

4 pages, 12–14-minute read

Introduction

As experts in small and mid-cap companies, we constantly anticipate changes that can greatly affect their performance. One such transformative change on the horizon is the advent of AI, which is bound to reshape the business landscape. In this paper, we will explore how AI may impact small and mid-capitalization companies.

To begin, let's clarify our definitions: small cap refers to companies with a market capitalization below \$5 billion, while mid-cap pertains to companies with a market capitalization below \$50 billion.

What is AI? Artificial intelligence, or AI, is a fascinating field that involves the development of computer systems capable of performing tasks that usually require humans. It's like having a digital brain that can learn, reason, and make decisions. AI algorithms are designed to analyze large amounts of data, recognize patterns, and generate insights, just like how humans process information. These intelligent machines can perceive their surroundings, understand natural language, and even interact with us through speech or text. AI has the potential to revolutionize various industries, such as healthcare, finance, transportation, and entertainment, by automating repetitive tasks, increasing productivity, and providing innovative solutions to complex problems. Simply, AI aims to replicate the impressive cognitive abilities of the human mind, creating a new era.

As keen observers of the market, we have studied AI and carefully considered its potential influence on companies within this space. AI's disruptive power cannot be overstated, and its effects are likely to extend to companies of all sizes, including small and mid-cap ones.

AI is transforming numerous industries, offering a wide range of applications that improve efficiency, accuracy, and decision-making processes. In healthcare, AI is used to analyze medical images, helping with early detection and disease diagnosis. It also enables personalized treatment plans by assessing patient data and genetic information. AI is also beneficial in transportation systems, optimizing traffic flow and predicting maintenance needs, resulting in safer and more reliable journeys. Additionally, AI powers virtual assistants that can understand natural language and automate tasks, simplifying daily routines and improving user experiences. In the financial sector, AI algorithms assist in fraud detection, risk assessment, and algorithmic trading. In manufacturing, AI enhances productivity and quality control through predictive maintenance and automated inspection. The entertainment industry benefits from AI-driven recommendation systems that provide personalized content suggestions based on user preferences. Overall, AI continues to revolutionize various domains, offering transformative solutions and reshaping the way we live and work.

The three branches of AI that are being talked about most right now by smaller companies are Machine Learning, Natural Language Processing (NLP), and Generative AI.

Machine learning focuses on the development of algorithms and statistical models, enabling computer systems to learn from and make predictions or decisions based on patterns without explicit programming. It involves training a model with a large amount of data, allowing it to identify and extract

meaningful features or relationships, and then using this knowledge to make accurate predictions or perform specific tasks.

Natural Language Processing, or NLP, helps computers understand and interpret human language. It involves giving computers the ability to read, understand, and respond to text or speech, just like we do. It's like teaching a computer to be a good listener and communicator. With NLP, computers can analyze text or speech to figure out what it means. They can understand the context, extract important information, and even detect emotions. This helps computers to answer questions, provide useful information, and engage in conversations with people. In short, NLP enables computers to understand and communicate with humans in a more natural and human-like way. It's all about bridging the gap between human language and computer understanding, making our interactions with technology easier and more intuitive.

Generative AI creates and generates new content, such as images, music, text, or even video, using machine learning algorithms. Unlike traditional AI models that are designed for specific tasks, generative AI models aim to learn the underlying patterns and structures of a given dataset and generate new, original content that resembles the input data.

Current Landscape of AI Adoption Among Small and Midsized Companies

There is growing interest across the entire business landscape in AI. Small and midsized companies are adopting AI at a more rapid rate each month. From start ups to medium sized companies, they recognize the potential for AI and see the benefits of improved efficiencies as well as improved decision making and ultimately gaining a competitive advantage.

Services such as cloud-based AI services on platforms like Azure, AWS, and Google Cloud all allow access to smaller companies to gain access to models and APIs. This reduces the competitive advantage that the larger players enjoy due to having more resources. Machine learning as a Service (MLSaaS) is another service that closes the gap between larger companies and smaller companies. Again, the larger players such as Amazon, Microsoft, and Google all have offerings in MLSaaS. IBM also has a presence. These platforms offer prebuild models and user-friendly interfaces to make the offerings usable for smaller players as well as scalable. Smaller companies can also gain access to AI powered automation tools and chatbots to automate customer service and reduce costs.

Benefits of AI for the Most Innovative Smaller Companies

By harnessing the capabilities of AI, companies can unlock new opportunities and significantly enhance their operations. AI has the potential to streamline processes, automate tasks, and improve decision-making, thereby increasing efficiency and productivity. These advancements can lead to cost savings, improved customer experiences, and ultimately, higher profitability for small and midcap companies.

If utilized properly, AI can aid smaller companies in gaining a competitive edge. With AI-powered tools, they can gather and analyze vast amounts of data, enabling them to make more informed business decisions. This data-driven approach can help identify market trends, anticipate customer preferences, and optimize strategies for growth. By leveraging AI, small and midcap companies can compete with larger players on a more level playing field.

AI will benefit the most innovative smaller companies in several ways. We see the benefits as follows:

Improved Efficiency. We believe that AI will enable greater efficiency within smaller companies and allow for the automation of repetitive tasks. This can enable overall efficiency and reduce the need for adding more personnel for tasks that can be done by AI. This enables smaller companies to remain nimbler and is an advantage over larger companies.

Cost reduction. AI enables day to day operations to run more efficiently. AI can help to optimize inventory management, improve production processes, and identify areas for cost savings.

Improved customer experience. The movement to digital has in a lot of cases improved the customer experience. With the use of AI, smaller companies can analyze customer behavior via the data collected and can provide targeted recommendations as well as customer support.

Data analysis and insights. AI allows for the synthesis of larger amounts of data very quickly and efficiently. This allows for the analysis of market trends, competitive analysis as well as granular details about customer preferences. It also allows for more proper forecasting of demand.

Supply chain optimization. AI can aid in the streamlining of the supply chain by analyzing historical data, current inventory levels, and market demand. It can aid in forecasting demand, managing inventory levels, and optimizing logistics routes. This streamlines operations and reduces costs.

Marketing and Advertising. AI technologies can optimize marketing and advertising campaigns. AI algorithms can analyze customer data, social media trends, and other relevant information to target specific customer segments, determine the most effective advertising channels, and optimize the content and timing of marketing campaigns.

Competitive advantage. The proper use of AI will allow smaller companies to gain a competitive advantage over other competitors that do not utilize the power of AI. AI tools will allow smaller companies to launch products quicker and improve overall efficiency. AI has the potential to level the playing field for smaller companies that utilize its power.

Innovation. AI will allow greater opportunities for innovation for smaller companies. From launching new products and services with intelligence to improving current offerings, AI can reduce the time of both research and development and marketing, offering an advantage with being nimbler.

AI is poised to bring significant changes to the business landscape, and small and midcap companies should be embracing its potential. While challenges may arise, the evolving AI ecosystem offers opportunities for smaller companies to leverage these transformative technologies and thrive in the evolving business landscape.

Practical Applications of AI

One example of how companies are using AI to drive efficiency and gain competitive edge is Wingstop (WING), an owner and franchisor of quick serve restaurants known for their chicken wings. In their latest quarterly call, they said the following. "As we continue to lean into innovation and pursue our aspiration of digitizing every transaction, we are excited about early results from a test we just completed around AI-enabled phone orders... The early results are promising as we see an improvement in the team

member experience, order time, guest satisfaction, and an increase in ticket size with the ability to capture this guest digitally.”

Revolve Group (RVLV) has leaned into using AI across many parts of their business. Revolve’s retail business, targeted mostly at younger women, is entirely online. In a recent earnings conference call, the company detailed how they leveraged AI technology to develop an innovative marketing campaign featuring outdoor billboards for their flagship Revolve Festival event. The company has used AI designs to create a limited-edition brand product capsule. Revolve is also leveraging AI to develop enhancements to its search capabilities. “We are excited by internal demonstrations of further application of AI technology, and we’ve shown a great deal of potential to drive impactful results in the future.”

HubSpot (HUBS), a leading provider of Customer Relationship Management (CRM) services to the Small and Medium Sized (SMB) business sector, said the following about AI’s impact on SMBs. “We are in the early stages of a transformative shift. Generative AI is rapidly changing the landscape in three fundamental ways. It helps businesses generate content, generate insights, and generate code, all using natural language.”

The Future of AI and Its Impact

It is too early to tell what the ultimate impact AI will have on the economy. We do believe that it is a seismic shift in the landscape. For smaller companies, it means opportunity for those that are on the leading edge of adoption. For those that observe from the sidelines, we see the same type of impact that came to those that eschewed the Internet in its early days, trouble. We study change and its impact on companies, especially among small and mid-sized companies. For the companies that are innovators, AI will be transformative and lead to market share gains combined with increased profitability. It will also allow the best smaller companies to compete on a global level with much larger companies. The ability to combine nimbleness with AI will be a significant competitive advantage for some small and mid-sized companies.

Conclusion

AI is transformative technology that will greatly impact the global economy for decades to come. It will affect small and medium-sized companies and provide opportunities for the most innovative companies. The benefits will be most evident in improvements in efficiency, reductions in costs, improved customer experience, optimization of marketing and advertising, increased competitive advantage, and improved innovation. For the best-in-class companies in the small and mid-cap space, this will mean increases in growth opportunities and profitability, a powerful combination.