ALBION FINANCIAL GROUP

Guiding Clients
To A Lifetime of
Good Decisions

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IN THIS ISSUE

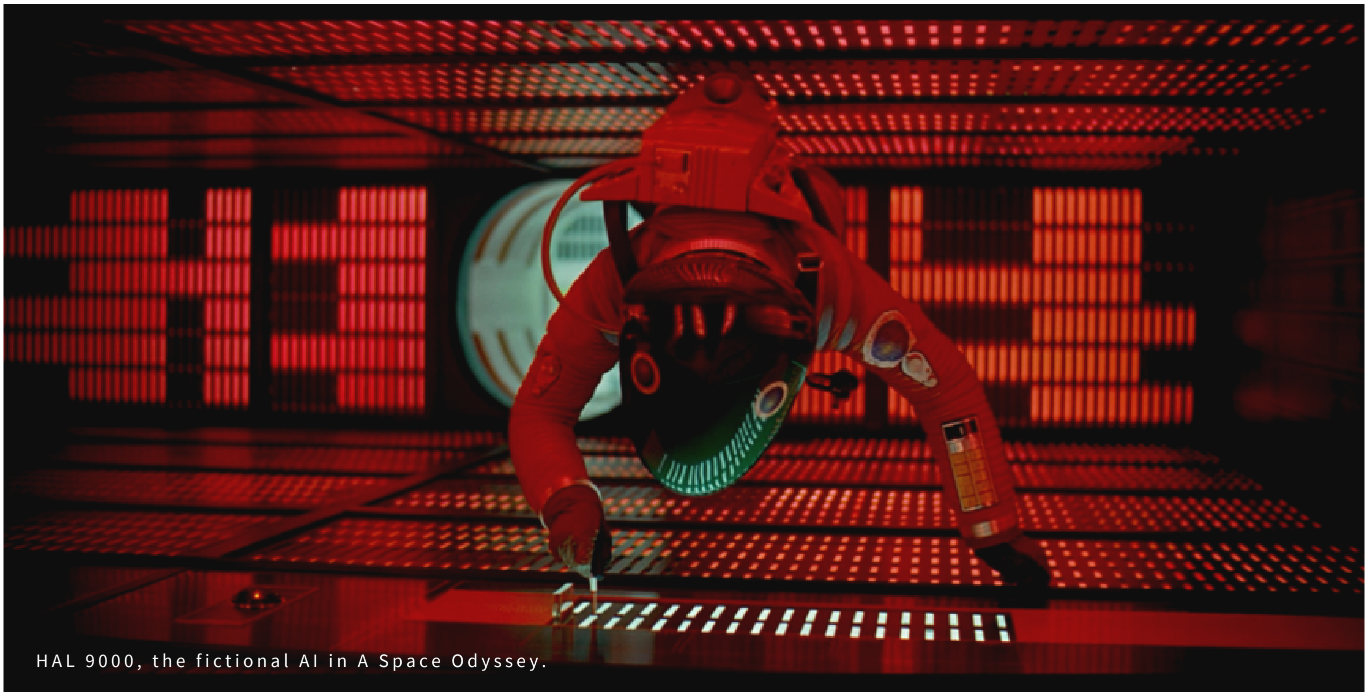
INTRODUCTION

The first half of 2023 is now behind us and in Utah we have fully transitioned from a winter with record snowfall into hot days and warm nights. These familiar seasonal patterns provide for easy analogy when considering and describing the complexities of our world. The Artificial Intelligence winter of the past has thawed into a fervent spring and John Bird sifts through the hype ahead. Then, Jason Ware gives a summary of the summery state of the markets and economy, which appears healthy at first glance. And for those of us transitioning into the autumn of our lives, Patrick Lundergan describes how different types of trusts can be used in estate planning. Finally, our Albion Community Update has details for how you can join the conference call we're hosting next week.

FROM JOHN BIRD'S DESK

"Just what do you think you're doing, Dave? Dave, I really think I'm entitled to an answer to that question. I know everything hasn't been quite right with me...but I can assure you now...very confidently...that it's going to be all right again. I feel much better now. I really do."

"Dave. I'm afraid. I'm afraid, Dave...Dave, my mind is going. I can feel it. I can feel it. My mind is going. There is no question about it. I can feel it. I can feel it. I can feel it. I'm a...fraid...Good afternoon, gentlemen. I am a HAL 9000 computer. I became operational at the H.A.L. plant in Urbana, Illinois on the 12th of January 1992."
– excerpt from final monologue of HAL 9000 in *2001: A Space Odysse*y (1968)



HAL 9000, the fictional AI in A Space Odyssey.

Those of you of a certain age may recall HAL, the all-controlling computer in Stanley Kubrick and Arthur Clarke's ground-breaking, sci-fi film *2001: A Space Odyssey*. In the film the near-sentient HAL who had been programmed to ensure the success of the mission determines the odds of success would be greatly enhanced if the humans on the spacecraft were eliminated.

We've always had an uneasy relationship with our technology as it eases aspects of our lives yet… simultaneously creates a dependency. The rapid advances in programming technology and the resulting Artificial Intelligence (AI) enabled tools have brought both the benefits and risks of AI to the fore.

What is Artificial Intelligence? There are a variety of evolving definitions that can be summarized as an ability, using computer science and large data sets, to perform complex tasks that normally require human intelligence including visual perception, speech recognition, decision-making, problem solving, and the ability to generate new concepts and directions of inquiry. In a nutshell it's the ability for a machine to learn from the results it generates, incorporate that learning into its algorithm, and design and execute additional programs and/or analyses independent of human input to further improve its knowledge base.

The foundations of such tools have been with us for a long time. A machine's ability to sort through massive troves of data and display patterns of interest is nothing new. What is new is the notion of the machine choosing what patterns to look for and iterating on its own – rather than being redirected by a human controller - to find relevant information.

Most of us are now familiar with ChatGPT, Dall-E 2, Lumen5 and some of the myriad other AI tools now available online. They are impressive. Enter a question and in seconds you'll receive a tailored response that while short on specific advice tends to provide an overview and a framework of the issues to be considered.

However there are also well documented fails in the AI space. At the core of any AI tool are human programmers and their worldview cannot help but be built in. This may result in a bias – intended or not - toward some products, processes, and people at the expense of others. There is also a significant privacy concern. AI algorithms advance by incorporating a massive amount of data including individual specific information such as residence, employment, purchasing history, search history, medical history, and anything else that can be quantified and included in a data set. As has been the case for the last fifty years of rapidly advancing technology the technology is far ahead of a regulatory structure to protect the rights of users. None of these factors are likely to change anytime soon.

How will AI influence our financial decision-making process? A significant part of investing and financial advising involves numbers. Company financial statements, long-term growth trends, global, national, and regional economic data, and portfolio analytics jump to mind. We've had tools to analyze such numeric data for a long time. AI in finance includes the attempt to capture and incorporate the human side of the investing and financial planning equation. Who are you? What's important to you? What do you hope to do with your life? And what are investors writ large thinking and feeling? How will those thoughts and feelings influence returns in financial markets? Capturing sufficient data to be able to answer the questions above will be very difficult. Turning that information into actionable decisions on behalf of a specific investor will be orders of magnitude harder.

Our perspective is that AI will become an additional set of tools in the toolbox. Just as our portfolio management software allowed for real time insights into each client account, and our financial planning software helps us quantify the impacts of personal financial decisions, we believe AI tools will give us another way to gain a bit more clarity on what's happening with each of our client families and the larger world.

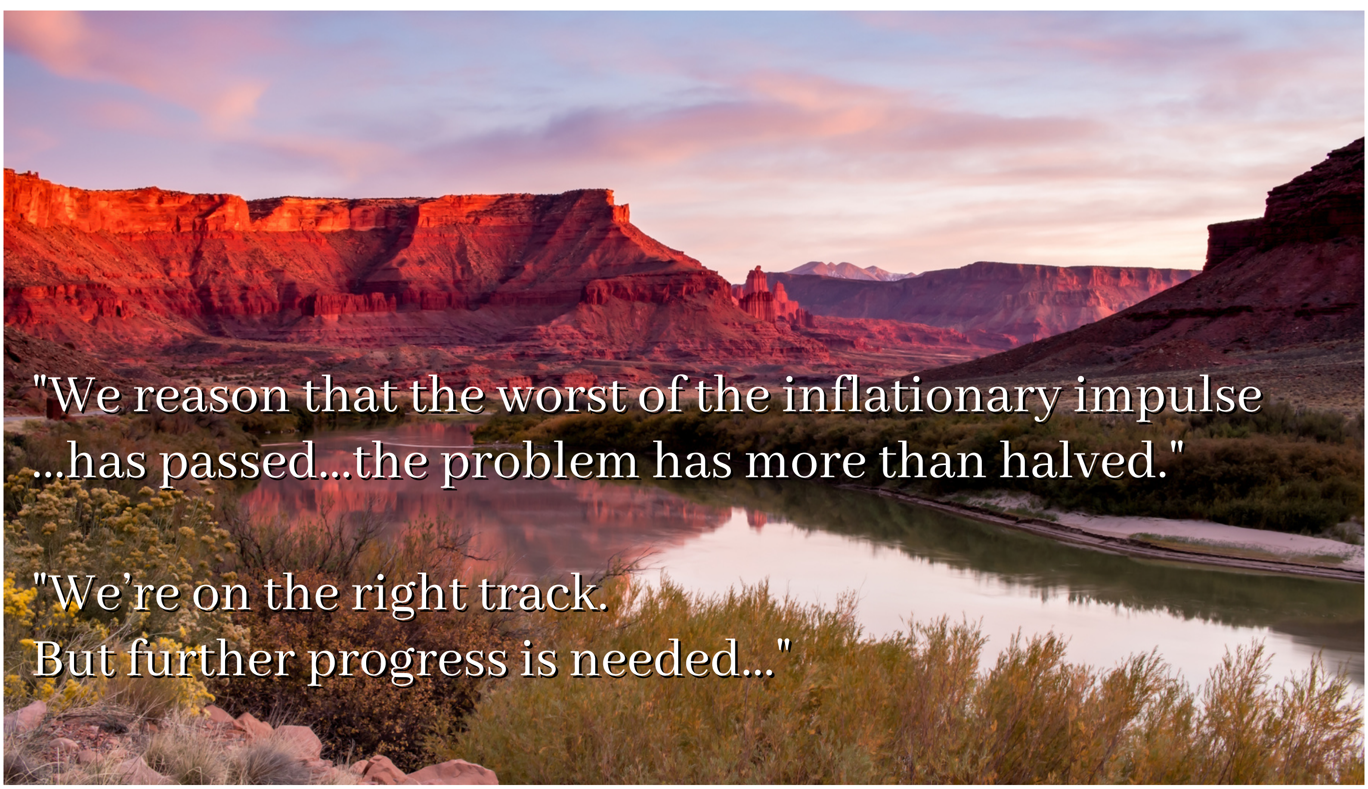
Boutique furniture makers used to use hand tools. Then power tools came along and provided a dramatic improvement in efficiency. Computer-controlled devices were developed allowing hands-off precision in bringing the designers idea to life. What didn't change is the importance of the creative vision of the craftsman who takes the time to understand what their customer is trying to accomplish, designs the piece to meet those expectations, and uses tools to create it. There may be a time when the human connection and creativity of the designer is replaced by a machine but as of now most of us prefer working with an actual person. Our business is not that much different. We have increasingly sophisticated tools but ultimately our role is to bring those tools to bear to help our clients along the path toward their desired financial outcome. We look forward to adding AI tools to our toolbox.

ECONOMY & MARKETS by Jason Ware

Another quarter has come and gone. And with it the US economy's resilience has endured. While in many respects there are clear signs of deceleration, two areas keeping the post-Covid expansion alive are *jobs* and *consumer spending*. The former feeds the latter in a virtuous cycle, and until we see the labor dam break aggregate demand may sustain for a while yet. To be clear, we are not suggesting that those strongholds are impervious to slowdown. They aren't. We'll revisit this later. For now, let's focus and celebrate the *positive* developments at the year's halfway mark.

Growth in the first six months of 2023 has boosted a variety of economic measures to record heights. From total output (GDP) and employment to household consumption and fixed private investment, at a glance the American economy looks healthy. Too, select weak spots pushed down by economic normalization and higher interest rates of the past sixteen (or so) months have recently revealed clues of stabilization. Most notably the housing market, but there are others. Auto sales have rebounded now that supply chains are largely sorted out. Factory orders have steadied. Consumer confidence has improved (some). Meanwhile, high inflation – a central figure in the post-pandemic economic funhouse – has firmly settled into *disinflation* (i.e., falling inflation). Indeed, in accordance with our belief over the past year price pressures peaked and have steadily cooled. That isn't to say problematic inflation is fixed. Rather we reason that the worst of the inflationary impulse caused by the pandemic has passed. From over 9% last June to about 4% today, the problem has more than halved. We're on the right track. But further progress is needed – a fact not lost on Jerome Powell. Nevertheless, inflation down into the 3%-range sometime in the second half of this year is likely.

This welcomed news, coupled with reduced banking stress and a Federal Reserve that's at / near the end of rate hikes, offered fertile ground for the stock market to move higher from lows late last year. It appears a "soft landing" has become the base case for many. Perhaps this view is correct. Though, grounded by the weight of the evidence we fear that *ultimately* it may not be. Regardless, for now the message from the S&P 500 is clear – "we're not worried!" And yet when digging deeper, a sober study of the broader stock market whispers a less rosy tale. For instance, the year-to-date *performance* gap between the standard "market-cap weighted" S&P 500 (disproportionately influenced by the largest companies) and its "equal weighted" counterpart (all stocks created equally) is the largest on record with the latter capturing but one-third the gains of the former. In plain English: most of the returns this year have come from just a handful of big winners. A similar disparity exists in other sections of the equity market (e.g., small caps, mid-cap, etc.), including at the sector level where eight of the eleven categories have underperformed the overall index (five of them sport *negative* returns as of this writing). One final point to drive it home, the median return year-to-date for the ~2,400 stocks listed on the NYSE is approximately +2%.



It's a skinny bull in search of nourishment.

So why the mixed signals?

We think that stocks writ large are exhibiting greater uncertainty concerning the course of the business cycle than the mega tech companies – freshly infused with the wonder and excitement of AI – are displaying. Our current assessment aligns with this view; an outlook shaped by our core leading indicators. Additionally, manufacturing is already in a slump, credit has become restrictive, global growth is slowing (with western Europe already in recession), and corporate profits have waned. Circling back on those two bastions of strength from our opening passage, on the consumer side – the wellspring of most US economic activity – across durable goods, retail sales, assorted discretionary categories, as well as data and commentary from consumer companies, signs of exhaustion are apparent. Much of the Covid stimulus savings buttressing household finances has now been spent. As for the jobs market, payrolls are rising but other parts of the labor milieu such as initial jobless claims, small business hiring plans, nominal wages, and average hours worked (per week) are shakier. We don't envisage an economic wipeout, but there are more risks near term than narrow parts of the stock market are reflecting.

Resultantly, amid market strength we have added a modest amount of "defense" to our growth portfolios, while remaining *fully invested*. This can dampen volatility plus provide a more stable source of funds to draw from if (when) lower prices arrive. We think this approach strikes a prudent balance between our north star as long-term investors, while respecting impending economic probabilities. We will continue to monitor general conditions and manage your portfolios using objectivity, humility, and poise. Thanks for your trust in us.

PLANNERS CORNER by Patrick Lundergan

Estate planning is a cornerstone of any good financial plan, delivering peace of mind and control over one's legacy. By crafting a well-designed estate plan, individuals can safeguard their wealth, shield loved ones, and shape the destiny of their assets.

Trust accounts play a crucial role in estate planning because they offer important benefits and protections. They allow individuals to have control over how their assets are managed and distributed, ensuring their wishes are carried out effectively. Trusts also help avoid the time-consuming and expensive probate process, which means less hassle and more privacy for beneficiaries. Moreover, trust accounts can provide flexibility during the grantor's lifetime, allowing for adjustments and changes as circumstances evolve.

"By setting up trust accounts, people can have peace of mind knowing that their assets are protected, their loved ones are provided for, and their legacy is preserved."

Several types of trust accounts are commonly used in estate planning, each with their own distinct use cases.

- **Revocable Living Trusts**: These trusts are created during the grantor's lifetime and can be modified or revoked by the grantor at any time. Revocable living trusts are popular among individuals who desire to maintain control over their assets while they are alive and ensure that their beneficiaries receive them after their passing. They also help avoid the often time-consuming and costly probate process.

- **Irrevocable Trusts**: Unlike revocable trusts, irrevocable trusts cannot be changed or revoked by the grantor once they are created. When assets are transferred to an irrevocable trust, they are considered separate from the grantor's estate, and the grantor relinquishes control over them. Irrevocable trusts can be utilized for various purposes, such as reducing estate taxes, protecting assets from creditors, or ensuring that assets are distributed to beneficiaries per the grantor's wishes.

- **Testamentary Trusts**: These trusts are created after the grantor's death through their will, and the assets are transferred to the trust upon their passing. Testamentary trusts can be used to ensure that assets are distributed to beneficiaries as per the grantor's wishes, protect assets from creditors, or provide for a beneficiary with special needs.

- **Charitable Trusts**: Charitable trusts are created for charitable purposes and can offer significant tax benefits to the grantor while supporting a charitable cause. There are two primary types of charitable trusts: charitable remainder trusts, which provide income to the grantor during their lifetime and then transfer the assets to charity upon their death, and charitable lead trusts, which provide income to a charity for a set period and then transfer the assets to the grantor's beneficiaries.

- **Special Needs Trusts**: These trusts are created to provide for the needs of beneficiaries with disabilities while allowing them to qualify for government benefits such as Medicaid or Supplemental Security Income. Depending on the grantor's objectives, special needs trusts can be revocable or irrevocable.

In summary, several types of trust accounts are available, each with unique use cases. It is recommended to consult an experienced estate planning attorney to determine which trust account is best suited for your specific needs and goals.

Individuals who do not have a trust or opt not to establish one can still take steps to avoid probate and ensure that their assets are distributed appropriately in the event of their passing. Here are some methods to set up accounts to avoid probate without forming a trust:

- **Joint Tenancy with Right of Survivorship**: This form of ownership is common among married couples and enables two or more individuals to own property together. When one owner dies, the property passes automatically to the surviving owner(s) without going through probate.

- **Payable-on-Death (POD) Accounts**: This type of account designates one or more beneficiaries who will receive the account balance upon the account owner's death. The account owner retains complete control of the account during their lifetime and can change the beneficiaries anytime.

- **Transfer-on-Death (TOD) Deeds**: This real estate document allows an owner to designate a beneficiary to inherit their property upon their death while retaining control of the property during their lifetime.

- **Life Insurance and Retirement Accounts**: These types of accounts allow the account owner to name a beneficiary who will receive the proceeds upon the account owner's death without going through probate.

It's important to note that while these methods can help avoid probate, they may not be suitable for everyone and may have certain limitations and drawbacks.

In summary, regardless of wealth or age, estate planning is important for everyone. Without a proper estate plan, the distribution of assets and property after a person's death can become a complicated and stressful process for their loved ones. Estate planning allows individuals to control how their assets will be distributed and to whom while also minimizing taxes and avoiding probate court. Additionally, estate planning can include documents such as a living will or healthcare directive, which outline a person's wishes regarding medical care in the event of incapacity. Overall, having an estate plan in place provides peace of mind and ensures that a person's wishes are carried out in the event of their death or incapacity.

ALBION COMMUNITY UPDATE

Conference Call Reminder

We are hosting a conference call on **Thursday, July 13th** at **9 AM MT** with panelists from our advising and investing teams addressing the most pressing questions of the day and the state of the economy and markets.

We invite you to attend the call and encourage you to ask questions live and/or submit your questions in advance. A recording of this call will be available on our blog and social media channels if you are unable to attend.

We hope you'll join us, and please extend this invitation to any friends or colleagues who you think could find our presentation informative or useful.

You can register to attend the conference call at ***albionfinancial.com/events***.

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