

The AI Bubble and the Golden Age of Income Investing

Navigating Risks and Opportunities

🕒 By Nico Tschanz, Head of Wealth Management at Dexbridge Capital

Dear Reader,

Markets are riding a wave of optimism fueled by artificial intelligence. Major equity indices have surged to record levels in recent weeks, and investor excitement is strong. Tech-heavy stocks at the core of the AI revolution are soaring – one leading chipmaker, Nvidia, briefly hit an unprecedented \$4 trillion market valuation. Volatility remains low as enthusiasm builds. And yet, as confidence in “the next big thing” runs high, we believe it’s also a time for careful reflection.

What Is the AI Bubble?

The AI bubble refers to the rapid surge in stock prices of companies tied to artificial intelligence, driven by investor enthusiasm and speculation. These stocks have hit all-time highs, but their valuations may outpace earnings, raising concerns about sustainability. For example, the Nasdaq 100, packed with AI leaders like NVIDIA, boasts a price-to-earnings (P/E) ratio above 35x, far exceeding its historical average of 25x. This overheated market, coupled with regulatory risks, signals a potential correction. Signs and several red flags point to an AI bubble:

- **High Valuations:** The S&P 500 now trades near 30x earnings, levels not seen since the late-1990s tech boom.
- **Market Concentration:** The AI-driven “Mag 7” — Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, and Tesla — did most of the heavy lifting in Q2 2025, gaining 18.6% and outperforming the other 493 S&P 500 stocks by over 14%.
- **Speculative Frenzy:** AI startups with minimal revenue attract massive investments.
- **Regulatory Risks:** U.S. and EU oversight, like the EU’s AI Act, could curb growth.

Having said that, excitement around AI is justified in our view – it’s a transformative technology – but investors should not ignore classic warning signs of froth. A rally led by dreams rather than fundamentals can be vulnerable to even a slight shift in sentiment.

What Does the Golden Age of Income Investing Mean?

Meanwhile, a very different opportunity is flourishing, often outside the daily headlines. We are arguably in a golden age of income investing – a backdrop not seen in over a decade. After years of ultra-low interest rates, bond yields remain attractive in 2025. Investors can now earn solid, predictable returns from high-quality bonds; yields on many government and investment-grade bonds are hovering around multi-year highs, finally providing meaningful income without excessive risk. Beyond traditional bonds, structured products and other income-oriented assets are delivering steady coupons regardless of day-to-day market turbulence. These income-generating investments tend to be less sensitive to sudden market swings, offering a measure of resilience. They don’t require betting on the next tech breakthrough – their appeal lies in dependable interest and cash flow. In a year where stock prices can swing on the latest AI news, income assets stand out for their predictability and stability.

U.S. Treasury: A Vote of Confidence, But Eyes Still on the Long End

Last week's 10-year U.S. Treasury auction surprised to the upside, drawing strong demand and offering a moment of relief for markets concerned about the growing U.S. deficit. The \$39 billion sale cleared at a yield slightly below market expectations, signaling investors' continued willingness to fund government debt—even after a five-day bond market selloff. Yields dropped across maturities, with the 10-year falling to around 4.34%, and markets welcomed the result as a sign of stabilizing sentiment. Now, attention turns to the 30-year Treasury auction—a more fragile segment of the market. The long bond's vulnerability lies in its duration: investors demand higher yields to commit capital for three decades, especially when inflation risks persist. Still, recent softer inflation data and rising jobless claims may support the auction. The outcome will be a key signal for whether the market continues to see U.S. long-term debt as a reliable source of income—or if nerves around fiscal policy will demand a steeper premium.

What Investors Can Do To Navigate This Risk:

To balance growth and stability:

- Diversify: Allocate to U.S. Treasuries and lock in high yields (4.4–4.9% yields) or buy investment grade corporate bonds
- Explore Structured Products: Consider coupon paying structured products with low downside protection barriers (e.g., 50%)
- Stay Vigilant: Monitor AI regulations and Fed rate decisions, which could sway markets

In a volatile world, there is comfort in knowing what your return will be. The strength of income-focused strategies this year has been a reminder that steady compounding can rival flashy growth, especially when markets turn choppy. A bursting AI bubble could trigger sharp declines in tech stocks, impacting indices like the Nasdaq, where AI firms dominate. A 10–15% correction could ripple to global equities, boosting volatility. Bonds and dividend stocks, less tied to tech, remain stable. We saw a strong demand at the July 2025 Treasury auction which suggests investors are already shifting to safer assets.

Why This Matters Today

The AI bubble's warning signs—sky-high valuations and regulatory risks—signal potential market turbulence. Meanwhile, rising yields and strong Treasury demand mark a golden age for income investing. By blending growth and income assets, investors can protect their portfolios and seize opportunities for steady returns. Now is the time to reassess and diversify. AI may be transformative, but income is timeless. In times of high valuations and potential volatility, investors need balance – not bets. A prudent portfolio doesn't reject innovation; it tempers it with stable, income-generating elements that can provide ballast if the growth stories falter. Now is the moment to ensure your excitement for the future is matched by a solid foundation from the present.

Balance means embracing the new without abandoning the proven. It means enjoying the upside of innovation while being prepared for bumps along the way.

For all those enjoying a well-deserved break, I wish you restful and joyful days with your loved ones. And for all those still at work, may this summer bring continued success and rewarding moments!

Warm Regards,

Nico

