

## DeepSeek DeepFreakout

January 27, 2025

The U.S. stock market – in particular, technology or tech stocks – is weak this morning following the rapid rise of DeepSeek which is a Chinese version of OpenAI. DeepSeek is now the top download in Apple's App store.

The market is fretting over DeepSeek's announcement that it is a low-cost AI model – one that allegedly cost \$5.5 million to build which is materially less than current spending by U.S. tech companies on Nvidia chips and the build-out of data centers.

In other words, the big run-up in U.S. tech company valuations and other secondary and tertiary beneficiaries such as natural gas companies have been driven by the belief that the US was beginning a new Industrial – or AI – revolution driven by significant amount of capital expenditures on GPUs (think Nvidia) and servers. DeepSeek's announcement brings into question how much other AI companies need to spend on infrastructure.

The stock market was not expecting this. Investors believed that the Mag7 would remain leaders for decades to come and out of nowhere a Chinese company appeared.

On the other hand, the near-term implications could be positive for U.S. tech firms if capital expenditures required to develop AI are materially less. That would mean more cash flows are available for shareholders. Longer-term, if the DeepSeek innovations turn out to be legitimate, this implies a faster acceleration of AI progress, which in turn could lead to faster diffusion of AI throughout the economy and paradoxically even more spending on chips and data centers. "Jevons Paradox" – a concept we wrote about last year – is a term you will likely be seeing more of over the coming weeks.

Finally, the leading AI firms are locked in a race to get to artificial general intelligence. This is a non-economic race where the players believe the implications of achieving AGI are so enormous that the near-term costs don't matter. Sergey Brin of Alphabet, Sam Altman of OpenAI and Mark Zuckerberg of Meta have said as much. DeepSeek's innovations in reinforcement learning could propel this race even faster.

This is a quick analysis of the weekend's news. The purpose of this letter was to inform you on today's big market move. The obvious question: Should you be buying or selling? We are working on a more detailed analysis.

Sincerely,  
The Team at Fort Sheridan Advisors