

Why We Own Alphabet

A public-records request in Arkansas has exposed an uncomfortable question at the heart of the artificial-intelligence boom: who pays for the electricity?

News reports based on documents released through that request said a Google subsidiary would contribute \$526 million towards a 600-megawatt solar project with 350 megawatts of battery storage, plus \$190 million for transmission, to support its planned West Memphis data centre. The documents are contested and some details remain confidential. An Entergy regulatory filing does independently confirm the special-rate contract, project scale and expected 2028 completion.

This is more than an energy story. It is a test of whether Alphabet can convert soaring demand for intelligence into durable cash flows without handing the infrastructure and environmental bill to customers and communities.

The physical constraint behind digital demand

Artificial intelligence may feel weightless, but it runs in buildings filled with chips, cooling systems and electrical equipment. The International Energy Agency reported in April 2026 that global data-centre electricity demand rose 17% in 2025 and is set to double by 2030. It also warned that grid connections, transformers, turbines and advanced chips are becoming bottlenecks.

That creates structural demand for compute, but not a free pass for its providers. More electricity may come from renewables, yet gas and other fossil generation will also expand. Local grids can be strained long before data centres become a large share of global electricity use. The winners will need affordable power, reliable capacity and social permission to build—not merely better algorithms.

What Alphabet does

Alphabet's economic engine remains Google Services: Search, YouTube, subscriptions, platforms and devices. Advertisers pay to reach users with commercial intent. Google Cloud sells infrastructure, data, security and AI services through consumption and subscription fees. Alphabet also funds earlier-stage businesses, including Waymo.

AI cuts across that structure. It can improve Search and advertising, increase engagement, expand Cloud demand and create new products. It can also weaken the familiar search interface, invite new competitors and require enormous investment before returns are visible.

Where it fits. Alphabet sits primarily within Delta's Climate Action theme because the AI buildout is making energy efficiency, clean-power procurement and grid investment part of the product economics. Its Nature Innovation exposure appears in water use, materials and supply-chain impacts. Human Advancement appears through access to information, digital tools and potentially useful AI applications. These secondary lenses matter, but they do not excuse weak capital returns or harmful outcomes.

Why Alphabet may keep winning

Alphabet's advantage is its integrated system. Search and YouTube provide global distribution and cash generation. Cloud provides enterprise relationships and a route to charge for AI infrastructure and software. DeepMind and Google's research base develop models. Custom tensor processing units can improve performance and reduce dependence on general-purpose hardware. The company can deploy improvements across billions of interactions, learn quickly and finance infrastructure at a scale few competitors can match.

Efficiency matters because compute is becoming power-constrained. In its 2026 Environmental Report, Google said its data centres achieved an average power usage effectiveness of 1.09 in 2025, meaning relatively little electricity was used beyond the computing equipment itself. It also reported more than three times the computing performance per unit of energy compared with five years earlier, and said its Ironwood processor was almost 30 times as power-efficient as its first Cloud TPU from 2018.

These are company-reported fleet and product measures, not proof that total environmental impact is falling. Better efficiency can lower the cost of each computation while cheaper, better services stimulate far more use. The economic moat is therefore not “green AI”. It is the ability to deliver useful intelligence at lower unit cost while securing the power, chips and customer trust required to scale.

How the advantage becomes earnings

The causal chain is clearest in Cloud. Customers consume infrastructure and subscribe to software. Higher usage becomes revenue; scale, utilisation and better hardware can spread fixed costs; operating profit can then fund more capacity and research.

Alphabet's second-quarter 2026 results show that mechanism accelerating. Revenue rose 24% to \$119.8 billion. Google Services revenue increased 15% to \$94.5 billion, while Google Cloud revenue rose 82% to \$24.8 billion. Cloud operating income increased from \$2.8 billion to \$8.8 billion. Group operating income rose 30% and the operating margin reached 34%.

But the capital bill is equally important. Alphabet generated \$39.1 billion of operating cash flow in the quarter and spent \$44.9 billion on capital expenditure. In June it raised \$49.6 billion of net proceeds through common and mandatory convertible preferred stock, partly to scale AI infrastructure and global compute, and established an at-the-market programme for up to a further \$40 billion.

Strong growth therefore does not settle the investment case. The test is whether incremental Cloud profit, advertising resilience and new AI revenues ultimately earn an attractive return on the power, chips, buildings and financing required. Scale is an advantage only when it produces cash flows per share, not when it becomes an expensive race nobody can stop running.

A financially strong business, not just a good story

A compelling AI story only matters if the company behind it can convert that demand into durable, per-share value. A business that cannot fund its own capacity, protect its margins, or turn growth into cash will struggle to win the intelligence race however strong its technology

looks. So before getting carried away with the story, we ask a simpler question: is this a genuinely well-run, profitable company? For the most part, yes - though the most recent numbers have to be read carefully, because a large one-off item currently flatters them.

Profitability. Alphabet earns strong and improving profits on the capital invested in the business. Return on shareholders' equity - essentially, how much profit it generates for every dollar shareholders have invested - has risen from around 26% in 2023 to nearly 32% in 2025. Its underlying operating margin has followed a similar path, expanding from around 27% to over 32% over the same period, while a broader measure of profitability, adjusted EBITDA margin, has risen from around 31% to over 37%. Few companies operating at this scale sustain returns and margins at this level.

Earnings growth. The profit Alphabet generates for shareholders has grown at roughly 33% a year over the past three years, comfortably outpacing revenue growth of around 13% a year over the same period - the clearest marker that the business is becoming more profitable as it grows, not just bigger. That said, the most recent year needs an important caveat: a large part of the jump analysts now forecast for 2026 net income and earnings per share reflects a one-off, non-cash \$98 billion mark-to-market gain on Alphabet's equity holdings recorded in the second quarter, not core operating performance. Stripped of that gain, core earnings per share in the quarter were roughly in line with consensus rather than the headline beat the reported figures suggest, and forecasts show earnings per share falling back by more than a quarter in 2027 as the comparison unwinds, before resuming growth of around 20% a year into 2028 and 2029. The underlying operating business - revenue up 24%, operating income up 30%, operating margin up two points to 34% in the second quarter - is growing in a way we can trust; the reported bottom line for 2026 as a whole needs translating first.

Shareholder returns. Ultimately, none of this matters to an investor unless it shows up in the share price. Over the five years to the end of 2025, Alphabet's shares delivered a total return - share price growth plus dividends - that compounded at close to 29% a year, a run that has continued into 2026 with a further 9% total return year-to-date, even after a 7% single-day fall following the most recent results. That average return has not been a smooth one: shares fell 39% in 2022 during the broader technology sell-off, a reminder that this is a genuinely volatile holding even when the multi-year outcome has been strong. This is a business whose shareholder returns have more than kept pace with its improving profitability, even allowing for that volatility along the way.

None of this is guaranteed to continue, and the scale of AI-related capital spending is a real test of it - but it gives us real confidence that Alphabet's core profitability, not just its most recent one-off gain, can keep funding the investment its AI thesis depends on.

Leadership we trust, with room to improve

A good business also needs to be well led, and Alphabet has a broadly sound governance and leadership structure in place. The roles of Chief Executive and Chair are held by separate individuals, giving a structural check at the top; core oversight functions such as the audit function are fully independent of management and the company; and the whole board stands for re-election every year, rather than serving staggered terms, giving shareholders a regular say over who governs the company.

There are areas where we would like to see improvement. Applying a stricter, tenure-based approach to independence, a majority of the board no longer qualifies as independent, and there is no genuinely independent chair or lead director to counterbalance that. Certain board committees fall short of independent-majority thresholds, the board's own self-assessment of its effectiveness is not made public, board tenure and refreshment skew heavily toward very long-serving directors, and a multi-class share structure concentrates voting control with founders and insiders well beyond their economic stake - limiting ordinary shareholders' influence over the election of directors and the size of executive pay.

Capital discipline is a clearer strength. Management has consistently generated returns on invested capital comfortably above its cost of capital, and has paired that with a sustained programme of share buybacks and a dividend that has grown every year since its introduction - a genuine sign of financial stewardship even as debt-funded investment in AI infrastructure has picked up.

The areas for engagement going forward are clear: greater board independence and refreshment, public disclosure of board effectiveness outcomes, and a narrower gap between economic ownership and voting control. Progress on these fronts, alongside the capital discipline we already trust, is what would give us full confidence in Alphabet's leadership.

Value, decision, and tension

We own Alphabet because three things line up, imperfectly but genuinely: a durable, structural source of demand in artificial intelligence and cloud infrastructure, met by a company with exceptional distribution, proprietary technology and financial capacity to serve it; a genuinely profitable, improving business behind that opportunity, with earnings growing faster than revenue and a shareholder-return record that has compounded at close to 29% a year despite real volatility; and a leadership team whose capital discipline we trust, operating inside a governance and voting structure that leaves real room for improvement. Few companies offer conviction on the first two fronts while leaving this much room for improvement on the third.

Valuation needs the same translation as the earnings figures above it. On the surface, Alphabet's shares do not look demanding for a business of this quality and growth, but that impression rests partly on a 2026 earnings figure inflated by the one-off equity gain described above; once that unwinds, the shares trade far closer to a fair reflection of their quality than headline multiples suggest. We do not think of Alphabet as obviously cheap; it is a business the market is still working out how to value through an unprecedented capital-spending cycle.

The central tension is that the same capital intensity and concentrated decision-making structure that let Alphabet commit close to \$200 billion to AI infrastructure in 2026 alone, at speed and without a binding shareholder vote, is also what limits ordinary shareholders' ability to slow or redirect that spending if the returns disappoint. A powerful, well-run company can still be a poor investment if its financing and capital expenditure dilute the value of future growth, or if governance concentration insulates decisions of this scale from adequate scrutiny. Valuation discipline, and the pace at which governance improves, are what ultimately govern position sizing here.

What could break the chain

A number of things could weaken this thesis, and we watch for all of them:

- Search and Cloud demand could disappoint. AI-native interfaces could erode traditional search query volumes and advertising economics faster than Alphabet can replace them, and Google Cloud's growth could slow if enterprise customers push back on pricing or if the more than 50% of backlog that is expected to convert to revenue over the next 24 months converts more slowly than management projects.
- The infrastructure programme may not earn its cost of capital. FY2026 capital expenditure guidance has already been raised twice, to \$195–205 billion, pushing free cash flow negative for the first time; construction timelines, chip cycles, and access to power, water and grid connections could all delay capacity or depress returns, and the \$49.6 billion equity raise and expanded debt capacity used to fund this spending raise the bar for per-share value creation even as they fund growth.
- Reported profitability is not yet fully comparable across periods. Much of the FY2026 net income and earnings-per-share growth reflects the one-off equity gain described above rather than core operating performance, and return on invested capital has already eased from around 28% to 23% as debt-funded capex rises; the thesis needs core profitability to hold up once the comparisons normalise in 2027.
- Governance concentration and regulatory exposure could disrupt the advantage. Alphabet's multi-class share structure entrenches founder control regardless of economic ownership, and a majority of the board does not qualify as independent under a stricter, tenure-based test. Separately, active US antitrust remedies in the search case, EU Digital Markets Act enforcement, and evolving AI regulation could all alter distribution economics and cost structures.
- The impact case can fail on its own terms too. Fleet-wide efficiency gains - such as a 1.09 power usage effectiveness ratio - do not guarantee absolute environmental progress: Google's own reporting shows ambition-based emissions rose 18% in 2025, driven mainly by supply-chain emissions even as operational emissions fell, and freshwater consumption rose 37%. A product can be more efficient per unit without total impact falling as usage grows.

The thesis would weaken materially if Cloud backlog failed to convert into cash at the rates management expects, if core earnings growth - stripped of one-off gains - failed to keep pace with the capital being deployed, if board independence and voting rights showed no improvement over a reasonable period, or if Alphabet's own environmental outcomes kept moving in the wrong direction as capacity scales. It would also weaken if the market's enthusiasm for AI monetisation proved as fragile as the 7% single-day share-price fall after an operationally strong quarter suggests it could be.

Outcomes as evidence

Alphabet's environmental report contains useful measures, but the boundaries matter. A 1.09 power usage effectiveness ratio and improving performance per watt indicate technical efficiency. More than 12 gigawatts of clean-energy contracts indicate procurement. Neither establishes avoided emissions on its own.

The company estimated that nine products enabled 41 million tonnes of carbon-dioxide-equivalent reductions in 2025. That is a modelled company estimate, not direct measurement of economy-wide causation. Its emissions and selected environmental metrics received limited assurance, which improves confidence in reported data but is not the same as assurance over every claimed customer outcome.

The Arkansas solar-and-storage facility is expected in 2028. Until it operates, the contribution, capacity and customer-savings figures are commitments or projections. The measurable test is what follows: generation actually connected; hourly carbon-free energy; grid reliability and household bills; data-centre utilisation; total emissions and water stress; and, ultimately, the cash return earned from the compute those resources support.

The ownership question

Alphabet embodies one of the defining investment tensions of this decade. Intelligence is becoming cheaper and more useful, yet its physical foundations are becoming more capital-intensive and politically visible.

The thesis compounds if Alphabet preserves the usefulness and economics of Search, turns Cloud and AI demand into rising core cash flows rather than one-off accounting gains, uses custom technology to improve unit economics, funds rather than externalises infrastructure costs, narrows the gap between its capital allocation and its governance structure over time, and delivers absolute environmental progress as capacity grows. It weakens if capital intensity overwhelms returns, communities carry the bill, concentrated control insulates decisions from scrutiny, regulation erodes distribution, or efficiency gains are swallowed by demand.

That is why we own Alphabet - for its impact-linked demand, its improving core profitability, and a leadership team whose capital discipline we trust even as we look for its governance structure to improve - and why the electricity bill, and the voting structure behind it, are both now part of the valuation.

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