The Ancora Advisory

An Investment Publication for Clients and Friends

Ancora Holdings Inc. consists of three business units; Family Wealth, Asset Management and Retirement Plans. With top-tier portfolio managers, unique investment strategies and an entrepreneurial spirit, Ancora delivers tailored solutions so you can achieve more ... on your terms.

Reflections on Recent Stock Market Volatility

David Sowerby, CFA

Managing Director, Portfolio Manager

Recent activity in the stock market has once again reminded investors that prices correct, and when they do, it can test the will of those claiming to be long-term investors. The S&P 500 has corrected 8% since late January and done so rather abruptly in the past week. The average S&P 500 stock is now off 15% from its 52-week high.

When the market witnesses this quick of a decline, we are often queried for the causes. In this particular case, investors were well aware that the market had witnessed over a year and a half of above average gains, without even a setback of 5%. This recent decline is primarily the result of higher than expected interest rates over the last month. To be sure, there were additional factors, including greater investor complacency and concerns that many assets were getting overvalued, to name but a few. As usual, when corrections occur, it is often easy to identify the causes.

In this case, not only the causes matter, but more relevant is the assessment of how deep this decline might be. More specifically, are recent events the start of a 20% or greater “Bear” stock market? When reviewing the main elements that historically signal market tops and impending Bear markets, this recent decline has few of those factors. More likely this is a more normal, but nevertheless unpleasant, 10% stock market correction which could well linger for multiple weeks.

A quick review of the U.S. stock market history shows that corrections occur once a year on average. In contrast, Bear markets of 20% or more occur about once every 3 ½ years. Importantly, the chances of a 10% setback becoming a more severe decline of 20% or more is about one in three. That likelihood is further reduced against the backdrop of an expanding economy and healthy corporate profit growth. The traditional Bear market indicators such as heightened M&A activity, poor capital discipline exhibited by companies, inflation rates above 4% commensurate with meaningfully higher interest rates and significant high yield bond market weakness, all of which foreshadow major stock market problems, are quite limited.

In closing, the recent stock market weakness could well linger for multiple weeks. Stock market data for the last fifty years shows that the average 10% type correction takes approximately four months on average to recover. For example, in the current Bull market we have witnessed corrections in 2010, 2011 and the most recent in early 2016, each one lasting for multiple weeks. Fortunately, for the majority of investors, their time horizon is longer than that. So, while we expect this heightened volatility and potential for down days to linger, our commitment to building enduring portfolios comprised of companies and strategies that are shareholder focused with superior capital allocation discipline and trading at more compelling valuations, is unwavering.

Thoughts on Interest Rates and the Yield Curve

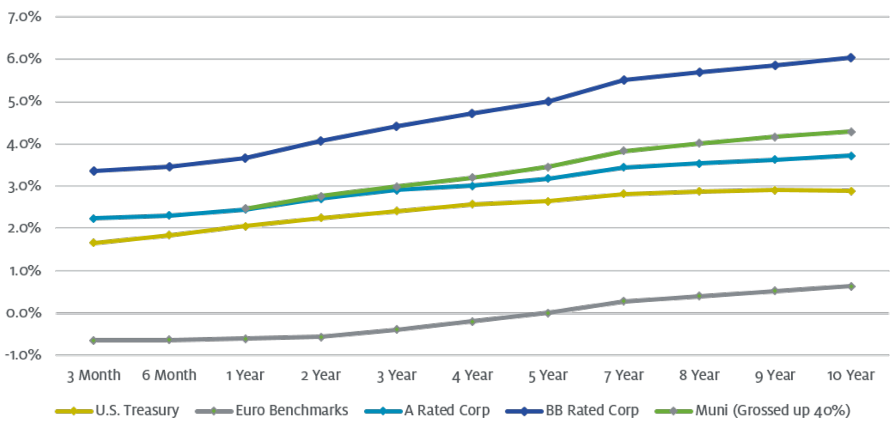
Jim Bernard, CFA

Managing Director, Fixed Income

Over the last six months intermediate term U.S. government bond yields increased just over 100 basis points, and year to date they have increased over 40 basis points. The actual yield curve remains relatively flat with 2 to 10-year yields differing by only 64 basis points. Historically, 10-year Treasury yields average about 100 basis points higher than 2-year Treasury yields. Continued low inflation numbers are a major reason longer term interest rates remain very low. Additionally, a very accommodating FED monetary policy has contributed to lower rates in recent years.

Going forward the primary questions surrounding interest rates are as follows. Will this recent movement higher continue? Will historically low credit spreads continue? How will worldwide interest rates and central bank policies around the world influence our interest rates in the next few years?

Yield Curves



Source: Bloomberg, March 5, 2018

As the adjacent yield curve illustrates, not only are yield curves relatively flat (as discussed above), but U.S. rates remain significantly higher than Euro sovereign bond yields. A more accommodating central bank policy in the Eurozone and Japan and economic growth that, in general, trails the U.S. recovery this cycle, accounts for lower rates overseas. Because of these historically low rates overseas and significant demand for yield, 5-year maturity high yield Euro bonds are currently trading at 3.00%, or just 35 basis points above the 5-year U.S. Treasury note. This means that high yield Euro corporate notes trade at lower yields than High Grade U.S. Corporate bonds, which obviously seems irrational.

We believe going forward this unusual pattern of U.S. rates versus Euro rates will serve to somewhat keep a lid on how high U.S. rates will go over the next few years. While we still expect three or more rate increases by the FED over the next year or so, and the potential for some credit widening associated with the FED balance sheet reduction program, we do not believe rates will take off on the upside for reasons discussed above. All of this assumes that inflationary pressures remain low for the foreseeable future. We believe a modestly steeper yield curve is likely since a little inflationary pressure may appear this year.

How Market Volatility Affects Retirement Income Planning

Howard Essner, JD

General Counsel, Family Wealth & Retirement Plan Advisor

The recent market volatility has reminded all of us of an important consideration when an investment portfolio is being used to support living and other expenses in retirement. This important consideration is called “sequence of return” risk. Sequence of returns is simply the order in which the annual returns of your portfolio occurs. Sequence of returns have only marginal impact on the performance of a portfolio over a long period during the accumulation phase. However, in retirement, sequence matters. Two individuals, with the same withdrawal needs and average rates of return over their lifetimes, can have very different results depending on when the good and bad investment return years occur. Stated simply, we want good returns early in our retirement, and can accept lower returns later in retirement.

Since we cannot always control the timing of portfolio withdrawals, and certainly cannot control the timing of market returns, how do we mitigate sequence of return risk?

Plan

A sound retirement income plan must include sequence of return risk analysis. That is, projecting retirement income with a simple average rate of return is not sufficient. At Ancora, we “stress test” multiple scenarios for every retirement plan using tools such as bad timing analysis, bear market safety margin analysis, and Monte Carlo analysis. All of these tools help us understand how sequence of return risk can impact a client’s plan. These tools also help us design an asset allocation that provides the appropriate level of risk and return to meet the client’s specific spending needs.

Use a Cash Reserve

A sound cash reserve, three to six months or more of spending needs, can alleviate the pressure to sell into declining markets. The cash reserve can be spent down, and then replenished when market returns are more satisfactory.

Maintain Diversification

Portfolio diversification, including stocks, bonds and alternative, low or negatively correlated assets, can minimize sequence of returns risk. With proper diversification, we can avoid selling underperforming asset classes to fund spending, helping to maintain the long-term prospects of the portfolio.

Develop an Income Stream

Income producing assets, such as high dividend paying stocks, can help reduce the need to rely on capital appreciation to fund spending.

Maintain Spending Flexibility

The most successful retirement plans are the ones with spending flexibility. If spending needs have a large fixed component, it is often not possible to avoid ill-timed drawdowns of the portfolio. However, the long-term success of a retirement plan can be significantly improved if discretionary spending can be deferred following years of poor market returns.

Please contact your Ancora advisor if you would like more information about our Lifetime Planning process, including retirement income planning.

Bitcoins, Bubbles and Blockchain

John P. Micklitsch, CFA CAIA
Chief Investment Officer

We continue to receive numerous inquiries regarding Bitcoin and other crypto-currencies and we have cautiously decided to share our thoughts with you on the subject.

In terms of what Bitcoin is, it is an alternative and 100% digital form of currency whose appeal is that it is not backed by any government and therefore lies outside the manipulation, regulation or trace of any sovereign entity. It is not the only crypto-currency out there, but it is the largest by size and therefore garners the majority of headlines. Bitcoins are "mined" via a computer through a series of complex computations. These grow progressively more difficult to solve the closer you get to the terminal number of Bitcoins, which in its case is approximately 21 million coins.

Just as physical gold miners may find it more difficult to find the next ounce of gold in the mine, Bitcoin miners face the same scarcity value of obtaining future coins. This is perhaps the most ingenious aspect of the Bitcoin's architecture and is an aspect that champions of the crypto-currency stress as a critical differentiator and potential hedge versus fiat currencies, which can be inflated and devalued by governments and monetary policies.

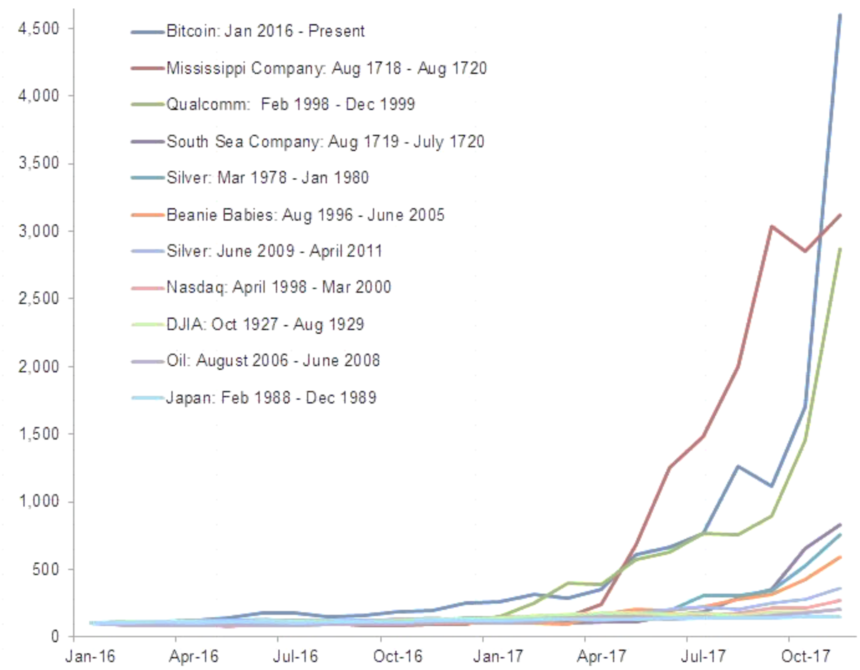
While there has been widespread focus on the price of Bitcoin and other cryptos, many believe the real breakthrough with digital currencies is the underlying technology, known as blockchain. In its simplest explanation, blockchain technology is a distributed ledger that uses the power of peer to peer computing to track, record and settle digital currency based transactions all over the world and without the requirement of a dedicated network. This open architecture aspect is what many believe is the most powerful and commercially scalable aspect of digital currencies and blockchain in particular. This potential is not lost on the world's largest financial institutions and technology companies who are actively evaluating the underlying blockchain technology itself for their own use and commercial development.

In terms of how far Bitcoin and other digital currencies can go, the adjacent chart puts the current Bitcoin frenzy into historical perspective relative to other famous bubbles. Note the chart is a few months old given the fast-paced pricing environment for Bitcoin, but as you can see, it ranks amongst the highest speculations of all time.

Nevertheless, despite rational, fundamental analysis of the risks associated with Bitcoin, it could still go higher, fueled "by the perfect intersection of ambiguity and animal spirits," as Robert Shiller described in an article in the New York Times.

The ambiguity, in this case, refers to the uncertain, fundamental value of Bitcoin itself. In contrast to Bitcoin, the value of

Bitcoin and Past Financial Bubbles

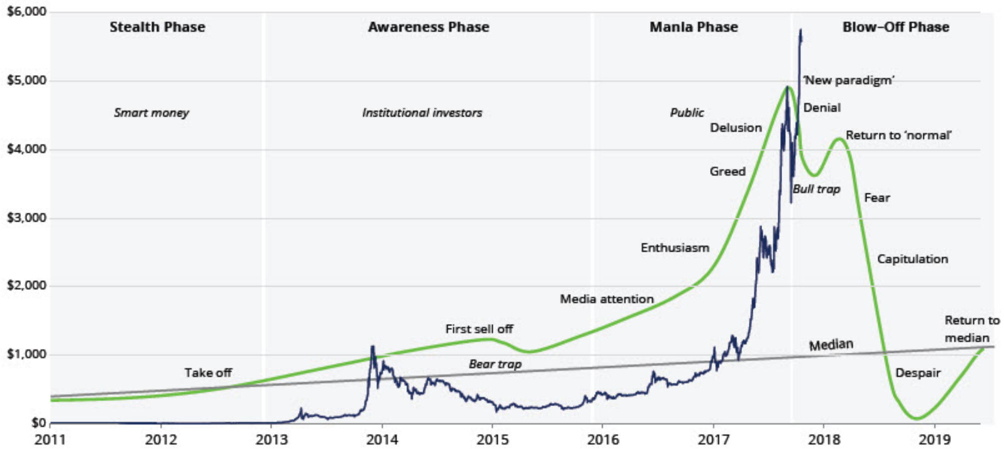


Source: Birinyi Associates via CNBC, October 2017 a company's stock is essentially the present value of its future cash flows. Within reason, this value can be approximated given assumptions about the business' future growth, risk and prevailing interest rates. However, neither Bitcoin nor gold, as it is often compared, produce cash flows, or anything else of an operating nature for that matter. Therefore, the value is less certain beyond what the next person in line is willing to pay for it.

When animal spirits take over in an ambiguously valued asset with ingeniously designed scarcity value, there is no telling how high or how far the price will go before the music stops. Eventually, though, it does stop because either the next buyer in line will simply not materialize, or in Bitcoin's case, governments decide to change the rules of the game in order to protect their interests, such as economic control and taxing authority.

As an additional visual reference, the following is a chart from Hartford Funds overlaying Bitcoin on the classic bubble pattern.

Financial Bubble Pattern



Source: Hartford Funds, Thomson Reuters Datastream, October 19, 2017

Maybe this time is different and crypto-currencies will escape the fate of past bubbles in terms of price, but we view this as unlikely. Recall that while Bitcoin itself has limitations on the number of coins that can be produced, there is no limitation on the number of crypto currencies themselves that can be launched, which can lead to an oversupply of issues similar to the deluge of new issues that ultimately contributed to the popping of the Internet bubble. The underlying blockchain technology, on the other hand, appears to have an enduring set of potential applications that bears close monitoring.

In closing, without a fundamental way to value the asset, it is virtually impossible to make a recommendation as to whether you should buy or sell Bitcoin or any other crypto currency. The one advice we will give you is that these bubble-like situations typically end badly for late adopters or for those who stick around too long. We would recommend treating any possible capital you are considering committing to digital currencies as pure speculation and as money that you are prepared to lose (potentially all of).

Additionally, if you do choose to speculate, it is imperative to find somebody who can help you with the safekeeping of your digital assets. Unlike gold or cash and securities stored in a regulated institution, Bitcoin and other crypto-currencies exist precisely to remain outside the reach of government, so you are largely without recourse at this point should anything go awry with the custody of your asset.

We hope this was helpful and if you have any additional questions, please feel free to contact your Ancora representative.