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### Overview

In the end, 2023 turned out to be a mirror image of 2022 resulting in the net return of the S&P 500 being essentially flat over the two years. During the fourth quarter of 2023 there was a massive rally in both the equity and fixed income markets with inflation and interest rates coming down.<sup>i</sup> The markets seem optimistic that inflation is under control and that business and individuals can weather through the current higher priced environment we find ourselves in. For the time being, structural changes in the labor market have kept employment relatively steady. This coupled with a rising real wage has contributed towards the allowance of continued consumer spending. That said, the willingness to spend has been somewhat surprising given reports about how stretched the consumer is with the higher prices and tighter lending standards.

While we entered and remained very cautious in 2023, many expected a potential recession was on the horizon, it has not materialized. In fact, we have seen a rolling wave of in and out of favor sectors and industries performing well and some that have not. Many companies have been trying to figure out the new normal as it relates to supply chains, pricing/inflation, consumer demand and spending, interest rates, labor dynamics and covid spending. 2024 may be the year we start to see a more normalized earnings picture.

Our focus at Anchor Capital remains on risk and downside protection at both the security and portfolio levels. We have difficulty investing in highly speculative or unprofitable companies even if they look attractive from a valuation perspective. Our goal is to find what we consider to be high quality companies trading at a discount to intrinsic value that can grow but also protect in down markets.

In down markets we have done well in executing on the goal of downside protection. It is turning points in the markets where speculative and unprofitable companies significantly outperform where we lag. In November, the markets rebounded higher on news that inflation was relatively contained and had decreased from previous highs. The Federal Reserve not only stopped raising interest rates they indicated that there is the possibility for up to four interest rate cuts in 2024.

While the overall market valuation is trending higher than average there are pockets that are attractive. The interest sensitive sectors of the market like bond proxies, utilities, and REITs, have been hard hit by higher interest rates. With interest rates coming down we are looking and beginning to see a good entry point and more attractive valuations for these sectors. Health Care has also been a laggard this year as numbers have normalized post pandemic and biotech funding pulled back. As a result, we see health care improving and think the space could provide interesting opportunities. The financial sectors, in particular banks, also dealt with high interest rates, funding costs and bank failures, but it appears to be behind them for the time being and seeing upside from here.<sup>ii</sup>

Mega-Cap tech stocks, and more specifically the Magnificent Seven stocks of the S&P 500 (Apple, Alphabet, Meta, Microsoft, Amazon, Nvidia and Tesla) drove performance in 2023.<sup>iii</sup> We believe that current valuations for these stocks are high relative to their growth profile and that significant outperformance from here will be more difficult to achieve.<sup>iv</sup> As we mentioned above, several value sectors have opportunities to recover and outperform in 2024 giving value room to shine.

### U.S. Equity Markets

All U.S. equity markets outperformed for the quarter.<sup>v</sup> The markets had a healthy pull back between August 1<sup>st</sup> and October 31<sup>st</sup> before rebounding strongly in November and December.<sup>vi</sup> The markets appear to be celebrating that the economy is avoiding a recession and that we will likely see a soft

landing. The sectors that outperformed were technology, REITs, and financials.<sup>vii</sup> After consistently raising rates since early 2022, the Federal Reserve has paused and signaled rate cuts could be coming. This pause and any potential cuts sets up to benefit and support those interest rate sensitive sectors impacted most by rising rates. On the flip side, the underperforming sectors were energy, consumer staples and health care.<sup>viii</sup> There continues to be normalization post pandemic, especially in the health care sector where many stocks were outsized beneficiaries of the pandemic.

### U.S. Fixed Income

In the span of four months, the yield on the 10-year Treasury bond has moved from 4.09% on August 31<sup>st</sup> to 5% on October 19<sup>th</sup> and back down to 3.95% at year end.<sup>ix</sup> A 200 basis points move in interest rates in such a condensed timeframe is significant. The shift down in interest rates has created strength in bonds markets. The iShares Core U.S. Aggregate Bond ("AGG") ended positive for the year<sup>x</sup> with all U.S. bond segments performing well. High yield and leveraged loans performed the best.<sup>xi</sup> Any Fed interest rate cuts in 2024 would benefit bond performance.

### Inflation

Inflation levels, as represented by the Consumer Price Index (CPI), remain above the Federal Reserve's targeted 2% annualized level.<sup>xii</sup> The November CPI reading was 3.1% annualized, which was a step down from the prior month. The Personal Consumption Expenditures (PCE) Price Index, a different way of measuring inflation, continues to show high services inflation and a decline in goods inflation.<sup>xiii</sup> Components of inflation like energy prices, food prices and rent are coming down while hourly wages have been increasing and are now outpacing inflation.<sup>xiv</sup> Inflation has is approaching more normalized levels after coming off 50-year highs (2022).

### Interest rates/Fed/Economy

In one of the fastest rate hiking cycles in history, the Federal Reserve increased interest rates eleven times from March 2022 through July 2023. The Fed has kept the Federal Funds targeted interest rate between 5.25 and 5.5%.<sup>xv</sup> In December, the Fed indicated that it was done raising interest rates and could potentially cut rates up to four times in 2024.<sup>xvi</sup> We believe that the economy will have to weaken significantly before the Fed starts cutting interest rates given that inflation is still above its targeted 2% level. However, the Fed is also dealing with a massive interest expense on the balance sheet and cutting interest rates would help to relieve that. The U.S. economy has remained resilient despite some soft economic data. Overall, we saw job opening levels and wages soften, bank lending tighten since the Silicon Valley Bank collapse, credit card and auto delinquencies increase, and manufacturing weaken. Consumers are spending savings. This coupled with the return of student loan payments will most likely put pressure on discretionary spending. Some economists are forecasting more economic weakness, but it may not be enough to tip into a full-blown recession.

### Performance Overview

The Anchor Capital Value Opportunities Portfolio outperformed the Russell 3000 Value index for the quarter. On a relative basis, the Portfolio benefitted the most from security selection in the Technology and Energy sectors as well as an overweighted allocation to the Technology sector. An underweighting in the Technology and Real Estate sectors as well as an overweighting in Consumer Staples were the greatest detractors from performance.

### Quarterly Attribution Highlights<sup>xxii</sup>

Sector - Top 3 Contributors			Sector - Bottom 3 Detractors		
Industrials			Energy		
Financials			Basic Materials		
Technology			Utilities		
Security - Top 5 Contributors	Avg. Weight %	Contribution %	Security - Bottom 5 Detractors	Avg. Weight %	Contribution %
Salesforce, Inc. (CRM)	1.96%	0.55%	Chevron Corporation (CVX)	2.30%	-0.34%
JPMorgan Chase & Co. (JPM)	3.05%	0.54%	Franco-Nevada Corporation (FNV)	0.52%	-0.14%
QUALCOMM Incorporated (QCOM)	1.43%	0.42%	NextEra Energy, Inc. (NEE)	0.03%	-0.08%
Microsoft Corporation (MSFT)	2.07%	0.40%	Boat Barn Holdings, Inc. (BOOT)	0.88%	-0.07%
Goldman Sachs Group, Inc. (GS)	0.98%	0.35%	Constellation Brands, Inc. (STZ)	0.97%	-0.04%

### Quarterly Transactions

Purchased	Sold
Goldman Sachs Group Inc (GS)	Franco-Nevada Corp (FNV)
McDonald's Corp (MCD)	Walt Disney Co (DIS)
	NextEra Energy Inc (NEE)
	Medtronic PLC (MDT)

### Purchases

**Goldman Sachs Group Inc (GS)** is in the process of exiting retail banking which was an ill-conceived strategic initiative. The firm does not have the DNA to cater to the mass market transactional banking and savings segment. Management is refocusing on its core IB and capital market competencies which are unparalleled on the global scale. We anticipate a pickup in capital market activities in 2024 following a two-year period of very low levels. At a minimum, it is reasonable to expect higher debt issuance and return of IPOs. The position was initiated at close to 1 x price to the tangible book value, a valuation level that historically corresponded with share price troughs. At purchases, shares DY was over 3%.

We believe **McDonald's Corp (MCD)** is in a position of strategic strength. The system is ripe for resumption of unit growth, especially in the US. In the past 3 years, underperforming franchisees have left the system, improving the quality of operators. The corporation and franchisees have been investing in the business judiciously. Digital and Rewards program have a long runway for growth. MCD owns the best properties in company operated markets, the value of which is at least 2-3x higher than the book value. Shares of MCD traded at 20x forward PE which has been the lowest valuation level since refranchising of the system in 2015-2017.

### Sales

**Franco-Nevada Corp (FNV)** is a high-quality gold royalty and gold stream company. The company's largest asset is Corbe Panama copper mine which accounts for over 25% of the company's NAV. The operator of the mine is First Quantum with whom FNV has a gold stream agreement. The government of Panama made an expected decision to renegotiate the contract with First Quantum. The development culminated in a national referendum to terminate the agreement. When that news hit the wires, we made a prompt decision to exit the position as risks became too high, helping us avoid the further downside in shares.

**Walt Disney Co (DIS)** is a global media and entertainment company. It has two separate divisions: Media, which includes cable, broadcasting, and direct-to-consumer; and Parks and Entertainment which includes the parks, consumer goods, studios and cruise lines. The legacy media business is declining, and the direct-to-streaming is growing but unprofitable. The company is struggling with growth and high costs. While the CEO, Bob Iger,

has implemented a big cost cutting program we don't think it's enough for the company to grow. There are too many moving pieces, and the stock was best exited.

**NextEra Energy Inc (NEE)** is a Florida based utility that has been focused on growing its renewable energy. Higher debt costs are weighing on earnings. That coupled with questions around political contributions has prompted us to sell the stock.

**Medtronic PLC (MDT)** is a global medical device maker. While still a big player in multiple markets, about 80% of its products are in low growth, mature markets and 20% in higher growth markets. We have seen Medtronic lose market share and overall growth levels have been anemic. We decided that there were better places to invest money and decided to exit the stock.

### Anchor's Positioning

We were defensively positioned for most of 2023 with concerns over how higher interest rates and inflation would affect the economy. As a result, the cash levels of Anchor portfolios increased. The higher levels of cash contributed to relative performance in October when the markets sold off, but subsequently detracted in November and December when the market rallied.

Despite the market volatility we have been active in seeking new stock opportunities to add to the portfolios. We found more attractive entry points for regional banks, REITs, and capital markets, which helped bring up our financials exposure. We trimmed or exited out of positions with higher valuations and those that met our price targets.

Our cash levels came down a little bit nearing year-end. We believe we are positioned well to capture upside from the areas of the market that have underperformed most recently. We remain excited about the existing portfolio holdings as we return to a more normalized environment post-pandemic.

### Outlook

We believe our discipline in managing risk and looking for attractive stock opportunities will help performance in 2024. While macro forecasting is not our forte, we consider how different variables may affect companies and different parts of the markets. With interest rates potentially a little lower and growth relatively stable that should support small and mid-cap stocks from valuation and opportunity. We continue to look for businesses that meet our value criteria that can participate on the upside, while protecting better on the down.



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<sup>i</sup> FactSet Financial Data & Analytics

<sup>ii</sup> FactSet Financial Data & Analytics

<sup>iii</sup> Ibid.

<sup>iv</sup> Ibid.

<sup>v</sup> Ibid.

<sup>vi</sup> Ibid.

<sup>vii</sup> Ibid.

<sup>viii</sup> Ibid.

<sup>ix</sup> Ibid.

<sup>x</sup> Ibid.

<sup>xi</sup> Ibid.

<sup>xii</sup> <https://www.wsj.com/economy/central-banking/how-hard-should-the-fed-squeeze-to-reach-2-inflation-77dbf56f>

<sup>xiii</sup> <https://www.cnbc.com/2023/11/30/pce-inflation-report-october-2023-.html>

<sup>xiv</sup> <https://www.youtube.com/watch?v=WtFzaol6yx8>, Charlie Bilello, 12/15/2023

<sup>xv</sup> <https://www.usatoday.com/story/money/personalfinance/2023/07/26/july-fed-rate-hike-economic-effect/70463169007/>

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<sup>xvii</sup> FactSet financial data & analytics; Attribution

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In order to enhance current and prospective investor understanding of our process, approach and views, this letter includes detailed discussions regarding selected positions in our Strategy portfolios. In doing so, we hope this transparency enhances your understanding of our views on the investment opportunities we see in the marketplace and why we have positioned the Strategy portfolios the way we have. With such information available to you, we believe current and prospective investors are better informed and equipped to understand and/or challenge our views and approach to determine whether an investment in a Strategy is consistent with the mandate of each individual investor.

