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Weekly Global Market Commentary

Sep 5, 2024

What Nvidia's Earnings Mean for the Market

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Nvidia chips are the favored choice for training artificial-intelligence (AI) systems and that's important to the overall market. To a large extent, the AI theme bolstered by massive capital spending has propelled the technology sector, and by corollary, the overall market to new heights this year.

Nvidia is the second largest component of both the S&P 500 and the MSCI World stock indexes, accounting for 6.2% and 4.2% of those benchmarks, respectively. Through the end of August, Nvidia stock had risen 141% on a year-to-date basis, accounting for about 16% of this year's S&P performance. The major indices are market-weighted meaning that larger companies can account for a disproportionate percentage move in the broader index.

Nvidia's rally took a breather last week even as it reported strong results and gave an optimistic outlook after the bell. The chip leader reported adjusted earnings of $0.68 per share compared to the expected $0.64. Revenue was $30.0 billion versus an estimated $28.86 billion. The company signaled an 8% quarter-over-quarter increase in the coming quarter which was above consensus, but likely lower than market expectations.

Nvidia continues to benefit from strong spending from its hyper scaler customers including Microsoft, Meta and Amazon to support their AI and accelerated compute initiatives, creating strong demand for its Hopper H100 and new H200 GPU platforms. Indeed, the company expects a stronger second half for Hopper with quarterly shipment growth in 3Q, and potentially higher again in 4Q depending on increasing supply for its next-generation Blackwell computer chip shipments.

In our shop, we consider economic moats in evaluating potential investments. An economic moat refers to a company's ability to maintain a competitive advantage over its rivals, which helps it protect market share and profitability over the long term. This advantage can be derived from various factors, such as brand strength, cost leadership, proprietary technology, network effects, or regulatory licenses, making it difficult for competitors to erode the company's market position. A strong economic moat allows a company to sustain higher profit margins, reduce the risk of competition, and deliver consistent returns to shareholders, ultimately contributing to long-term business stability and growth.

Nvidia clearly possesses a wide economic moat due to its market leadership in graphics processing units (GPUs), hardware and software tools needed to power the rapidly growing market artificial intelligence market. In the long run, we expect tech titans to strive to find second-sources or in-house solutions to diversify away from Nvidia in AI, but most likely, these efforts will reduce, but not supplant, Nvidia's AI dominance.

Nvidia's GPUs handle parallel processing workloads, using many cores to efficiently process data at the same time. In contrast, central processing units, or CPUs, such as Intel's processors for PCs and servers, or Apple's processors for its Macs and iPhones, process the digital data bits in a serial fashion. The wheelhouse of GPUs has been the gaming market, and Nvidia's GPU graphics cards have long been considered best of breed.

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More recently, parallel processing has emerged as a near-requirement to accelerate AI workloads. Nvidia took an early lead in AI GPU hardware, but more important, developed a proprietary software platform, Cuda, and these tools allow AI developers to build their models with Nvidia. Therefore, Nvidia not only has a hardware lead, but benefits from high customer switching costs around Cuda, making it unlikely for another GPU vendor to emerge as a leader in AI training.

Looking ahead, both Nvidia and the market likely need to consolidate after respectable rallies through the end of this summer. Historically, September and October have been two of the weakest months of the calendar for risk markets. Moreover, we are just two months away from the US election results in early November.

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