eyeballs captured.
- **Today's companies are seasoned entities with established businesses generating double-digit margins, double-digit growth and tens of billions in cash flow each quarter to help fund their AI endeavors.** Will some of these businesses need to be rewritten for the age of AI? Undoubtedly, in much the same way that we are all recalibrating our day-to-day activities to take advantage of the new tech. Still, these companies are proven survivors and adapters in a gruelling industry where continual change is the only constant.
- When the dotcom bubble burst in 2001-02, companies did not stop using the internet. Their internet infrastructure and strategies were already built and in flight, a response to the need to stay competitive and innovative in areas such as digital communication, e-commerce, supply chain coordination and global networking. **In five years, no one will be talking about playing an AI stock – just like today we don't talk about buying an internet company.**

Glimmers of hope amidst the murk

Tech valuations already seem to encapsulate many of the unknowns since price-to-earnings ratios for most are well below where they started the year. Market participation by the "other 493" (the other components of the S&P 500 Index that aren't one of the Mag 7 stocks) has started to broaden. In fact, earnings increases this quarter are expected to be stronger for the 493 than for the Mag 7. Just this week, for example, most of the major hotel chains and many pharmaceutical companies reported earnings that were stronger than expected while outlining constructive outlooks for the remainder of the year and into 2027. Last week, it was 3M, GE, Coca-Cola and Hasbro.

Businesses are scaling agentic AI quickly, realizing time savings and boosts to individual productivity even if it's tough to measure directly, given the multitude of other things (tariffs, inflation, rising healthcare costs) that are impacting their margins. Interestingly, in response to the uptick in activity, companies that had laid people off (claiming they were AI-inspired rationalizations) are finding they need to hire them back to manage the armies of agents and the increase in client-facing activities the technology provides.

Considering all the terrestrial pushback against data centers, a number of companies are fast forwarding their capabilities to put data centers in space. Of course, it's untested and early days, but figuring out how to put them on satellites might solve at least some of the (real estate and other) problems on Earth.

Implications for investors

Definitive answers are hard to come by in what is by rights still a nascent industry. The scramble to build capacity, and develop end markets, solid client relationships and durable business models is fraught. **Volatility in the last few months has reset valuations, suggesting many of the darkest fears may already be priced in – but the long-term opportunity less so.** A healthy broadening of market participation seems to be underway, at the same time filtering down to smaller companies. We maintain our belief that a solidly performing economy, employed consumers and a continued steady pace of AI and infrastructure buildout should benefit investors who have long time horizons. However, volatility will likely stay high, particularly as newly elected politicians take their seats.

Curious about the "recombobulation area" at Milwaukee's international airport, I discovered it's famously unique. While a formal recognition of the need for recombobulation may be rare, it's a reminder for investors that it's wise to occasionally take a break and regain perspective. Especially necessary at this particular muddy middle moment in time.

Next week in North America

A much quieter week for economic data – although earnings season rolls on in both countries. Investors will be waiting for and wondering about progress on Anthropic's IPO (targeted for debut in the U.S. just before Thanksgiving). Will recent volatility in tech stocks delay it?

Monday 11/9:	**U.S.** Wholesale trade sales and inventories | **Canada** Bloomberg Nanos confidence
Tuesday 11/10:	**U.S.** NFIB Small business optimism, CPI | **Canada** none scheduled
Wednesday 11/11:	**U.S.** Mortgage applications | **Canada** none scheduled
Thursday 11/12:	**U.S.** Weekly jobless claims, existing home sales, Federal budget balance | **Canada** Building permits
Friday 11/13:	**U.S.** PPI | **Canada** Manufacturing sales and wholesale sales

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Benchmark data does not reflect actual investment performance but reflects benchmark results of the underlying indices referenced. You cannot invest directly in an index.

[i] US Data Center Boom Relies on Hard-to-Find Electrical Equipment - Bloomberg

[ii] The E-mini Nasdaq 100 futures contract (NQ) is a cash-settled equity index futures contract traded on CME Globex. Each NQ contract represents $20 × Nasdaq 100 Index, with a minimum tick of $5.00 per tick (0.25 index points). **Nasdaq-100 Index,** is a broad-based, modified capitalization-weighted index that tracks 100 large-cap companies that span major industry groups.

[iii] Trump's midterm drubbing demonstrates the power of data center opponents | Reuters