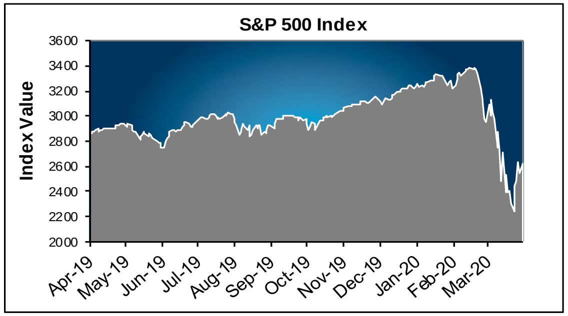
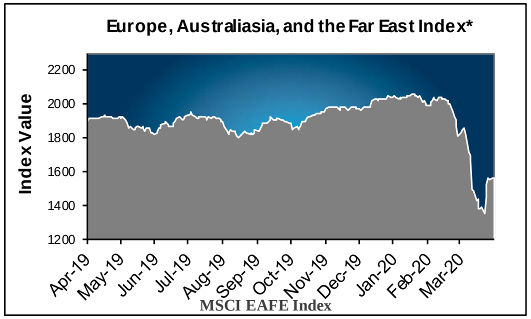
Stock Market Analysis

Unprecedented Times





The insidious COVID-19 virus has rapidly spread throughout the globe and changed our very existence - the way all humans live, work, shop and congregate. We all hoped when we wrote this newsletter a month ago that the virus spread would be contained in Asia but unfortunately that has not been the case, as modern transportation sealed our fate. While we have seen the pandemic movies, few people expected to see most major cities around the World virtually shut down with millions of people suddenly unemployed. Most of us fortunate enough to have a job are working at home next to our family and pets. Suddenly all our priorities have changed.

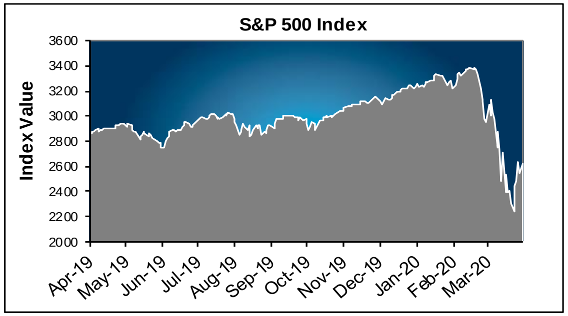
Anchor's team remains focused on making sure your portfolio will weather this storm and rebound when the clouds clear. It is impossible to predict tomorrow's headline, but we are confident that the virus case curves that we study every day will eventually bend down and the world will get back to business. Some daily habits will change forever but peoples' lives will go on. Those of us who have witnessed the Crash of 1987, the Tech Bubble and the Great Financial Crisis are skeptical optimists. We have learned that fear is the greatest enemy of long-term investors and know that many investors will sell everything at significant losses and remain in cash when the markets anticipate the inevitable economic recovery. Long-term investment allocations should not be altered in the midst of any crisis. At the same time our team is focused on positioning portfolios to weather the economic downturn and to benefit when the news gets brighter. While we know that the sudden shutdown of many industries will cause a short-term economic shock, current fiscal and monetary policies around the world should be sufficient to limit permanent impairments for certain investments. We will likely experience several quarters of double digit negative global GDP growth but expect that to be followed by improving trends as people go back to work and consumer confidence returns.

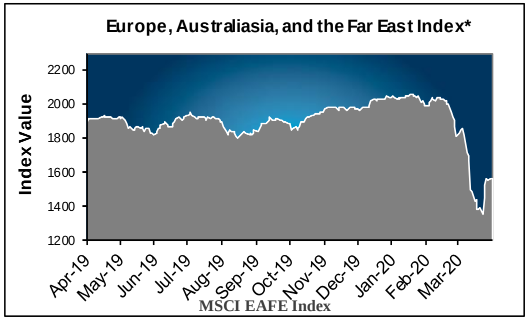
The MSCI ACWI Index recovered some of its losses in late March but fell 21.4% in the first quarter with the U.S. S&P 500 Index tumbling 20%. International markets, as measured by the MSCI EAFE Net Total Return Index fell by 22.8%, and the MSCI Emerging Markets Net Total Return Index sank 23.6%. Cyclically sensitive sectors witnessed larger losses, while utilities, telecoms and staples held up better. The sudden demand shock and OPEC's unwillingness to adjust supply caused energy prices to collapse more than 60%. As a result, energy shares led the market declines with the MSCI ACWI Energy sector plunging 44% in the quarter. Falling interest rates and credit concerns weighed on the financial sector with the MSCI ACWI Finance sector sinking 32%. Banks recouped some of their losses at the end of the quarter as many countries introduced consumer and business bailout packages and central banks calmed the markets with programs used during the Financial Crisis.

MSCIEAFE Index All stock index returns are adjusted for 30 percent foreign withholding tax.

Stock Market Analysis

Unprecedented Times



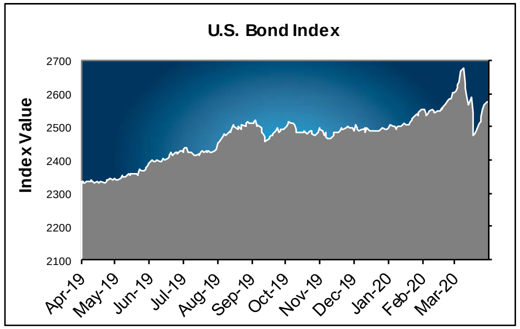


As we pointed out last month - if history is any guide, there will be a point that the market dispassionately ignores the virus-related headlines and looks towards the future and when it does, quality companies with secular growth should perform exceptionally. When we recognized the potential devastating impact on the travel industry, we sold both Air Lease and Delta in March. The former has lost 41% since our sale and the latter has fallen 17%. We sold Aramark in late February, recognizing that there was a major risk to their food service businesses at sports arenas, universities and other institutions. The shares have collapsed 47% since the sale. The selloff has offered opportunity to pick up a few high-quality companies with strong competitive positions. One company we added was Microsoft ("MSFT"). It is very likely that many of you who can work from home are using Microsoft products and in fact are completely reliant on its cloud infrastructure. Azure, MSFT cloud platform, is a $7 billion business growing almost 100% per year. We believe it will exhibit similar growth for the medium term and may, in fact, see increasing adoption as companies realize the need for cloud redundancy and remote working. The company sports an impressive moat with high switching costs (would you cancel your Office 365 subscription?) and network effects (everyone seems to use MSFT products). When we consider the virus and China, we like to use an accounting term – FIFO (First In, First Out). China is indeed recovering first and getting back to normal. A clear winner from this virus crisis is Tencent. Tencent's enormous user base and network effect makes it a virtual monopoly in China when it comes to messaging. We Chat is used by over a billion users in China and ranks as the number one app. It is integral to payments and communications in China. Tencent also is a dominant provider of online gaming which has seen a dramatic surge from China's enforced quarantine measures .

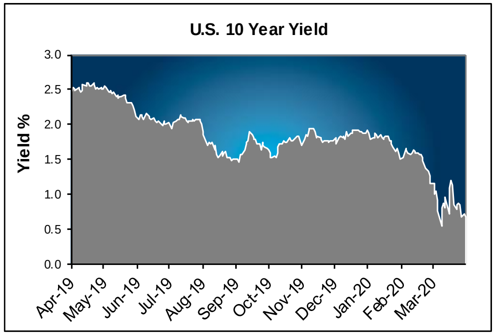
MSCIEAFE Index   All stock index returns are adjusted for 30 percent foreign withholding tax.

Fixed Income Analysis

March Madness



Merrill Lynch US Corporate & Government Index



U.S. 10 Year Treasury Yield

Each year in March the NCAA basketball tournament commonly referred to as “March Madness” takes place. Although “March Madness” didn’t occur on the court this year, it was unfortunately very much in effect throughout financial markets as it became clear COVID-19 was going to be the catalyst for a global recession. Specifically, the near total shut down of western economies for an unknown amount of time. Markets don’t like uncertainty and the search for safety that ensued was rapid.

The greenback rallied as investors sought safety in the world’s reserve currency and money flowed into Treasuries pushing yields down across the curve. The 10-Year Treasury yield compressed 47bps to end the month at 0.67%. The plunge in equity prices resulted in margin calls, and unwound levered trades, corporate credit sold-off across the board, regardless of tenor, sector or rating. Cracks were beginning to appear. The largest corporate bond ETF traded at a 6% discount to its net asset value as money flowed out of the space. Corporate credit spreads widened far more than the credit default swaps, a derivative that is pure measure of credit risk. The common denominator in both of these anomalies: A lack of liquidity and as a result, the baby was being thrown out with the bathwater. Unfortunately, it was difficult to take advantage of the panic selling as traders reduced their inventory risk by demanding huge bid/ask spreads.

Eager to stymie the carnage in credit markets and grease the wheels of the financial system, the Fed acted very swiftly and cut Fed funds rate 1.50% to the zero bound (over two announcements). The Fed also re-instituted and expanded the scope of the market supportive policies enacted in the GFC, supporting primary dealers, money market funds, and expanding its dollar swap lines with foreign central banks. In addition to these policies, the Fed announced it would support the municipal bond market and investment grade corporate debt markets – both primary and secondary. This is the Fed's version of "whatever it takes", akin to the action of the of the European Central Bank in the European Debt Crisis. Essentially, unlimited quantitative easing to ensure markets can function. This was bullish for corporate credit, which rallied since the announcement. For the month of March, the ICE Bank of America US Investment Grade index returned -7.4%, while the ICE Bank of America US High Yield Index returned -11.8%. Meanwhile the ICE Bank of America US Treasury index rose 3.3%. The Fed’s actions and the passage of the government’s stimulus bill appears to have stemmed the rapid price decline of risk assets. Nonetheless, the US is in recession so we remain wary and would not be surprised to see volatility remain elevated. No one knows how long it will take for western economies to get back up to speed or when the COVID-19 induced shutdown ends. The sudden halt of business will cause bankruptcies (levered energy, retail, industrial and travel companies are at high risk) and the headlines are likely to be negative for some time to come. Having said this, we are comfortable with the credit quality of the companies in our fixed income portfolios and are evaluating attractive risk/reward opportunities in the space.