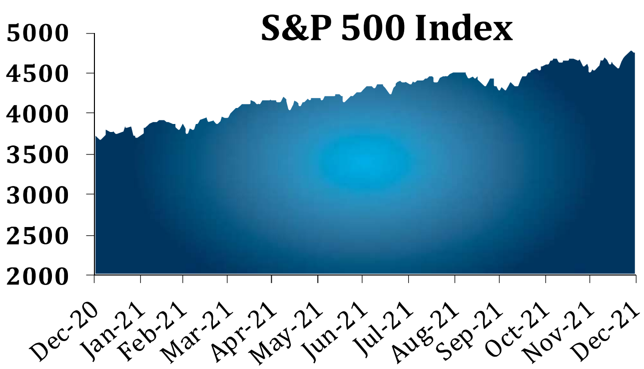
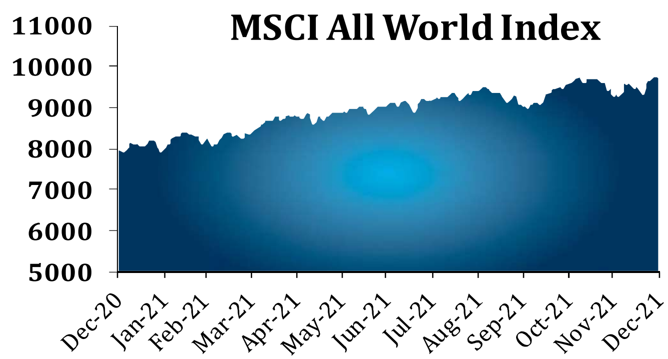
Internal

Stock Market Analysis

Prudent Stock Selection is Rewarded





ANCHOR
Investment Management

Investors began 2021 optimistically, hoping economic activity would recover from the impact of the Covid pandemic as vaccines were rolled out. Few people forecasted a year of multiple waves of virus variants shutting down cities across the globe as governments struggled to vaccinate their populations. Over nine billion vaccine doses have been administered worldwide. During the pandemic we have learned a life lesson in human tenacity. People and businesses have adjusted to the new normal. Despite the health challenges, we have discovered new ways to communicate, shop, exercise and even travel. Economic activity rebounded as most people got back to work and play. The rebound was so strong and the covid disruptions so persistent that supply chains could not keep up with surging demand causing inflation to rise.

Few professionals would have predicted strong double digit returns in the equity indices in 2021, especially considering the impact of Covid, rising inflation and supply chain issues. It was a year of prudent stock selection following 2020 when the indices were driven by a narrow group of mega-cap shares. Anchor was fortunate to manage the market volatility, producing strong alpha in our equity portfolio in 2021. **The Anchor equity portfolio returned 7.5% in the quarter and 25.2% for the year (after management fees) compared to 6.5% and 18.0% for the MSCI All Country World Net Total Return Index benchmark.**

Looking ahead to 2022, we understand that there are ongoing health and economic challenges, but we are confident that the companies in the Anchor portfolios are positioned well to continue to produce strong returns. We are dealing with some headwinds, with the U.S. Federal Reserve withdrawing liquidity from the market and their intention to begin rate hikes in the second half of the year. The personal consumption expenditures price gauge, which the Fed uses for its 2% inflation target, increased to 5.7% in November from a year earlier, the highest reading since 1982. But the Fed reaction to rising inflation has been cautious and their loose monetary policy has left the risk of “free money” on the table. The “Dot Plot” indicates that they will only raise the Federal Funds rate by 1.5% over the next two years.

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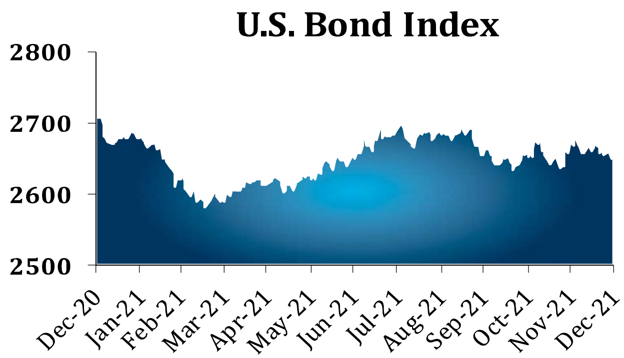
Stock Market Analysis

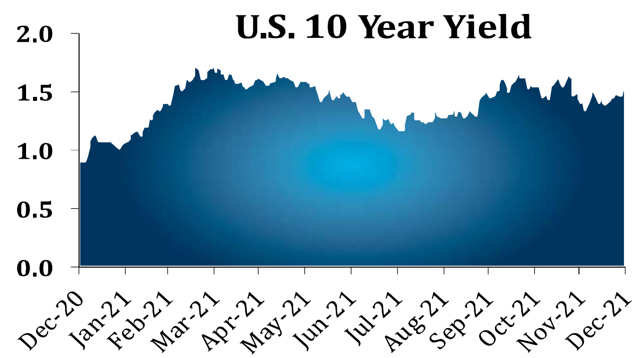
We recognize that there has been considerable speculative activity due to accommodative central banks around the World. We have already witnessed some of the market excesses reverse in the fourth quarter with the sell-off of crypto currencies and high valuation stocks. Despite rising inflation and monetary headwinds, there are several reasons why the economic rebound should continue this year. Congress approved a $1 trillion bipartisan bill to upgrade America's roads, trains, electricity grid and other infrastructure. New Covid treatments, including pills from Pfizer and Merck, should further improve the health outcomes from people exposed to the virus. ESG investments present significant new growth industries, as the transportation, energy and utility sectors reinvent themselves. New investment themes include artificial intelligence, clean energy, nuclear fusion, robotics and the metaverse. We believe selective investment in reasonably valued companies with strong management teams and distinct economic moats will continue to be rewarded.

Internal

Fixed Income Analysis

The Year of Inflation's Return





ANCHOR Investment Management

In the early December Federal Open Market Committee (FOMC) meeting, Chairman Powell announced they would decrease the pace of asset purchases (tapering). Tapering is now set to be completed by the end of March 2022. In addition, the FOMC dots (which show individual member forecasts for the path of the fed funds rate) show a median expectation for three rate hikes in 2022, up from only one in the previous meeting. Market reaction was muted to the announcement as Chairman Powell had already set market expectations in his November testimony to the Senate Banking, Housing, and Urban Affairs Committee. Another Powell pivot was complete – from a dovish assessment of "transitory" inflation and still recovering labor market, to a more hawkish tilt with a focus on inflation deemed no longer transitory.

Interestingly, there was no word from Powell on whether the Fed plans to shrink the balance sheet while also raising the fed funds rate. Note that this situation came to an ugly head in Q4 2018, where credit spreads flared, and the equity market sold off. This ultimately culminated in the first Powell pivot (stopped shrinking the balance sheet and reduced the terminal fed funds rate expectation). Another point to note is that from 2023 onwards, market expectations for short-term rates (such as fed fund futures and overnight index swaps) are well below the FOMC dots median projections, indicating the market's expectation for fewer rate hikes than the Fed is projecting in this cycle. These are two factors we will be watching in 2022.

Looking back on 2021, the emergence of inflation was the biggest story for bondholders on the macroeconomic front. The consumer price inflation index (CPI) reached a year-on-year (YoY) high of 6.8% in November, driven by supply chain issues, favorable base effects, and strong consumer demand for goods. However, it's interesting to note that the 10-year treasury peaked at 1.74% on March 31st. The latest CPI figure at that time was 2.6%. The YoY CPI would then increase almost every month until the end of the year. This is a great example of the market's forward-looking nature. The market does not believe that the current elevated inflation figures will be a lasting phenomenon. Going into 2022, we have the Fed tapering asset purchases (and then raising rates), much tougher base effects, and less fiscal spending. This would suggest YoY inflation figures should begin to decline as the year progresses.

Internal

Fixed Income Analysis

Credit spreads spent the entirety of 2021 in historically tight territory driven by investor reach for yield and low default rate expectations. These periods of tight credit spreads can last for extended periods. However, nothing lasts forever. We don't know when, but a point will come when spreads start to widen. Given that corporate bonds are less liquid than stocks, when there is a mass move to the exit, liquidity gets thinner, and price declines become more severe. We saw this play out with a bang in March 2020. While we're not calling for a similar blow-off, our views on corporate credit have become more cautious at the margin given valuations and the Fed's hawkish pivot. As a reminder, our high yield positions are mostly comprised of companies in the highest-rated cohort of the high yield universe, which we expect to be upgraded to investment grade in the near future.

The U.S. dollar was the strongest performing developed market currency in 2021, driven by favorable growth and interest rate differentials. This outperformance was most notable versus the euro and yen. The dollar is a momentum currency and typically outperforms when the U.S. is growing faster than global growth ex-U.S. or when there is a widespread risk-off move. As such the trajectory of the dollar in 2022 will somewhat depend on whether (and if so the extent to which) China stimulates its economy given the flow through to the economies of emerging markets and Europe through exports to China. Another factor is the reaction function of the world's most economically influential countries in dealing with future outbreaks of COVID-19 and variants. A permanent slackening/abolishment of restrictions could fuel global growth and lead to a period of dollar weakness.