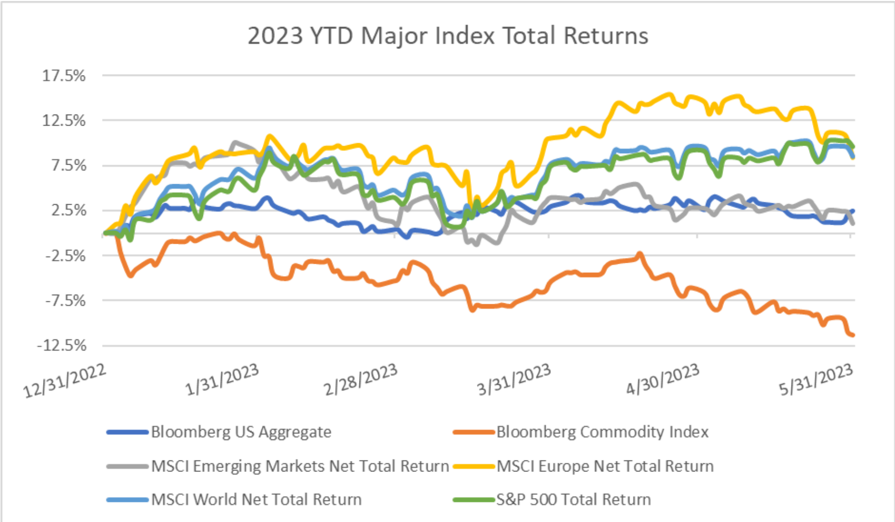
MAY 2023 MARKET REVIEW

Market Recap: There is an adage in markets that says, "sell in May and go away", as historical data suggests that portfolios tend to perform better in the first half of the year. While we typically ignore overly simplistic rules of thumb like this (as each market environment and client portfolio is unique), these mindsets can be self-fulfilling and can truly affect investment outcomes. Investment markets continue to act resiliently, rewarding those who remained invested following a dismal 2022, and frustrating the wide swath of economists who have called for a recession and coinciding market selloff. It is easy to understand why many have quite negative outlooks at the moment – various data points are flashing red, which have historically been precursors to recessions. The fact that there is such economic pessimism can also prove to be self-fulfilling, affecting spending, consumption, employment, and thus, economic growth. Despite these seasonal pressures and widespread cynicism, equity markets continue to march higher.

Portfolios have surely outperformed many clients' initial 2023 expectations. Through the end of May, US equities have returned over 9.5% and US bonds have returned 2.5%; and, while both markets are below their early 2022 levels, they have recovered nicely over the past 8 months. As we have touched on in prior months, many assets that struggled last year have performed significantly better in 2023. Technology companies were hit hard in 2022 after a stellar multi-year run, but have now regained their form; this time led by companies that are innovating in the artificial intelligence (AI) space across software, hardware, and chipmakers. The question that portfolio managers are facing currently is whether we are in another technology bubble (a lá first-generation internet companies), or if we are in the early stage of an AI boom that can overcome already expensive valuations.

Recently, there has been a massive amount of investment geared towards the development of AI, most notably Microsoft's $10B+ investment in OpenAI, the company behind ChatGPT. These types of technologies have the potential to alter most (if not all) parts of the economy, increasing efficiency and accelerating GDP growth. The best performing companies in the S&P 500 so far this year (NVIDIA, Meta, and Advanced Micro Devices) are all innovating towards AI solutions and have on average returned over 120%.

How does this impact our perspective? The future for companies operating within the AI ecosystem offers the opportunity to drive outsized returns, and the hype seems legitimate to us given the applicability and potential use cases across many industries. According to Apple, one of these use cases is blending digital content with our physical space, which the company discussed in their "Vision Pro" device launch last week. Whether consumers are willing to spend over $3k to sit on their couch and watch TV through high end goggles is, however, a major uncertainty. Our investment process often results in rebalancing portfolios back to asset allocation targets on the heels of outsized market moves. A good example of this is when we added to equities during the downturn in markets through much of 2022, and trimmed certain positions during the ensuing rally that has continued through May. Therefore, while there is a potential for large gains in companies driving innovation, the prudent decision is to trim positions, take profits, and reallocate funds to portions of the portfolio that have not fared as well. There will surely be winners and losers in the AI arms race, just like any other market, however the blue-sky scenario is that these technological advances have the ability to improve overall portfolio returns, rather than just increase the value of a handful of individual companies.



Data Source: Y Charts

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