CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

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Artificial Intelligence…
...and Other Matters

By

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Throughout 2023, as the Federal Reserve was raising interest rates sharply to bring inflation back down to earth, the expectation was that a recession lay directly ahead. As it turned out, there was no recession in 2023. The US economy remained fairly strong and employment continued to grow. (Note, however, that part-time jobs accounted for all the growth in total jobs. Full-time jobs fell last year. Is this a healthy employment market?) At the Fed's meeting last week, it again left interest rates unchanged and indicated that it still expected to begin cutting rates this year. The Fed's current plan is to cut rates three times by a total of 0.75%. Given the fairly steady economy even with interest rates at high levels, the Fed has the luxury of time as it considers when to ease monetary policy.

Given the Fed's placid schedule and the continuation of economic growth, the stock market has been exceptionally strong this year. Recent stock market gains exceed underlying growth in corporate earnings and revenue; thus one should not expect the market to sustain its present growth rates indefinitely. However, excitement inspired by artificial intelligence ("AI") has generated economic activity and has lit a fire under the stock market.

Nvidia is the best-known firm in AI; Core has an investment in it. It is the maker of semi-conductors (sometimes called 'chips'), networking equipment, and other hardware and software all at the root of AI. Apart from Nvidia, a large number of companies, huge and small, are intently engaged in AI work. The tech giants, Microsoft, Amazon, and Alphabet (the owner of Google), are deeply involved with AI, as are a number of other hardware and software makers. It is not a stretch to expect that AI will prove to be as important and influential in our lives as has been the internet. Core's investment in Nvidia, begun earlier this year, may have seemed a bit late, in that Nvidia's appreciation in 2023 was substantial. However, it has appreciated significantly since our purchases began. Moreover, the years ahead will likely witness much greater AI activity than so far underway. For example, the head of semiconductor maker Advanced Micro Devices expects sales of AI chips to increase nine-fold in the next three years. The future for AI investment is bright.

Japan. Our investment in Japanese stocks has been a successful also, having appreciated by more than forty percent since our initial purchase last year. Like Nividia and other AI investments, I fully expect to see further growth in our Japanese investment. In brief, the story is as follows: Shinzo Abe, Japan's long-serving prime minister, assassinated in 2022 after he left office, undertook a series of farranging reforms in many elements of Japan's institutions and practices. These reforms included corporate business matters. For many years, Japanese companies typically held their profits, unlike the situation in the United States, where cash not needed for corporate investments and operations is generally returned to shareholders through dividends and share buybacks. Through various forms of incentives (including shaming), Mr. Abe encouraged the enhancement of shareholders returns. His strategies and incentives bear fruit, as the returns on Core's broad investment in Japanese companies show.

Moreover—and also akin to the situation with Nvidia and other AI investments—the good news is quite likely to continue. Japanese households tend to hold large amounts of their savings in cash and only small amounts in securities investments. This also contrasts with the American situation where investment holdings are proportionally far greater than in Japanese households. Should the Japanese convert even a modest portion of their cash holdings to securities investments, the effect on Japanese markets would be dramatic indeed. Such household investments, joining the ongoing corporate activities, will likely give rise to much higher Japanese stock prices.

Gold. At the risk of breaking my arm from patting myself on the back, I also point out that gold, in which we have had a modest investment for some five years, has, in the last week, traded at an all-time high and exceeded $2200 per ounce in price. We have held it as a hedge against geopolitical mayhem. It appears from publicly available data that certain central banks, especially China's and Russia's, have been major buyers of gold in the last year and more. This probably relates in part to the sanctions imposed on Russia by the US and European countries after Putin's invasion of Ukraine. Among other things, the sanctions froze Russia's assets held outside of Russia. In order to avoid having their assets frozen or even seized, as may happen with Russia's foreign holdings, some governments appear have decided to hold gold stored in their own countries, rather than US Treasury bonds and the like, held in Europe or America.

Other holdings. As I have written in previous letters over the last couple of years, Core's clients have investments in US Treasury bonds. In part, the reason for such holdings was that, in the recession that I thought lay directly ahead, these bonds would rise in price significantly. Because the recession has not come, such appreciation has not yet occurred. We continue to hold a modest position in Treasuries and, unless the business cycle has been repealed, these will enjoy the expected appreciation in the fullness of time. Meanwhile, we also have meaningful holdings of government securities money market funds. These are paying us about five percent per year in the context of the Fed's holding short-term rates so high. Finally we hold a decent-sized position in Indian equities that has appreciated in encouraging fashion since our purchase last summer. Further gains are in prospect.

It's spring. Things are blooming nicely.

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