On the Minds of Investors

How are we evaluating the AI boom?

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Meera Pandit
Global Market Strategist

> **The reasons why AI is a compelling investment opportunity persist, but how we invest in AI has evolved.**

The AI trade has stumbled out of the gate to start 2026 compared to recent years. In fact, concerns about AI have been brewing since last year, with several distinct pullbacks in tech stocks over the course of 2025. However, while the AI trade may be more volatile in 2026, there is little reason to doubt the broader AI boom, supported by earnings, valuations, adoption and strong balance sheets.

As we EVALuate the AI boom, several dynamics underscore the directional momentum in this theme:

(E) **Earnings:** Tech profits have been spectacular since the launch of ChatGPT in November 2022. The Magnificent 7 have enjoyed double-digit profit growth since early 2023, and earnings surprises have exceeded 10% in recent quarters, compared to the market average of 7.5% over the same period. Last quarter, hyperscaler cloud revenues grew 27% y/y on average, evidence that AI is being monetized. As we look ahead, Mag 7 earnings have been revised up by 6.9% for 2026 since the start of 4Q25, while the S&P 493 have been revised lower by 0.4%. The past, present and future of AI profitability is bright.

(V) **Valuations:** Together, the Mag 7 sport a P/E of 28.6x, not much higher than their collective P/E in spring of 2023. While that is expensive, it is by no means extreme, and investors have gotten what they've paid for given valuations have barely budged while profits have soared. It is also dramatically less than info tech's peak valuation of nearly 70x during the internet boom.

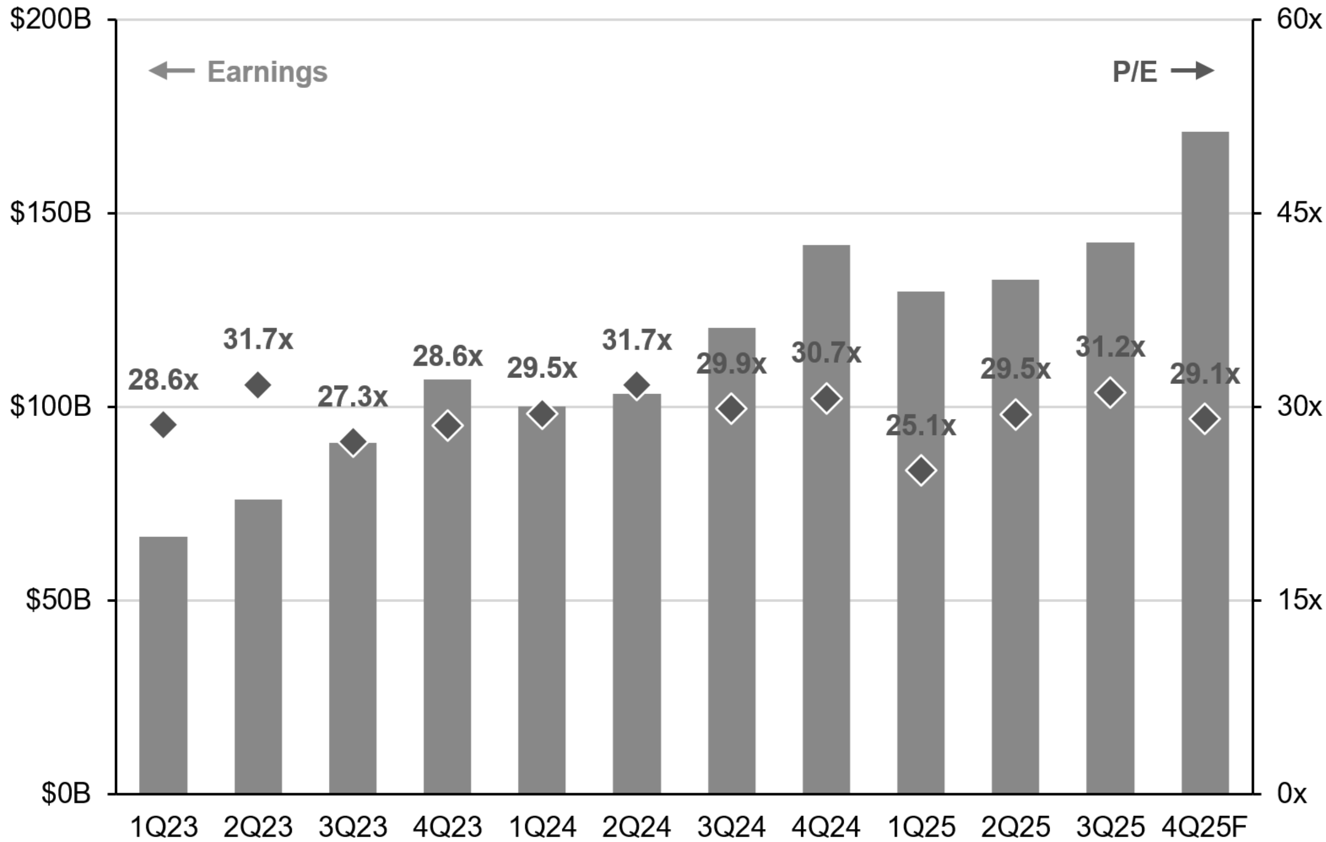
(A) **Adoption:** In order to justify the massive hyperscaler capex spend, demand must also be robust. As we show on page 24 of the Guide to the Markets, 17% of U.S. businesses now report AI adoption, and even more (45%) pay for AI subscriptions. Many of the leading tech CEOs note "insatiable" demand, citing the bigger risk is underinvesting, not overinvesting.

(L) **Leverage:** Excessive leverage followed by a credit crunch has caused many booms to go bust. However, while the hyperscalers have increasingly been tapping the bond markets and private funding vehicles, they do have the cash to support their investments but are opting for a more sensible capital structure. Despite taking on more debt, hyperscaler net leverage is 0.9x compared to 2.6x for the average investment grade issuer.

The reasons why AI is a compelling investment opportunity persist, but how we invest in AI has evolved. The Mag 7, down 1% so far in 2026, are no longer synonymous with AI. Instead, the theme has broadened out to other AI innovators within tech, as well as AI enablers in sectors like industrials, utilities and materials, all of which boasted double-digit earnings growth in the most recent quarter. Although we do not believe AI is a bubble, it does not preclude one from forming, which is why we don't want to chase the herd but rather employ thoughtful stock selection and diversification.

Mag 7 earnings have soared while its P/E has barely budged

Earnings and forward P/E ratio



Source: Factset, J.P. Morgan Asset Management. Forward P/E ratio is as of respective quarter-end. Data are as of January 14, 2026.

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