INVESTMENT COMMENTARY

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RGA INVESTMENT ADVISORS LLC

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AI Bottleneck Mania: Crashing Up, and the Opportunities Left Behind

In our last two commentaries, we detailed how we are infusing and enriching our investment process with AI. Our progress continues to compound, and we will share more in due time. Today, we want to talk about the market tensions created by the AI trade and cover a few new companies we bought over the past several months.

The second quarter kicked off one of the wildest market extremes we have seen in our time as professional investors, subsequently leading to one of the most active periods in our portfolio's history.

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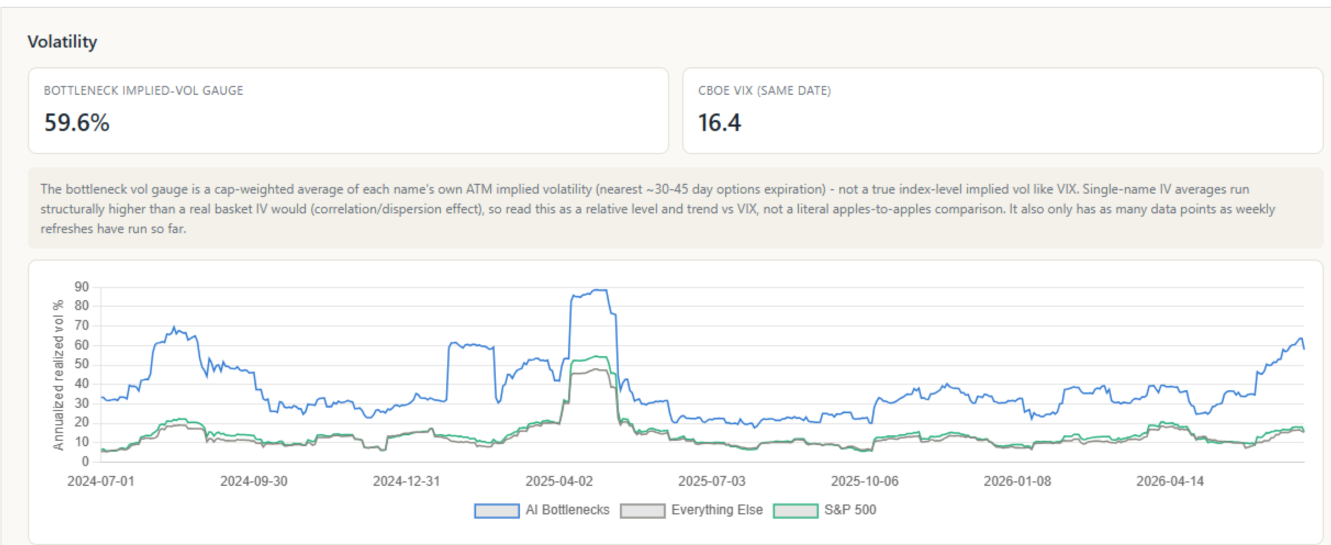
AI Bottleneck Mania

With the help of Claude, we divided the S&P into two groups of stocks:

- The AI Bottleneck 40
- Everything Else

The AI Bottleneck 40 includes all of the companies that sell critical infrastructure for the construction of data centers. This ranges from semiconductors and telecom components to power and cooling infrastructure. The AI Bottleneck 40 performed roughly in line with the S&P from the ChatGPT moment in 2022 through mid-2025, before separating from the pack and ultimately going parabolic from April through July of this year. On the surface, the market did not look volatile, as evidenced by a mid-teens VIX:

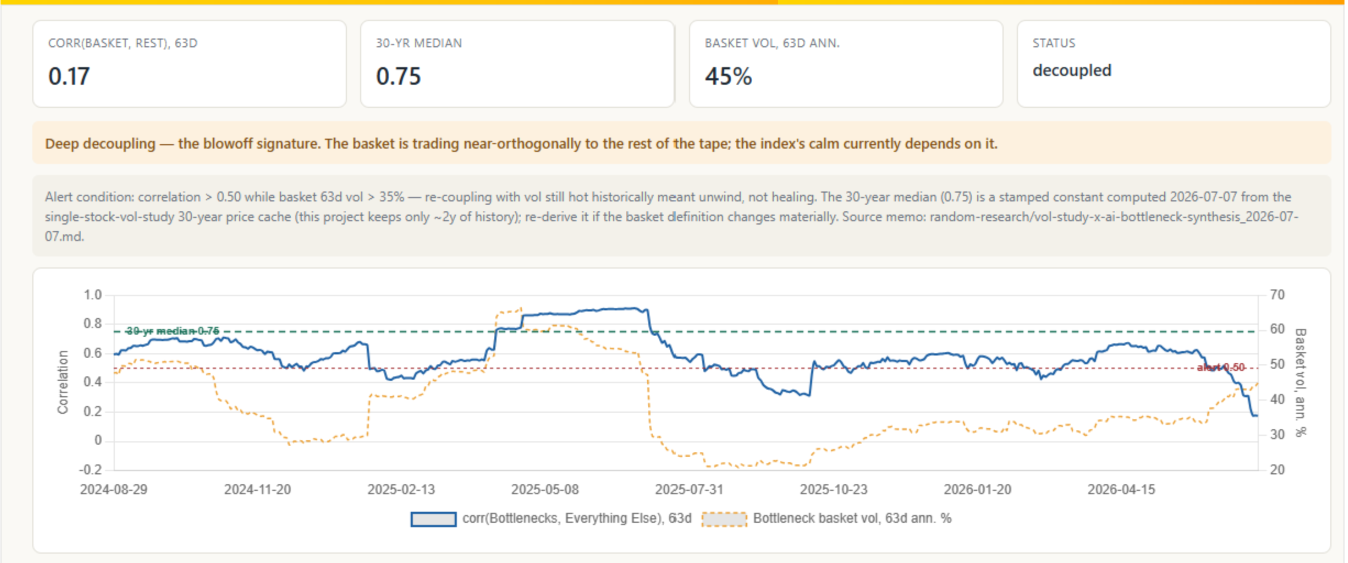


AI Bottleneck 40 realized volatility vs. S&P 500 and the CBOE VIX. Basket implied-vol gauge reached 59.6% against a VIX of 16.4. (Source: FMP, analyzed in Claude Code.)

However, beneath the surface, the volatility of the AI Bottleneck 40 was soaring. The realized vol for this group of stocks, as seen in the image above, reached nearly 60%. This is a level typically reserved for sharp market corrections and crashes, yet these stocks were soaring higher. As a friend stated, “these things are crashing up!” We have more answers today about how this happened, though that story will be told another time (if you want a good read in the meantime, we recommend this profile from the NY Times).[1]

Collectively, these 40 stocks account for around 20% of the S&P 500’s value, up from 14% at this time last year. Although these stocks historically traded in tight correlation with the market, this basket had almost entirely decoupled from the market at large (of note, this correlation bottomed at 0.01 on the morning the Aschenbrenner liquidation headlines hit).

1. https://www.nytimes.com/2026/07/31/business/situational-awareness-leopold-aschenbrenner.html



63-day correlation between the AI Bottleneck 40 and the rest of the market. Correlation collapsed to 0.17 vs. a 30-year median of 0.75, with basket volatility running at 45% annualized. (Source: FMP, analyzed in Claude Code.)

At the time, we were talking daily about how the AI trade was "sucking the oxygen out of the rest of the market." Stated another way, the AI trade had gotten so big and extreme that it could not go up without people selling out of other pieces of their portfolio. This was the most the market had ever felt like 1999, where many great companies saw their share prices decline while investors flocked to Dot Com names. We are not invoking 1999 to debate the merits of AI. As we have made clear, we are quite sanguine on AI in general. Rather, we are suggesting that an emergent market distortion was registering extreme levels of concentration, volatility and tension. Since the quarter ended, many of these forces started resolving, and it remains unclear whether the tensions will reemerge. We will certainly revisit these themes over time, as both the parallels and simultaneously contrasting features between these two market periods are both fascinating and undeniable.

Amidst this intense factor violence, overall market volatility remained suppressed. Said differently, segments of the market (i.e., the AI Bottleneck 40) had experienced highly elevated levels of both implied and realized volatilities while the broader market as a whole, as indicated by the VIX, was still rather tame. Generally speaking, we are drawn to these disconnects in the broader market structure, and we saw this as a positively skewed opportunity to capitalize on some sizable dislocations outside the realm of AI.

In our Q4 2025 commentary, we shared how we were dividing our idea funnel into three distinct buckets: 1) the AI beneficiaries; 2) the AI losers; and 3) far removed from AI. We had been deep in the weeds on this work and made four moves that are nicely spread amongst these buckets.

GitLab (NASDAQ: GTLB) – the covert AI beneficiary

We bought shares in GitLab. GitLab is a software company offering DevSecOps and git management for enterprises, serving as an essential "orchestrating" layer for companies to securely manage their codebase and IP. AI is unquestionably driving demand for GitLab's offerings, but there is concern around its traditional per-seat pricing model versus a consumption-based model. If AI reduces the number of employees in technical roles at large enterprises, this presents a headwind to growth. This headwind has slowed top-line growth faster than GitLab's budding consumption-based models for AI agents have been able to replace the lost revenue. As it stands today, AI-based revenues are a small piece of the pie, but we expect substantial growth over time. At sub-4x EV/sales, around 20x EV/EBITDA and a free cash flow yield over 5%, we think the valuation is compelling for a business still growing its top line in the high teens and playing an increasingly important role in enterprise AI workflows.

Adobe (NASDAQ: ADBE) – an AI loser so cheap that it will win

We had watched and studied Adobe with admiration for many years following their evolution from selling licensed software to subscription software. Adobe became the template by which numerous other software companies pivoted to SaaS and the rest, as they say, is history. Or so we all thought. Over the past several years, Adobe's shares have dropped dramatically. At first, the concern was competition from Figma and Canva. Then Adobe became Exhibit 1 in the "AI losers basket." We think Adobe is far more resilient than fears suggest. Similar to GitLab, there is seat-based pricing risk; however, in many industries, Adobe's offerings are irreplaceable, even with AI. Moreover, Adobe is in a great position to become the layer on top of which key AI workflows are built. Data and context are critical to these workflows, and Adobe has considerable advantages in both. We acknowledge some of the risks Adobe faces, but at a P/E of sub-10x and a FCF yield north of 10%, the market is pricing the stock as a melting ice cube while growth is still right around 10%. The company is using its healthy balance sheet and robust free cash flow to repurchase shares at a healthy clip. We think this is a potent setup as the company proves its resilience for the AI era.

Adyen (AMS: ADYEN) – the software loser that is actually an infrastructure winner

Adyen is a company we admired from afar for years, thinking its gaudy valuation would forever preclude us from owning shares. In 2022, we came close to buying shares after intense competition led to a slowdown in growth. Today, the shares trade at a similar price, while the company has more than doubled both its top and bottom lines. Stated another way, you get twice as much value for each share today versus 2022. Meanwhile, the competitive intensity in the space has been waning following the consequences of uneconomic behavior at some competitors as well as further industry consolidation.

Earlier this year, shares declined precipitously when growth was guided to 20–22% instead of 21–23%. No, this is not a typo. Investors abandoned ship over a 1% delta in the growth outlook. We think this was exacerbated by Adyen's prowess as a unified software stack, leading to the perception that Adyen is software. We do think the software is part of Adyen's differentiation, but beyond software, we think Adyen's role as a merchant acquirer and bank in many of its key geographies allows swifter payout to customers, better auth rates than most, and one unified global analytics platform for customers. We have spoken to numerous payments customers through the years and the glowing remarks about Adyen stand out over time. We bought Adyen at a mid-teens EV/EBITDA and a P/E just north of 20x, while growing upwards of 20%. The company holds a considerable net cash position, equating to a high-teens percent of market cap.

Mips AB (STO: MIPS) – whether AI wins or loses, we all should protect our noggins

You might recognize Mips as the little yellow dot on your ski/snowboard or bike helmet. The company has risen to prominence for their ubiquitous rotational impact protection insert across all key helmet manufacturers. Mips is an ingredient company that sells some know-how (IP) and a small insert that the manufacturer buys and integrates for a small piece of their overall cost of goods sold. The company has been growing by signing new helmet OEMs, expanding its share with existing OEMs and innovating, all of which opens doors to more performant helmets and new verticals like safety and moto. Shares had suffered as the company disclosed a considerable portion of their net income would be spent in order to defend one of their OEMs from a patent troll lawsuit.

At the time of our purchase, Mips was trading at a high-teens P/E when adjusted for these legal expenses, while growing upwards of 30% FX-adjusted. We had identified the case, followed it closely and felt good about Mips' range of possible outcomes. Since purchasing shares, the litigation settled for a nominal sum, which we think is a strong deterrent for other potential IP trolls. We like the outlook for Mips over the coming years and think the rise of e-bikes creates an incredible opportunity to take the fairly mature cycling vertical into a whole new growth wave.

In aggregate, we funded these acquisitions with the sale of Lattice Semiconductor, Disney and Workday, as well as a modest trim from our Alphabet position.

Mips' rotational-impact insert on a Smith Forefront 2 helmet in the field.

One more position of note:

Roku finds a new home (ROKU / FOXA)

On June 15th, Roku announced that it would be acquired by Fox Corp (FOXA). We first bought shares in Roku in late 2018 and what a wild ride it has been. We sold shares several times along the way and bought meaningfully more when the remaining position almost fully round-tripped to our basis. Had you told us the outcome ex ante in 2018, we would have been excited. Yet it all feels bittersweet, with solid overall returns accompanied by a half-dozen impactful lessons that continue to shape how we approach underwriting stocks, portfolio management and the tax consequences of selling.

As with many companies and investors, COVID led to some behavioral changes that were costly. Roku was distinctly on the right track toward correcting those errors by right-sizing the cost structure, building a robust strategy to drive ARPU and commencing a share repurchase program to capitalize on a cheap stock and healthy balance sheet. We applaud Roku's execution following their course correction.

In the end, each share of Roku will receive $96 of cash and 0.9693 shares of FOXA. We are likely to hold the FOXA shares upon closing of this transaction, given our enthusiasm around the acceleration in growth at Roku itself and the revenue synergies between the two assets.

We are excited about the opportunities in front of us and grateful for the trust you continue to place in us.

If anything in this commentary prompts questions, please reach out. You can contact any of us at 516-665-1945 or through our direct lines listed below.

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