



HCM MARKET BRIEF

Episode 2: Macroeconomic Implications of AI & Market Fundamentals

In this episode of the Market Brief Podcast, [Doug Johnson CFA and Dan Rinck](#) examine the recent market volatility driven by artificial intelligence (AI) narratives and the broader implications for investors. The conversation centers on the rapid rotation occurring across sectors, the disconnect between market reactions and fundamentals, and whether the current AI-driven turbulence represents a structural shift or a temporary overreaction.

The discussion begins with observations about the ongoing sell-off in various sectors, initially concentrated in software but now expanding to financial services, logistics, commercial real estate, and other industries. The driving force behind these moves is the perception that AI will disrupt or even replace large segments of the economy. Doug describes the market's current tone as "shoot first, ask questions later," where even minor AI-related developments can trigger massive sell-offs in established industries.

Dan notes that small AI innovations—sometimes launched by relatively insignificant companies—have led to billions of dollars in market value being erased from large, established firms. For example, a small custodian's AI tax-planning tool prompted sharp declines in major broker-dealers and advisory firms. Similarly, a tiny logistics-related company claiming to dramatically improve efficiency caused widespread selling in transportation stocks. In some cases, these companies have questionable histories or minimal scale, yet markets respond as if industry-wide disruption is imminent.

Doug compares this environment to the blockchain and cryptocurrency craze, referencing how small companies rebranded themselves during the crypto boom and saw their stock prices surge despite having little real exposure to the technology. The current AI cycle shows similar characteristics—headline-driven enthusiasm and fear, often disconnected from fundamentals.

Despite acknowledging AI's potential to create substantial efficiencies, both Doug and Dan express skepticism that widespread job displacement or full industry replacement will happen overnight. Doug raises practical concerns, such as accountability. For instance, while AI can assist in preparing tax returns, consumers still rely on human professionals for

oversight, error correction, and representation in case of audits. The idea that individuals would blindly trust AI outputs without verification raises significant risk.

The conversation then broadens to consider more extreme scenarios. Doug presents a thought experiment: if AI were to eliminate 10% of full-time jobs—roughly 10 million positions—that would exceed the job losses during the COVID-19 pandemic, which triggered massive government stimulus, emergency monetary policy, and unprecedented fiscal support. Such a shock would likely require structural economic adjustments, potentially including government intervention or even discussions around universal basic income. Dan agrees that while such scenarios are theoretically possible, they are far from imminent.

They explore the conflicting narratives surrounding AI's macroeconomic impact. On one hand, AI could be highly deflationary by reducing labor costs and increasing efficiency. On the other, if governments step in to offset job displacement with stimulus or income support, the outcome could be inflationary and negative for the U.S. dollar. These competing possibilities highlight the uncertainty embedded in current market pricing.

Doug argues that many stocks appear to be trading as if the most extreme AI outcomes are guaranteed to occur quickly. He cites the example of prior AI-related volatility, such as when a new AI model caused a sharp sell-off in mega-cap technology stocks, only for markets to normalize shortly afterward. He also points out that large corporations are committing enormous capital expenditures to AI infrastructure, even suspending stock buybacks to fund these investments. This signals conviction in AI's long-term importance, even if the short-term disruption narrative is overblown.

Rather than a broad “risk-off” move, the market is experiencing rotation. Investors are shifting away from perceived AI-vulnerable sectors and into companies that produce tangible goods or are seen as more insulated. Consumer staples and industrials have become crowded trades, reaching historically overbought levels even as the broader market remains near all-time highs. This unusual dynamic suggests investors still want equity exposure but are reallocating based on perceived AI risk.

Energy stocks are also performing well, though oil prices remain moderate. Doug notes that in prior cycles, energy leadership often preceded economic trouble when oil prices spiked high enough to hurt consumers. Today, oil in the \$60–\$65 range does not present the same headwind, suggesting current leadership may have a different foundation—possibly tied to AI infrastructure demands and energy consumption.

Emerging markets are another area of focus. Doug views this rotation as potentially more durable. Emerging markets combine attractive valuations, strong earnings growth, leverage to a weakening dollar, and exposure to both AI supply chains (particularly in Asia) and natural resources (notably in Latin America). He highlights that emerging markets recently reached 18-year highs on an absolute basis and appear to have significant relative upside compared to the S&P 500.

While small caps and value stocks have also outperformed, Dan remains cautious about assuming a permanent shift away from mega-cap growth leadership. He believes diversification is currently working well within portfolios, as exposure to value, mid-caps, small caps, and international markets has helped offset weakness in large growth stocks. However, he ultimately expects growth and mega-cap leadership to reassert themselves unless something fundamentally breaks.

Fundamentally, the macro backdrop remains supportive. Earnings growth is in the low double digits, inflation readings are stable, job numbers have surprised to the upside, and the 10-year Treasury yield has remained range-bound. These conditions are typically constructive for equities. The sharp reactions to earnings reports in some sectors appear disconnected from actual financial performance, reinforcing the idea that selling has been indiscriminate and sentiment-driven.

The conversation concludes with a discussion of Ray Dalio's recent commentary about a changing global order. Dalio argues that investors may need broader diversification beyond traditional stocks and bonds, potentially incorporating assets such as gold, commodities, and other uncorrelated strategies. While reactions to Dalio's views have been polarized, Doug sees merit in considering diversification strategies that hedge against currency debasement or structural change. Over the past decade, a simple stock-and-bond allocation worked well, but the next cycle may demand broader exposure.

Dan acknowledges Dalio's long-standing emphasis on global shifts and alternative assets. While he does not fully embrace the more extreme interpretations, he agrees that thoughtful diversification—including exposure to assets uncorrelated to U.S. equities and bonds—can enhance resilience.

Overall, the podcast presents a balanced perspective: AI is transformative and will produce both winners and losers, but current market reactions appear exaggerated relative to fundamentals. Diversification is working, earnings remain strong, and macro conditions are stable. While structural changes may be underway, the hosts believe that cooler heads will

likely prevail and that investors should focus on disciplined positioning rather than reacting to daily AI-driven headlines.