ANCHOR
Investment Management, LLC

Q3 COMMENTARY 2019

October 22, 2019

Market/Index	2016 Close	2017 Close	2018 Close	2018 Change	As of 09/30/19	2019 Change
DJIA	19,762.60	24,719.22	23,327.46	-5.63%	26,916.83	15.39%
NASDAQ	5,383.12	6,903.39	6,635.28	-3.88%	7,999.34	20.56%
S&P 500	2,238.83	2,673.61	2,506.85	-6.24%	2,976.74	18.74%
Prime Rate	3.75%	4.50%	5.50%	1.00%	5.00%	-0.50%
10-year Treasury	2.45%	2.40%	2.69%	0.29%	1.68%	-1.01%

Market Overview … U.S. equity markets marked their best third quarter since 1997, recapturing gains that were lost in the final quarter of 2018. The market's resilience has allowed stock and bond prices to elevate higher even with the headwinds of trade tensions and recessionary concerns. Meager bond yields worldwide also fueled a gravitation towards stocks as investors sought more attractive yields in the form of dividends.

Additional rate cuts in Europe by the European Central Bank (ECB) pressured bond yields lower in Europe and Asia but US bond yields edged higher in September, rebounding from the lows reached in August. The 10-year Treasury bond yield rose from 1.47% at the beginning of September to 1.68% at the end of the month. Low mortgage rates continue to fuel home sales nationally, with the rate on a conventional 30-year fixed mortgage at 3.64% at the end of September, down from 4.51% at the beginning of the year.

Currency markets reacted to slightly higher U.S. rates in September, sending the U.S. dollar to its strongest levels in over two years. Various factors such as consistent consumer demand and a stable economic environment, relative to other global economies, helped drive the demand for the dollar.

A key inflation indicator, the Consumer Price Index (CPI), moved higher with its fastest annualized growth since 2008. The CPI, which measures the price of various goods and services such as food, housing, and medical expenses, rose 2.4% over the past year. Medical insurance and healthcare related expenses saw some of the largest increases.

Federal Deficit Projections Top $1 Trillion The Congressional Budget Office (CBO) has projected a 2020 federal budget deficit exceeding $1 trillion. Over the next 10 years they project an average annual budget deficit of $1.2 trillion between 2019 and 2029. The estimate represents a deficit of 4.4% to 4.8% of GDP, above the 50-year average. Even though tax revenues are estimated to grow, GDP is expected to expand at a more conservative pace. Current estimates show GDP growing at 2.3% in 2019, yet the CBO projects an average annual GDP growth rate of 1.8% over the next 10 years.

The three largest expense items for the federal government have been and are projected to be Social Security, health care programs, and interest paid on government debt. Rising interest rates could have a dramatic effect on the US Government budget, but for now we remain at historic lows.

In This Issue...

The REPO Markets and the Federal Reserve

On the morning of Tuesday, September 17, the New York Federal Reserve announced it was going to put $53 billion into the super-short-term repo market. For people who watch banks at all, this news was alarming because the Federal Reserve hasn't done this in 10 years, literally since the last financial crisis. We got a few calls and emails asking us what was going on and, more specifically, if this was a sign of a financial crisis. It's not. Here is what happened and why.

"Repo" is short for repurchase agreements. It's an overnight liquidity market for banks that you can compare to a pawnshop. A bank is required to keep a certain amount of cash on their balance sheet for liquidity purposes, and from time to time they may not hold enough due to excess withdrawals or a lack of new deposits. All banks hold lots of US Treasuries, which is the safest investment in the world. When a bank has a need for cash, they will go to the Repo market and find another bank with excess cash and borrow the cash they need using US Treasuries as collateral. In essence they will pawn their Treasury Bond to a second bank in exchange for, say, $100, and agree to repurchase the Treasury bond the next morning for $100.01, which is second bank's interest payment. This happens every day and all banks take advantage of the Repo market from time to time.

On September 16th, banks of all sizes had some abnormal draws on their cash holdings. It was corporate tax day, and payments were sent to the federal government; it was also a day where a lot of Treasury Bond purchases settled, and cash was needed to pay for them. Therefore, the entire banking system was short cash and banks that needed to borrow money in the Repo market found that there were not enough banks with excess cash to lend to them. To offset the imbalance the Fed stepped in to lend money in the Repo market, $53 billion on that first day, and they've been loaning tens of billions of dollars a day ever since. Fortunately this situation will work itself out as more and more deposits are put into the banking system. In 2008 the Repo market froze because banks were wondering if the collateral, US Treasuries, would default. That's no longer a concern, and the Federal Reserve has just become a temporary pawnbroker of last resort.

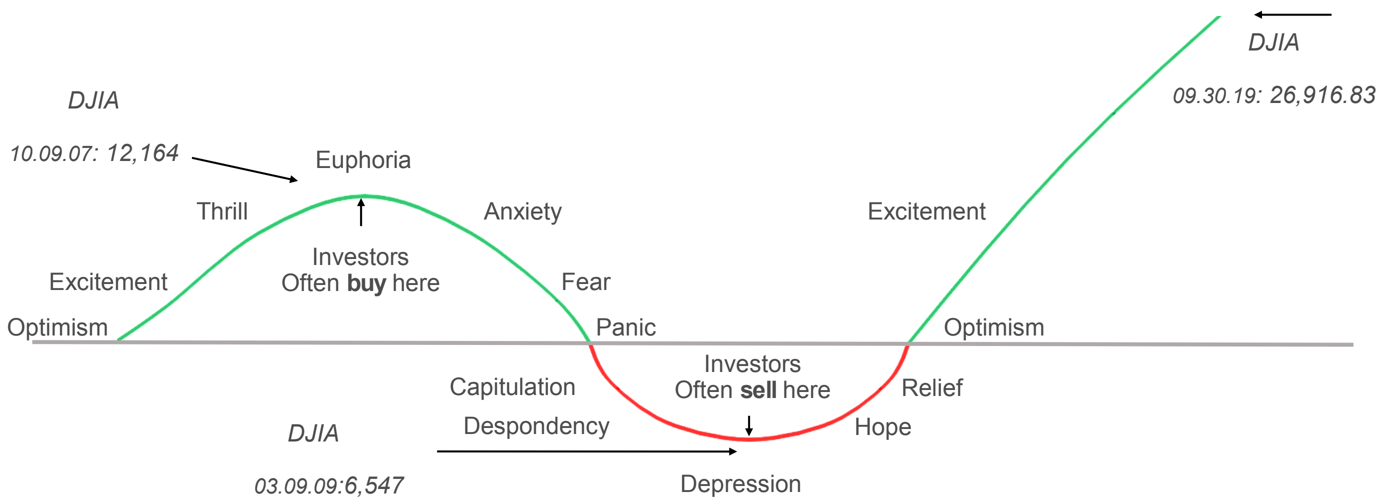
The WeWork IPO

Last Quarter we wrote about the tremendous number of startup companies that are preparing to go public at inflated valuations. The largest one was WeWork, a company that leased short-term office space and had been valued close to $50 Billion during their last Venture Capital investment stage despite losing $900 Million in the first 6 months of 2019. Common sense has finally prevailed and WeWork has become the poster child for excess valuations.

On August 11, WeWork filed their IPO prospectus filled with, quite frankly, bizarre information. This real estate leasing company stated, "We are a community company committed to maximum global impact. Our mission is to elevate the world's consciousness." It was reported that the CEO, Adam Neumann, had borrowed millions of dollars from WeWork, bought office buildings with the money, and then rented those buildings back to WeWork. Maybe the most amazing detail in the prospectus was that Adam Neumann trademarked the word "We" then changed his company's name to "We" and made the company pay him $5.9 million in stock for the rights to use the name "We."

Sanity prevailed and investors refused to purchase shares at the inflated price. WeWork's valuation fell from $50 Billion, to $20 Billion, to $15 Billion, and they officially pulled the IPO when the valuation fell below $10 Billion. Since then, Adam Newman has been removed as CEO was forced to give back the $5.9 Million in stock for the "We" trademark. The company has sold the $65 Million jet, is laying off 2,000 employees, and is shuttering many side businesses it had started. In short, someone is finally trying to run it like a business. We expect this to be a turning point in the history of venture capital.

2007- 2019 Investment Cycle



As we enter the holiday season, all of us at Anchor Investment Management wish you and your families a joyous time filled with love and happiness. We appreciate your trust and confidence and look forward to seeing you at our Annual Office Party on Tuesday, November 5th from 4:00pm - 7:00pm!

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