CIO Insights

AI Trade: From Euphoria to Entry Point

10 July 2026

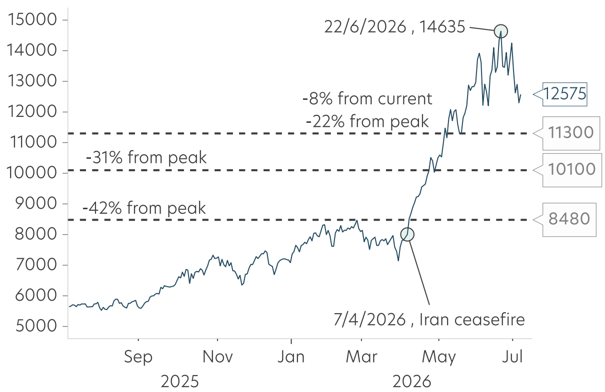
Key Takeaways:

- Correction underway: Equities could face a 5%-7% index level correction, with AI infrastructure winners vulnerable after crowded positioning and stretched expectations.
- Rotation emerging: Leadership may shift from semis and AI infrastructure into underowned healthcare, biotech and low-volatility strategies as investors seek resilience.
- Investment conclusion: Use volatility to accumulate preferred AI beneficiaries: accelerators, memory, photonics, power generation, cooling and thermal management.
- Key risks: Iran-driven oil spike, renewed inflation fears, hawkish Fed rhetoric and hyperscaler capex cuts could pressure tech and AI infrastructure sentiment.

The market is finally doing what it was supposed to do. In our 2H market outlook (Resilience over Perfection) at the start of June, we argued that equities were vulnerable to a correction after a powerful, increasingly narrow AI-led rally. That correction now appears to be underway. Investors should not confuse this with the end of the AI cycle. This looks more like a necessary air pocket, with index-level downside potentially extending to the 5-7% range before the market finds firmer footing.

The more important move is not just the correction itself, but the rotation beneath the surface.

Figure 1: SOX Index

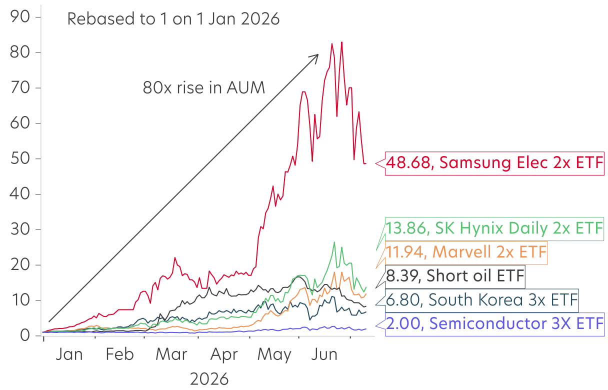


Source: Bloomberg, UOB Private Bank

For most of the past year, the market has rewarded one trade above all others: AI infrastructure. Semiconductors, power equipment, data-centre enablers and AI-adjacent cyclicals became the default hiding place for growth investors, momentum funds and, eventually, retail leverage. That trade is now being tested. It does not mean the structural story is broken. It means positioning became crowded, expectations became heroic, and too many latecomers started treating volatility as optional.

The SOX Index (**Fig 1**) is the cleanest expression of this tension. The semiconductor complex remains in corrective mode, with key supports sitting roughly 8% and 18% below current levels. A shallow test would be healthy. A deeper test would be uncomfortable, but not abnormal given the magnitude of the prior run. The sector has earned a breather. Trees do not grow to the sky, even if they are cooled by liquid immersion systems and powered by nuclear small modular reactors.

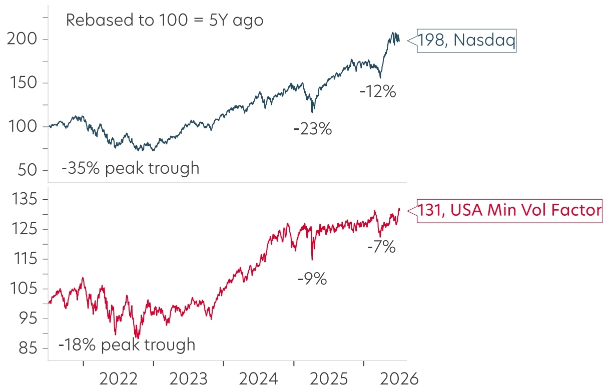
Figure 2: Change in AUM of leveraged ETFs



Source: Bloomberg, UOB Private Bank

The second pressure point is leverage (**Fig 2**). Assets under management in leveraged exchange-traded funds remain too elevated for comfort. These products are useful as short-term trading tools, but they become dangerous when retail investors use them as conviction substitutes. A proper correction usually requires some forced humility. In plain English, the leveraged ETF complex likely needs to deflate further before the market can clear out weak hands and rebuild on stronger foundations.

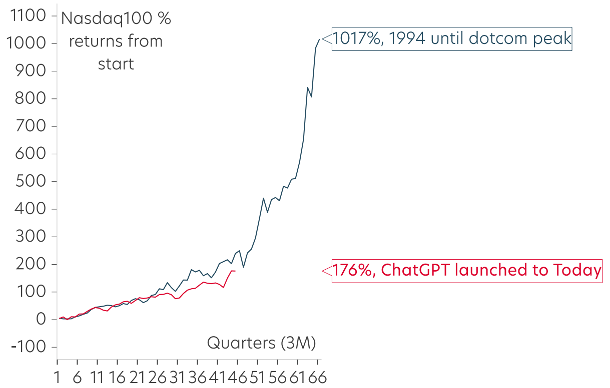
Figure 3: Low volatility strategies



Source: Bloomberg, UOB Private Bank

This is why low-volatility strategies (**Fig 3**) deserve attention. When markets move from "buy anything with an AI ticker" to "please explain your cashflows", investors rediscover the appeal of lower-beta, steadier compounders. Low-vol strategies are not designed to win the cocktail-party performance contest during melt-ups. Their job is to reduce drawdowns, dampen portfolio swings and keep investors invested when the market starts behaving like a badly caffeinated teenager. Today, they offer a useful hedge against index weakness, while benefiting from rotation into defensive areas.

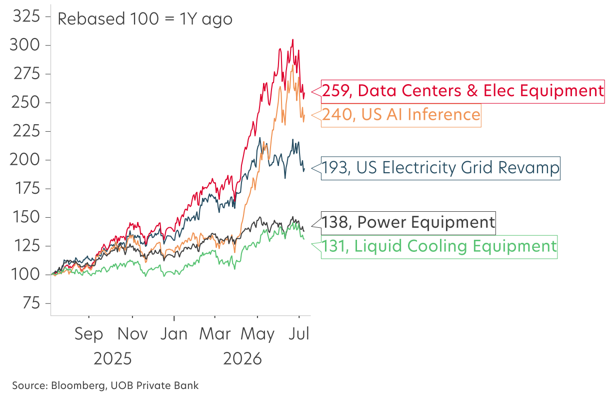
Figure 4: AI today vs dotcom in 1990s



Source: Bloomberg, UOB Private Bank

This is where the current episode differs from a simple bearish reversal (**Fig 4**). The comparison between returns since ChatGPT's launch in November 2022 and the dotcom boom is instructive. If this cycle continues to rhyme with the late-1990s playbook, the market may still have one final upward leg before a final top forms. That is not a forecast to chase indiscriminately. It is a reminder that secular manias rarely end neatly after the first correction. They usually shake, rotate, recover, broaden, and only then become truly dangerous.

Figure 5: AI infrastructure stack performance



Source: Bloomberg, UOB Private Bank

Investment conclusion

For investors who missed the first leg of the AI trade, this volatility should be treated as an opportunity, not a punishment. The key is to avoid buying yesterday's winners blindly. We prefer using weakness to accumulate exposure in the parts of the AI supply chain where demand is still supported by hard infrastructure needs: accelerators such as GPUs, XPUs and CPUs; memory makers; photonics; power generation; and cooling and thermal management.

At the same time, capital is likely to rotate into areas neglected during the AI feeding frenzy. Healthcare, biotech and low-volatility strategies look particularly interesting. They offer a combination of underownership, defensive characteristics and valuation support. They are not as glamorous as AI chips, but glamour is rarely what investors want during a positioning washout.

The message is simple. This correction can go further, and investors should respect that. But it is more likely a reset than a regime break. Use the volatility to upgrade portfolios, broaden exposure and buy structural AI beneficiaries with a better margin of safety. The tourists are being shaken out. Long-term investors should be getting their shopping lists ready.

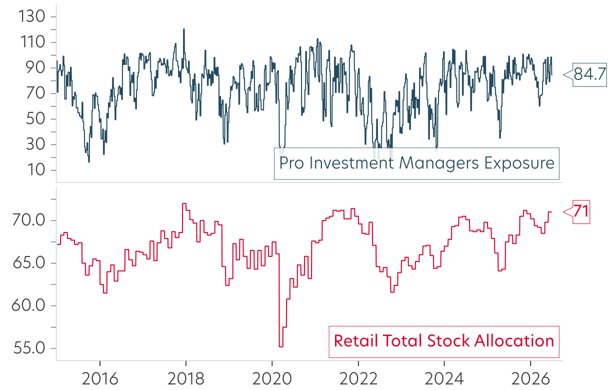
Figure 6: SOXX ETF (1 year)

Source: Bloomberg, UOB Private Bank

4 key risks to watch

There are, however, macro risks investors should watch closely. The first is a renewed flare-up in the Middle East, particularly involving Iran, which could send oil back above USD100 per barrel. That is not our base case. The US administration still has a strong incentive to keep energy prices contained and pursue a deal before the midterm elections. But markets do not need the base case to change before they start pricing tail risk. A few missile headlines and a spike in crude would be enough to unsettle an equity market already sitting on stretched positioning (**Fig 7**).

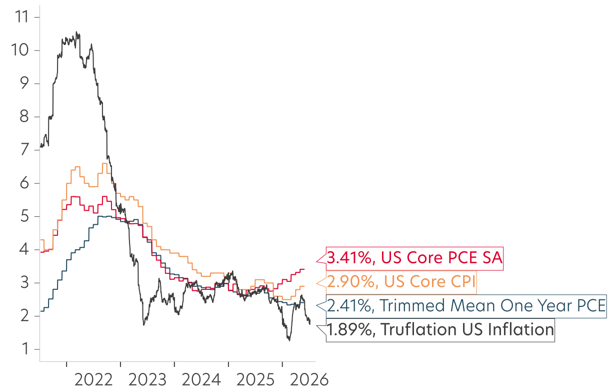
Figure 7: Investor indicative positioning



Source: Bloomberg, UOB Private Bank

The second risk follows directly from the first. What investors had previously dismissed as a one-off inflation bump could start to look stickier if energy prices rise again. That would complicate the comfortable disinflation narrative that has supported risk assets. However, higher frequency data (**Fig 8** Truflation vs PCE & CPI) gives us comfort that price spikes are under control. The third risk is the Fed's reaction function. If inflation concerns return, Fed communication could turn more hawkish, even without actual rate hikes. That would be enough to temper market multiples, especially for long-duration equities. Translation: technology stocks, which have benefited from falling discount-rate expectations, would be first in the firing line.

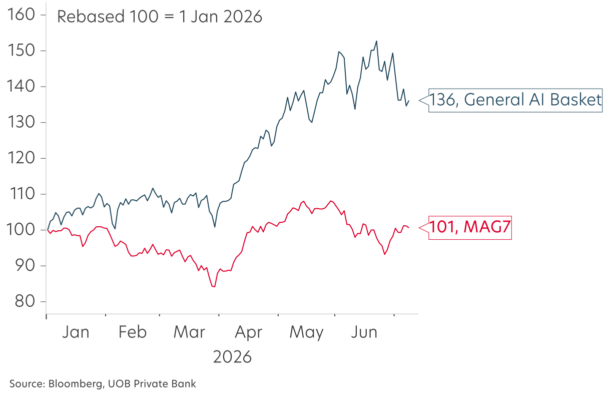
Figure 8: Inflation data



Source: Bloomberg, UOB Private Bank

The final risk is more specific to AI. The market has assumed that hyperscaler capital expenditure will remain aggressive because nobody wants to lose the AI land grab. That assumption is powerful, but not bulletproof. If one major hyperscaler signals a capex pullback, or even a shift towards stricter return-on-investment discipline, sentiment across the AI infrastructure stack could be hit quickly. The biggest damage would likely fall on the prior winners: chips, networking, power, cooling and other picks-and-shovels beneficiaries that have outperformed on the belief that AI spending is effectively immune to budget gravity.

Figure 9: MAG7 vs Broad AI trade



Source: Bloomberg, UOB Private Bank

Ironically, that kind of disappointment could mark the start of a rotation back into the Magnificent Seven and the hyperscalers themselves (**Fig 9**). If investors conclude that management teams are refocusing on returns rather than racing blindly for market share, the market may reward the platforms over the suppliers. In other words, a capex scare could hurt the AI infrastructure trade, but help the companies writing the cheques. The narrative would shift from "who sells the most shovels?" to "who actually monetises the gold rush?"

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