Swing state

Themes and opportunities 2025

welcome to brighter

Foreword

Since 2020, a series of significant shocks to the global economy — the Covid-19 pandemic, escalation of the conflicts in Ukraine and the Middle East, resultant inflation, and the vertical adoption curve of generative AI that has driven US exceptionalism — have dominated investor focus. The knock-on effects of this series of events continue to reshape our world and have challenged conventional portfolio thinking, in particular the benefits of diversification. These impacts warrant in-depth analysis and consideration as the slower-burning repercussions are felt across portfolios. Equally, as the 'acute' and reactive phase of these events ends, we believe it is time for investors to lengthen their perspective to consider other longer-term risks and opportunities.

The theme of this year's report, "Swing state", reflects look-forward views from an investment environment characterized by several potential swing dynamics:

- Market concentration levels have swung to a secular high.
- Rates have begun a downswing as inflation appears to have been brought under control.
- Government debt burdens in developed economies are at strained levels. A new administration in the White House, won on a pledge of tax cuts, raises questions about whether debt will continue to swing higher.
- Emissions continue to rise despite progress in cleaner technologies, due in part to increased energy demand.

While some of these swing dynamics remain in full flow, it is prudent to consider common-sense laws of financial gravity — what swings up must eventually swing down. The 'tiger' or 'miracle' sector in any time period eventually rotates into another, inflation responses eventually work (and have largely already done so), and serious environmental problems are eventually regulated.

Through the course of this paper, we outline some of the key themes and opportunities we see over the next five years and beyond. To make sense of this evolving landscape, we categorize our themes as follows:

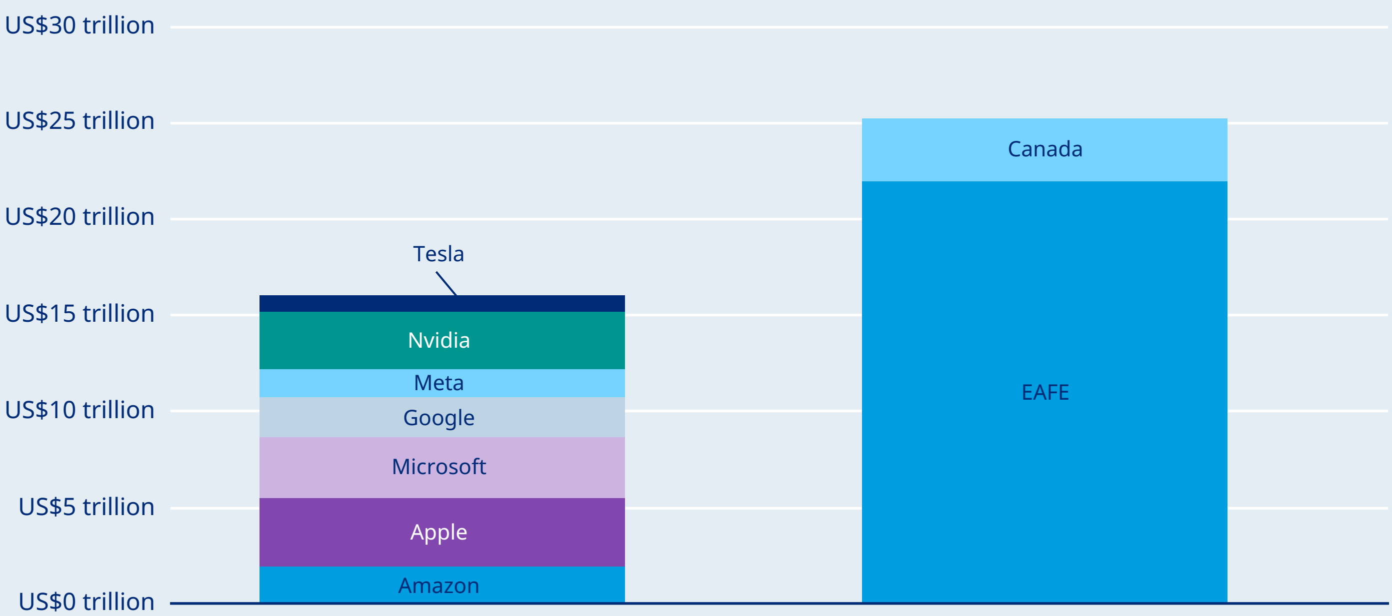
- **Regime changes** — One-off, enduring shifts in conditions.
- **Super-cycles** — Classic economic super-cycles (debt and commodity cycles) and the super-cycle of socioeconomic paradigms (Kondratieff waves or Strauss-Howe saecula).
- **Megatrends** — Multi-decade transitions gradually reshaping the world.

1. Regime change

The highs and lows of benchmarks

In recent times, equity markets have become increasingly concentrated in a few large stocks which have disproportionately influenced overall market movements. Large swings in single stock valuations can lead to material portfolio losses, exemplified in the stock market turmoil seen in September 2024.[1]

Figure 1. Mega cap technology stocks looming large in indices



Source: Bloomberg. Data as at 30 September 2024. MSCI EAFE and MSCI Canada used.

Markets have also become generally more concentrated in US equities, due in part to strong cash-flow driven growth in mega cap tech companies. High expectations for future earnings make it more challenging for US equities to deliver on the past decade's combination of increasing profit margins and valuations plus low volatility.[2]

As market concentration increases, diversification can appear to be "diworsifying," but it is important not to give up on diversification. Concentration risk creates inefficiencies as a focus on dominant stocks may cause investors to overlook broader market trends and emerging opportunities. What goes up must come down, and as the global economy rotates at some point to a different paradigm (for example, shifting to focus on resources or consumption), investors should be prepared to potentially benefit from diversification as concentration unwinds.

Our view is that portfolios should remain diversified into areas that have underperformed in recent years, such as developed ex-US equities, value or emerging markets.

In the context of a divergent multipolar world, emerging market (EM) equity indices exhibit stronger exposure to revenues coming from some of the fastest-growing market economies in the world and therefore warrant maintaining a strategic allocation at around market-cap weighting. Investors should be aware of the return erosion that can come from "selling low."

In a deconcentration phase of the market, active management is favored, further supporting an allocation toward alpha-seeking strategies, particularly diversified hedge funds.

Options to consider

- **Don't give up on diversification:**
  - Ensure the portfolio is diversified into areas that have underperformed in recent years, such as developed ex-US equities, value or EM exposures.
- **Consider increasing risk budget for active management:**
  - An unwind in concentration is not guaranteed, but active management will likely be rewarded when/if it occurs.
  - Employ hedge funds to capitalize on the alpha opportunities.
- **Review equity structure to evaluate unintended risk:**
  - Evaluate whether a completion portfolio would make sense to remove unintended risk.
- **Ensure that performance monitoring provides sufficient context and attribution:**
  - A portfolio may be underperforming a benchmark but still performing as expected in the prevailing market conditions.

State of rates

The effects of rising interest rates can take time to play out across the real economy, and we are only beginning to experience the full impact of the recent increases. Although rates are expected to decline in the near term, they are unlikely to revert to the ultra-low levels seen in the decade following the global financial crisis (GFC).

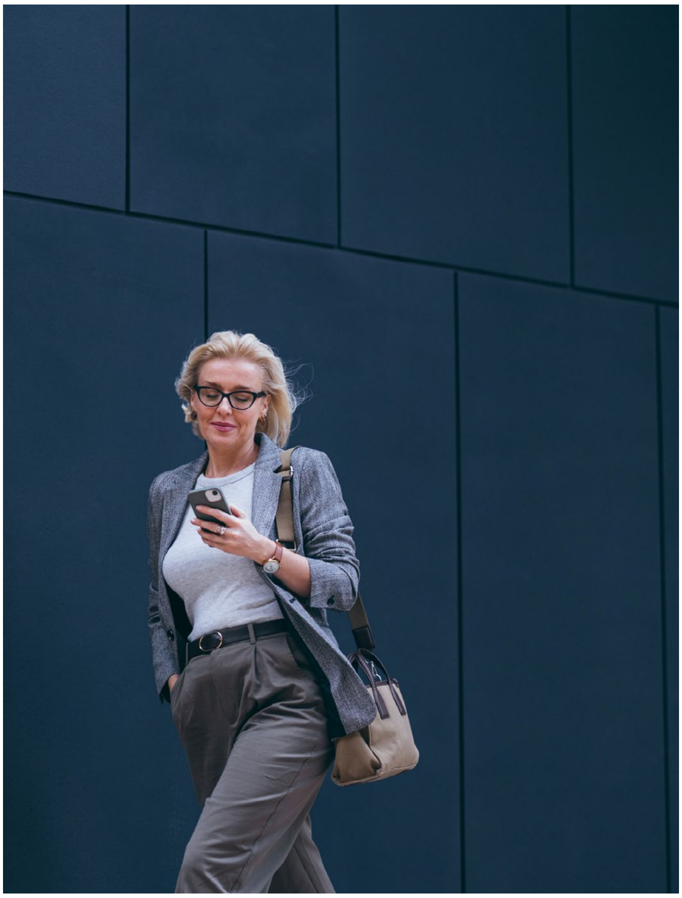
During that time, central banks pushed yields to historical lows, meaning investors who wanted to maintain overall returns from fixed income portfolios had to take on greater credit risk, extending maturities and accepting more illiquidity. As a result, asset classes such as private debt, securitized credit and sub-investment-grade loans experienced significant growth. The search for yield also spilled over into alternative asset classes, including infrastructure and real estate. We continue to be supportive of investment in private markets, but investors can consider whether their risk levels remain appropriate in the context of the opportunity set available today.

In a higher-interest-rate environment, investors can employ flexible strategies that capitalize on opportunities from across the risk spectrum; for example, by investing in high-quality government securities while also strategically allocating a portion to high-yield and private debt. By focusing on these two ends of the ratings spectrum, investors can potentially enhance returns and manage risk more effectively while avoiding the less-favorable medium-risk assets that may not offer adequate compensation.

Despite the increased attraction of core fixed income assets, private debt remains an attractive asset class. We believe investors should be cautious of crowded areas but can instead focus on deals that require thinking outside the box. Instead, they should focus on sectors with inherent structural advantages, including asset-backed and structured strategies, where we continue to see strong opportunities.

Options to consider

- **Draw from the full spectrum of fixed income opportunities to tailor portfolios to your needs:**
  - Higher rates offer choice, but beware of historically tight spreads.
- **Employ flexible, dynamic strategies to capitalize on an evolving opportunity set:**
  - For instance, exposure via a multi-asset credit portfolio offers diversification across areas such as EM debt and loans and provides flexibility for the manager to be more opportunistic.
- **Private debt remains attractive:**
  - For investors with a liquidity budget, private debt strategies continue to offer relatively attractive yields.
  - However, employ flexible mandates to reduce exposure to crowded areas; asset-backed and structured strategies, along with rated debt, can offer regulated investors efficient capital treatment.



Private markets de-siloed

In recent years, private markets have increased in size and become a mainstay of portfolio construction. Private market programs that adopt a holistic (de-siloed) approach may more effectively capture the full breadth of available opportunities. Lines between asset classes are increasingly blurred, particularly in areas such as data centers and the energy transition, along with waste management and wastewater treatment.

Figure 2. Potential benefits of a holistic cross-asset-class private market strategy design

Private equity ← **Private debt** → **Real assets**

Increased collaboration
GPs are fostering collaboration across investment teams and sectors, leading to more integrated strategies.

Data sharing
Enhanced data sharing and technology enable better insights and decision-making across siloes.

Cross-asset opportunities
Opportunities that span asset classes (e.g., private equity, real assets) can enhance returns and diversify risk.

Holistic approaches
These approaches embody a shift toward holistic strategies that consider multiple factors and asset classes rather than isolating them.

Liquidity spectrum
Integrating public and private markets into strategy design breaks down the liquid and illiquid bucket siloes.

Enhanced innovation
Innovative investment solutions are created by combining expertise from different areas.

Improved risk management
A more integrated approach enhances risk management via a broader view of market dynamics and potential risks.

The challenging exit environment in private markets, particularly in private equity, has spurred innovative fund structures even as existing vehicles that provide limited partners with liquidity have gained popularity. The rise of semiliquid funds, secondaries and continuation vehicles reflects investor demand for liquidity solutions.

Global secondary transaction volumes, in particular, have grown significantly as the market matures, increasing more than 10% per year over the past decade.[3] Secondaries offer unique benefits, such as accelerated capital deployment, potentially avoiding the dip in the J curve and allowing for tailored investment solutions that seek to enhance portfolio diversification.

General-partner-led transactions now account for around half of secondary market volumes (57% in H1 2024).[4] Increasingly, general partners (GPs) are looking to hold on to their most compelling "trophy" assets for longer, aiming to capitalize on the growth and expansion potential of these companies.

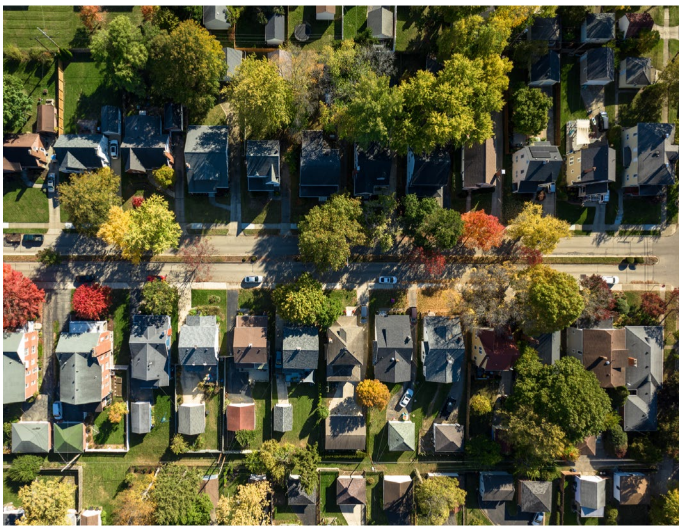
Despite the notable growth in secondaries, annual secondary transaction volumes still account for a small fraction of overall private market AUM, making this segment particularly attractive.

For sophisticated investors, co-investing in prime private market assets with quality GPs presents an opportunity. These investments carry more risk but provide significant benefits: experienced limited partners (LPs) with strong GP networks that can capitalize on selectivity and favorable terms; lower fees; accelerated capital deployment to mitigate J-curve effects; and opportunities from current market dislocations.

Real estate has struggled in recent periods, but it is approaching the tail of its most recent correction. This provides historically attractive entry pricing for most assets. Given the heterogeneous characteristics and imperfect information of the asset class — different regions offer highly differentiated opportunity sets — global real estate offers many compelling opportunities with strong absolute-return prospects. Sector allocation and stock selection are the most important factors determining outperformance. For investors with a higher risk appetite, there is potential to achieve outsized returns from market dislocations.

Options to consider

- **Private market programs should be developed holistically, spanning underlying asset classes:**
  - Exposures should recognize opportunities to create solutions that cross asset classes, particularly in structural trends, where private market time horizons are more aligned than those of public markets. The lines between asset classes may be blurred; for example, the rise of generative AI and digitalization in general has led to the creation of assets like hyperscale data centers which have both infrastructure and real estate-like characteristics.
  - Incorporating allocations to secondaries and capitalizing on co-investment opportunities may improve investor outcomes.
- **Global real estate today offers a broad suite of opportunities with compelling absolute-return prospects:**
  - Real estate has struggled in recent periods but now provides historically attractive entry pricing.
  - Given its heterogeneous nature, sector and stock selection are crucial factors driving performance.



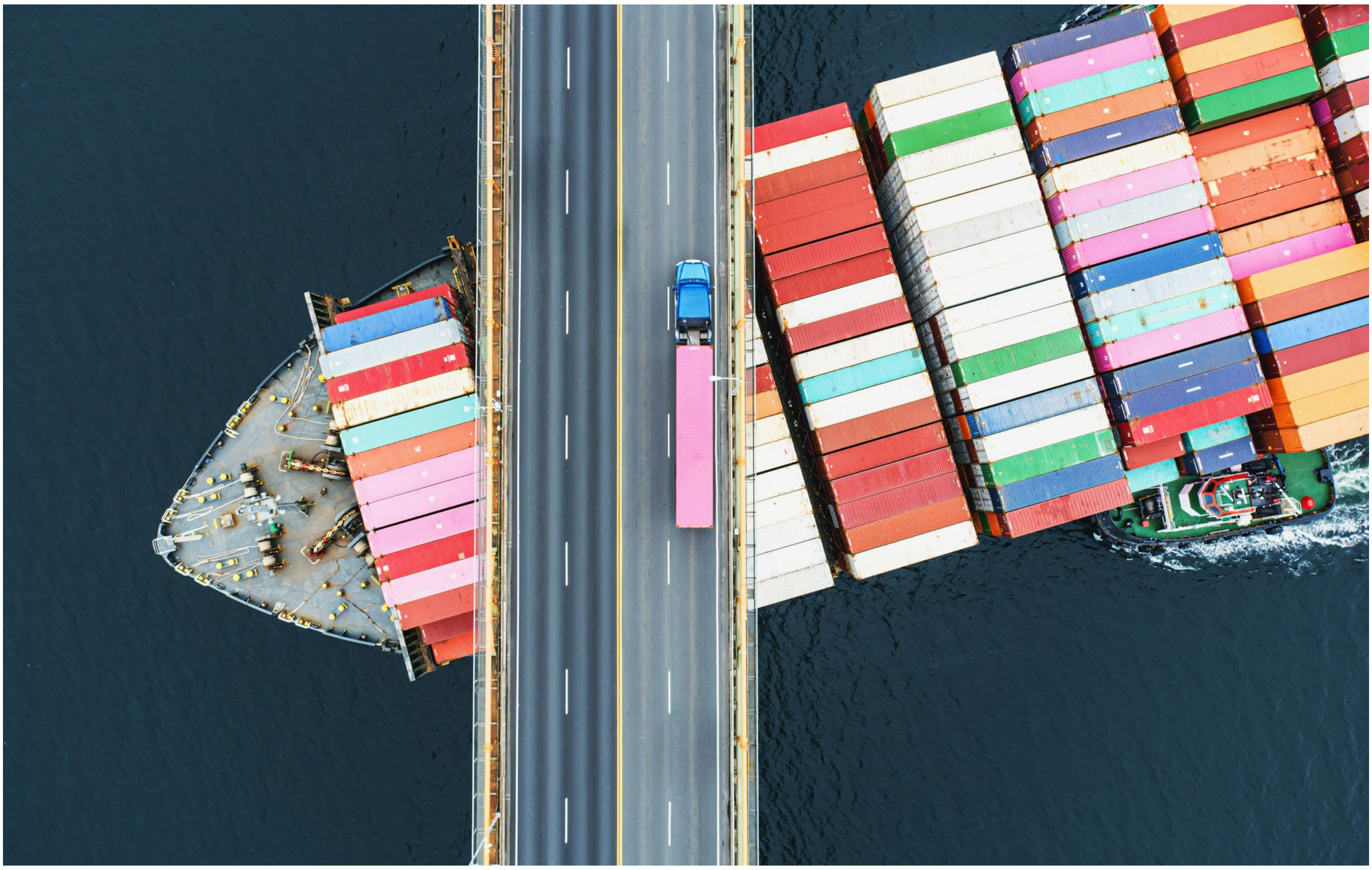
2. Supercycles

The security of everything

Geopolitical tensions can have profound and far-reaching consequences for the global economy and financial markets. Recent events have intensified focus on all aspects of security: energy, resources, supply-chain fragility, supply-side inflation shocks, cyber risk and the potential for debt weaponization.

The systemic impacts of energy shocks and supply-chain disruptions triggered by the pandemic and then exacerbated by Russia's invasion of Ukraine — causing countries to reevaluate their commodity sourcing[5] — serve as examples of the amplifying effect that geopolitical tensions can have on already complex risks.

Energy security and power generation, in particular, will remain prominent challenges for the many nations in which the energy transition will accelerate the electrification of the economy. From the rise of electric vehicles and the AI-driven digital infrastructure boom to the move away from gas-fired appliances, accelerated electrification will bend the demand curve for electricity in the coming years. At the same time, rapidly expanding renewable energy programs increase the proportion of "homegrown" power for most countries, thereby increasing energy security, provided that power generation is matched with storage capacity and grid buildout.



Elsewhere, competition between the US and China is leading to trade tensions, particularly around dual-use technologies. Although we do not believe the world is deglobalizing, we do believe it is fracturing into blocs.[6] The realignment of trading blocs and resultant supply-and-demand shocks should play out over a long timeframe with material uncertainty. The proliferation of protectionist trade policies, for example, demonstrates this global realignment process in action. Since 2020, countries have implemented nearly 150 new trade policies targeting clean technology, compared to 40 in the previous five years.[7]

The realignment of supply chains is both a risk — for supply-side inflation — and an alpha opportunity; for example, by investing in logistics or strategically important companies, such as those associated with critical minerals. In an increasingly multipolar world, EM strategies provide diversification via more direct exposure to EM revenues.[8] Active management is preferred to capitalize on alpha opportunities and also for reasons of risk mitigation. Dynamism is needed to respond quickly to developing sovereign risk given that country risk is a much larger factor in emerging markets than it is in developed markets.

In an increasingly factionalized world, currency movements can have a material impact on investment returns. Whether this is beneficial or detrimental to risk-adjusted returns depends on market conditions as well as an investor's circumstances and, critically, their domicile. Investors with a globally diversified portfolio understand that a decision not to hedge currency exposure is not a passive decision.

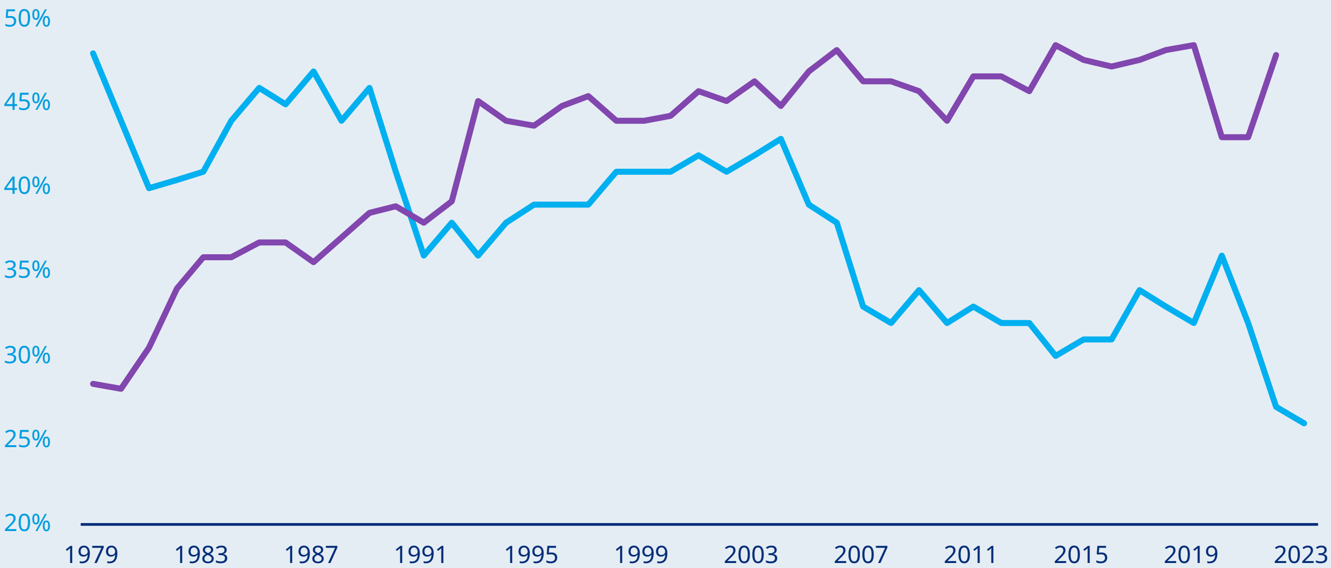
Options to consider

- **Keep energy transition allocations ahead of demand:**
  - Allocations to renewable power — including grid, storage and "next gen" assets — should stay ahead of the demand trajectory.
  - Companies mining or recycling critical minerals should benefit from structural demand as well as any reversion to value.
- **Develop a tailored currency policy.**
- **Investors averse to short-term inflation shocks should incorporate an allocation to commodity futures:**
  - Inflation resilience for the long term may be achieved through equities and private real assets.
- **Develop robust cybersecurity programs:**
  - Continue to update them with advances in technology.
- **Consider strategically important companies:**
  - A small universe of (private and public) funds targeting security-linked companies is emerging.

Balancing the economy

While Wall Street can take some comfort in inflation's deceleration, it is cold comfort for people on Main Street who are left with cost-of-living increases. Overall economic growth remains robust, but it has come with distributional problems, creating a disconnect between economic indicators and the realities of everyday living conditions. This disparity is contributing to rising public distrust in institutions. In advanced economies, a key feature of the social contract — that each generation is likely to earn more than their parents — has disappeared.[9] Wealth accumulation also presents a challenge as an unprecedented intergenerational wealth transfer from the baby boom generation is expected to buttress unequal outcomes for the next generation.

Figure 3. Social indicators weakening



Percentage of people with a great deal or quite a lot of confidence in major institutions (lefthand axis)
GINI US Dispersion of Income (0=perfect income equality, 100=perfect inequality) (righthand axis)

Source: Gallup and FRED.

The gap between economic growth and social well-being presents a unique opportunity for targeted investment. Strategic investments that focus on addressing social progress, such as affordable housing, healthcare infrastructure, food transition and cost-of-living solutions, offer the opportunity to make a significant impact and have the potential to provide attractive financial returns.

Sustainability index products can struggle to keep pace with emerging themes, such as nature, and the breadth of ESG concerns, such as social harm and loss of privacy with social media companies. Although many indices linked to environmental, social and governance (ESG) factors exclude industries such as heavy greenhouse gas emitters, weapons manufacturers and tobacco companies, they have not been as responsive to other risks. Many tech companies, for example, have come under scrutiny for their role in spreading misinformation, yet they remain mainstays of ESG-driven portfolios.

If progress is not made in addressing distributional problems and the cost of living, it is possible that populist political movements will continue to gain ground. It is important for investors to consider scenarios that include the real-world economic outcomes of rising populism, such as increased public debt, restrictive trade policies and lower equity returns.[10]

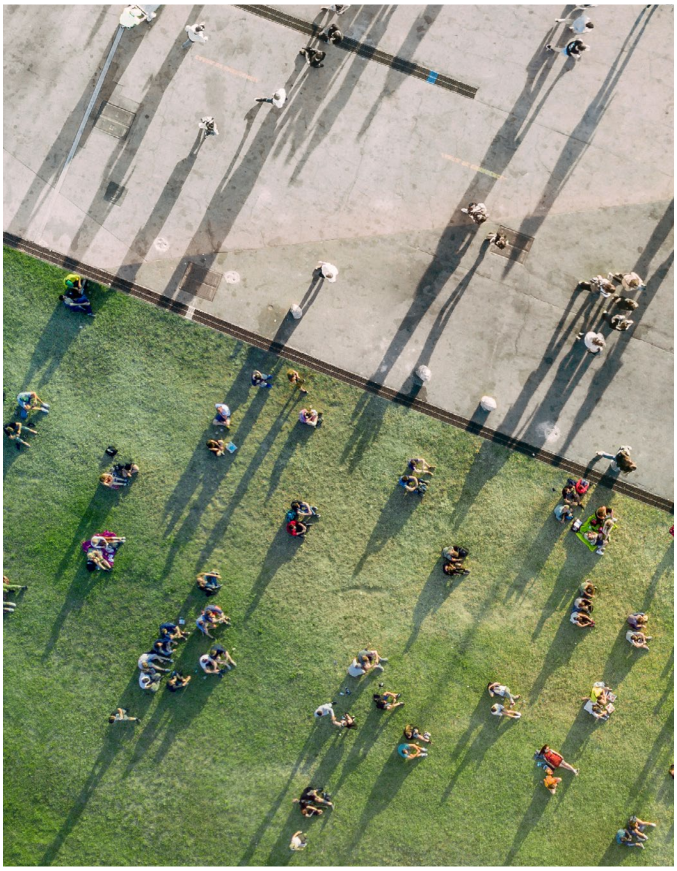
The government debt cycle in developed countries, particularly the US, has contributed to the buildup of imbalances and tension, with concerns that the annual burden of debt, now roughly equivalent to defense spending, will slow growth in the US economy. Debt levels may increase further from here under an administration promising individual and corporate tax cuts.

As public debt levels scale new heights in the US, it is worth considering the position of the purchasers of US government debt. Japan remains a natural purchaser due to a significant yield pickup over domestic issuance and fears of yen weakness. It is worth noting that while China's Treasury holdings have fallen off, its purchases of agency mortgages have increased, indicating that the US's deep public markets remain a natural home for China's vast foreign reserves.

Evidence of EM central banks looking to diversify reserves from USD assets has been seen in gold purchases, which have been metronomic in their regularity since the GFC. H1 2024 saw the highest net gold buying by central banks on record.

Options to consider

- **Employ scenario testing to assess the possible portfolio impact of increased populist policies:**
  - Stress-test the possibility of lower equity returns over the medium term amid the rise of populism-related inflation (this is not our base case given the much-anticipated boost to productivity from AI).
- **Investment opportunities associated with broadening inclusion may offer both return potential and capacity to meet impact objectives. These include:**
  - Affordable housing, social infrastructure.
  - Broader-based impact funds in both the public and private space are emerging.



3. Megatrends

Transition today

The transition is progressing at pace. Between 2018 and 2023, global solar PV capacity tripled. In 2025, renewables — solar PV, wind and hydropower — are set to generate more electricity than coal for the first time.[11] This threshold has already been passed in the EU. Investments in clean-energy technologies, dominated by solar, now far outweigh those in fossil-fuel-energy-related projects as the drivers of growth have moved beyond the clear and present needs of climate transition to the attractive economics of a lower levelized cost of energy and the appeal of greater energy security.

Despite the growth in renewables, emissions continue to rise, and at ~1.45°C above the 1850–1900 average, 2023 was the warmest year in the 174-year observations, clearly bringing into question our ability to remain below the critical threshold of 1.5°C.

Investment needs to accelerate further, and there are many opportunities for investors in next-generation infrastructure and technology. Grids need to be upgraded and better connected to accommodate new renewable energy rollout while being supported by sufficient energy storage. Future growth areas are those associated with the transition of hard-to-abate sectors, such as sustainable fuels and hydrogen, as well as carbon capture, utilization and storage (CCUS), and, critically, adaptation solutions.

Allocations to emerging markets, where rising energy demand could offset any emissions reductions, will be important to achieving the transition. However, the financing gap remains significant for emerging markets, estimated at US$4 trillion annually.[12] Current predictions signal the two largest emitters in 2050 being China and India.[13]

An investor looking to deliver on transition objectives can take a holistic approach across the following five areas: impact of physical risks, needs of climate adaptation, dependencies and impact on natural capital, benefits of circular-economy initiatives and the notion of fair carbon budgets. We believe investors should consider how their allocations can deliver real-world changes to emissions alongside attractive financial returns rather than simply improving emissions metrics across the portfolio.

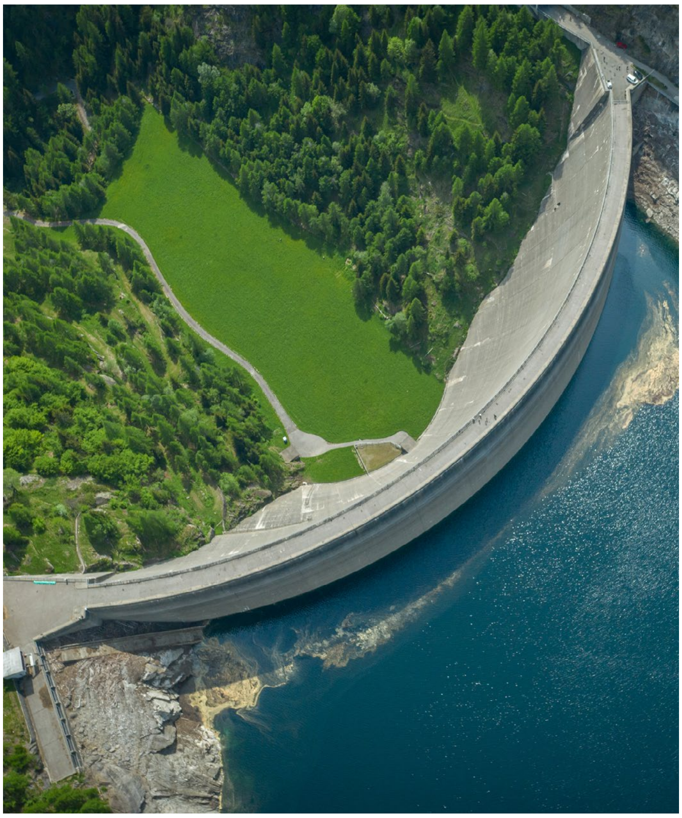
We believe building an active forward-looking investment portfolio that accounts for the transition should broadly focus on three key areas:

- **Portfolio decarbonization** — This means investors should perform emissions attribution analysis and incorporate Scope 3 GHG emissions into climate strategies.
- **Climate transition alignment** — Investors should conduct bottom-up portfolio analysis to assess not only the carbon footprint of their investments but also the full contribution their investments are making to the transition.
- **Investing in climate solutions** — As discussed above, investors should also consider making a specific allocation toward climate solutions, with defined impact goals.

We consider investments in the circular economy and natural capital, also critical to transition, in the next two sections.

Options to consider

- **Energy transition investment can extend beyond "traditional" renewable energy:**
  - Options include grid and storage opportunities as well as hydrogen and sustainable fuels.
  - Nascent adaptation solutions are also emerging.
  - Investors can further support the transition by boosting emerging market investments.
- **Transition risk management approaches should consider how to move with the data and technology:**
  - Evolving climate conditions necessitate the reevaluation of risk on a semi-regular basis. Adaptation risks in particular are not well understood.
  - Portfolio analysis needs to be forward-looking and incorporate consideration of Scope 3 emissions.



The circular economy

The concept of the circular economy revolves around extracting value from what is typically considered waste. This approach goes beyond recycling and waste management. It influences how products are designed, built and maintained in circulation. This shift emphasizes the importance of extending product life cycles, reducing resource input and, in some cases, transitioning from a sales model to a leasing model. This allows manufacturers to maintain ownership of both the product and the materials within it, ensuring continuous material circulation and value retention.

By integrating circularity into their operations, businesses can unlock substantial cost savings, reduce environmental impact, position themselves for long-term resilience and success in an increasingly resource-constrained world, and improve the resilience of their supply chains.

Overall, the circular-economy is estimated to represent an US$883 billion–US$1.5 trillion opportunity, equivalent to 4%–7% of US GDP, while mitigating 370–852 million tons of CO_2 emissions.

Figure 4. Circular-economy opportunities

Industry	Key materials	Economy opportunity*	Climate opportunity[1]
EV and grid-scale batteries	Battery metals	US$6 billion–US$24 billion	2 million–5 million tons of CO_2E reduction
Built environment and infrastructure	Steel, concrete, aluminum	US$575 billion–US$1.1 trillion	298 million–538 million tons of CO_2E reduction
Electronic equipment	Plastic, aluminum, battery metals, steel	US$301 billion–US$388 billion	73 million–311 million tons of CO_2E reduction
Total		US$833 billion–US$1.5 trillion economic value (4%–7% of US GDP)	370 million–852 million tons of CO_2E reduction

Source: Oliver Wyman. Ellen MacArthur Foundation & Oliver Wyman, An Innovation Pathway to Decarbonization: circular economy solutions for policymakers and industry in the US (2024).

* Oliver Wyman analysis

Governments are also increasingly considering regulations that encourage circular-economy principles, such as the right to repair. The EU is the leader in this effort, with several regulations in the area, including its flagship disclosure rules in the Corporate Sustainability Reporting Directive (CSRD), which mandates circular-economy reporting for numerous companies. We believe investors should consider preparing for regulation — those outside the EU can consider the EU regulation as a possible template for what could come their way.

Options to consider

- **Incorporate circular-economy principles into a risk management framework:**
  - Prepare for regulation; become familiar with the rules emerging from Europe as they represent a template for regulation from other regions.
  - Data permitting, investors can look to integrate circular-economy metrics into portfolio analysis over time.
- **Target leaders:**
  - There is a small but emerging universe of circular-economy funds focused on the leaders, although many broader-based, sustainability-oriented funds have been incorporating circular-economic considerations into processes for many years.
  - Venture capital is expanding, particularly in areas such as battery recycling.
- **Explore sustainable timberland/regenerative agriculture:**
  - This is covered in The natural (re)order section below but referenced here given the link to circular economy principles and practices.

The natural (re)order

Many investors today are balancing competing demands by incorporating both climate and biodiversity considerations into their portfolios. Over the long term, we expect both government policy and social expectations to grow, encouraging investors and corporations to consider how we are maintaining and bettering the natural environment, including improving biodiversity and addressing water scarcity and habitat destruction.

We believe an important starting point for achieving this balance is revisiting sustainability beliefs and policies, particularly as nature and biodiversity are intrinsically linked to climate change.[14] Incorporating nature-positive practices not only helps prevent unintended environmental damage but also enhances long-term returns. For example, nature-based solutions, such as restoring forests and wetlands, offer carbon-sequestration benefits, contributing to net-zero goals while creating investment opportunities.

To address these complex demands, investment stewardship is crucial. Engagement-oriented investors should ensure their asset managers are engaging with companies on nature-related issues such as biodiversity risks and climate impacts. Frameworks like the Taskforce on Nature-related Financial Disclosures (TNFD) provide guidance for investors on holding companies accountable, particularly in sectors critical to environmental sustainability.[15]

Investors should consider the investment case for funds focused on sustainable agriculture, forestry and ocean conservation, which are designed to improve natural capital, an economic term for the services and resources such as pollination that nature provides for free. These funds not only help mitigate biodiversity loss but also offer exposure to emerging sustainability markets. Some strategies, such as ecosystem restoration, offer a primary benefit of ecosystem environmental impact and the possibility of financial returns from biodiversity credits, carbon credits and added-value management techniques like the creation of ecotourism concessions.

One of the areas that exemplifies the systemic impacts of nature degradation and the investment opportunity found in improving these conditions is the production of food. We believe the human food system is undiversified, inefficient, misallocated and unhealthy. Globally, most agricultural activities focus on three crops, wheat, rice and maize, which are grown in monocultures — fields of genetically similar or identical plants, where the same plants are planted year after year.[16] Monoculture as a practice typically has a negative impact on pollinator species and increases the risk of pest and blight outbreaks.

Solutions to these challenges, such as regenerative agriculture, vertical/indoor farming, cold storage, precision fermentation and biotechnology research and development (R&D) all present compelling investment opportunities over the long term.

Options to consider

- **The opportunity set extends from more defensive strategies to innovative transformative solutions:**
  - Vertical farming incorporates circularity and minimizes the use of pesticides.
  - Precision fermentation can be orders of magnitude more efficient at producing proteins.
  - Pesticides can be engineered to target individual pest species instead of broadly killing many species in the area.
- **Sustainable timberland is underappreciated:**
  - Historical returns are more robust than often appreciated.
  - Population growth and demand for sustainable construction material provide strong long-term structural support.
  - Prefer regional diversification to diversify idiosyncratic risks.
- **Regenerative agriculture combines revived, less-harmful traditional practices with advanced technological solutions.**
- **Investors with impact goals may also wish to explore solutions such as biodiversity restoration projects.**

AI into everything

AI experienced a breakout year in 2023, with rapid adoption by individuals, governments and businesses. As discussed under Section 1 in 'The highs and lows of benchmarks', this growth has helped drive the exceptional concentration in stock markets, which has been compared to the dot-com bubble at the turn of the century. However, this focus on the large-cap tech giants is distracting from the rapidly developing world of emerging tech companies and other market segments that use AI.

The full suite of AI applications has yet to be appreciated across all sectors of the economy. Current applications represent only a fraction of what is possible, and future developments in areas like machine learning, natural language processing and autonomous decision-making will significantly expand AI's impact on industries.

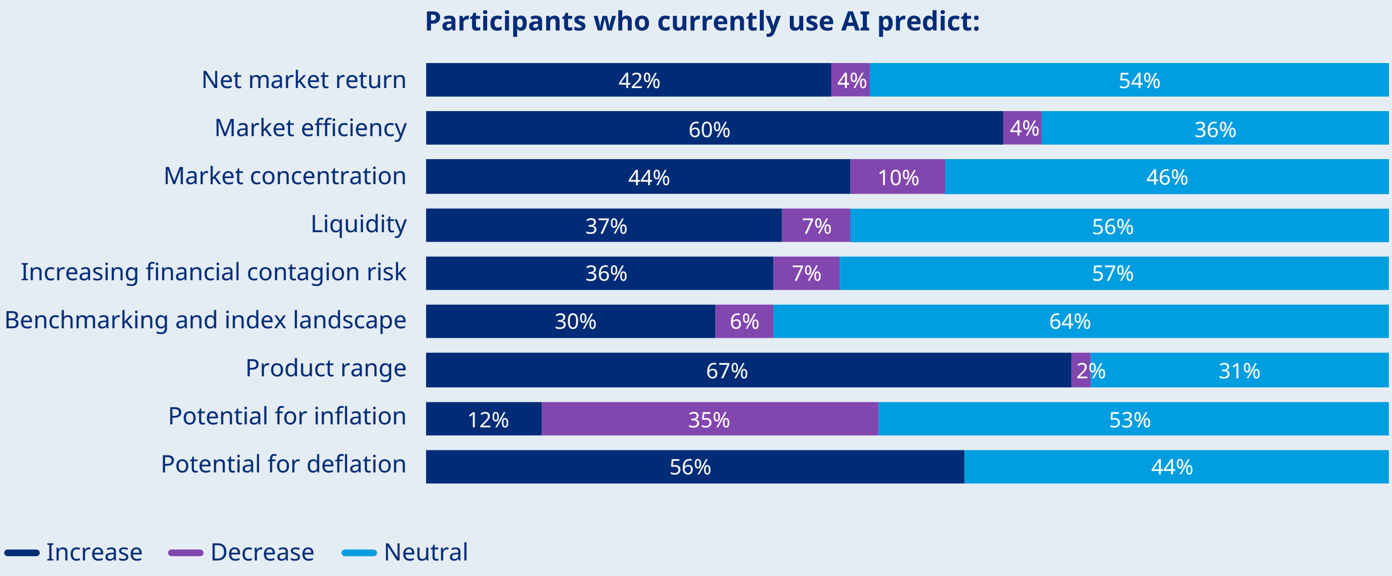
AI presents a compelling investment opportunity across multiple sectors. In healthcare and life sciences, AI applications are poised to revolutionize drug discovery, DNA sequencing and genome editing, accelerating innovation and enhancing patient outcomes. Companies leveraging AI in these areas could offer promising returns. AI's role in sustainability is also significant. By driving efficiency gains and addressing sustainability challenges, companies that develop AI solutions for energy efficiency, renewable energy and sustainable practices can offer attractive investment prospects. As the global focus on sustainability intensifies, these firms should be well positioned for growth. Whilst AI is a valuable tool in solving sustainablity challenges we should also note the increases in emissions that can result from its power needs.

Investors considering the next winners in this technological revolution should think about AI adoption in four distinct groupings:

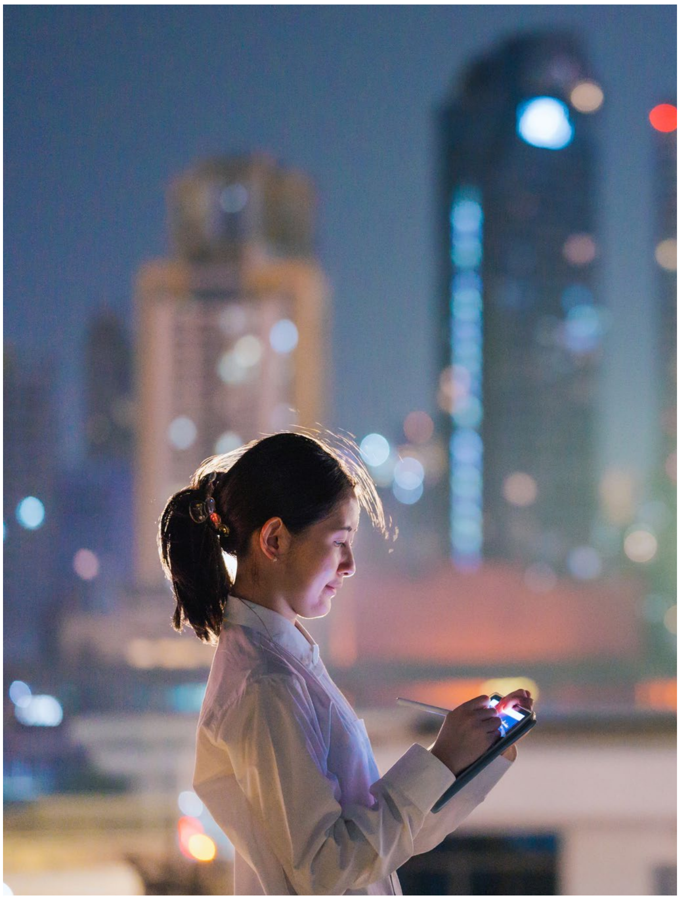
- **Providers** — Companies that create AI models or the necessary hardware
- **Enablers** — Providers of vital infrastructure, such as power utilities
- **Deployers** — Companies that effectively deploy AI to improve productivity
- **Disrupters** — New entrants that use AI to disrupt processes

Our recent survey, *AI in Investment Management*,[17] found that nine out of 10 investment managers reported current or planned use of AI in their investment processes. The question is no longer if or when but how managers are implementing AI capabilities. Indeed, many early AI pioneers came from within the investment industry and have been employing AI techniques since the 1990s.

Figure 5. AI opportunities in the investment industry



Source: Mercer. AI in Investment Management Survey 2024.



Options to consider

- **Opportunities exist across public and private markets:**
  - Companies are offering solutions in sectors being transformed by technology; e.g., healthcare, vertical farming and product tracing.
  - Specialist hedge funds capitalize on divergence between leaders and laggards (or M&A) via long/short techniques.
  - Early-stage venture capital offers the best access to the next frontier of technology; for example, innovation in deep learning processes.
  - Across the broader public markets universe, companies with expansive R&D programs are likely to win out.
- **It is imperative that appointed asset managers and internal investment teams include expertise in AI:**
  - Research into investment opportunities associated with AI requires expert knowledge of a fast-evolving space.
- **Develop robust cybersecurity programs and continue to update them with advances in technology.**
- **Incorporate AI into operational processes:**
  - Examples include performance monitoring and data analysis/quality.

Appendix

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Endnotes

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