



## CIO Insights

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# Narrowing of the AI Valuation Gap: China Vs. US

*Sustainability of AI Business Model Should Warrant More Market Attention*

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# Sustainability and Visibility Drive Terminal Valuation Multiples

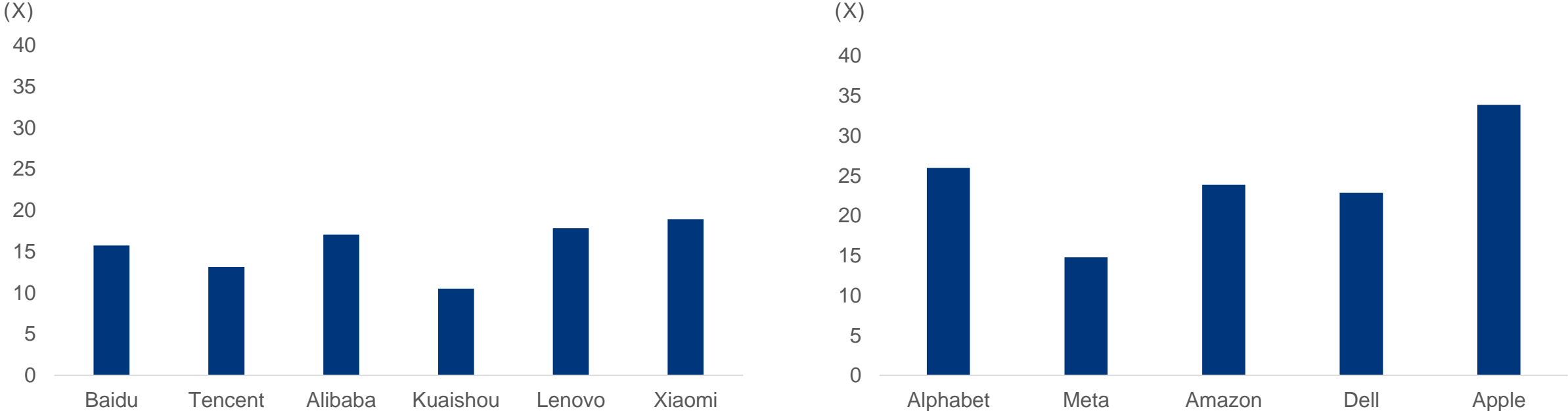
## This Serves as a Long-Term Re-Rating Potential for the China AI Sector

- The conventional equity research framework evaluates AI through a narrow, hardware-centric lens — penalizing Chinese AI assets for semiconductor supply-chain constraints while awarding a growth premium to U.S. mega-caps based on unconstrained compute access. This framework fundamentally misprices the long-term sustainability of both business models.
- In classical DCF valuation theory, a terminal multiple is not determined solely by near-term growth. It is equally tied to earnings **sustainability and forward operational visibility**. The higher the political, institutional, and social predictability of a business model, the lower its cost of equity — and the higher its justified terminal multiple.
- We argue that the ultimate constraint on AI monetization will not be hardware throughput, GPUs, or LLMs. The true cap is institutional and societal. When evaluated against the 1,000-year historical super-cycle of Superpower national decay, **the US AI deployment model represents an unstable, hyper-disruptive optimization of capital that violates the domestic social contract. China's AI ecosystem, engineered for B2B industrial integration and state-directed structural alignment from inception**, achieves vast regulatory visibility and earnings sustainability.

# US Tech/AI Stocks Are 53% More Expensive Than China's

The Sustainability of the Revenue Model for the Chinese AI Is Yet to Be Reflected

12M Forward PE



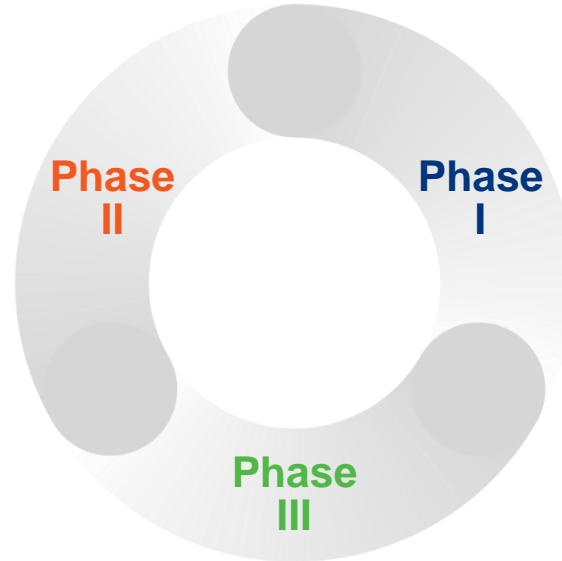
Source: Bloomberg, KGI

# AI Technologies Will Disrupt the Current Economic Balance

**Together With Inflation and Sovereign Debt Issues, the Discount Rate for the US Has to Rise**

## **Inflation as Soft-Default (Indirect Taxation)**

When nominal debts exceed real productive output, sovereigns turn to monetary debasement. Expanding the monetary base dilutes purchasing power, executing a soft-default that benefits capital owners while imposing a hidden regressive tax on the working class through eroding real purchasing power.



## **The Productivity-Wage Trade-off**

As technologies mature, they shift from labor-complementary multipliers to highly centralized, capital-intensive substitutes. Corporate monopolies capture 100% of marginal productivity gains while real wages of the mass population stagnate, creating a "K-shaped" economy that fractures the social contract.

## **The Sovereign Debt Trap & Gridlock**

When debt service outpaces nominal GDP growth, the state must persistently borrow to service legacy interest liabilities. Acute political polarization leads to legislative gridlock; the fiscal authority captures the monetary authority, forcing continuous monetization until a flight from the reserve currency occurs.

# Technological Advancement Always Drives Social Disruption

## 1,000 Years of History Showing How a Superpower Decline

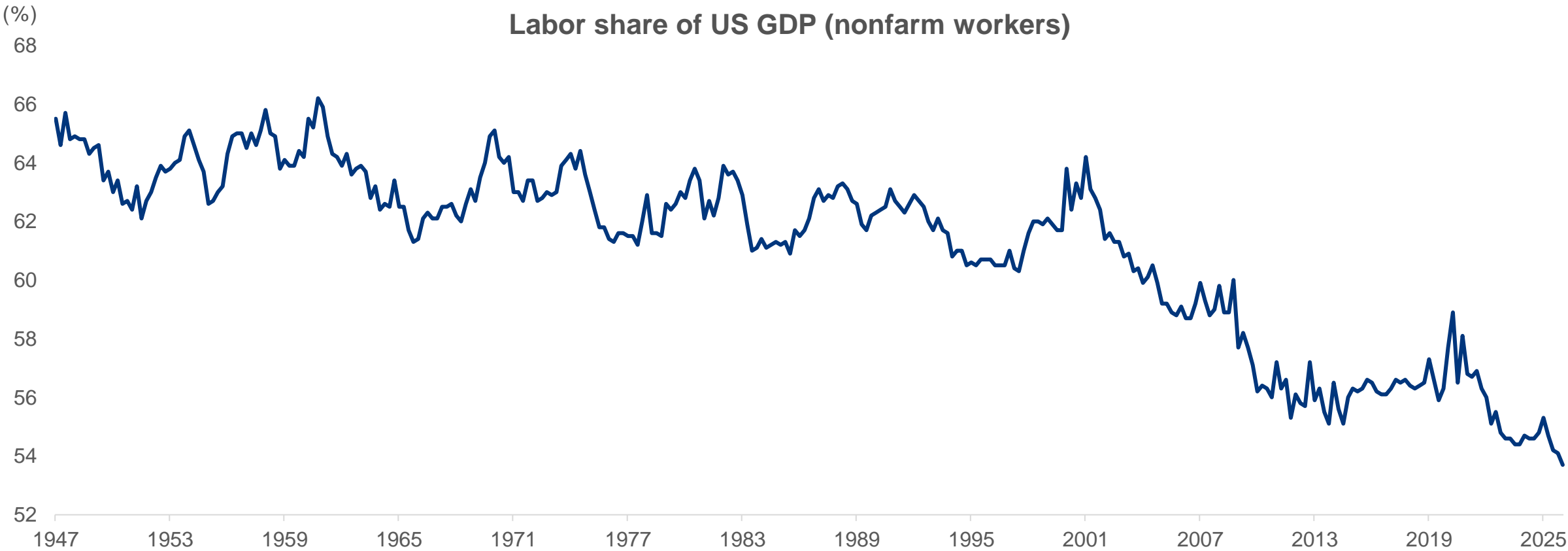
Epoch / Hegemon	Peak Era & Debt Profile	Phase 1: The Tech-Wage Wedge	Phase 2: Inflation as Indirect Tax	Phase 3: Sovereign Debt Trap & End State
<b>Song Dynasty (1050 to 1279)</b>	Peak: ~1100: Debt funded via unbacked paper issuance.	Industrial metallurgy and hydraulic mechanization concentrate wealth in state-sanctioned elite cartels.	Over-printing of Jiaozi and Huizi notes to fund frontier defense results in hyperinflation and hollowing out of the middle class.	Political gridlock between Wang Anshi's Reformists and Conservatives; total dependence on monetary debasement; collapse of currency.
<b>Spanish Empire (1556 to 1659)</b>	Peak: ~1580: Multiple sovereign defaults (1557, 1575, 1596).	Transatlantic shipping and mercury silver extraction enrich crown monopolies; domestic manufacturing and labor base hollowed out.	Flux of silver drives the "Price Revolution." Deficit spending on global wars soft-defaults on state debt while crushing real wages.	The Cortes falls into gridlock over aristocratic tax exemptions; crown debases copper currency (Vellón); total loss of international credit.
<b>Dutch Republic (1688 to 1795)</b>	Peak: ~1720: Provincial debts exceed 200% of tax revenues.	Industrial sawmills and Fluyt shipping scale corporate VOC fortunes; financialization shifts capital from labor to global credit markets.	Excess capital inflows drive asset inflation, operating as an indirect tax on domestic workers facing structural wage stagnation.	Fractured polarization between Orangists and Patriotten; structural fiscal gridlock; Bank of Amsterdam currency run and collapse.
<b>British Empire (1870 to 1947)</b>	Peak: 1910: Debt-to-GDP peaks at over 240% post-WWII.	Industrial mechanization and global supply infrastructure decouple corporate productivity from urban labor power.	Suspension of Sterling gold convertibility, monetary expansion soft-defaults on wartime debts via structural inflation.	Institutional gridlock between Labour and Conservative parties; Bank of England monetization; Suez Crisis triggers capital flight from Sterling.
<b>United States (1971 to 2026)</b>	Peak: 1999: National debt exceeds \$34T; Debt-to-GDP > 120%.	Digital architecture, software automation, and Generative AI maximize corporate capital margins; labor power is systemically decoupled.	Prolonged quantitative easing and M2 expansion trigger sticky, structural inflation, eroding working-class purchasing power.	Bipartisan congressional gridlock; permanent reliance on Federal Reserve debt backstopping; emerging global de-dollarization.

Source: KGI

# Return on Capital Has Been Increasing – +Ve for Corporates

Labor Has Been Losing Share of the GDP. Unfortunately, the Labor Is the Majority

US Workers Get Smallest Slice of Economic Pie on Record  
In 3Q 2025, so-called labor share fell to lowest since data begin in 1940s



Source: Bureau of Labor Statistics, KGI

# Mounting Views From Politicians on Regulating AI Companies

- The US government may take stakes in AI companies (through donation from the AI companies). The US president told reporters on 5 June that he discussed a deal with major AI labs in recent days in which the federal government “essentially becomes a partner with the companies”. Big Tech groups such as Anthropic, OpenAI and xAI would further discuss the proposal at the White House, Trump said.
- While Trump may see the potential stake holdings as a way to make money, the next administration may see the **government’s stakes in the AI companies as a tool to implement the social agenda.**
- At the same time, **Senator Bernie Sanders said he would propose a bill to impose a one-off, 50% tax on AI labs’ stock** and use the proceeds to create a US sovereign wealth fund. Sanders said the move “would guarantee that the trillions created by AI are used to improve the lives of all of us.”

## Aggressive Labor Protections

Punitive taxation on automated workflows (e.g., "robot taxes") and mandatory human-in-the-loop legislative guardrails to protect displaced workers.

## Antitrust and Legal Liability

Heightened regulatory targeting of tech monopolies, coupled with complex copyright and data-provenance litigation that will persistently disrupt corporate earnings visibility.

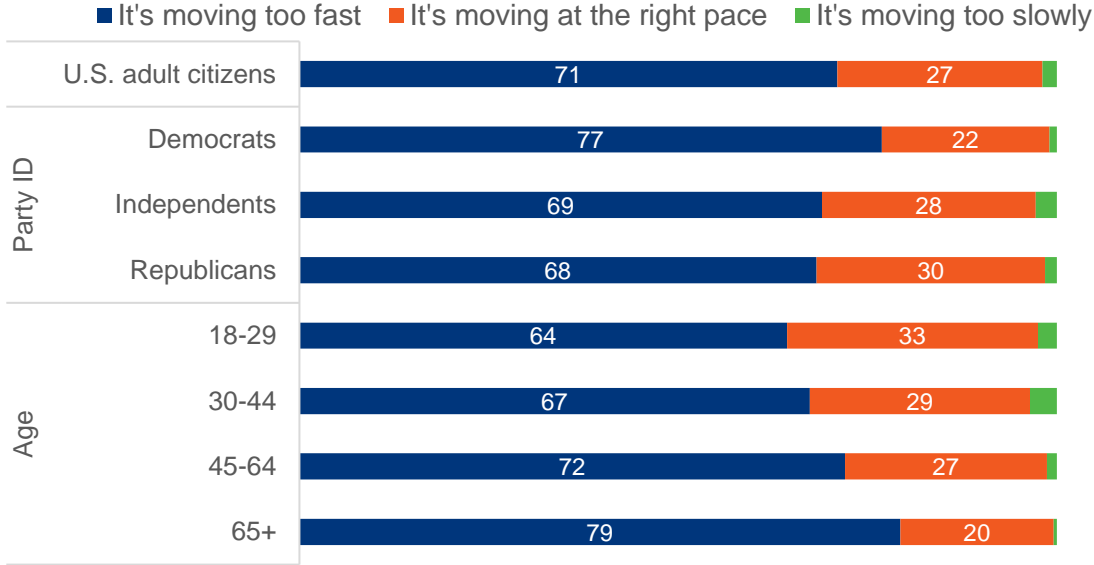
## Social Instability

Widespread populist unrest demanding universal basic income (UBI) frameworks funded directly by the corporate tech sector to preserve social cohesion.

# Polls Show Increasing Concerns From the Public on AI

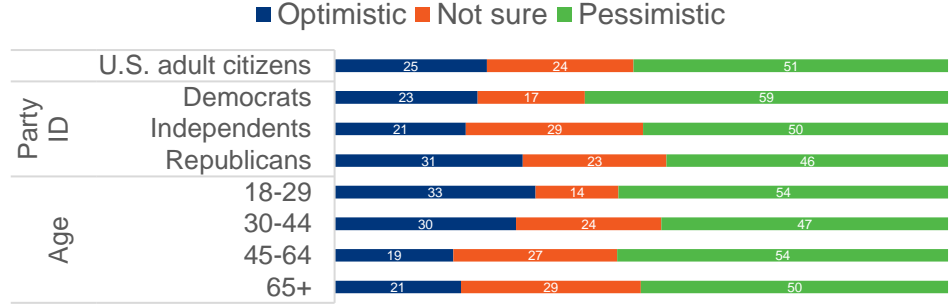
- 53% of the 4,531 respondents to the survey conducted by Reuters from June 3 through 8, were concerned that their household will lose their job because of artificial intelligence (AI).
- According to an Economist/YouGov Poll, 63% of Americans believe AI will lead to a decrease in the number of available jobs, while only 7% believe it will create more jobs.

Most Americans say AI is moving **too fast**  
 How do you feel about the pace at which AI is advancing? (%)

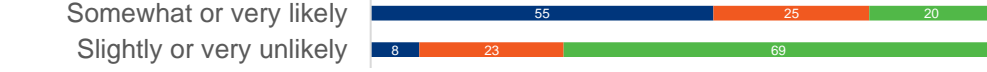


Twice as many Americans feel **pessimistic** about AI's long-term effect on society than feel **optimistic** about it

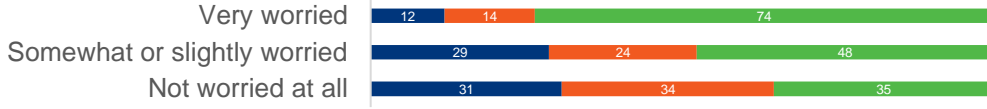
Overall, are you optimistic or pessimistic about the long-term impact of AI on society? (%)



### View of likelihood AI will create economic gains benefiting everyone



### Worry about AI replacing jobs



Source: YouGov, KGI

# AI Development With a China Characteristic

## China AI Features Top-Down and Government Participation From Inception

- The sovereign does not act as a retrospective regulator imposing limits on mature technology; rather, it functions as a foundational architect, defining the structural vectors of AI deployment beforehand.
- AI is not a standalone revenue generator. AI is being integrated into the existing business ecosystem. The strategic imperative of Chinese AI is the systematic enhancement of existing industrial, manufacturing, and enterprise ecosystems. Rather than deploying AI as a disruptive, margin-grabbing substitute for human labor, Chinese enterprises utilize AI to drive systemic efficiencies and create new commercial opportunities within traditional sectors.
- Because this development vector is structural rather than purely substitutionary, the negative externalities imposed on the domestic labor market are structurally minimized. AI operates as a deflationary efficiency multiplier that supports, rather than shatters, the domestic social contract.

Strategic Dimension	US AI Model	China AI Model
Government Role	Retrospective Regulator	Foundational Architect
Primary Deployment Vector	Labor Substitution (B2C)	Industrial Augmentation (B2B)
Labor Market Impact	Highly Disruptive	Structurally Minimized
Social Contract Alignment	Fracturing	Reinforced
Regulatory Visibility	Low / Unpredictable	High / Embedded in Plan
Earnings Sustainability	Structurally Capped	Structurally Supported

# Investment Strategies

- **China AI/tech sector is a low beta but strong alpha play.** The so-called “AI revenue” line in the P&L is not so visible. Instead, we are likely to see improvement in revenue and operating margin as a result of AI deployment enhancing the efficiency of existing businesses.
- **Application over Technology.** Much of the market focus on AI since several years back has been on the technology itself. This is a completely understandable behavior when a technology is at its growing phase, similar to the emergence of internet during the late 90’s. In the mid-1990s, Netscape was the definitive catalyst that brought the internet out of academic and tech-nerd obscurity and into the mainstream public consciousness. But the company is nowhere to be seen anywhere now.
- **Companies making best use of the technology win.** On the other, the companies which make the best use of the technology wins. Facebook (Meta), Amazon, Microsoft and Google.....etc. Apple does not invest as much capex as its peers into AI development. This capex war is not a everyone’s game. From Apple’s perspective, it will use whatever cost-efficient AI model on the street as it knows that its best talent continue to be on application development.
- Therefore, we believe companies with the largest ecosystem in China (such as the dominance of iPhone OS) will turn out to be the long-term beneficiary of the AI race.

# Top Picks Focus On the Downstream of the AI Supply Chain

## Hardware and LLM Model Companies Which We Believe Are Relatively More Expensive

Name	Mkt Cap (bn HKD)	Price	Revenue growth	EPS Growth	Forward P/E	Forward P/S
Baidu	313	115.2	7.7	18.0	13.4	1.9
Tencent	4,206	461.0	9.4	11.0	11.9	4.0
Alibaba	2,094	109.0	11.4	54.0	12.4	1.5
Kuaishou	201	46.3	6.9	13.6	9.3	1.1
Xiaomi	682	26.3	16.3	29.8	14.6	1.0

### FY2027 Estimate

Name	est. EBIT Margin	Est. ROE	FCF (bn HKD)	Est. FCF Yield	Volatility 90 Days
Baidu	11.5	5.8	14.8	4.7	45.8
Tencent	33.1	18.6	234.7	5.6	38.0
Alibaba	10.9	10.4	-23.2	-1.1	45.6
Kuaishou	12.0	16.3	10.9	5.4	50.0
Xiaomi	7.5	12.6	43.2	6.3	40.5

Source: Bloomberg, KGI

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