CIBC PRIVATE WEALTH

THE STAN CLARK FINANCIAL TEAM'S

PERSPECTIVES

IN THIS ISSUE:

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STAN CLARK
Senior Wealth Advisor

Intuition can serve us well in decision-making – but, as I note in this issue's behavioral finance article, it has to be the right intuition. In investing, beware of the gut-feeling type. Michael Chu explains the likely business and economic impact of artificial intelligence, e.g., ChatGPT software that simulates human conversation. And, dispelling the myth that budgeting is difficult, Tom Cowans offers simple, sensible, stress-reducing ways to save for retirement. Your future self will thank you!

Stan

Stan Clark is a Portfolio Manager and Senior Wealth Advisor for The Stan Clark Financial Team at CIBC Wood Gundy. Stan has direct responsibility for the team and oversees all areas of financial planning, investment selection and investment management.

Behavioral Finance

TRUST YOUR INTUITION? SOMETIMES – BUT NOT FOR PICKING STOCKS

By Stan Clark, Senior Wealth Advisor

An art expert glances at a museum's proud new purchase. "It's a fake," she declares.

A veteran fire captain fighting a small fire in a kitchen yells to his men, "Let's get out of here!" Seconds later, the floor collapses into a much bigger fire in the basement.

At an auto show, the manager of a mutual fund sees the latest vehicles from a big-three auto company. Impressed, he buys millions of shares in the company.

All three of the above scenarios are examples of what we might call "intuition at work." The first is from Malcolm Gladwell's *Blink: The Power of Thinking Without Thinking*. The second, from Daniel Kahneman's *Thinking, Fast & Slow*. Both show intuition at its best and most valuable. But the intuition in the third scenario is one that no smart investor familiar with behavioral finance should ever trust. Let's study the differences.

First, let's examine what we mean by *intuition*. Renowned psychologist Herbert A. Simon, a Nobel Prize winner in economics for his work on decision-making in organizations, says of intuition: "The situation has provided a cue; this cue has given the expert access to information stored in memory, and the information provides the answer. Intuition is nothing more and nothing less than recognition."

In the examples of the fake statue and the fire, we are dealing with something you might call expert intuition, which can only come from years of experience and study. In the example of the stock pick, we are looking more at a gut feeling, a decision made mostly for emotional reasons and therefore not a reliable one.

To be sure, it may turn out through sheer luck that the stock pick was a good one. But in the long run, the fund manager who relies on personal judgments is going to make as many, if not more, bad decisions as good ones.

As we have been saying in many of our previous articles on behavioral finance, formulas- and rules-based decision systems are better than subjectivity and intuition in making many types of decisions.

Kahneman refers to studies in a variety of disciplines. He notes that in 60% of studied cases, decision-making based on simple rules was a lot better than personal judgments. In no case was the rules-based approach worse.

Kahneman and other researchers have found that simple algorithms based on a limited set of parameters, five or six at most, outperform expert opinions and predictions. This is true from investing to such diverse fields as predicting wine prices, interpreting X-rays, choosing good political leaders and forecasting who will do well at college. The more subject something is to irregularity and random fluctuations, the less accurate will be the subjective judgments of experts.

An investor, whether professional or not, operates where there are hundreds, possibly thousands, of variables. These can range from who is on a company's board of directors to a global political situation. The variables all can and do affect stock performance. Very often an investor's success can be put down to pure luck – but just as often, that luck may be wrongly ascribed to skill.

That is why you shouldn't trust the subjective stock picks of experts, no matter how confident they are about them. As Kahneman says, "The confidence that people have in their intuitions is not a reliable guide to their validity."

Stock-picking is an area where, in the long run, systematic, rules-based systems will outperform intuitive ones.

TEAM TALK

Stan Clark
Senior Wealth Advisor

Stan and Joanne with friends in Vietnam

Any major events in the family over the past year?

This past year was the year of the move in our family. The first was Lindsay, Tom, Ryan and newborn Ellie moving from Vancouver to within 5 minutes of us in South Surrey. So much fun having them close! Then, Joanne's parents moved from their house of 35 years to a lovely retirement home close to us. It was a lot of work downsizing but so worth it. They wish they did it earlier. And our younger daughter Jess and her husband Dan are in the process of buying their first home in Vancouver. Very exciting for them. Joanne and I are the only ones who haven't moved!

Did you go on any trips this year?

We've been on a few since things started opening up from Covid. In August we went to our niece's wedding in Aspen. That was our first time in Aspen, quite the place. We then did a cycling trip to Greece in September that was originally scheduled for May 2020. And in March we did a Mekong River cycling cruise from Vietnam to Cambodia. Cycling is a wonderful way to see a country and we absolutely loved Vietnam and Cambodia.

Investing

WHAT CHATGPT IS – AND HOW IT WILL IMPACT OUR LIVES

By Michael Chu, Senior Wealth Advisor

In late 2022, OpenAI released ChatGPT, an *artificial intelligence* (AI) chatbot (computer software able to simulate human conversation) with astonishing capabilities for producing detailed replies over a broad range of topics. With ChatGPT's emergence, AI now commands centre stage. Among all the hype around it, forecasters point to a wide range of scenarios, from "nothing to see here" to "an uncontrollable and irreversible technology."

First, some definitions. AI is a broad term, but it basically involves automated decision-making by computers. *Machine learning* (ML), a form of AI, is "trained" – meaning it predicts future output based on output historically associated with a given set of inputs. This replaces traditional, explicit programming instruction. Think of the movie recommendations Netflix gives you, e.g., it has learned that you enjoy tongue-in-cheek whodunits, so it will suggest you watch *Glass Onion*. ML is already very prevalent in our lives: Amazon shopping recommendations, Siri, autocorrect and social media feeds like Instagram, to name a few.

ChatGPT is a type of ML, but the scale is huge: 175 billion parameters plus an unprecedented level of human training. This produced a huge leap in the response quality, which fuelled a surge of interest in AI. The uptake broke records, reaching 100 million active users in just two months.

Chances are we all know someone who's used ChatGPT. The GPT in ChatGPT stands for *generative pre-trained transformer*. Generative AI is an AI model that generates content in response to a prompt, producing a wide variety of credible writing in seconds. This can benefit many organizations, saving time and resources – and allowing them to pursue other opportunities.

But generative AI is not without its risks. It will confidently produce inaccurate, plagiarized or biased results without any indication these may be problematic. That's because the AI models are trained on the Internet – hardly a universally reliable source! ChatGPT can "hallucinate" facts and make reasoning errors. For that reason, great care should be taken when using ChatGPT in high-stakes contexts. Before use, be sure to subject it to human review.

Just released: GPT-4, based on an estimated 100 trillion data points (over 500x more than GPT-3). GPT-4 is more reliable and creative, and can handle more nuanced instructions compared to the previous version. GPT-4 can also take images as an input. However, like its predecessors, GPT-4 has been shown to hallucinate and have biases.

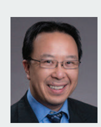
Where does this leave us? Unquestionably, AI can benefit nearly all industries, from logistics to customer service to Internet search to advertising. Recent breakthroughs are both exciting and terrifying. Many warnings cite the dangers of technology; even call for a pause in development and regulations coming from its creators.

The fact is that, like most technology, AI can be used for good and bad. The rapid pace of uptake and advancement alone increases the potential for causing harm. On the bright side, AI will prove to be a powerful tool for many workers, improving their capabilities and expertise – and providing a boost to the economy. However, down the road, companies could also use it to destroy traditionally automation-proof jobs, well-paying ones that currently require creative skills and logical reasoning – doing little for economic growth.

The impact will probably include a bit of both. Technology will increase productivity, which would boost consumer income and spending. While some jobs will be eliminated by innovation, new and better-paying jobs would also be created – boosting living standards. So, while some things will be substituted, there's also potential for expansion.

Top economist Ed Yardeni writes, "In the past, technology disrupted animal and manual labor... The focus was on brawn. The Great Disruption is increasingly about technology doing what the brain can do." Yardeni says AI could spark another Roaring Twenties for the stock market. The original roaring (19)20s were an exuberant decade that included amazing stock market returns – but ultimately ended with the most devastating depression in modern history. There's no reason that history must exactly repeat itself – but we should be prepared for a range of possibilities, while at the same time staying rational.

Lastly, this article, like all articles in Perspectives, was written by a human.



Michael Chu is a Portfolio Manager and Senior Wealth Advisor for The Stan Clark Financial Team at CIBC Wood Gundy. Michael is a specialist in investment research and information technology.

Financial & Estate Planning

BUDGETING BASICS, SMART GOALS – AND PAY YOURSELF FIRST!

By Tom Cowans, Wealth Advisor

Previously we've introduced the concept of preparing for your future self. We've discussed the importance of getting into the habit of saving early – and touched on some of the ways to do that. Now let's look at how to reach the point where you can indeed start putting money away.

First, back to the basics of saving: setting up a budget and learning to monitor spending. For some people, budgeting has a bad reputation – but that bad rep is undeserved. Contrary to popular belief, budgeting need not be time-consuming and restrictive, a task always pushed onto tomorrow's to-do list.

When implemented correctly, using a budget puts you in a position of control. Not only that, but budgeting can help you reach your financial goals with relative ease. It can even help you plan for the occasional splurge – guilt-free!

The basic concept of creating a budget is simple: *Spend less than you make*. The first step in setting yourself up for financial success is to look at where your money is going. That is, to track your spending. You can start by creating a few categories for your after-tax income:

- **50% on *needs***: rent/mortgage, utilities, car payment, phone bill, groceries, debt, insurance, etc.
- **30% on *savings***: retirement, emergency fund, savings for future purchases, e.g., a down payment on a house.
- **20% on *wants***: eating out, shopping, vacations, etc.

If the above is new to you, and you realize your budget needs a few tweaks, this is where prioritization comes in. Take some time to reflect on your monthly purchases. Become aware of what is costing you the most after your needs and savings are taken care of. How are you spending the majority of your money in your wants section? Prioritize those purchases. Anything low on the list should be scrapped to make room for what is highest. For example, maybe a few birthday dinners require your attendance this month. Meanwhile those daily lunch runs are sapping your cash supply. Consider taking your own lunch to work, thereby creating a more flexible budget for celebrating with your friends and/or planning for that future vacation.

We recognize that sticking to a budget can be a difficult task and that our 50/20/30 guidelines won't work for everyone. The key is to categorize your expenses monthly so you can see exactly where your money is going. If your savings targets are too aggressive or you're spending too much on wants, you may find that some months require adjustments. But by being realistic and sticking to your monthly sum, you'll be well on your way to reaching your personal financial goals.

To be effective, your budget should feel somewhat restrictive. We all like to indulge from time to time, but everything in moderation! If you can develop the habit of saving and being frugal, that will pay dividends in the long run. Think of the satisfaction in seeing your debt paid down and your assets accumulating. Your future self will thank you for it.

Set SMART goals – and remember to pay yourself first!

Budgets are the essential foundation for helping to reach goals, both short- and long-term. Budgeting helps clear the fog away so that you realize exactly how much you are making after tax. You see where your money is going – and where your money should be going.

Okay, so you've identified your fixed and variable expenses. Now it's time to evaluate. Suppose the money coming in covers neither what is going out in expenses nor your savings goals. You have two options: Boost your income or lower your expenses. Here's where you may need to make some tough decisions and scale back on some of your spending.

First, create a **SMART** goal, one that is:

- **S**pecific
- **M**easurable
- **A**ttainable
- **R**ealistic
- **T**imely

Once you have a clear vision for yourself, saving becomes easier. Resisting purchases here and there won't be as challenging.

There are many ways to go about this. Say you are too easily tempted to spend your cash and could use some extra discipline. We recommend separating your monthly funds into separate "buckets" for each category of your spending. Then, if your funds for dining out are gone by the end of the month, you know it's time to crack open the cookbook and experiment.

Luckily, in today's world we have many resources literally at our fingertips. There are some wonderful apps out there to help you track your spending and input your savings goals. However, we do recommend carefully researching any of these apps before using them.

Here's a simple way to save. If your paycheque is sent to your chequing account each month, you can set up automatic monthly withdrawals to go into a separate savings account.

There are other, less direct ways to save. One we recommend is meal planning, then transferring those plans to a grocery list. So, when you go to the grocery store, you have that plan to adhere to. You're not roaming through the aisles and whim-buying a mix of things beyond what you need for the week's meals.

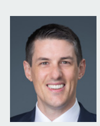
Another tip: At the grocery store, keep in mind the premium price put on brand-name products. Try no-name brands when you can.

What this all comes down to is that making conscious decisions now will set you up for success later. Those saved pennies add up! Even the little decisions you make can affect how much money you will have for future purchases – right through to your retirement.

Last but not least, we have one basic rule for you: **Pay yourself first**. Saving should be the first priority on the list of where your money goes. Figure out what is reasonable for you and put that amount away each month automatically. Once you choose the budget plan that will work best for you, saving will be more straightforward.

Most important, you need to be realistic. Reward yourself! You may start out gung-ho and refrain from buying any fun things at all. That's going to be impossible to maintain. Treat yourself once in a while – it's the only way the light will stay bright at the end of the tunnel.

With these tips in mind, your savings will add up faster than you think.



Tom Cowans is a Portfolio Manager and Wealth Advisor for the Stan Clark Financial Team at CIBC Wood Gundy.

SCFT Trivia

Play our trivia – support the cure!

For every correct entry we receive in our trivia contest, the Stan Clark Financial Team will contribute $1 to CIBC's "Run for the Cure" to raise money for breast cancer research. Each correct entry will also be entered into the draw for this month's prize. Email or phone in your entry today.

Answer all four questions to be entered into the draw for this month's prize. *Hint: You can find the answers inside this newsletter.*

1. A good way to think of intuition is:
   a. According to Herbert A. Simon, "The situation has provided a cue; this cue has given the expert access to information stored in memory, and the information provides the answer. Intuition is nothing more and nothing less than recognition."
   b. If it's expert intuition, it comes from years of experience and study.
   c. If it's intuition based on a gut feeling, it is mostly emotional and therefore not that reliable.
   d. All of the above.

2. Artificial intelligence (AI) is a broad term, but it basically involves automated decision-making by computers:
   a. True b. False

3. Generative Artificial Intelligence is an AI model that:
   a. Can do all your work for you.
   b. Should be avoided, as the content it produces is unreliable.
   c. Generates content in response to a prompt, producing a wide variety of writing in seconds.
   d. Produces totally accurate content that never needs checking.

4. Despite its negative reputation, budgeting is fairly simple. For example, if you have some restaurant dinners with friends planned, reconsider making those daily lunch runs from the office. Instead:
   a. Skip lunches altogether.
   b. Make your lunch at home and take it to work, thereby creating a more flexible budget for other things.
   c. Tell your friends you can't join them for dinners out.
   d. Keep buying lunch out every day – there's always a chance you'll win the lottery.

Email answers to: **stanclarkfinancialteam@cibc.ca** or call (604) 641-4361

One prize winner will be chosen by a draw from all those who submit correct answers. The draw will take place on June 30, 2023.

Trivia challenge runs June 1 - 29, 2023. No purchase necessary. There is one prize to be won. Simply complete the trivia questions correctly to be entered in the draw. Limit 1 entry per person.

Chances of winning depend on number of eligible entries and whether you correctly answer the trivia questions. Open to adult Canadian residents (excluding Quebec). For full challenge rules, write to: The Stan Clark Financial Team, CIBC Wood Gundy 400-1285 West Pender St, Vancouver, BC V6E 4B1. © Stan Clark 2023

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Phone: 604 641-4361 | Toll-free: 1 800 661-9442 | Fax: 604 608-5211 | Email: stanclarkfinancialteam@cibc.ca | www.stanclark.ca