

# Artificial Intelligence

## Looking at New Technology From The Investor's Viewpoint

by Jeffrey Steele



Many forecasters believe artificial intelligence will prove to be one of the most important developments ever to impact the investment industry. The technology's implications are profound and are felt on more than one level.

On one hand, AI promises to make many tasks required of investors simpler, faster and more effective, with as yet unknown ramifications regarding investment performance. On the other hand, the advent of AI holds promise of creating whole new companies, funds, exchange-traded funds and other investments, which savvy investors may be able to identify and ride to the land of robust profits.

Like any other largely untried technology, AI also serves up a dark side to go along with its bright promise. The threats of algorithmic biases, dangers of lack of transparency and AI's not-yet-known impact on employment and the economy all provoke concerns among investment professionals, as well as many individual investors. In the pages ahead, we examine the promise and peril of AI and how you can make the most of the tool.

### ENHANCED OUTCOMES

The impact of AI on all of us could be enormous, said Erik Severinghaus, founder and CEO of Bloomfilter, a fast-growing Chicago-area company that uses AI-driven process mining for software development. "Picture this: AI algorithms crunching numbers faster than you can say 'bull market,' analyzing heaps of financial data in real time to spot trends and predict market movements," he said. "It sounds like something out of a sci-fi movie, but it's real, and it's changing the way we invest."

Agreeing about the enormity of the potential impact is Bas Kooijman, CEO and asset manager at Luxembourg-based DHF Capital S.A. Terming the possible effect "monumental," Kooijman said artificial intelligence may provide access to advanced analytics and automation up until now reserved for institutions. AI-propelled insights could help investors pinpoint trends, reduce risks and gain profitable opportunities with increased exactitude and quickness. The technology could also facilitate customized investment strategies personalized to the preferences and goals of individual investors.



“With responsible implementation and oversight, AI has the potential to enhance investment outcomes and democratize access to wealth creation,” Kooijman said.

Michael Platner, managing partner at Lewis Brisbois Bisgaard & Smith, a national law firm headquartered in Los Angeles, believes AI has the potential to place individual investors on a footing not unlike that of professional investors.

He also envisions the costs of funds using AI being lowered, allowing individual investors a broader selection of lower-cost, high-performing funds to contemplate for possible investment. Investors who trade stocks themselves and oversee their own investments will likely benefit from even more intelligent decision-making. Finally, Platner believes the most valuable, time-sensitive information once possessed only by the most sophisticated professional investors may trickle down to individual investors. “A lot of investor decision making is about the time it takes to do research and due diligence on the investment,” he added. “AI can expedite that and create greater speed and once again greater overall intelligence. [It] can be a resource for individual investors that puts the individual close to being on the playing field of a professional investor.”

AI isn’t likely to allow individual investors to correctly forecast market patterns and price changes or beat the market, said Michael Ashley Schulman, CFA, partner and chief investment advisor at Running Point Capital Advisors in El Segundo, Calif.

But in attempting to negotiate volatile financial markets, investors may parlay AI into better real-time insights and decision-making abilities than they’d otherwise possess. Schulman sees AI for the most part serving as a financial coach and collaborator for individuals and families, assisting them in deciding overall asset allocation by asking the right questions and reminding them to regularly fund 529 plans for their children, or individual retirement accounts, SEP IRAs or 401(k)s for themselves.

AI’s real value may be in removing the many human behavioral biases including:

- **disposition effect** or the premature selling of assets that have increased in value while keeping those that dropped in value;
- **recency bias**, favoring current trends over historic, long-term ones;
- **endowment effect**, or valuing stocks or funds you already own over others;
- **familiarity bias**, or investing in what you know;
- **and anchoring**, in which individuals fixate on a target number or value, impairing portfolio performance over the long run.

Schulman also foresees AI serving in a capacity not unlike Google Maps. He envisions AI asking about investors’ starting points and goals or end points, then showing various pathways to reach those goals while providing real-time updates as life-altering events take place. “The really smart and collaborative AI will also know when to tell you to seek personal professional guidance from a multifamily office or financial advisor,” he said.

“I suspect each of the major investment custodians — Vanguard, Schwab, Fidelity, Merrill — will develop its own in-house web-based AI for clients and potential clients to use. But these may have the issue of being biased toward their own products.”

As impactful as all these developments will be, they may be just touching the surface of AI’s potential, said New York City-based Cloris Chen, CFA, CEO of Cogito Finance. Chen and colleagues expect exponential growth of AI over the course of the next decade. That means that today’s AI is still in its infancy. “What we call AI right now is so-called narrow AI, which functions very well in handling repetitive or not-so-demanding tasks,” she observed.

“AGI, Artificial General Intelligence, is the next step that both SingularityNET and OpenAI are calling for. This will allow us to not only act upon trained data, but also reason with it and draw conclusions on investment decisions.”

For his part, Severinghaus believes AI doesn’t simply make investing smarter, it makes it more efficient as well. Algorithms will detect market inefficiencies quickly, helping investors make more informed decisions and more effectively manage risk. With AI-powered trading systems, investors will be able to strike with lightning-like speed when market opportunities present themselves, and lower their trading costs as well.

Smart investors understand they need to set goals, targets, criteria and screens, and conduct research and diligence, Platner observed. He predicted AI will reduce the costs of performing all these best practices, will help them be accomplished more quickly and will provide enhanced insights for the investor to consider.

AI will go beyond today’s “program trading,” integrating enormous amounts of disparate data into the decision-making process. Investors who select among funds or professional money managers will have to ask a few additional questions before those selections, including how they are using AI in selecting investments and how they implement AI to decrease the costs and increase the returns to investors, Platner said.

## STRATEGIES FOR THE AI ERA

How can investors ride the AI wave? Severinghaus suggests one approach would be to go the passive route by investing in index funds or ETFs that track AI-powered indices. “It’s like hitching a ride on the AI bandwagon without having to pick individual stocks,” he said. “Or if you’re feeling adventurous, you can dive into the world of AI-driven stock picking, either on your own or through specialized investment funds.”

Ryan Smith, AI and cybersecurity expert, and founder of QFunction, suggested a different approach. “Depending on the investor’s goals and appetite for risk, investing in AI generally means investing in individual stocks and ETFs,” said Smith, whose Torrance, Calif.-based company parlays breakthroughs in AI and machine learning to detect anomalies and threats within client companies’ data. “Investing in individual stocks for AI is easier, as a lot of the well-established larger companies are already making significant investments in the AI space. These



companies include NVIDIA, Microsoft, Google, Meta and Amazon. If you want something a little more diversified, an AI-focused ETF would be your best bet, such as Global X Artificial Intelligence & Technology ETF (ticker: AIQ). There are even ETFs whose trading decisions are dictated by AI, such as QRAFT AI-enhanced U.S. Large Cap Momentum ETF (AMOM)."

Severinghaus agreed on the wisdom of investing both in index funds and ETFs on one hand and individual AI stocks on the other. He also noted that venture capital presents opportunities to back early-stage entrepreneurial ventures on the leading edge of AI innovation. Of course, investors must prioritize thorough research and consideration of the inherent risks of each investment vehicle. "By diversifying across different AI investment options, individuals can capitalize on the transformative potential of this disruptive technology, while managing risk effectively," he added.

### POTENTIAL NEGATIVES

With the growing integration of AI into investing in the future, investors should remain aware the potential exists for an assortment of negative effects, Kooijman said. One potential drawback eliciting concern is the possibility of algorithmic biases, in which AI models may perpetuate failed investment decisions founded on biased data inputs or inadvertently maintain prejudiced practices. In addition, the rapid spread of AI-fueled algorithmic trading could worsen market volatility and heighten the danger of flash crashes or systemic disruptions, he said.

The often-voiced concern about AI's threat to employment, with the possibility that upwards of 300 million jobs worldwide could be placed in jeopardy by AI's growing power, yields as-yet-unknown ramifications. "This aspect warrants careful consideration," Kooijman said. "It not only affects individuals' livelihoods, but also poses wider economic and societal implications."

Severinghaus echoes some of the same concerns, observing, "AI isn't all sunshine and rainbows." In addition to too great a reliance on algorithms, with its tendency to spur herd behavior and market volatility, AI poses a risk regarding transparency. "AI algorithms can be clear as mud, leaving us in the dark about how decisions are made."

The issue of transparency is a concern for Chen as well. "We have to acknowledge the current state of AI, where the model itself is a black box," she said. And while there are research areas, such as Explainable Artificial Intelligence (XAI), we are nowhere near the end goal within the industry. "Currently, a lot of machine learning models used for investing are under the strict scrutiny of whole research teams, supposing it involves asset management worth millions of dollars."

If it hasn't been fully tested before being presented to investors, AI in addition has the potential to recommend poor investment decisions, Smith reported. "There's also a high risk of individual investors seeing AI as a 'get-rich-

quick scheme,' of sorts, letting the AI make all the investment decisions while the investor has no idea what AI is investing in," he commented. "Related to this risk is the concept of brain drain within the investment industry due to AI, although I believe there will always be a need for investors who know the nuts and bolts of various investment strategies."

Like many tools placed in the wrong hands or relied upon too heavily, AI poses the danger of lulling investors into a false sense of safety or assurance in the conclusions of AI mechanisms, Platner said. Smart investing depends as heavily on risk management as it does on seeking returns. There will likely be some people who rely too heavily on AI, without implementing checks and balances on performance. "Of course, AI might become a better risk manager ultimately as well," Platner acknowledged.

### WHERE TO?

Within the next five to 10 years, look for AI to usher in a sea change in every industry, Kooijman said. In patient care, AI-enabled diagnostics and treatment recommendations will lead to more precise medical care and more improved health outcomes. In transportation, self-driving vehicles could translate to lowered traffic congestion and crashes, and increased convenience and accessibility. Similarly, he said, "in finance, AI-driven algorithms could help optimize investment strategies, providing investors with real-time insights and predictive analytics to navigate volatile markets."

Smith said he believes an increased number of companies will pivot towards AI for their products and services, which will exert an influence on their investment decisions. As the amount of financial information produced grows steadily larger, we all will witness increased use of automation in guiding investment decisions. "More sophisticated AI algorithms applied to finance will also continue to be developed," Smith predicted.

Platner sees parallels between AI's promise and the gains reaped by universal adoption of smartphones. In much the same way the phones have made humans more effective in completing a wide range of tasks, he said, "AI will overall serve to extend the reach of human capacity and create overall enhanced intelligence. We already have seen the growth of AI capabilities surpass the predictions of the last decade by a wide margin."

In the final analysis, AI will likely take its place alongside a long list of advancements. In serving up powerful tools and insights to improve their investing, AI will be a game changer for individual investors. But it's not without its pitfalls, Severinghaus said. "So, it's crucial to stay informed, observe and remember that while AI can be a great ally, nothing beats good old-fashioned human judgment," he added. "So, buckle up, fellow investor, for the AI revolution is here, and it's time to make the most of it."

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