

# The Ancora Advisory

An Investment Publication for Clients and Friends

*Ancora is a private wealth advisor and institutional asset manager focused on building distinctive investment strategies and robust wealth and risk management solutions that help you achieve more*

## What's Next for Artificial Intelligence?

John Micklitsch, CFA, CAIA

President & Chief Investment Officer

Growing up, a friend's dad would often make statements on sports figures as if they were novel observations. Commenting on Michael Jordan (who at the time was probably in his sixth year in the league and had already won the NBA scoring title a handful of times), I remember him saying, "You know, I think this Michael Jordan is going to be a pretty good ball player." Today, that would be like talking about Artificial Intelligence's potential and saying, "You know, I think this AI stuff is going to be a pretty big deal." While factually correct, neither would qualify as bold statements at the time they were made. Perhaps the more interesting question when it comes to Artificial Intelligence would be, where AI is going at this point, and what's next in its evolution.

To answer that question, let's first start with the money that is being spent to build the underlying infrastructure to train, develop and deploy AI models. It is estimated that the aggregate capital expenditures over the next twelve months from just five large publicly traded hyper-scalers, Microsoft, Alphabet, Amazon, Meta and Oracle, will top \$375 billion. That means that roughly 40% of the estimated annual \$1.0 trillion of cap-ex in the S&P 500 is currently going towards AI infrastructure. The logical next questions might be how we are going to use all this AI capacity and whether the hyper-scalers will ever earn attractive returns on their investments.

For that, let's look at JP Morgan, which is reported to spend roughly \$18 billion per year on information technology, of which \$2.0 billion is earmarked for AI use case development within the bank's many departments and processes. It is estimated that AI, across 450+ internally-developed use cases, is now saving JP Morgan employees 15 million hours annually, has resulted in nearly \$2.0 billion in productivity gains and has saved something approaching \$1.5 billion in preemptive fraud detection losses annually. How ever you measure it, that sounds like a pretty good return on investment. Now, who gets to keep all those gains? Is it JP Morgan and its shareholders, is it customers, is it the hyper-scalers who built the infrastructure? The answer is probably all of the above. But it is real, and it is happening now.

I think we are all waking up to the potential of AI—both personally and in the businesses, organizations and enterprises we are involved in. We are just starting to scratch the surface. We believe we are entering a period where attention will begin to shift from the hyper-scalers building massive AI infrastructure to the use cases that will now permeate corporate earnings reports and success stories throughout the rest of the economy.

And as far as jobs go, we believe Nvidia CEO Jensen Huang summed it up well when he said, “You won’t lose your job to AI, but you may lose it to somebody who is using AI.” So, the time is here to lean in, experiment, try to automate something that is a nuisance to you, or if you have never used it before, try asking a question in the prompt window of any of the popular AI chatbots. You might be pleasantly surprised. Because, as my good high school friend’s dad would say, “This AI thing looks like it’s going to be a pretty big deal.” ♦

## The Days of 4% Money Market Rates May be Numbered...

Kevin Gale

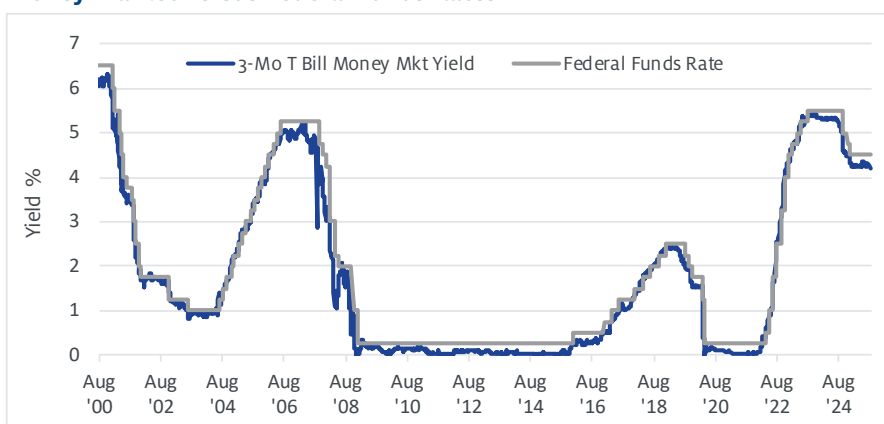
Managing Director, Head of Fixed Income

As expectations continue to rise that the Federal Reserve will cut the Federal Funds rate (the interest rate banks charge each other for overnight borrowing of reserves), money market rates will in turn also be impacted. Investors should consider how these changes may impact their portfolios and how best to prepare for a lower-rate environment.

Most investors maintain a certain level of cash invested in a money market mutual fund within their portfolio. Over the past several years, we have been able to enjoy returns in excess of 4% on that cash. In addition to the excess cash investors have, due to the higher money market returns, investors have been tempted to also keep their fixed income investment allocation in a money market fund. While this strategy may have worked over the past two years, with the Federal Reserve likely on the cusp of resuming interest rate cuts, it may be a good time to rethink this strategy.

We’ve seen historically that as the Fed begins to cut rates, returns on money market funds steadily decline as their yields closely track the Federal Funds rate. The following chart displays the 3-month Treasury bill money market yield versus the Federal Fund rates.

**Money Market versus Federal Funds Rates**



Source: Bloomberg, as of 8/15/2025

### What should I be doing with my cash now?

For those holding cash for short-term liquidity needs, a money market fund continues to be a good option. However, for those holding their portfolio’s fixed income allocation in a money market, we believe now is the time to begin moving to longer maturity fixed income securities to lock in the higher yields. At Ancora, our fixed income team typically prefers a laddered bond portfolio approach with staggered maturity dates, as we believe that can be beneficial for investors seeking to manage risk-generating income. The laddered bond portfolio approach allows investors to capture various points of the yield curve, essentially locking in yields for an extended period of time. In addition, in a laddered portfolio, when a bond matures, investors can choose to reinvest the principal at the current market rates, redeploy the principal in a different asset class such as equities, or simply keep the funds in cash for liquidity needs. Please reach out to your Ancora advisor to further discuss how to better position your fixed income portfolio for different interest rate environments. ♦

## Profits, Policy and Portfolios: Navigating the Tariff-Tax Tradeoff

David Sowerby, CFA

Managing Director, Portfolio Manager

Markets have meaningfully recovered from their April 8th lows. The majority of domestic stock indices are up between 20-30% and this rebound following a 20% sell-off has been significant when compared to the average recovery following a bear market.

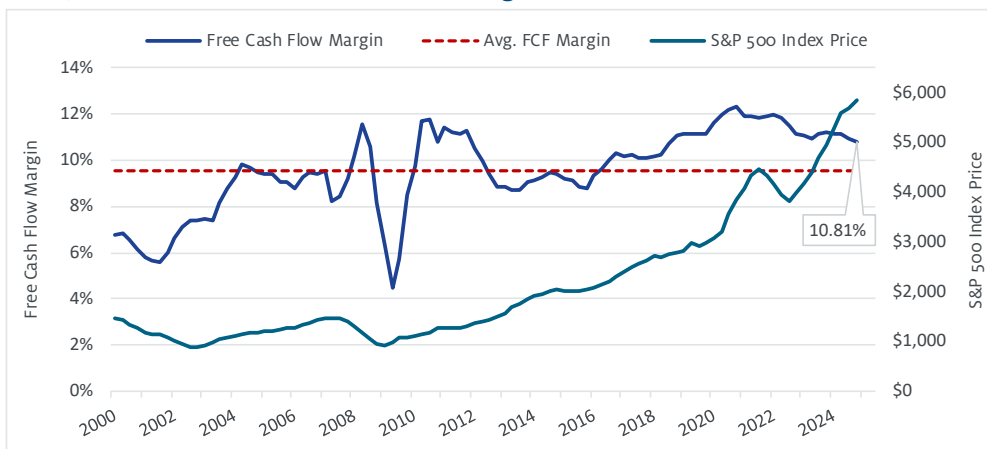
Central to the prospects for further gains is the ongoing tug of war between the economic cost of tariffs, which are providing a drag on growth, versus the positive forces of the recent tax bill: making the 2017 tax cuts permanent, plus accelerated expensing of research and development for corporate capital spending. When one adds in the likelihood of lower interest rates as an additional source of stimulus, it would seem the prospects of recession have declined significantly since the tariff liberation day.

As of the latest data in June, the average U.S. tariff rate is nearly 10%, up from 2.5% on January 1st. The latest estimates with announced tariffs put the likely average tariff rate at 14-15%. That equates to an indirect tax increase of \$400-\$500 billion. In contrast, the tax cuts and easier monetary policy are largely offsetting the cost of tariffs in 2025. The larger impact from the tax and monetary stimulus is expected to have a greater impact in 2026.

Regarding the cost of tariffs, past experience has implied that for every \$100 in tariff cost, producers absorb roughly \$30-\$40 of the cost, and pass on \$60-\$70 of the cost to the end consumer. This, of course, varies by industry; however, past tariff costs have been absorbed more by households than by businesses. In the end, the tariff is nothing short of an indirect tax on the U.S. economy.

Noteworthy for investors to consider is the potential net impact of tariffs versus tax cuts on corporate profitability. Early results are encouraging on the corporate earnings front. The majority of S&P 500 Index companies have reported second-quarter profits and, in aggregate, they are +11% versus year-ago levels. Moreover, estimates for the next year look favorable. One measure to closely monitor for corporate profit and cash flow success is the free cash flow margin of the S&P 500. Encouragingly, free cash flow margins have been steadily improving for the last decade, even longer, correlating well with the success of the U.S. stock market. The following chart depicts the steady progress free cash flow margins have witnessed, continuing into the second quarter.

### S&P 500 Index Price & Free Cash Flow Margin



Source: FactSet, as of 6/30/2025, quarterly data smoothed

The success of corporate free cash flow generation, owing in part to better capital allocation for U.S. businesses, is perhaps the most important metric when assessing the prospects of the stock market. The latest estimates have free cash flow per share growth of +11% in 2025 and continued low double-digit growth into 2026. When valuing the tradeoff between the cost of higher tariffs versus the stimulus in the latest tax bill, I expect this will be a key metric for assessing current portfolio holdings and potential new investments. ◇

## Hedging Q&A: Managing Risk, Preserving Wealth

Ryan Hummer, CFA

Director, Alternatives Portfolio & Risk Manager

With several equity markets near all-time highs, we posed a few questions to Ryan Hummer, a portfolio and risk manager at Ancora, to discuss and explain the role of hedging within dedicated alternative investment strategies, and some use cases in private wealth management.

### **Q: Ryan, you've spent your career around hedging and portfolio-level risk management. In a nutshell, how would you describe what hedging is and the role it can provide in a portfolio?**

A: Hedging aims to reduce systematic, or macroeconomic, risk. Systematic risk, measured as beta, can be thought of as the tide that lifts or lowers all boats. With systematic risk reduced through effective hedging, a portfolio is left to primarily face just the idiosyncratic or business-specific risks affecting the stocks it holds.

Most, if not all, of our investors have portfolios that include a good deal of systematic exposure. In many instances, these beta-oriented return streams depend on whether the aforementioned "tide" of the markets is rising or falling. This is where hedged alternatives can come into play to help offset the systematic risks faced by a portfolio. Ancora's alternative strategies largely seek to generate the lion's share of returns through capturing alpha, or business-specific outperformance by the stocks we own, rather than through the overall market's direction.

In general, such funds may have lower correlation to the overall market and therefore can be used as a tool to help reduce the overall volatility of an investor's portfolio. These types of hedged strategies and lower-correlation return streams can help build a more diversified portfolio for the investor and capitalize on the only "free lunch" in investing: true, multi-asset class portfolio diversification.

### **Q: Can you describe the Wall Street infrastructure that allows for hedging? Who takes the other side of the hedge? Do they see the same risk differently?**

A: The options market is very liquid and is becoming more so every year as interest and trading become more prevalent. Furthermore, the exchanges continue to roll out new contracts and products that make our ability to precisely hedge particular risks easier. Zero-day to expiration options are an example that has grabbed headlines lately. Wall Street banks make markets in these options, and the trading volumes are robust, especially in the largest stocks and the major indices. These banks or market-makers are typically taking the other side of these trades (if not, other investors who are taking an opposite view do), and the Options Clearing Corp (OCC) guarantees performance, so there is no counterparty risk for listed options.

The market-makers are able to hedge their option exposures through building long or short positions in the underlying instruments. They are typically trying to make a small spread on the bid-ask and then hedge out their directional exposure using a technique called delta hedging. They use this to limit directional risk in any single stock or index.

### **Q: What intelligence can the hedging markets provide that may help inform an investor's other decisions in a portfolio? (excessive bullishness, bearishness?)**

A: The options market does provide insight on sentiment and positioning that you cannot typically glean from other stock market or sentiment-related indicators. It can show when investors are complacent, chasing a rally they largely missed, when positions are full and need to limit risk or when the market is bombed out and full of fear.

One unique indicator I track is the S&P 500 Index (SPX) returns versus the Chicago Board Options Exchange's CBOE Volatility Index (VIX), which measures the change in implied volatility of options on that index. Implied volatility is how options are priced. Typically, the VIX is down when the SPX is up and vice versa, but there are days when both the SPX and the VIX are up. When we see a series of days with both indices up, it may portend weakness in the coming months. Conversely, when we experience a series of days when

both the SPX and VIX are down, that typically signals a near-term bottom.

Another example is option skew. Skew compares the implied volatility or price of out-of-the-money options versus at-the-money options. Normally, call skew is flat to downward-sloping, meaning out-of-the-money call options trade equal to or cheaper than at-the-money call options. When there's a chase to the upside, or excessive optimism, we see out-of-the-money calls get bid up above at-the-money calls. In certain "meme stocks," we've seen extreme call skew with far out-of-the-money calls trading at massive premiums to at-the-money calls.

**Q: Within alternative investments, how can hedging contribute to lower correlated return streams compared to traditional stock and bond exposures? Any examples of where hedging lowered market correlations in recent memory, or is that something that has to play out over time to get a portfolio benefit?**

A: A traditional balanced, or 60% equity / 40% fixed income, portfolio relies on a negative correlation between stocks and bonds in difficult times, but there is no guarantee that correlations will hold through all investment periods. In 2022, we saw the traditional negative correlation between stocks and bonds break down, and both asset classes lost money.

Hedges in our funds do not rely on correlations holding because they cover the markets to which our long book is exposed. 2022 was a great year to have exposure to true hedged strategies. This is why we consider the alternatives asset class to be an important "third leg of the stool" at Ancora. Over long cycles, hedged strategies may provide significant compounding benefits by preserving capital in down markets and reinvesting at better prices during both sharp and drawn-out bear markets.

**Q: How are hedging applications similar or different in private wealth management than in a dedicated alternative investment strategy approach?**

A: There are a number of ways hedging can be useful in the private wealth setting. Hedging can be useful for concentrated, legacy positions and overall portfolio exposure management. The IRS makes sure you pay taxes if you effectively sell your stock, so using options on an underlying stock to hedge will typically have negative tax implications. However, one can often find highly correlated ETFs on which options trade as a useful hedging tool. In certain situations, buying long-dated, out-of-the-money calls may also be an interesting strategy to gain hedged long exposure when speculating on future returns.

A call is equivalent to long stock + a put since you can only lose the premium paid for the call, but as previously mentioned, out-of-the-money calls typically trade at a discount to at-the-money calls, so this can create potentially advantageous skew if your directional view on the security or markets comes true. Bottom line, however, is that the key in any hedging or options strategy is to identify the problem you are trying to solve for and then find the best fit to address it via options markets.

Thank you, Ryan. If anybody has questions about hedging or the dedicated strategies within Ancora that utilize them, please reach out to your advisor. ♦

*As always, don't hesitate to contact your Ancora advisor or relationship team if you have any questions or would like to learn more about these topics. Visit our website at [www.ancora.net](http://www.ancora.net) to find other news and insights from the investment professionals at Ancora.*



## Market Data Center

As of 7/31/2025

Stocks	1 month	3 months	6 months	YTD	1 year	3 years
S&P 500	2.3%	14.3%	5.6%	8.4%	16.1%	58.4%
Dow Jones	0.2%	9.0%	-0.2%	4.5%	9.7%	40.4%
Russell 2000	1.7%	12.9%	-2.7%	-0.2%	-0.9%	21.4%
Russell 1000 Growth	3.7%	20.2%	7.8%	9.9%	23.4%	82.0%
Russell 1000 Value	0.6%	7.7%	1.8%	6.4%	8.5%	33.2%
MSCI EAFE	-2.1%	5.1%	12.4%	17.8%	12.1%	43.0%
MSCI EM	0.7%	12.0%	14.7%	17.2%	15.8%	29.3%
NASDAQ 100	2.4%	19.0%	8.4%	10.8%	20.5%	81.6%

Dividend Yield	NTM P/E	P/B
1.13%	22.4x	5.0x
1.51%	19.9x	5.4x
1.12%	23.2x	1.9x
0.40%	30.9x	12.8x
1.84%	17.0x	2.8x
2.91%	15.0x	1.9x
2.41%	13.2x	1.8x
0.50%	28.1x	7.8x

Fixed Income	Yield	1 month	3 months	YTD	1 year	3 years
U.S. Aggregate	4.65%	-0.3%	0.6%	3.8%	3.3%	4.3%
U.S. Corporates	5.11%	-0.1%	2.2%	4.4%	4.0%	7.0%
Municipal Bonds	4.23%	-0.3%	0.0%	-0.9%	-0.5%	3.9%
High Yield Bonds	7.33%	0.1%	3.7%	5.1%	8.2%	20.0%

Key Rates	7/31/2025	6/30/2025	4/30/2025	1/31/2025	7/31/2024	7/31/2022
2 yr Treasury	3.94%	3.71%	3.59%	4.20%	4.26%	2.90%
10 yr Treasury	4.36%	4.23%	4.16%	4.55%	4.05%	2.64%
30 yr Treasury	4.89%	4.79%	4.69%	4.80%	4.34%	2.98%
30 yr Mortgage	6.80%	6.80%	6.85%	7.01%	7.04%	5.28%
Prime Rate	7.50%	7.50%	7.50%	7.50%	8.50%	5.50%

Commodities	Level	1 month	YTD
Oil (WTI)	69.41	6.6%	-3.2%
Gasoline	2.08	1.6%	3.3%
Natural Gas	3.10	-11.1%	0.2%
Propane	0.72	-5.8%	-7.3%
Ethanol	1.66	6.8%	12.6%
Gold	3,344	1.1%	26.6%
Silver	36.80	1.7%	25.8%
Copper	5.57	10.7%	39.7%
Steel	855	-2.8%	20.6%
Corn	3.94	-3.7%	-14.1%
Soybeans	9.74	-5.8%	-3.4%

Data Reflects Most Recently Available As of 7/31/2025

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