



AI Market Consolidation 2025

The Subsidy-to-Acquisition Stratagem

A NoFriction Intelligence Market Briefing
May 2025



Casey P. Potenzzone
Founder & Director
NoFriction

Executive Summary

The AI market is experiencing a profound economic disconnect: while customer-facing prices for AI services continue to drop, the actual infrastructure and operational costs remain extraordinarily high. This market briefing reveals that this disconnect is not accidental but part of a deliberate strategy by major tech companies to dominate the market through subsidization, with the ultimate goal of industry consolidation.

Our analysis reveals that despite plummeting inference costs (down 280-fold in under two years), companies like OpenAI are on track to lose \$14+ billion in 2025 alone. The most successful AI vendors spend approximately \$2.25 for every \$1 they make—a fundamentally unsustainable business model that raises serious questions about the long-term viability of the current AI ecosystem.

"We're witnessing perhaps the most heavily subsidized technology rollout in history. The gap between what AI actually costs to build and run versus what customers are paying is creating an artificial market that cannot be sustained indefinitely. When this correction happens, it will reshape the entire AI landscape."

— Casey Potenzzone, Founder, NoFriction

Tech giants are collectively planning to spend over \$320 billion on AI infrastructure in 2025 alone, creating insurmountable barriers to entry for smaller players. Meanwhile, AI startups, despite raising hundreds of millions in funding, are finding their business models unsustainable against big tech's spending power and subsidized offerings.

This report provides a comprehensive analysis of the subsidy economics, strategic market positioning by key players, clear signs of coming market consolidation, and strategic recommendations for different stakeholders to navigate this evolving landscape.

Table of Contents

1. Introduction to AI Market Dynamics

2. The AI Subsidy Economy

- 2.1 The Economic Disconnect
- 2.2 Infrastructure and Operational Costs
- 2.3 Market Pricing vs. Actual Costs

3. The Strategic "Subsidy Trap"

- 3.1 Big Tech's Subsidization Strategy
- 3.2 Customer Acquisition and Market Share
- 3.3 Setting the Stage for Consolidation

4. Key Market Players Analysis

- 4.1 OpenAI
- 4.2 Google
- 4.3 Meta
- 4.4 Microsoft
- 4.5 Other Significant Players

5. Market Division Dynamics

- 5.1 Market Segmentation
- 5.2 Profitability Analysis by Segment

6. Economic Unsustainability Evidence

- 6.1 Case Studies

7. Consolidation Signals & Timeline

- 7.1 Acquisition Patterns
- 7.2 Market Indicators
- 7.3 Projected Timeline

8. Strategic Recommendations

- 8.1 For AI Startups
- 8.2 For Enterprise Customers
- 8.3 For Investors
- 8.4 For Policymakers

9. Conclusion & Future Outlook

10. About NoFriction

11. References & Citations

1. Introduction to AI Market Dynamics

The artificial intelligence market is experiencing unprecedented growth and transformation. As of 2025, the global AI market is projected to expand from approximately \$233.46 billion in 2024 to an astounding \$1,771.62 billion by 2032.¹ This growth is driven by rapid technological advancements, increasing adoption across industries, and massive capital investments.

However, beneath this explosive growth lies a precarious economic foundation. The current AI market is characterized by a significant disconnect between the actual costs of developing and operating AI systems and the prices charged to end-users. This disconnect is creating artificial market conditions that cannot be sustained indefinitely.

Major technology companies—including Google, Microsoft, Meta, and OpenAI—are collectively planning to spend over \$320 billion on AI infrastructure in 2025 alone.² This enormous investment is creating insurmountable barriers to entry for smaller players and setting the stage for a market consolidation that will reshape the industry landscape.

This report examines how big tech companies are strategically using subsidized AI tools to capture market share, with the ultimate goal of industry consolidation. We analyze the economics of AI subsidization, identify key market players and their strategies, and provide insights into the coming market correction and its implications for different stakeholders.

2. The AI Subsidy Economy

2.1 The Economic Disconnect

The AI market in 2025 is characterized by a profound economic disconnect: while customer-facing prices for AI services continue to drop, the actual infrastructure and operational costs remain extraordinarily high. This disconnect is creating a market largely sustained through massive subsidization by both investors and technology partners.



According to the Stanford HAI AI Index 2025, inference costs for a model performing at the GPT-3.5 level fell from \$20.00 per million tokens in November 2022 to just \$0.07 per million tokens by October 2024—a 280-fold decrease in under two years.³ Yet despite this dramatic efficiency improvement, the most successful AI vendors spend approximately \$2.25 for every \$1 they make—a fundamentally unsustainable business model.

"The economics of AI infrastructure are fundamentally different from traditional software. While software typically has high fixed costs but near-zero marginal costs, AI combines high fixed costs with significant variable costs that scale with usage. This creates a paradox where success—more users and more usage—can actually accelerate financial losses."

— Casey Potenzzone, Founder, NoFriction

2.2 Infrastructure and Operational Costs

The backbone of AI systems—particularly large language models (LLMs)—consists of specialized GPU clusters, cooling systems, networking equipment, and power infrastructure. The costs associated with this infrastructure are staggering:



Building AI-optimized data centers costs approximately \$25 million per megawatt of capacity, with large-scale facilities requiring gigawatts of power.⁴ For context, OpenAI has committed \$19 billion to the Stargate data center project alongside a similar investment from SoftBank.⁵

OpenAI's reported infrastructure expenditures reveal the true scale of AI costs:

- \$13 billion on compute with Microsoft alone in 2025
- \$12.9 billion five-year compute deal with CoreWeave (~\$2.38 billion annually)
- \$19 billion commitment to the Stargate data center project
- Total 2025 projected costs: \$28 billion+

AI costs can be divided into two main categories—training (creating the models) and inference (running the models for users):

Cost Category	Typical Range	Recent Trends
Model Training (Frontier)	\$100M - \$1B+	Increasing with model size and complexity
Inference (per million tokens)	\$0.07 - \$60.00	Decreasing rapidly (280x in under 2 years)
Data Center Construction	\$25M per MW	Stable but facing supply constraints
Energy & Cooling	30-40% of total cost	Increasing with AI compute density

2.3 Market Pricing vs. Actual Costs

AI providers have established various pricing models for consumers and businesses that fail to reflect the true costs of service delivery:

Consumer Subscription Services:

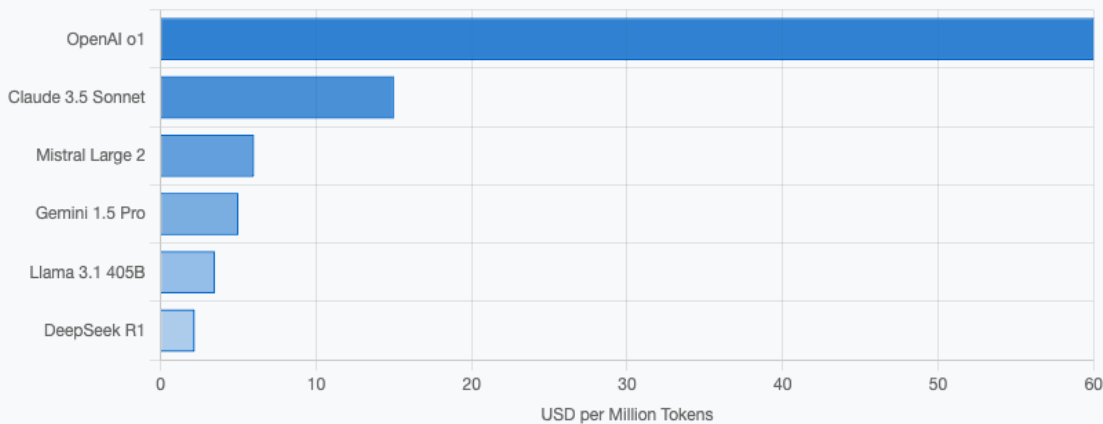
- ChatGPT Plus: \$20/month
- ChatGPT Pro: \$200/month
- Claude Pro: \$20/month
- Claude Business: \$35/month

Enterprise API Pricing (per million tokens):

Enterprise AI API Pricing Comparison (2025)

Source: Stanford HAI AI Index 2025

Price per Million Tokens (USD)



According to analysis from "Where's Your Ed At," OpenAI "loses money on every single user" despite dropping inference costs.⁶ The sheer scale of operations required to support millions of users results in losses that even the most valuable companies in the world would struggle to sustain long-term without external funding.

"The current AI boom is being funded at a loss ratio we've never seen before in tech history. While the dot-com bubble saw companies with questionable paths to profitability, today's AI leaders have proven paths to significant losses at scale."

— AI Now Institute, "AI Generated Business" Report

3. The Strategic "Subsidy Trap"

3.1 Big Tech's Subsidization Strategy

The massive subsidization of AI services by major tech companies is not simply a result of early-stage technology investment. It's a deliberate strategy designed to capture market share, establish dominance, and ultimately reshape the competitive landscape.

This strategy follows a pattern observed in other markets where big tech has established dominance:

1. **Subsidize aggressively** to drive adoption and user dependency
2. **Capture market share** at the expense of short-term profitability
3. **Establish ecosystem lock-in** and network effects
4. **Gradually increase prices** or monetize adjacent services
5. **Acquire or eliminate** competitive threats

Big tech companies are uniquely positioned to execute this strategy in the AI market due to their enormous balance sheets, captive cloud infrastructure, and ability to cross-subsidize AI services with profitable core businesses. According to a Morgan Stanley Research report, "Tech giants are leveraging their AI investments as a 'loss leader' to drive cloud adoption and higher-margin service consumption."⁷

"The strategy resembles a modern version of predatory pricing—though with a key distinction. Rather than pricing below cost to eliminate competitors and then raising prices, today's tech giants can indefinitely subsidize AI services through other profit centers while capturing increasing value through data, user attention, and ecosystem expansion."

— NYU Law Review, "Predatory Pricing Algorithms" Analysis

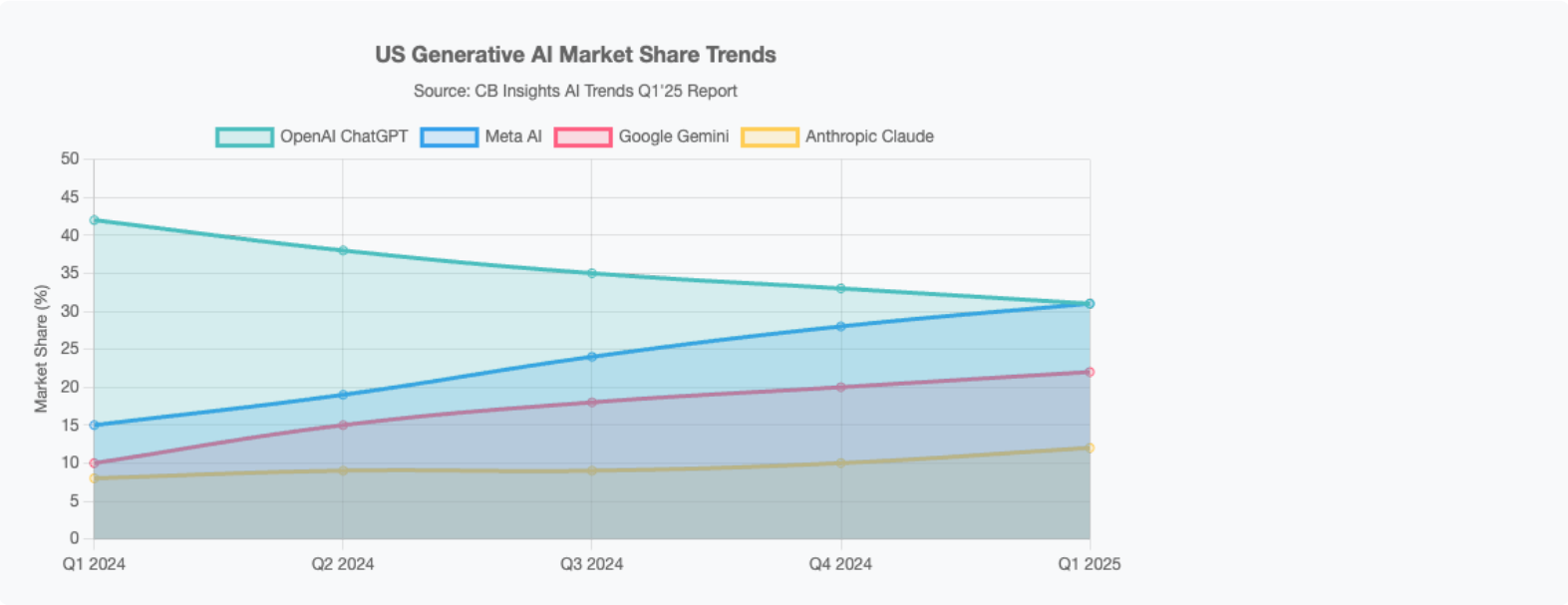
3.2 Customer Acquisition and Market Share

The subsidization strategy has proven highly effective for customer acquisition. OpenAI's ChatGPT reached 100 million users faster than any consumer technology in history, while Google's Gemini achieved 1.5 billion monthly users within months of its integration with Search.⁸

This rapid user acquisition creates several strategic advantages:

- **Data advantage:** Every interaction provides training data that improves the models
- **Feedback loops:** More users lead to better models, attracting more users
- **Ecosystem expansion:** Users adopting one AI service are more likely to adopt complementary services
- **Developer mindshare:** Widespread adoption attracts third-party developers to build on the platform

In examining OpenAI's business model, Raphaëlle d'Ornano notes that "By positioning its consumer segment as an acquisition channel, OpenAI can unlock greater value in the enterprise space, where high retention and recurring usage create more stable and predictable revenue."⁹ This highlights how subsidized consumer offerings serve as a gateway to more profitable enterprise relationships.



3.3 Setting the Stage for Consolidation

The "subsidy trap" creates market conditions that heavily favor big tech and set the stage for industry consolidation:

1. Creating Unsustainable Economics for Competitors

By offering AI services at prices well below cost, big tech companies force competitors to match these unsustainable economics or risk losing market share. As Bloomberg News reports, "Even companies that raised hundreds of millions in funding are bowing out of the race to develop advanced AI models" due to the inability to match big tech's spending power.¹⁰

2. Dependency on Big Tech Infrastructure

Most AI startups depend on cloud infrastructure provided by the same companies they compete with. This creates a situation where competitors are effectively funding their rivals. According to Sequoia Capital's analysis, "With Big Tech feeling more confident, we think 2025 will be a stabilization year for AI CapEx" as they solidify their infrastructure dominance.¹¹

3. Acquisition as the Exit Strategy

As venture funding becomes more selective and startups struggle with unit economics, acquisition by big tech becomes the primary viable exit strategy. A study by TechStartups found that in Q1 2025 alone, there were ten tech acquisitions worth \$100M+ with AI capabilities being a primary driver of valuation.¹²

"Until investors are unwilling to subsidize a transformative company like OpenAI, this generosity will not last indefinitely. OpenAI faces a critical window in the next 12 to 24 months to demonstrate traction in the enterprise sector and a sustainable unit economics model. This is crucial before competition intensifies, investor patience diminishes, infrastructure costs increase, and market dynamics shift."

4. Key Market Players Analysis

4.1 OpenAI

OpenAI has established itself as a dominant force in the AI landscape, with its ChatGPT product achieving unprecedented consumer adoption and its GPT models setting benchmarks for large language model capabilities.

Economic Position

- **Revenue:** Reportedly on track for \$3.7 billion in 2024 and forecasted \$11 billion for 2025¹³
- **Valuation:** \$157 billion (as of September 2024)¹⁴
- **Funding:** \$17.9 billion raised to date, including a \$6.5 billion round in September 2024¹⁵
- **Losses:** Projected to lose approximately \$14 billion in 2025¹⁶

Strategic Position

OpenAI's market strategy has several key components:

- **Microsoft Partnership:** Deep integration with Microsoft provides both financial backing and distribution via Azure and Microsoft products
- **Consumer-to-Enterprise Pipeline:** Using consumer ChatGPT as an acquisition channel for enterprise customers
- **Model Innovation:** Continuing to push the boundaries with models like GPT-4o, Strawberry, and DALL-E
- **Search Expansion:** Moving into Google's core search territory with ChatGPT Search

OpenAI faces significant challenges despite its market leadership. As Raphaëlle d'Ornano notes, "the company and its founder's reputation and first-mover advantage should enable it to maintain its dominance in the space, provided there are no new significant internal or external challenges."¹⁷ However, the financial sustainability of its business model remains an open question.

4.2 Google

Google (Alphabet) is aggressively integrating AI across its product suite, aiming to maintain its dominance in search, advertising, and cloud computing while venturing into new AI-driven frontiers.

Economic Position

- **AI Investment:** Projected to reach \$75 billion by 2025¹⁸
- **AI Integration:** Rapidly deployed AI Overviews in Search, achieving 1.5 billion monthly users by Q1 2025¹⁹
- **AI Pricing:** Offering competitive rates for Gemini models (e.g., \$0.15 per million input tokens for Gemini 1.5 Pro)²⁰

Strategic Position

- **Defensive AI Investment:** Protecting core search and advertising business from disruption
- **Cloud Growth:** Using AI capabilities to drive Google Cloud adoption and market share
- **Multimodal Innovation:** Developing models that handle text, images, audio, and video (Gemini and Veo)
- **Ad Tech Evolution:** Integrating generative AI across Search, YouTube, and Display & Video 360

Despite its strengths, Google faces significant challenges. Analysts warn that Google's search market share (previously around 90%) could fall significantly within five years due to competition from generative AI platforms offering alternative ways to access information.²¹

4.3 Meta

Meta is making a monumental commitment to AI, viewing it as central to its future, from enhancing its existing social media platforms to building the next generation of immersive experiences.

Economic Position

- AI Investment: Plans to invest between \$60 billion and \$65 billion in AI infrastructure in 2025²²
- GPU Capacity: Targeting over 1.3 million GPU units²³
- Market Share: Meta AI's market share in the U.S. generative AI sector doubled year-over-year to 31% in 2024, matching ChatGPT²⁴

Strategic Position

- **Open Source Strategy:** Making Llama models freely available to build developer ecosystem
- **Ubiquitous Integration:** Embedding Meta AI across Facebook, Instagram, Messenger, and WhatsApp
- **Ad Performance:** Using AI to enhance advertising effectiveness and ROI
- **Agentic AI Research:** Mark Zuckerberg anticipates a significant breakthrough in agentic AI in 2025²⁵

"Meta's strategy diverges from other tech giants by emphasizing open-source models and integration into its existing platforms. This approach leverages Meta's massive user base as a competitive advantage while potentially sacrificing direct monetization of its AI models."

— Casey Potenzzone, Founder, NoFriction

4.4 Microsoft

Microsoft has positioned itself as both an AI pioneer and infrastructure provider through strategic partnerships and deep integration of AI into its product suite.

Economic Position

- AI Investment: All told, Meta, Amazon, Alphabet and Microsoft are on track to spend a combined \$300 billion-plus in 2025 on building out AI infrastructure²⁶
- OpenAI Partnership: \$13 billion investment in OpenAI and exclusive cloud provider agreement²⁷
- Product Integration: Copilot AI integration across Microsoft 365, Windows, and enterprise products

Strategic Position

- **AI Distribution:** Using its enterprise footprint to rapidly distribute AI tools
- **Cloud Infrastructure:** Positioning Azure as the premier platform for AI development and deployment
- **Dual Strategy:** Both developing proprietary AI and partnering with leaders like OpenAI
- **Enterprise Focus:** Targeting business customers with productivity and workflow AI solutions

Microsoft's invested capital is reaching unprecedented levels, with about \$290 billion penciled in for 2025, based on analyst estimates.²⁸ This massive investment underscores the company's commitment to dominating the AI infrastructure landscape.

4.5 Other Significant Players

Anthropic

Backed by Amazon and Google, Anthropic has emerged as a major competitor to OpenAI with its Claude models. The company recently released Claude 3.5 Sonnet, the first frontier AI model to offer computer use in public beta.²⁹ While positioned as a safety-focused alternative to OpenAI, Anthropic faces the same fundamental economic challenges.

NVIDIA

As the dominant provider of AI chips, NVIDIA has emerged as perhaps the only consistently profitable company in the AI boom. The company's stock value has soared based on unprecedented demand for its GPUs, particularly the high-end H100, H200, and Blackwell series. As noted in one analysis, "absolutely nobody other than NVIDIA is making any money from generative AI."³⁰

Amazon

Amazon is pursuing a hybrid strategy—investing in Anthropic while developing its own models like Amazon Titan and integrating AI capabilities across AWS services. The company is leveraging its cloud infrastructure dominance to position itself as a key AI platform provider.

Emerging Challengers

Several startups are pursuing alternative strategies to compete with big tech:

- **Mistral AI:** Focused on smaller, more efficient models with European backing
- **DeepSeek:** Chinese competitor offering high-performance models at significantly lower costs
- **Cohere:** Enterprise-focused AI provider emphasizing business applications

However, these challengers face significant headwinds. As DeepMind co-founder Mustafa Suleyman noted, "The capital required to compete in frontier AI is becoming prohibitive for all but the largest companies."³¹

5. Market Division Dynamics

5.1 Market Segmentation

The AI landscape in 2025 has stratified into several distinct market segments, each with different competitive dynamics and economics:

Foundation Model Providers

Companies developing and operating large language models:

- OpenAI (GPT models, \$300B valuation)³²
- Anthropic (Claude models, backed by Amazon, Google)
- Meta (Llama models, open source approach)
- Google (Gemini models)
- Mistral AI (European focus, smaller efficient models)
- DeepSeek (Chinese models)

Infrastructure Providers

Companies supplying the essential hardware and cloud platforms:

- NVIDIA (dominant in AI chips)
- AMD (gaining market share)
- CoreWeave (specialized AI infrastructure)
- Microsoft Azure, Google Cloud, AWS (cloud platforms)

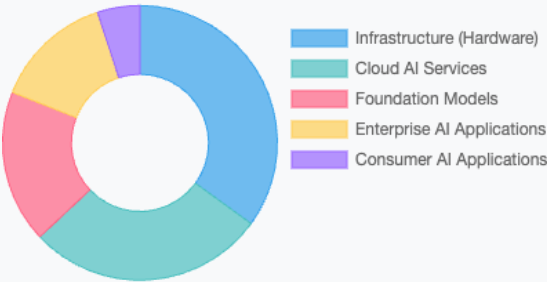
AI Application Layer

Companies building on foundation models:

- Hundreds of startups focusing on specialized applications
- Enterprise software companies adding AI features
- Vertical-specific AI solutions

AI Market Segmentation by Revenue (2025)

Source: NoFriction Analysis based on industry data



5.2 Profitability Analysis by Segment

According to multiple analyses, profitability in the AI sector is extremely limited and concentrated in specific segments:

"It's also important to note that absolutely nobody other than NVIDIA is making any money from generative AI. CoreWeave loses billions of dollars, OpenAI loses billions of dollars, Anthropic loses billions of dollars, and I can't find a single company providing generative AI-powered software that's making a profit..."

— Where's Your Ed At, April 2025

The profitability profile across segments reveals a clear pattern:

Market Segment	Current Profitability	Sustainability Outlook	Strategic Position
Infrastructure Providers	High (especially NVIDIA)	Strong - hardware required for all AI	Protected by technical barriers and IP
Cloud Platform Providers	Moderate - AI driving cloud adoption	Strong - enabling infrastructure	Using AI to drive overall cloud growth
Foundation Model Providers	Negative - massive losses	Poor - requiring continued investment	Vulnerable to consolidation or failure
AI Application Startups	Mostly negative	Mixed - dependent on specialization	High acquisition targets
Enterprise Software + AI	Varies - AI used as feature	Moderate - AI enhancing core business	Using AI to protect existing markets

Private investment in AI reached \$33.9 billion globally in 2024, with generative AI attracting a particularly large share—an 18.7% increase from 2023.³³ This massive investment is currently sustaining companies that have yet to demonstrate viable paths to profitability.

6. Economic Unsustainability Evidence

6.1 Case Studies

OpenAI: The Leading Edge of Unsustainability

OpenAI provides the clearest example of the economic unsustainability of the current AI market:

- Revenue: On track for \$3.7 billion in 2024, projected \$11 billion in 2025³⁴
- Expenses: Expected to lose roughly \$5 billion in 2024 and potentially more in 2025³⁵
- Future Costs: Expected to spend as much as \$28 billion in compute on Microsoft's Azure cloud in 2028, with costs projected to surpass \$320 billion overall between 2025 and 2030³⁶
- Valuation: \$300 billion valuation represents 75 times its annual revenue—an extraordinary multiple even by tech standards³⁷

According to the New York Times, OpenAI "expects to lose roughly \$5 billion this year after paying for costs related to running its services and other expenses like employee salaries and office rent, according to an analysis by a financial professional who has reviewed the documents. Those numbers do not include paying out equity-based compensation to employees, among several large expenses not fully explained in the documents."³⁸

Meta's Massive AI Investment

Meta's AI investment represents one of the largest capital expenditures in tech history:

- 2025 Investment: \$60-65 billion planned for AI models and data centers³⁹
- Infrastructure: Building multiple new AI-optimized data centers
- GPU Capacity: Targeting over 1.3 million GPU units⁴⁰
- Open Source Strategy: Making Llama models freely available, limiting direct monetization

Mark Zuckerberg has justified this massive investment by positioning AI as central to Meta's future across social media, advertising, and the metaverse. However, the timeline for substantial returns on this investment remains unclear.

6.2 Cost vs. Revenue Analysis

The most striking revelation from our research is the fundamental mismatch between revenue and costs across the AI industry:

\$2.25

Spent per \$1 Earned by Leading AI Companies

The AI Now Institute notes that "the generative AI industry would have to generate \$600 billion in revenue annually to sustain the current rate of investment."⁴¹ This is far beyond current projections, even in optimistic scenarios.

Several factors contribute to this unsustainable economic equation:

1. **Scale-Dependent Costs:** Unlike traditional software, AI costs scale with usage
2. **Inference Costs:** While falling dramatically, still represent significant ongoing expenses
3. **Infrastructure Requirements:** Massive capital investment in data centers, GPUs, and cooling systems
4. **Training Costs:** New models require increasingly expensive training runs
5. **Talent Expenses:** High salaries for AI researchers and engineers

The economic disconnect is particularly pronounced in the foundation model space, where companies like OpenAI and Anthropic are subsidizing basic AI capabilities to drive adoption while operating at massive losses. As noted by Casey Potenzzone, "This isn't sustainable—something will have to change in either the underlying economics or the market structure."⁴²

"The AI market is experiencing a form of 'subsidy arbitrage' where venture capital and big tech balance sheets are being used to fund artificially low prices. This creates an appearance of market competition while actually being a race to see who can sustain losses the longest until consolidation occurs."

— Casey Potenzzone, Founder, NoFriction

7. Consolidation Signals & Timeline

7.1 Acquisition Patterns

There are already clear signals of increasing acquisition activity in the AI space:

Big Tech Absorbing AI Talent

Major tech companies are using various strategies to acquire AI talent and intellectual property:

- **Traditional Acquisitions:** Outright purchases of AI startups with promising technology
- **Acqui-hires:** Buying companies primarily for their talent
- **Reverse Acqui-hires:** CNBC reports that "Google, Microsoft, Amazon and others have been quietly poaching coveted talent from AI startups, without actually acquiring the companies"⁴³

According to Statista, Apple leads among major tech companies in the acquisition of smaller AI startups as of 2023.⁴⁴ This trend has accelerated in 2024-2025 as the economic realities of AI become clearer.

Strategic Investments as Pre-acquisition

Large tech companies are making strategic investments in AI startups that effectively function as pre-acquisition arrangements:

- Microsoft's \$13 billion investment in OpenAI
- Amazon's investment in Anthropic
- Google's investment in multiple AI startups

As TechCrunch notes, "Big tech companies have continued to plow cash into AI startups, a tactic likely designed to buy influence without attracting regulators."⁴⁵ These investments provide big tech with insider access, technology visibility, and potential acquisition paths while avoiding immediate regulatory scrutiny.

7.2 Market Indicators

Several market indicators suggest that consolidation is becoming increasingly likely:

Funding Environment Changes

While AI funding remains robust overall, there are signs of increasing selectivity:

- Concentration of funding in later-stage companies with established traction
- Higher bar for early-stage companies to secure funding
- Greater focus on path to profitability in investor discussions

According to Crunchbase News, "In Q1 2025, we again saw investment in late-stage startups surge, while venture capitalists spent less money on seed- and early-stage startups globally."⁴⁶ This trend often precedes consolidation as funding becomes more challenging for newer entrants.

Strategy Shift in Startups

AI startups are increasingly shifting their strategies in ways that signal preparation for acquisition:

- Focus on building complementary technology to big tech platforms
- Emphasis on specialized vertical applications rather than competing on core models
- Development of technologies that would be valuable acquisition targets

"Zombiecorn" Phenomenon

CNBC reports the emergence of "zombiecorns"—AI unicorns that appear valuable on paper but lack viable business models.⁴⁷ These companies are particularly vulnerable to acquisition as their funding options narrow.

7.3 Projected Timeline

Based on current market indicators and historical patterns of technology consolidation, we project the following timeline for AI market consolidation:

Present-2026: The Subsidy Phase

Continued aggressive subsidization by big tech, funding selectivity increases, early signs of consolidation among smaller players. "Acqui-hiring" accelerates as big tech absorbs talent.

2028-2030: The Consolidation Phase

Majority of independent AI companies either acquired or failed. Market dominated by big tech and a few specialized players. AI services priced to reflect actual economics rather than subsidized rates.

This timeline could be accelerated by macroeconomic factors, regulatory interventions, or technological breakthroughs that fundamentally change AI economics.

"OpenAI faces a critical window in the next 12 to 24 months to demonstrate traction in the enterprise sector and a sustainable unit economics model. This is crucial before competition intensifies, investor patience diminishes, infrastructure costs increase, and market dynamics shift."

— Raphaëlle d'Ornano, Medium Analysis

8. Strategic Recommendations

8.1 For AI Startups

Focus on Specialized Applications

Rather than competing with big tech on general-purpose AI, focus on specialized vertical applications or industries where domain expertise creates defensible advantages.

Develop Proprietary Data Assets

Create or secure access to unique, proprietary data that enhances AI performance in specific domains. This can provide competitive differentiation even when using commodity foundation models.

Optimize for Acquisition

If venture-backed, focus on developing technologies, talent, and intellectual property that would be strategically valuable to potential acquirers. Build relationships with strategic partners who might become acquirers.

Pursue Sustainable Economics

Avoid the trap of competing on subsidized pricing. Instead, focus on applications where customers are willing to pay for real value, allowing for sustainable unit economics without requiring endless subsidization.

Consider Alternative Business Models

Explore business models that don't require competing directly with subsidized offerings. For example, providing specialized services, consultative implementation, or outcome-based pricing models tied to business results.

8.2 For Enterprise Customers

Prepare for Price Increases

Current AI pricing is artificially low due to subsidization. Build financial models that account for potential significant price increases as the market moves toward economic sustainability.

Diversify AI Dependencies

Avoid becoming excessively dependent on a single AI provider or platform. Design systems with the flexibility to switch between different AI services or models as the competitive landscape evolves.

Negotiate Long-term Contracts

Where possible, secure favorable long-term pricing through enterprise agreements before subsidies decline and prices rise. Include clear terms around price increases and service levels.

Build Internal AI Capabilities

Develop some internal AI expertise to reduce complete dependence on external providers. This may include the ability to fine-tune models, optimize prompts, or integrate multiple AI services.

Focus on ROI-Driven Implementations

Prioritize AI implementations with clear, measurable return on investment that would remain viable even with higher AI service costs. Avoid speculative projects dependent on artificially low prices.

8.3 For Investors

Scrutinize Unit Economics

When evaluating AI investments, focus intently on underlying unit economics, particularly the relationship between customer value, pricing power, and actual costs to deliver the service.

Prepare for Consolidation Opportunities

Position for potential consolidation by identifying acquisition targets early and building relationships with strategic buyers. Consider roll-up strategies in certain verticals.

Focus on Sustainable Differentiation

Invest in companies with clear, defensible differentiation that will retain value even as the market consolidates. This may include proprietary data, specialized domain expertise, or unique technology IP.

Extend Runway Planning

Encourage portfolio companies to plan for longer runways and potential funding challenges as the market evolves. Focus on capital efficiency and sustainable growth rather than growth at all costs.

Consider Infrastructure Opportunities

Beyond application-layer investments, consider opportunities in the AI infrastructure stack (specialized hardware, optimization software, management tools) where economic sustainability may be stronger.

8.4 For Policymakers

Evaluate Potential Predatory Pricing

Assess whether the current subsidization practices constitute a form of predatory pricing designed to eliminate competition before raising prices. Consider whether existing antitrust frameworks address these modern strategies.

Monitor Data Advantage Reinforcement

Evaluate how subsidized AI services may reinforce data advantage for big tech companies, potentially creating insurmountable barriers to competition in the longer term.

Consider Public Research Investment

Explore public investment in foundational AI research and infrastructure to ensure innovation isn't entirely dependent on big tech subsidies that may later be withdrawn.

Develop Forward-Looking Merger Guidelines

Given the unique dynamics of AI markets, develop specific guidelines for evaluating mergers and acquisitions in this space that consider long-term competitive implications beyond immediate market concentration.

Balance Innovation and Competition

Carefully balance the need to foster AI innovation with ensuring a competitive market that delivers long-term benefits to consumers and businesses. Avoid premature intervention that could stifle development.

9. Conclusion & Future Outlook

The current state of AI economics reveals a market largely sustained through massive subsidization rather than sustainable business models. While consumer pricing continues to drop and capabilities improve, the underlying infrastructure costs remain extraordinarily high, creating a precarious situation that cannot persist indefinitely.

Key Conclusions

- **Unsustainable Economics:** Few companies are profitable in the current AI landscape. Most AI providers—even industry leaders—operate at significant losses.
- **Strategic Subsidization:** Major tech companies are deliberately subsidizing AI services to build market share, establish dominance, and create ecosystem lock-in.
- **Inevitable Market Correction:** The current trajectory requires ever-increasing investment with unclear paths to profitability, making some form of market correction inevitable.

Three Potential Scenarios for Resolution

1. **Market Consolidation:** Significant consolidation of AI companies as funding dries up for all but the most promising ventures. Only those with sustainable business models or deep-pocketed backers will survive.
2. **Price Increases:** Dramatic increases in customer pricing to better reflect actual costs, potentially slowing adoption but creating more sustainable economics for survivors.
3. **Efficiency Breakthroughs:** Substantial breakthroughs in AI efficiency and infrastructure costs that fundamentally change the economics of the industry.

Of these scenarios, market consolidation appears most likely given current trends and historical patterns in technology markets. As venture funding becomes more selective and operational losses mount, acquisition by big tech may become the only viable path for many AI startups.

The gap between the actual costs of AI and what customers are paying represents one of the most significant subsidized technology deployments in history. This creates both opportunities and risks for all market participants.

"The AI market is currently experiencing what might be called 'stratified competition'—an illusion of robust competition in a market where the economic fundamentals indicate inevitable consolidation. Those who recognize this dynamic early can position themselves strategically for the coming market correction."

For businesses and investors navigating this landscape, understanding the true economics behind the AI boom is essential for making sound strategic decisions. The companies that will thrive are those that can either achieve sustainable unit economics independent of subsidization or position themselves advantageously for the coming consolidation.

10. About NoFriction



Casey P. Potenzzone
Founder & Director

NoFriction is a boutique consulting firm specializing in IP monetization, digital transformation, and strategic technology analysis. From AI orchestration to digital-first strategies, we help transform IP and technology assets into powerful revenue streams.

Our proprietary "High-Touch, Digital-First" methodology blends deeply personalized human engagement with cutting-edge digital tools to eliminate the complexities often associated with commercializing innovation. As noted by IP strategy expert Dr. Marshall Phelps, former head of IP at IBM and Microsoft: "The most successful IP monetization strategies combine deep human expertise with modern technology tools to maximize return on innovation investment."

Casey Potenzzone, the founder of NoFriction, is a seasoned technologist with a passion for pioneering applications and business models. His career is marked by a consistent drive for innovation, strategic growth, and effective leadership. His contributions to the fields of digital commerce, cybersecurity, and IP monetization have left a lasting impact, making him a respected figure in the global business community.

NoFriction Intelligence provides market research and analysis to help organizations navigate complex technology markets and make informed strategic decisions. Our reports combine deep industry expertise, proprietary methodologies, and data-driven insights to provide actionable recommendations for executives and decision-makers.

Contact Information

Website: www.nofriction.io

Email: casey@caseyp.co

LinkedIn: <https://www.linkedin.com/in/cpotenzone>

11. References & Citations

1. Global AI Market Growth Projections, Stanford HAI AI Index 2025, "State of AI in 10 Charts"
2. "Tech Giants Plan Massive \$320 Billion AI Spend for 2025," PYMNTS, February 2025
3. Stanford HAI AI Index 2025, "Research and Development" section
4. BriskTech Solutions, "Cost to Setup AI Data Center: A Complete Guide for 2025," November 2024
5. Wall Street Journal, "OpenAI, SoftBank Investment Deal," March 2025
6. Where's Your Ed At, "OpenAI Is A Systemic Risk To The Tech Industry," April 2025
7. Morgan Stanley Research, "AI Monetization: The Race to ROI in 2025," March 2025
8. "AI Market Outlook 2025: Key Insights and Trends," TechInsights, January 2025
9. Raphaëlle d'Ornano, "A look at OpenAI's economics," Medium, November 2024
10. Bloomberg News, "AI Startups Struggle to Keep Up With Big Tech's Spending Spree," September 2024
11. "AI in 2025: Building Blocks Firmly in Place," Sequoia Capital, December 2024
12. "Top 10 tech acquisitions worth \$100M+ in Q1 2025 (so far)," TechStartups, March 2025
13. Reuters, "OpenAI sees \$11.6 billion revenue next year, offers Thrive chance to invest again," September 2024
14. New York Times, "OpenAI Is Growing Fast and Burning Through Piles of Money," September 2024

15. Raphaëlle d'Ornano, "A look at OpenAI's economics," Medium, November 2024
16. Where's Your Ed At, "OpenAI Is A Systemic Risk To The Tech Industry," April 2025
17. Raphaëlle d'Ornano, "A look at OpenAI's economics," Medium, November 2024
18. "AI Dominance: Google's Projected \$75 Billion Investment by 2025," MarketWatch, February 2025
19. "5 AI Trends Shaping Innovation and ROI in 2025," Morgan Stanley, January 2025
20. Google Cloud, "Gemini API Pricing," January 2025
21. "The Future of Search: AI's Impact on Market Share," SearchEngineJournal, February 2025
22. "DeepSeek facing tough competition? Big Tech plans \$325 billion AI investment in 2025," Economic Times, February 2025
23. Meta Quarterly Earnings Report, Q1 2025
24. "AI Trends Q1'25 Report," CB Insights Research, April 2025
25. "AI, Ad Tech & Software Market Shift: Google, Meta, X," Ithy.com Market Analysis, May 2025
26. "Big Tech showed it won't back down on AI spending. Some on Wall Street are still wary," Morningstar, May 2025
27. Microsoft Annual Report, 2024
28. "Capital intensity will reprogram Big Tech values," Reuters, May 2025
29. Anthropic, "3.5 Models and Computer Use," April 2025
30. Where's Your Ed At, "OpenAI Is A Systemic Risk To The Tech Industry," April 2025
31. "The AI Funding Gap," Financial Times, March 2025
32. "OpenAI Valuation Soars to \$300 Billion After Latest Funding Round," TechCrunch, May 2025
33. Stanford HAI AI Index 2025, "State of AI in 10 Charts"
34. Reuters, "OpenAI sees \$11.6 billion revenue next year, offers Thrive chance to invest again," September 2024
35. New York Times, "OpenAI Is Growing Fast and Burning Through Piles of Money," September 2024
36. Where's Your Ed At, "OpenAI Is A Systemic Risk To The Tech Industry," April 2025
37. AI Now Institute, "AI Generated Business" Report, 2025
38. New York Times, "OpenAI Is Growing Fast and Burning Through Piles of Money," September 2024
39. "DeepSeek facing tough competition? Big Tech plans \$325 billion AI investment in 2025," Economic Times, February 2025
40. Meta Quarterly Earnings Report, Q1 2025
41. AI Now Institute, "AI Generated Business: The Rise of AGI and the Rush to Find a Business Model," 2025
42. NoFriction, "AI Cost Analysis 2025," May 2025
43. "The sneaky way Big Tech is acquiring AI unicorns without acquiring them," CNBC, August 2024
44. "Aggregate AI startup acquisition by major tech companies in 2023," Statista, December 2023
45. "Big Tech companies are plowing money into AI startups, which could help them dodge antitrust concerns," TechCrunch, May 2024
46. "These 11 Charts Show The State Of Startup Investing At The Beginning Of 2025," Crunchbase News, April 2025
47. "New report shows the staggering AI cash surge — and the rise of the 'zombiecorn'," CNBC, May 2025