

The Super Seven: Masked Heroes or Villains

The Super Seven are the larger-than-life figures of today's stock market environment comprised of Apple, Microsoft, Nvidia, Amazon, Meta, Tesla, and Alphabet. Apple hovers near a \$3 trillion valuation, Microsoft \$2.5 trillion, and the other five companies enjoy valuations north of \$1 trillion or quickly moving toward that mark. Have exposure to the S&P 500? Well, these Seven represent nearly 28% of that entire index, with Apple and Microsoft collectively accounting for 14.5%. The power of the Seven comes to light when you look at the first half performance of the S&P 500, up 16.89%, versus the Dow Industrials, up only 4.94%. One difference that explains this divergence is that the Dow Jones only includes Microsoft and Apple.

The first half excitement surrounding these names, in large part, is because of the market's interest in AI or Artificial Intelligence. The proliferation of data and recent advances in computing power and machine learning have led to more sophisticated AI algorithms and models. The expansion of AI is leading to advances in autonomous vehicles, medical diagnosis, fraud prevention and more. Microsoft has their popular ChatGPT, Nvidia is producing highly advanced AI chips, Tesla is moving toward self-driving cars, Apple and Meta are advancing visual AI, and Amazon, Google and Microsoft power AI through their cloud offerings.

Of course, these Seven have to be looked at as Heroes helping to lift the markets out of last year's swoon created by rising interest rates, rising inflation, and the fear of recession. But what if these Seven masked heroes are really masked villains instead? Are they masking the lack of strength seen in the rest of the market and economy? The Mid-cap and Russell 2000 indexes are up half as much as the S&P this year, and the Micro-cap companies have seen

a mere 1.87% gain. As mentioned previously, the Dow Jones has rallied only 4.94% this year.

Larger parts of the economy are still struggling from persistent inflation such as housing and rental costs, new and used car prices, and food costs to name a few. Interest rates are too high and growth that is seen in some areas is absent in others. People are spending money to travel, but retail sales are weak. Housing has not collapsed under these higher rates mainly because of a lack of inventory. Who wants to put their house on the market and lose their low mortgage rate that they refinanced into over the last few years. Uncertainties in the broader economy are exacerbated by much of the pandemic stimulus money now depleted, and students and renters will soon be forced to restart regular payments to landlords and loan companies.

Are the Super Seven Heroes or Villains? Well, they are most likely masquerading as both. They are beacons of growth and represent the future and promise of Artificial Intelligence, the Fourth Industrial Revolution.

They are helping to uplift and mend an economy that has been hit with body blows and needs expanded and profitable growth. On the other hand, the Seven, and their dominance within the S&P 500, are masking the underperformance and uncertain nature of the broader economy. This uncertainty stems from high interest rates and more expensive consumer and business loans. Under the Villain role, if these Seven were to falter, the problems of the underlying economy would be center stage and the markets could falter.

Where do we see the economy and stocks going from here? We have pointed out both sides of the investment environment for many months now, but we have sided more to the positive as we believed inflation would continue to moderate, the economy would remain resilient and recession forecasts

would be pushed back. So far so good. As we know, markets are discounting mechanisms. This year's strength can be read as market participants anticipating a further move down in inflation toward the Federal Reserve's 2% target. If this is the case and employment remains resilient, a further rally is anticipated. Heroes or Villains? In super-hero adventures, there are usually both.

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