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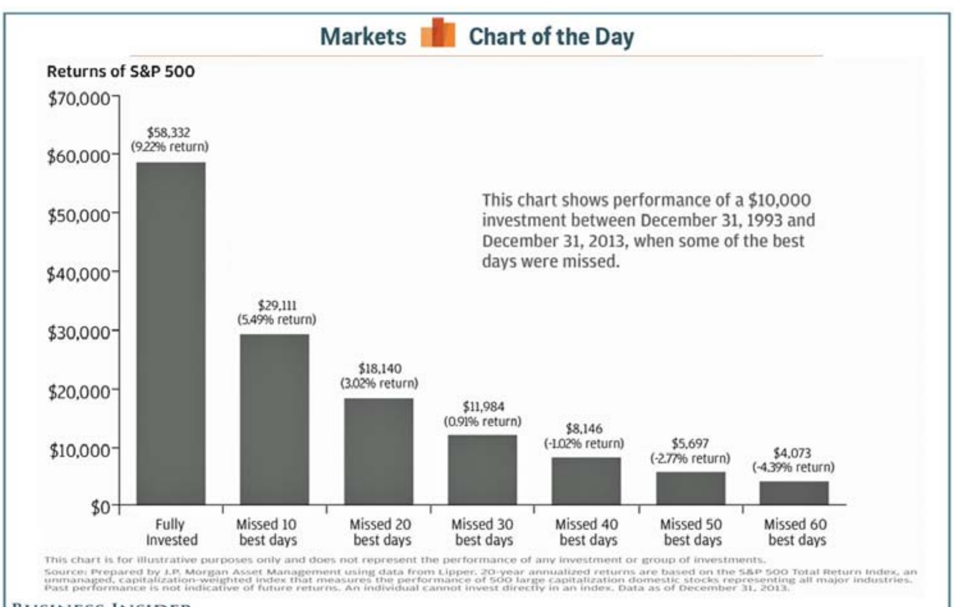
LATEST ARTICLES

Tune Out the Noise

John Micklitsch, CFA, CAIA
Chief Investment Officer

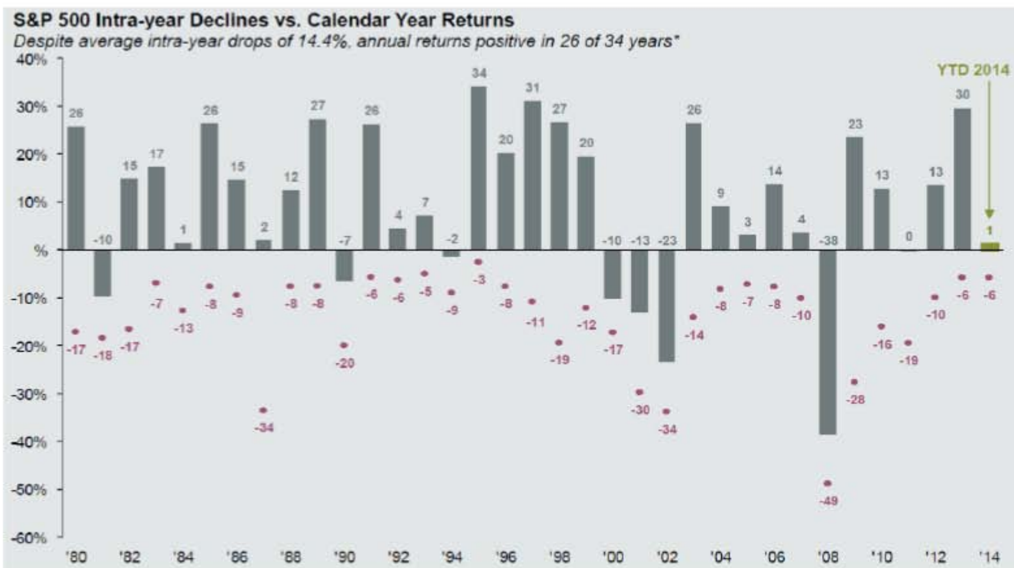
If you have cable television, satellite radio or a smart phone, it is nearly impossible to escape the constant chatter of 24x7 news and talk. The recent NFL draft has to have set records for buildup and coverage as we followed prospects in every aspect of their preparation to become instant millionaires. Like sports talk, politics dominate the airwaves for much of every evening as pundits entrenched on one side of the aisle or the other spew forth with guests that typically think just like them. Occasionally, a guest with an opposing view is invited to the set to be skewered like a sacrificial lamb. All of this talk is designed to keep us glued to the next segment in order to keep ratings up and advertisers writing checks. But what does all of this cost you? In the case of sports and political talk, all it really costs you is time. In the case of 24x7 market talk, however, the consequences can be much more costly.

Many people have seen the statistics regarding trying to time the market, but it bears repeating that being out of the market for the best days is costly. As the following chart illustrates, the cost of missing the ten best market days on a $10,000 investment in the S&P 500 for the 20-year period ended 2013 was approximately $29,000.



Furthermore, every year the market experiences some sort of pullback. Frequently it is of a magnitude that has investors thinking about moving to the sidelines. The following chart from JP Morgan's Guide to the Markets illustrates each year's largest peak to trough pullback going back to 1980. The average pullback over the period was 14.4%, which puts this year's 6% peak to trough pull back during Q1 into perspective. It only feels worse because we live in a 24x7 connected world that makes you feel like a sucker if you aren't doing something in response to the market update that just buzzed on your smart phone. But remember, it is hard to be correct on market timing once, let alone twice, because eventually you have to get back in as most would agree that cash is not a viable long-term investment strategy.

Historical Volatility



Source: Standard & Poor's, FactSet, J.P. Morgan Asset Management.

Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. *Returns shown are calendar year returns from 1980 to 2013 excluding 2014 which is year-to-date.

Guide to the Markets – U.S.

Data are as of 3/31/14.

Interestingly, over the 34 ¼ year period in the above chart, despite experiencing pullbacks ranging from 3% to 49% every year, the S&P 500 ended in positive territory in 26 of the 34 years and $1,000 grew to approximately $44,000 on a total return basis. Volatility has been a part of the equity landscape for a long time. The difference now is the connectivity and 24x7 news cycle that taunts us to do something every time the market declines 1%. There is a very important difference between having real time information and having to do something with that information. Understanding the difference can have enormous long-term financial consequences for investors.

The point of all this is that volatility is a part of equity investing. Risk, as defined by the volatility of one's overall portfolio, is better addressed, in our view, through proper asset allocation than market timing. Of course not all information is bad and there are certainly tactical adjustments one can make in response to changing fundamentals and market signals. However, as Warren Buffett so famously said, "In the short term the market is a voting machine, in the long term it is a weighing machine." In our view, the odds are in your favor playing the weighing machine and addressing risk management not through market timing, but rather through a proper asset allocation that adjusts with your needs and investment horizon over time.

John Micklitsch, CFA, CAIA is the Chief Investment Officer at Ancora Advisors LLC a SEC Registered Investment Advisor.

Fixed Income Q&A with Jim Bernard

Jim Bernard, CFA
Managing Director, Fixed Income

Q. What is your outlook for interest rates and the economy?

A. We will continue to see modest (2%-3% real GDP) domestic economic growth over the next few years, and if our forecast proves to be fairly accurate we would expect the 10 year U.S. Treasury to yield modestly above 3% either later this year or early in 2015. We further expect the FED to complete the current QE (Quantitative Easing) Program later this year or in early 2015. However, even when this program concludes we believe it will likely be six to twelve months before the FED takes any action to increase short-term interest rates.

Q. What risks do fixed income investors face at this point in the interest rate cycle?

A. As we enter the 5th year of historically low short-term interest rates, investors appear to be getting impatient earning very little on their short-term investments. It appears many are "throwing in the towel" and seeking out higher levels of investment income by either embracing longer duration bonds or lower credit quality bonds, both of which can add significant investment income to one's portfolio. Obviously the risk is that inflation may at some point reappear and force interest rates higher and thus drive down the prices and values of longer duration and/or lower credit quality bonds.

Q. What changes, if any, do you anticipate in Federal Reserve policy under Janet Yellen's leadership?

A. We see very little changes in policy or philosophy under Janet Yellen when compared to the last few FED Chairmen. Not only do we not see any fundamental differences at the helm, it also extends to the overall membership of the Board of Governors. All of which suggests a continued accommodative FED.

Q. How is the Detroit bankruptcy process going and what impact do you think it is having or will have on the municipal bond market?

A. There is still a long way to go in restructuring the debt and related expenses for Detroit. To date there has been little accomplished except for an approximately $100 million "haircut" for the owners of roughly $360 million of Unlimited Tax Obligation (UTGO) debt. The elephant in the room continues to be how the pension bondholders and/or current city employee benefits will be cut under as of yet to be negotiated deals. Our view continues to be that a long-term restructured debt plan with some additional "haircuts" and modest benefit cuts is the likely outcome of this situation. We believe this is only possible with some form of State of Michigan guarantee which we believe will likely occur. If this plays out as we have outlined it would be very positive for the municipal market but there is still lots of work to be done.

Q. What role does fixed income play for investors in such a low interest rate environment?

A. We believe conservative, risk adverse investors should have some exposure to investment grade debt at the minimum to act like an anchor for stability purposes in one's portfolio. Fixed income can produce reasonable investment income and stability and at times (like now) you have to focus more on the stabilizing benefits which are still important to achieving one's goals. We also continue to seek out some alternatives to traditional bonds as appropriate including dividend paying equities, REIT's, MLP's, Merger Arbitrage, etc.

Jim Bernard, CFA, is the Managing Director, Fixed Income at Ancora Advisors LLC a SEC Registered Investment Advisor. He is also a Registered Representative and Registered Principal of Safeguard Securities, Inc. (Member, FINRA/SIPC)

The Corporate Cash Dilemma

Sonia Mintun, CFA
Director, Portfolio Manager

According to ISI Group, the Standard and Poor's 500 largest companies had over $1.9 trillion in cash outside of the U.S. at the end of 2013, which is four times the level a decade ago. Since the financial crisis, many companies have focused on fortifying their balance sheets with cash. In fact, U.S. Trust put out a ranking showing that Apple's corporate cash hoard was greater than that of the cash reserves of Malaysia, Turkey and Poland.

Exhibit 2: Global Cash Reserves – Top U.S. Companies vs. Nations.

(Cash and international reserves levels)*

Rank	Company/country	Cash/reserves ($billion)	Rank	Company/country	Cash/reserves ($billion)
1	Apple	159	26	South Africa	42
2	Malaysia	130	27	Colombia	41
3	Turkey	109	28	Qatar	41
4	Poland	99	29	Chile	39
5	Indonesia	93	30	Germany	39
6	Microsoft	84	31	Oracle Corporation	37
7	Denmark	82	32	Lebanon	36
8	Israel	80	33	Italy	36
9	Iraq	74	34	Angola	32
10	Philippines	74	35	Qualcomm	32
11	UK	70	36	Johnson & Johnson	29
12	UAE	67	37	Kuwait	29
13	Peru	63	38	Spain	29
14	Google	59	39	General Motors	28
15	Canada	58	40	France	27
16	Sweden	55	41	Merck	27
17	Norway	55	42	Intel	26
18	Verizon Communications	54	43	Ford Motor	25
19	Czech Republic	54	44	Argentina	25
20	Pfizer	49	45	Amgen	23
21	U.S.	48	46	Coca-Cola Company	20
22	Cisco Systems	47	47	Ukraine	19
23	Hungary	46	48	Kazakhstan	19
24	Romania	45	49	Morocco	18
25	Australia	43	50	EMC	18

*International reserves exclude gold holdings.

Sources: Company filings and Moody's Financial Metrics; IMF.

Data as of 2013.

U.S Trust bank

Furthermore, corporate cash is concentrated in a few hands with the top 50 cash holders accounting for 62% of the total. Moody's has a recent study which shows the five largest cash holders-Apple, Microsoft, Google, Verizon and Pfizer with $404 billion in collective cash at the end of 2013 which was 16.4% greater than the end of the previous year. Technology, healthcare and industrial sectors dominate the top cash holders, often because these industries move intellectual property and patents to low tax jurisdictions to avoid paying a U.S. tax rate of 35%.

For investor, what are the implications of these large cash positions?

1. While many say that cash is king, it has also made some of these companies targets for activists. One example of this is Carl Icahn putting pressure on Apple to return cash to shareholders. Companies are also winning fewer proxy fights with activists increasingly in the fold, 35% win rate in 2013 versus 65% in 2010 according to Moody's.

2. Companies could look to make more large foreign acquisitions such as a General Electric's $17 billion bid for the electricity assets of France's Alstom, or Pfizer's cash and stock bid for AstraZeneca valued at $117 billion. As part of the Pfizer/ AstraZeneca deal, Pfizer would reincorporate their headquarters in the UK for significant U.S. tax savings. With this corporate inversion, Pfizer would retain its material operations in the U.S. About 15 companies have moved their U.S. headquarters overseas due to higher U.S. corporate tax rates since 1999 including Eaton, AON, Weatherford and Actavis as examples.

3. Companies can take a large tax hit to bring funds back to the U.S. eBay recently announced that they are bringing back $9 billion back to the U.S., resulting in a $3 billion tax charge or 4% of their market cap.

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4. Companies can increase their debt while keeping tax dollars overseas. Some top U.S. companies have increased borrowing in the last three years while keeping their cash dollars overseas and avoiding taxes. Companies such as Merck, Chevron, Cisco and Apple have all used the proceeds from debt issuance to increase dividends and stock buybacks.

5. Companies can spend shareholder money to lobby for a lower U.S. corporate tax rate.

One thing is without question; many U.S. corporations haven't forgotten the credit crunch and have a lot of cash at their disposal. More importantly, many companies are better positioned to face uncertain times than they were in 2007. The cash cushion allows them the flexibility to make new investments, return capital to shareholders, support the dividend or increase their R&D effort when the competition may not be able to. Finally, it also raises the awareness for corporate tax reform and increases the potential for corporate activism.

Sonia Mintun, CFA, is a Director, Portfolio Manager at Ancora Advisors LLC an SEC Registered Investment Advisor. She is also a Registered Representative of Safeguard Securities, Inc. (Member FINRA/SIPC)

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