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PHILEQUITY CORNER

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Deepseek sparks global tech selloff

Last week, a Chinese AI company called Deepseek sparked a massive selloff in global tech stocks. Its latest product topped app charts and was comparable to its best US rivals in benchmark tests despite having a cheaper cost to develop. Its breakthrough has sparked concerns that AI would be cheaper to develop and the US dominance in technology would be challenged by China.

Biggest one-day loss in one company

Nvidia plunged 17% last Monday after news about Deepseek came out. It was Nvidia's worst day since March 16, 2020 which was early in the COVID-19 pandemic. Nvidia lost nearly \$600b in market cap, the biggest one-day loss for one company in US history. As a result, Nasdaq fell 3.1% as many tech stocks followed Nvidia's plunge. Moreover, Nvidia slid from the most valuable company in the US to third in the rankings behind Apple and Microsoft.

What is Deepseek?

Deepseek is a startup formed in 2023 by Chinese entrepreneur Liang Wenfeng. He was the co-founder High-Flyer, a quantitative hedge fund focused on AI. Deepseek's open-source AI models became available for download in early January. Its latest product called R1 surged to the top of app download charts, surpassing OpenAI's Chat GPT.

More efficient and cheaper

Deepseek's R1 was reported to be comparable and more efficient than the best products offered by US tech companies. Despite this, Deepseek incurred lower costs to train and develop its models. Deepseek claimed that training one of its models reportedly cost only \$6m and took two months to develop. This is only a fraction of the costs incurred by US tech companies to develop their large AI models. Moreover, Deepseek was able to do this without relying on the most powerful chips which became harder to buy in China because of US export controls. It appears that Deepseek's Chinese engineers were able to work around US chip restrictions.

“Wake-up” call for tech companies

Trump said, “The release of Deepseek AI from a Chinese company should be a wake-up call for our industries that we need to be laser focused on competing.” Trump commented that Deepseek’s low-cost model should be a “positive development” for AI. He added that “instead of spending billions and billions, you’ll spend less, and you’ll come up with, hopefully, the same solution.”

Jevons paradox

Microsoft CEO Satya Nadella said that with Deepseek’s breakthrough, the Jevons paradox now applies to AI. The phrase was named after William Stanley Jevons, a 19th century economist. The Jevons paradox occurs when more efficient use of a resource leads to lower costs. This consequently results in higher consumption and increased overall demand. Nadella added, “As AI gets more efficient and accessible, we will see its use skyrocket, turning it into a commodity we just can’t get enough of.” Meta Platforms CEO Mark Zuckerberg said, “In AI, I expect that this is going to be the year when a highly intelligent and personalized AI assistant reaches more than 1 billion people.”

Implications of Deepseek’s breakthrough

In light of Deepseek’s breakthrough, it is expected that there will be increased competition from China in the AI battle. In the near future, China may be able challenge the dominance of the US in the areas of AI and tech. Deepseek’s success shows that there are ways to train and develop AI models that are cheaper and more efficient. Deepseek’s cheaper AI models stoked concerns about the massive investments of big tech companies on AI infrastructure.

The latest development surrounding Deepseek will shape how AI is being used and developed. Relying on less powerful and fewer chips can increase the demand for the types of chips that Nvidia and other chipmakers supply. However, this will likely result in lower margins for chipmakers like Nvidia. But based on Jevon’s paradox, the increased usage and faster adoption of AI may compensate for lower margins. AI models and applications would be built faster and cheaper while becoming more available to the public. This can usher greater proliferations and the commoditization of AI. Just like computers, internet, smartphone, and cloud, AI will eventually be hugely beneficial for the global economy and tech stocks.

PSEi drops 4% in one day

While the US experienced the biggest one-day drop in one stock, the PSEi also had its biggest one-day drop in years. Last Friday, the PSEi fell 4% due to index rebalancing. This was the PSEi’s biggest one-day drop since March 14, 2022. Last Friday’s close of 5,783 was the PSEi’s lowest since October 3, 2022. Value traded was heavy at P21.6b. China Bank Corp (CBC) and AREIT, Inc (AREIT) were included in the PSEi, replacing Nickel Asia Corp (NIKL) and Wilcon Depot, Inc (WLCON). To accommodate the inclusion of CBC and AREIT in the PSEi, there was a reduction in weight across all index constituents, thus resulting in heavy selling among many index stocks.

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