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David Yarbrough, AAMS®, AIF®

Senior Vice President, Investments

Raymond James

(615) 904-2739 / david.yarbrough@raymondjames.com

100 E Vine St, Suite 310

Murfreesboro, TN 37130

Market Stats & Commentary

Market Vital Signs as of 5/31/2023

Stock Indexes	May	YTD	1 Year
S&P 500	0.43%	9.65%	2.92%
Dow Jones Industrial Average	-3.17%	0.25%	1.96%
NASDAQ Composite	5.80%	23.59%	7.07%
Russell Mid Cap Index	-2.79%	0.61%	-4.51%
Russell 2000 Small Cap Index	-0.92%	-0.04%	-4.68%
MSCI EAFE Developed Int'l Index	-4.23%	6.81%	3.06%
MSCI Emerging Markets Index	-1.68%	1.05%	-8.49%
Bond Indexes			
BBgBarc US Aggregate Bond Index	-1.09%	2.46%	-2.14%
BBgBarc US Corp High Yield Bond Index	-0.93%	3.65%	0.12%
Interest Rates	5/31/23	12/31/22	5/31/2022
Fed Funds Target Range	5.00%-5.25%	4.25-4.50%	.75%-1.00%
10 Yr U.S. Treasury Rate	3.63%	3.84%	2.84%

Data courtesy of Raymond James

May was a mega cap tech kind of month. The NASDAQ had a big month which kept the S&P 500 in the green for May. Unfortunately, the rest of the equity indexes were not so positive. Concerns of slower economic growth globally and the tempering of hopes for multiple Fed interest cuts in Q4 2023 kept most domestic and international indexes decidedly negative for the month.

At this point, you may be asking why there was such a large disparity of returns between the NASDAQ and everything else. There are two very simple reasons. The first is a two-letter acronym – A.I. - more on that in a bit…

The second is that the NASDAQ composite index is extremely concentrated in a few companies (see table 1 to the right) – most of which are leaders or involved in A.I. As you can see, if Microsoft, Nvidia, Alphabet, and Meta have good months – the NASDAQ is going to have a good month.

Table 1 **NASDAQ Composite**

TOP 10 COMPONENTS BY WEIGHT

TICKER	NAME	WEIGHT
AAPL	APPLE INC.	13.21%
MSFT	MICROSOFT CORP	10.87%
AMZN	AMAZON.COM INC	5.36%
NVDA	NVIDIA CORPORATION	3.47%
TSLA	TESLA INC.	3.32%
GOOG	ALPHABET CL C CAP	3.14%
GOOGL	ALPHABET CL A CMN	3.13%
META	META PLATFORMS INC.	2.39%
AVGO	BROADCOM INC.	1.35%
PEP	PEPSICO INC	1.27%

All Information as of 03/31/2023. *Data provided by NASDAQ OMX*

Bond indexes were down for May, driven by interest rates creeping a bit higher. Continued strength in the labor market and comments out of a few Fed governors made market participants rethink their view of multiple rate cuts in Q4. As I said last month, I think the 3 cuts anticipated by the market a month ago was too optimistic. I do, however, still see possibility for one rate cut by the end of the year.

Artificial Intelligence – The Topic Du Jour

Artificial Intelligence has been around a while now, helping humans find things (think Google search) and do things (think robotic assembly lines) or even turn your TV on (think amazon Alexa). We are now used to those things, and they don't seem too scary at this point. However, the type of A.I. that is in focus these days is different – it is "generative" and language based. This means it can scan enormous amounts of data in milliseconds **and generate a statement, an answer, or even its creation** rather than just track down information that may be relevant to your search or question. In other words – it thinks, it learns, and it expresses itself.

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I learned several things from movies growing up in the 80's and 90's. Ferris Buehler taught me how to ditch school, Clark Griswald taught me the meaning of a family Christmas, and The Terminator and The Matrix taught me that machines thinking on their own was bad. Really bad.

Is this the rise of the machines?

To be honest, **no one** knows. I was recently on a Zoom talk put on by Harvard Business School which discussed this issue, as well as the possible economic implications of generative A.I. Governments and the scientific community both realize the potential for good and bad outcomes of generative A.I. and there seems to be consensus forming around some sort of regulatory framework, with first priority being that it should be *"human centric"*. This means being mindful of not just a rise of the machines type scenario but also how it could fundamentally change employment prospects for tens of millions of people worldwide.

But before you get too nervous, be aware that the current generative A.I. leaders – Chat GPT and Alphabet's Bard – have a problem. An accuracy problem, actually. Turns out that machines, like humans, can get things wrong. And when they do, they exhibit another human trait of doubling down on wrong answers. I suspect that this issue works itself out over time, but for now it is a real barrier to A.I. actually replacing lots of jobs.

Now for the question on everyone's mind – what does all this mean for my investments?

As with all prior industrial or technological revolutions, this one will create new businesses, kill off some old businesses, and make many industries more efficient. It is also important to remember that generative A.I. is still in its infancy and its course is completely unpredictable at this point. It will most certainly be a big deal and there will be winners, but the road will also be littered with lots of losers along the way. It happened with the railroads, then automobiles, then the birth of the internet and e commerce and I'm guessing it will happen with A.I. as well.

On the HBS Zoom talk I mentioned before, the host discussed areas he sees of opportunity: providers of A.I. programs (Microsoft, Alphabet, Meta) – healthcare, where A.I. apps aid doctors in diagnosing symptoms - and biotech, where A.I. programs can analyze enormous amounts of data to speed along drug research. There are also a few well-funded start-up chip companies to challenge Nvidia, AMD and other established names. And don't forget that someone has to power all these machines, so electric grids and power plants may need capital investment to keep up with demand.

There will also be areas that are negatively affected – primarily certain areas of the labor market. As generative A.I. gets better it will undoubtedly replace humans in some jobs. I've read a few different articles listing certain jobs that have a high probability of risk and those include copy writers, legal researchers and data analysts. On the flip side, there are certain jobs that computers can't do (at least yet) like what we think of as skilled trades – plumbers, electricians, builders, etc. However, I did hear about a robotic brick mason a couple years ago (https://www.youtube.com/watch?v=6s17IAj-XpU)... I would also add healthcare services to the list. If you are in the hospital, it is highly unlikely that your nurse or doctor is a robot. They might be assisted by robots in new ways, but it is hard to see them replaced by robots.

From an investment standpoint, I think it is not so important to directly invest in A.I. focused companies, as I think it will create efficiencies across numerous industries which will lead to increased profitability and net earnings. I do think, however, that investors will want to avoid sectors that are vulnerable to becoming obsolete. Think of it as winning by not losing.

David

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Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary.

Index Descriptions

S&P 500: Representing approximately 80% of the investable U.S. equity market, the S&P 500 measures changes in stock market conditions based on the average performance of 500 widely held common stocks. It is a market-weighted index calculated on a total return basis with dividend reinvested.

Dow Jones Industrial Average Total Return: The Dow Jones Industrial Average is a composite of 30 stocks spread among a wide variety of industries, such as financial services, industrials, consumer services, technology, health care, oil & gas, consumer goods, telecommunications, and basic materials. The index represents approximately 23.8% of the U.S. market, and is price weighted (component weightings are affected by changes in the stocks' prices). Maintained by the Averages Committee, components are added and deleted on an as-needed basis.

Russell Midcap: A subset of the Russell 1000 index, the Russell Midcap index measures the performance of the mid-cap segment of the U.S. equity universe. Based on a combination of their market cap and current index membership, includes approximately 800 of the smallest securities which represents approximately 31% of the total market capitalization of the Russell 1000 companies. The index is created to provide a full and unbiased indicator of the mid-cap segment.

Russell 2000: Based on a combination of their market cap and current index membership, this index is comprised of approximately 2,000 of the smaller securities from the Russell 3000. Representing approximately 10% of the Russell 3000, the index is created to provide a full and unbiased indicator of the small cap segment.

MSCI EAFE (Europe, Australasia, Far East) Index: A free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada. As of June 2, 2014, the index consists of 21 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

MSCI Emerging Market Index: A free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. As of June 2, 2014, the index consists of the following 23 emerging market country indices: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Peru, Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey, and the United Arab Emirates.

Bloomberg Barclays U.S. Aggregate (BCAG): A representation of SEC-registered, taxable, and dollar denominated securities. The index covers the U.S. investment grade fixed rate bond market, with index components for asset-backed securities, government and corporate securities, and mortgage pass-through securities. Must be rated investment grade (Baa3/BBB- or higher) by at least two of the following rating agencies: Moody's, S&P, Fitch; regardless of call features have at least one year to final maturity, and have an outstanding par value amount of at least $250 million.

Bloomberg Barclays U.S. Corporate High Yield: Covers the universe of fixed rate, non-investment grade debt which includes corporate (Industrial, Utility, and Finance both U.S. and non-U.S. corporations) and non-corporate sectors. The index also includes Eurobonds and debt issues from countries designated as emerging markets (sovereign rating of Baa1/BBB+/BBB+ and below using the middle of Moody's, S&P, and Fitch) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included. Must publicly issue, dollar-denominated and non-convertible, fixed rate (may carry a coupon that steps up or changes according to a predetermined schedule), and be rated high-yield (Ba1 or BB+ or lower) by at least two of the following: Moody's, S&P, and Fitch. Also, must have an outstanding par value of at least $150 million and regardless of call features have at least one year to final maturity.