

# How AI Creates Mispricings in the Market: The Three Orders of Impact

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## Executive Summary

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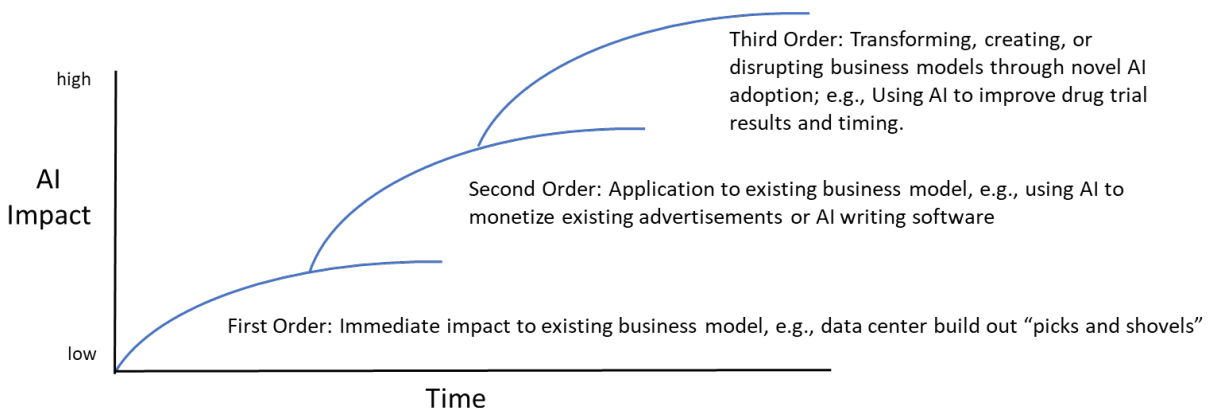
- **Process Beats Emotion:** We believe stock prices are more volatile than the underlying fundamentals that determine value, but the market is slow to recognize a build of value. We use a disciplined investment process to exploit the gap between the market narrative and fundamental reality.
- **The Three Orders Framework:** We analyze Artificial Intelligence (AI) through a three-tiered rubric—Infrastructure (First Order), Integration (Second Order), and Transformation/Disruption (Third Order).
- **Temporal Tensions:** Companies can simultaneously benefit from AI in the short term (integration) while facing long-term terminal value risk (disruption).
- **High-Conviction Discipline:** We prioritize finding businesses with strongly embedded characteristics and durable business models that can withstand or evolve with the impact of AI.

The history of capital markets is an enduring testament to the fact that while technology evolves at an exponential pace, human nature remains remarkably constant. At Cornerstone Investment Partners, our foundational belief that stock prices are more volatile than the underlying fundamentals that determine value serves as the primary lens through which we seek to identify market mispricing. The gap between the market’s emotional, short-term reactions and the stable, long-term trajectory of a business’s earnings power creates the opportunities that a disciplined, process-driven manager seeks to exploit.

As Artificial Intelligence (AI) follows the path of other potentially transformative technologies, it matures from a speculative concept into a pervasive driver of global capital expenditure and operational transformation. The challenge for the fundamental investor is not merely to identify the "winners" but to understand the temporal and structural layers of that winning. To navigate this complexity without falling into the trap of defining success by the current cycle, a timeless investment framework is required—one that allows for the constant reassessment of positions as new data becomes available.

### The Framework: Three Orders of AI Impact

We view AI as having three orders of effects, each with potential impact on stocks. First-order effects are more immediate; we already see them today. Second-order effects require integrating AI into existing business models, while third-order effects transform or disrupt existing business models through novel applications that did not exist in the same form before AI. These effects are both risks and opportunities, so our analysis must consider both lenses. What may be an opportunity today can become a risk in the future. AI is unlikely to be entirely good or bad for any stock’s fundamentals.



## The First Order: Infrastructure and the "Picks and Shovels"

The first order concerns companies that benefit directly from the physical buildout of the AI ecosystem. These include semiconductor leaders such as NVIDIA (NVDA), Taiwan Semiconductor (TSM), Micron (MU), and KLA Corporation (KLAC). Their earnings power is currently tethered to the "scale is significance" phase of development, where massive capital expenditure is required for accelerated computing.

Within this order, we also identify hybrid winners. Meta, for instance, is a first-order winner not because it sells chips, but because it has successfully used massive AI investment to monetize its advertising engine, driving immediate fundamental value. Our analysis here focuses on the degree of mispricing relative to its earnings power, ensuring we do not overpay for a narrative that the market has already fully discounted.

## The Second Order: Integration, Efficiency, and the "SaaS Train Wreck"

The second order encompasses companies that integrate AI into existing business models to drive efficiency (e.g., Alphabet (GOOGL) or face potential disruption, such as Adobe (ADBE) or Intuit (INTU). The emergence of agentic tools such as Anthropic's Claude Code and Claude Cowork has created what some call a "SaaS train wreck," where the market fears that AI-native tools will replicate the institutional fabric of traditional software whether creating documents or preparing taxes.

A vivid illustration occurred in February 2026, when the announcement of Claude Code Security sent cybersecurity stocks such as CrowdStrike and Okta down 8% to 9% in a single session. The market "sold first and sorted the details later." Our fundamental review process exploits these behavioral errors by determining if a "headline" move truly threatens the technical boundary of a company's platform or if the sell-off is an emotional overreaction.

## The Third Order: Transformation and Agentic AI

The third order represents the transformative stage in which businesses are reimaged. IQVIA (IQV) serves as a possible example, pivoting toward "Agentic AI"—autonomous systems that solve complex problems rather than merely providing recommendations. Through a strategic collaboration with NVIDIA, IQVIA is developing healthcare-grade AI to compress commercial planning timelines from 18 months to as little as 4 months and increase the precision of patient identification by 15x, but there is also a risk that increased efficiency will reduce the number of drugs that require Phase III trials.

Our process is designed to address the ambiguity inherent in AI by verifying whether past fundamentals are repeatable and assessing management's success over time. We specifically mitigate behavioral biases by refusing to meet directly with C-level executives, who often possess strong sales skills that can mask underlying business flaws.

## Conclusion

The emergence of AI does not change the fundamental rules of investing; it increases the stakes of failing to follow them. Whether a company is a First-Order provider of infrastructure or a Third-Order transformer like IQVIA, every security must meet our rigorous valuation standards. By staying focused on long-term earnings power and eliminating emotional bias, we seek to exploit the volatility that the "AI era" creates, ensuring our portfolios are positioned to thrive during good periods and withstand weaker ones.

Volatility in the prices of individual stocks or industry groups provides a barometer of market perceptions of where individual stocks are along this continuum. Such volatility does not guarantee where the stock will settle. The market price merely reflects the current perception. In cases where market concerns are misplaced or overdone, volatility represents opportunity to the patient and disciplined investor.

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