ANCHOR
Investment Management, LLC

Q2 COMMENTARY 2022

July 12, 2022

Market/Index	2019 Close	2020 Close	2021 Close	2021 Change	As of 06/30/22	2022 Change
DJIA	28,538.44	30,606.48	36,338.30	18.73%	30,775.43	-15.31%
NASDAQ	8,972.60	12,888.28	15,644.97	21.39%	11,028.74	-29.51%
S&P 500	3,230.78	3,756.07	4,766.18	26.89%	3,785.38	-20.58%
Prime Rate	4.75%	3.25%	3.25%	0.00%	4.75%	1.50%
10-year Treasury	1.92%	0.93%	1.52%	0.59%	3.10%	1.58%

As we close out the first half of 2022, we think it's safe to say that, other than 2008-2009, this is the most challenging market we have seen. COVID-19, and the response to it, have produced a market with multiple personalities. There is no historical equivalent that we can look back on to understand this market which proves how valuable having a financial plan is and how lucrative being able to stick to that plan can be. There are four things we are trying to make sense of, and we think it's important that you know them as well.

1. The Economy and Inflation

The economy continues to be remarkably strong. In the first quarter, US GDP increased 10.6% over where it was a year earlier, Business Investment increased by 18.6%, Retail and Internet Sales are up 6%, and S&P 500 Earnings are up 54.3%. Wages have risen 11.6% and the unemployment rate is 3.6%. Consumers have more money than ever before and they are spending it as fast as they can make it. This phenomenon in turn has caused supply chain and inflation issues.

At this point, supply chain issues are a combination of slow manufacturing (chips, parts…) and continued strong demand for goods (cars, houses…). The US is currently importing 30% more goods and services than we did before COVID. The world's manufacturing sector simply cannot keep up with the worldwide demand for products. A scarcity of products + high demand = rising prices; inflation is now at 8.5% - a 40-year high. The Federal Reserve has stated that it will *stop at nothing* to bring this number down.

2. The Federal Reserve

The Federal Reserve Chairman, Jerome Powell, arguably has the most watched and least desirable job in the world right now. He is being chastised for not raising rates sooner, not raising rates enough, and raising rates too much. He needs to take excess money out of the system by quantitative tightening, which he is doing by selling $47.5 billion of bonds per month that were purchased during the period of quantitative easing. (The sales will increase to $95 billion per month starting in September.) He is also in the process of systemically raising overnight Fed Funds rates, most recently by 75 basis points in June. The market expects him to continue raising rates aggressively through the summer, at which time he may stop to avoid being seen as influencing the midterm elections. Unfortunately for the economy, The Federal Reserve's moves will probably have very little effect on inflation.

3. Oil Prices and the US Government

Currently, the primary driver of inflation is the price of oil and gas. Gasoline has increased from $2.40 to $5.10 per gallon in the last 17 months. The increase is being blamed on many factors, past and present administration policies, the Russian invasion of Ukraine, corporate greed, OPEC manipulation, etc. But we know for sure that the only way to reduce the price of gasoline is to decrease demand or increase supply. In the short term, a recession is the only way to reduce demand, so we find ourselves in a situation where the only way to reduce inflation is to increase the supply of oil, which is not an overnight event from both a physical and policy standpoint. Just a few years ago, the US was energy independent - and as we now see, there is real value in that position.

So, will we solve it by raising rates and tilting to recession or by increasing production of energy? We should know in near future.

4. Commodities and Global Unrest

The war in Ukraine has caused upheaval in many commodity prices. Oil and gas are obvious, but food commodities will probably cause the most harm. Ukraine is the world's fifth-largest exporter of wheat, fourth-largest exporter of corn, and top exporter of sunflower oil and meal. Countries worldwide rely on Ukraine for grain used for bread, pasta and packaged goods: Egypt is the top importer of Ukrainian wheat, and countries such as Lebanon and Pakistan get a majority of their wheat from Ukraine. Ukrainian wheat also serves a critical role in humanitarian efforts, as about half of the World Food Program's wheat comes from the country. Ukraine's ports have suspended activities due to Russian blockades, and grain exports in May were down 64% compared to the same timeframe last year. The U.N. estimates about 20 million tons of harvested grain are stuck in the country. In turn, the high cost of staple foods has increased food insecurity. Nearly 250 million people are on the brink of famine. If the war drags on and supplies from Russia and Ukraine are limited, hundreds of millions more people could fall into poverty. We are hopeful, like you, for a better outcome.

What does this mean for your investments?

First of all, the market is a group of companies, not a group of stocks, and the companies you own are still performing well; S&P 500 Revenues and Earnings are at all-time highs. The market selloff is primarily due to a reduction in P/E Ratios - investors are not willing to pay high multiples like they would in the low interest rate past. Second, a market pullback is normal, particularly in the face of recent events. It helps insure that long term prices remain realistic. To the savvy investor, a down market offers many good values and opportunities for long term success. Warren Buffett, for instance, is buying at a faster pace than he has in a decade. Unless you believe that capitalism is coming to an end, which it's not, you should continue to seek profitable investments. When you're buying, don't try to time the bottom. For bond buyers, the recent increase in rates is a welcome event versus "zero" rates of the past. Stay diversified and buy good companies with good balance sheets and management teams who will be able to weather the storm. When you look back at this market in 5 years, you'll be glad you did.

All of us at Anchor would like to thank you for your business and the trust and confidence you put in us each day. We look forward to working with you in the years to come and hope you have a fantastic 2022!

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