BRIAN D. LOWDER, INC.

QUARTERLY NEWSLETTER

Volume 26, Issue 2 July 2023

INSIDE THIS ISSUE

FINANCIAL MARKET OVERVIEW

At first glance, the 2023 year-to-date performance of stocks is spectacular. The overall stock market index is up over 16% and the S&P 500 stock index was up 16.78% during the first half of 2023 compared to a negative 20% or more during 2022. The NASDAQ stock index, which is dominated by technology stocks, was up 32%. If we combine only eight large technology stocks - Apple stock (up 48% year-to-date), Nvidia stock, (up 189% year-to-date) and six other large tech stocks- those eight stocks combined were up 85% during the first half of 2023.

However, the average stock in the S&P 500 index was up only 6%, the Dow Jones Industrial Average rose less than 4% and the small-company stock Index, the Russel 2000, was up 7% through June 30, 2023.

Large-company ***growth*** stocks (dominated by tech stocks) were up nearly 29%. However, large-company ***value*** stocks (older and established companies) rose only 5%. Small and mid-size ***growth*** stocks were up 15.8% and 13.5%. Small and mid-size ***value*** stocks were up only 5% and 2.53% during the first half of 2023.

U.S. stock market performance year-to-date was dominated by less than two dozen very large technology stocks.

International stocks rose 12.5% and emerging markets (smaller-country international stock indexes) only advanced about 5%.

Investment real estate prices (real estate investments trusts) only advanced about 3.5%. Water utility stocks were down just over 5% during the first half of 2023 and energy stocks were also down by an average of 7%. Gold was up just over 5%.

Fixed income or bond prices for short-term and intermediate-term maturities were down during the second quarter, but posted a modest gain of less than 1% and 2% respectively over the first half of 2023 (after posting -4% and -14% last year). Rising interest rates adversely impacts bond returns. While investors still receive the interest income, the loss in value exceeds the interest income.

The following chart displays sample returns of various asset categories year-to-date and during the second quarter of 2023:

Year-To-Date 2023	2nd Qtr. 2023	Index Return *includes dividends reinvested*)
+ 3.80%	+ 3.41%	Dow Jones Industrial Average (^DJI)
+ 16.78%	+ 8.68%	Standard & Poor's 500 Index (^GSPC)
+ 16.12%	+ 8.34%	DJ U.S. Total Stock Market (VTI)
+ 28.92%	+ 12.79%	Large-Company Stocks-Growth (IWF)
+ 5.05%	+ 4.08%	Large-Company Stocks-Value (IWD)
+ 15.88%	+ 6.22%	Mid-Size Stocks – Growth (IWP)
+ 5.16%	+ 3.81%	Mid-Size Stocks – Value (IWS)
+ 13.53%	+ 7.14%	Small-Company Stocks- Growth (IWO)
+ 2.53%	+ 3.22%	Small-Company Stocks- Value (IWN)
+ 12.47%	+ 3.23%	International Stocks (EFA)
+ 5.18%	+ 1.05%	Emerging Markets Stocks (EEM)
+ 3.48%	+ 1.77%	Real Estate Investment Trusts (VNQ)
Fixed Income (includes appreciation)		
+ 0.97%	- 0.63%	Short-term U.S. Treasury (SHY)
+ 1.96%	- 1.88%	Intermediate U.S. Treasury (IEF)
Alternative Investment Category		
+ 5.09%	- 2.70%	Gold (GLD)

**All returns calculated using adjusted historical quotes from finance.yahoo.com*

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FINANCIAL MARKET OUTLOOK

By the end of 2022, stocks had declined 20% or more and the value of bitcoin(s) crashed. Investors were eager for a new theme to fall in love and make money with, and then it appeared: AI or Artificial Intelligence – using computers, machines and software to mimic the problem-solving and decision-making of the human mind. Think of robots on steroids using software to physically and mentally solve a task or problem, summarize tons of research into one concise paper and so much more in a matter of minutes. You thought making commands to Amazon's Alexa or using Google search was cool to inquire about a subject, word, or ask a question …. well AI is much bigger and more creative. The applications of AI appear limitless at this time. The rush to invest in AI stocks is all the rage in 2023.

The S&P 500 stock index is up 16% this year. This stock index holds 500 of the largest (companies) stocks. However, if you remove eight of the big tech stocks from the S & P 500 Index, the average return for the remaining 492 stocks *drops from 16% to just 6% year-to-date*. Those eight tech stocks were up 85% during the first half of 2023.

The Dow Jones Industrial Average (30 of the biggest stocks) is up less than 4% over the first six months of 2023, but the NASDAQ stock index – which holds many technology companies, is up a **whopping 32%** during the first 6 months of 2023.

The bottom line is the stock market rally through June is *<u>not broad-based</u>* – it is limited to approximately 15 technology (AI) stocks. This new theme (AI stocks) has everyone's attention and the rally in tech stocks could not be deterred even with all of the interest rate increases by the Federal Reserve, a series of bank failures, and not even the possibility of Congress not voting for a debt-ceiling increase. 2023 is the year of AI nirvana.

This is not the first time that we have experienced stock market rallies led by some new application of software technology. The late 1990's, 3-D printing, autonomous driving, the blockchain (bitcoin), and recently the Metaverse; a three-dimensional virtual space where humans experience life in ways they could not in the physical world.

It's time to consider or be aware of what has been called the ***Hype Cycle-*** a tool for tracking new technology's progress and first introduced in 1995. The Hype Cycle is a predictable pattern or life cycle that has four parts – hype, disillusionment, realism and eventually productivity (the actual use and profitability of new technology applications).

The most recent example is metaverse. Facebook went all in and even changed its name to Meta Platforms in 2021. CEO Mark Zuckerberg did get social networking right (Facebook), but he spent a ton of money on AI (virtual world) where users could experience a virtual world through headsets. The stock price jumped 140% over the following 15 months. Within a year, Meta's stock tumbled 71% and returned to its original price over the 12 months after the name change to Meta Platform. That reversal in stock price is the second stage of the Hype Cycle – disillusionment.

The third phase is realism – where stock prices return to a rational valuation – a sustainable price per share that is not jumping or swooning according to headline hype or traders rushing in and out of the stock(s). The last phase is productivity. This phase begins years later and after the initial hype. Companies find both useful *and profitable* applications of the technology that result in growing revenues and profits. This is the phase where new technologies will have sustainable revenue and profits.

In summary, we might be experiencing a new example of the Hype Cycle similar to what occurred with social networking, the cloud, blockchain (bitcoin) and now Artificial Intelligence. Understand the life cycle (Hype Cycle) before deciding to invest in stocks touting artificial intelligence (AI) today, or at least have a plan in place with specific actions (if any) you will

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take for both the possible upside and downside - before it happens.

The second big change that has occurred for nearly a year now that should get your attention is the ***inverted yield curve***. A yield curve simply plots the interest rates paid on U.S. Treasuries with maturities ranging from 6-months to a 30-year maturity date. "Normally", the longer the maturity of a U.S Treasury, the higher the interest paid to investors and the yield curve has an upward slope (not downward sloping or inverted). Investors should be paid higher interest rates for any fixed income or bond investment that has a longer the maturity date. Why? Because of uncertainty.

Longer-term bonds pay higher interest because of the chance of higher inflation in the future and interest rate uncertainty rises over time. Who knows what the economic environment will be in 5, 20 or even 30 years from now. The more the uncertainty and the longer the maturity date, the higher the interest rate paid to compensate investors for uncertainty – a classic upward sloping yield curve (the longer the bond maturity, the higher the interest paid).

For nearly a year, the interest paid on a Treasury with a 6-month up to a 1-year maturity is *higher* than the interest paid for 2-year, 10-year or even 30-year maturity U.S. Treasury. The interest or yield on a 2-year Treasury Note is more than 1% higher than on the 10-year note.

Fact: ***An inverted yield curve*** (when higher interest is paid on short-term maturity bonds compared to longer-term bonds) ***has preceded EVERY U.S Recession since the 1950's***. Also, a fact: an inverted yield curve DOES NOT predict the *severity* of a coming recession – could be mild or could be significant.

Add in other economic indicators: employment or the job market is reasonable, inflation is still double the desired rate, but currently one-half of last year's inflation rate, and corporate profits are moderate. The case can be made that the economic outlook is neither above average or horrible. The "problem is" stocks are currently more than generously valued today based on current earnings and tech stocks are in extreme valuation territory. Further, the stock market averages - excluding technology stocks, are rising very slowly or at a below-average pace.

Lastly, if you care to add in other uncertain factors into your forecast, such as: (1) geopolitics (Russia/Ukraine, Taiwan, China etc.), (2) the U.S. government debt is at the highest level in history (over 30 trillion) and growing, and (3) we have the most divided political parties in decades, sometimes it feels eerily quiet out there and the future outlook is not clear at all.

INVESTMENT OUTLOOK AND RECOMMENDATIONS

We are still taking a middle-of-the-road stance and are cautious over the short-term. The elephant in the room is the recent stock market rally that has been fueled by just 15 (AI) tech stocks. A broad-based stock market rally confirms confidence and is necessary to experience a *sustainable* rally. Either the rest of the stocks in the S&P 500 catch up to the 15 mega-cap technology stocks and the gains continue by broadening out to all companies, or the 15 tech stocks that have powered this rally fizzle out. Also, the inverted yield curve should not be ignored. Lastly, the Presidential election kicks off in the fall of 2023 - adding another smothering layer of uncertainty.

Early in 2022, we began reducing stocks in our managed accounts and reinvested those funds into short-term (1-year or less maturities) Treasuries and CDs. At the time of purchase one year ago, the yield or interest was approximately 4%. Today, the yield or interest on new one-year Treasuries or CDs is over 5%. Most of these Treasuries purchased in early 2022 have recently matured in May and June 2023. Another portion will mature later this year. Most client portfolios now have several short-term Treasuries and CDs maturing continuously every 60-90 days.

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These funds will eventually be re-allocated back into stocks in the future.

Whenever a sustainable stock market arrives, the easiest way to participate is to first re-allocate funds into the broad market stock indexes. Small-company U.S. stocks are even more attractive. This category has lagged in performance due to last year's stock market decline, but this category excels above the market averages when sustainable stock market advances are underway. Emerging markets (small-company stocks of smaller international companies) will also be on the list for new purchases as well as mid-cap stocks.

We have identified several stock investments that we intend to add to client portfolios and will continue to add new selections to this recommended list as the year progresses. Ideally, we will begin adding additional stocks to client portfolios carefully and slowly within the next 12 months.

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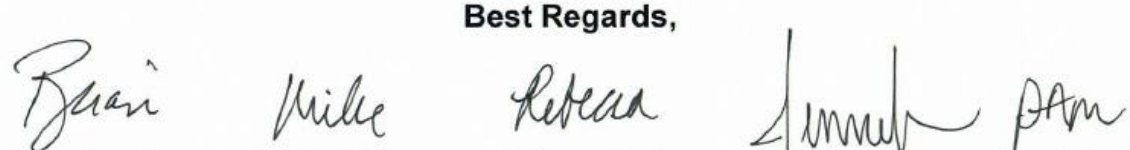

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