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DeepSeek: PROPAGANDA vs. PROGRESS

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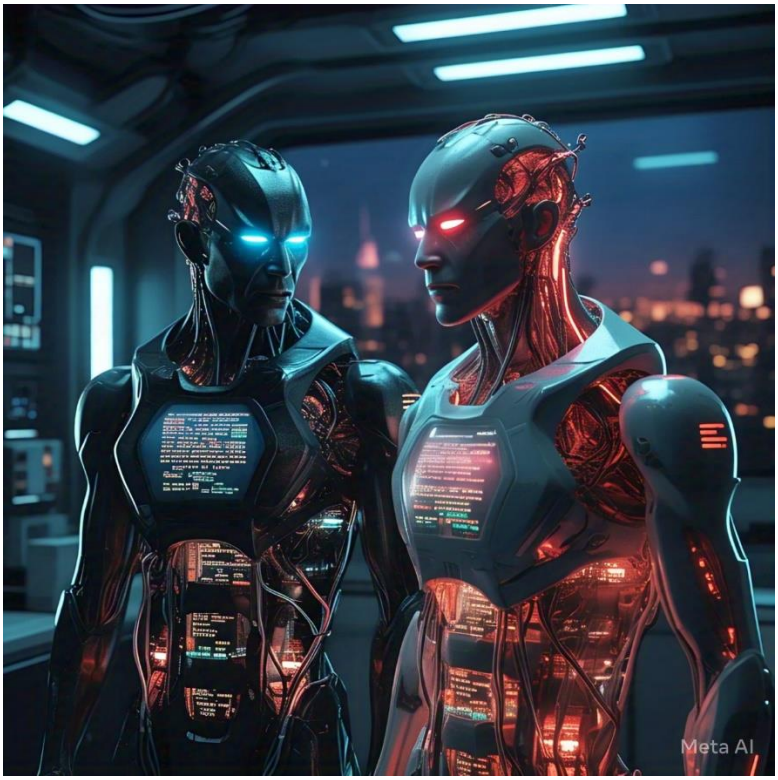

It's hard to miss that DeepSeek represents Beijing's calculated response to tightening AI controls by the West—its hyped v3 R1 version was strategically timed to coincide with the U.S. presidential inauguration. Yet, we believe that investors should bypass this geopolitical noise, which often skews media coverage and clouds investment perspectives.

Marc Andreessen's framing of DeepSeek as a "China AI-Sputnik" moment echoes past overestimations, such as the panic over Japan's economic rise or the fear of China's AI capabilities today. History reminds us: Sputnik marked the peak of Soviet advantage, but the Soviets never landed on the moon. Similarly, DeepSeek is no Apollo.

Far from being a fully autonomous Large Language Model (LLM), DeepSeek identifies itself as derivative, piggybacking on foundational models like ChatGPT and emphasizing efficiency over innovation through its narrow, elliptical responses. One can think of DeepSeek as a student preparing for the Bar or CFA exams using practice tests rather than mastering the full syllabus. While test prep might help you pass the exam, it won't make you a top legal mind. Without foundational source material, practice tests are helpful shortcuts but not transformative tools for expertise-building.

However, DeepSeek introduces a notable innovation: a two-tier AI model where the Base Layer (e.g., ChatGPT) can handle foundational training and costs, while the Inferential Layer (e.g., DeepSeek or any newcomer) can derive narrower, more accessible solutions. This setup can boost efficiency and catalyze AI adoption but doesn't signal technological leadership.

As AI is moving its focus from language to nature, DeepSeek lags the prowess to solve the critical challenges in fields like physics or biology, underscoring its limitations.

Still, we estimate that DeepSeek's financial and economic impact is potentially broadly positive:

- Productivity Gains: Two-tier AI can lead to wider adoption faster and cheaper, driving innovation and growth, which supports investments.
- Cost Savings: Lower reliance on high-end processors can benefit the broader economy albeit temporarily deflating high-end semiconductor demand.

- Disinflationary Effects: Productivity-driven innovation can counter inflationary pressures—a net market positive.
- No Monopoly: As an open-source tool, DeepSeek hardly presents a risk for monopoly power, reducing its geopolitical leverage. China's decision to flaunt DeepSeek as a propaganda splash may backfire. Keeping it discreet might have offered more strategic value for them.
- Energy Efficiency: A two-tier AI model can mitigate the insatiable energy demands of siloed AI.

Source: https://arxiv.org/abs/2501.12948