

NOTES FROM THE TRADING DESK

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MARKET MOVERS & SHAKERS

It was another historic week in the marketplace. However, the history-making took place in the oil market, not the equity market — but we will get to that in a little. U.S. Equities slowed last week after their recent ascent over the last few weeks. The Dow fell 1.93%, while the S&P 500 dropped 1.32%. The Nasdaq was down 0.18%, and the Russell 2000 bucked the trend once more this week as it actually closed higher 0.32%. Despite the down week, defensive sectors performed the most poorly. REITs, Utilities and Staples were down 4.23%, 3.76%, and 3.19%, respectively. More cyclical corners of the market, such as Energy and Consumer Discretionary stocks were actually amongst some of the best performers. The Energy outperformance was surprising given the 32.3% drop in WTI Crude — oil's worst one-week fall on record. The outperformance of Consumer Discretionary stocks could also be considered a little surprising given the expectations for JC Penney and Neiman Marcus to file for bankruptcy. Consensus now seems to be that there could be a wave of bankruptcies in both Retail and Energy. Elsewhere, Treasuries were mostly flat. The 10-year continues to trade around 0.60% — the bottom end of its recent trading range. Gold traded higher once more, as the precious metal looks determined to test its previous all-time highs set back in 2011.

Last week, we discussed the possibility of Crude trading below \$0, but even then it seemed unlikely. Unfortunately, this nightmare scenario for oil producers came to fruition on Monday as the May WTI Crude Futures contracts traded below \$0 for the first time in history. At its worst levels last Monday, the contract was down some 320% intraday! The contract for a barrel of crude was actually trading at -\$40, which, as *The Wall Street Journal* pointed out, effectively means that sellers were paying buyers to take Crude off of their hands. The issue at hand is two-fold. One, there has been a massive decrease in demand as the global economy has come to a screeching halt the past few months. Two, there is an enormous glut of oil right now. In fact, oil is currently so oversupplied relative to demand that producers are running out of storage space for the commodity. This lack of immediate storage space is one of the key drivers behind the negative prices. The contract ultimately closed above \$0 per barrel before settlement, but should the imbalance between supply and demand not correct by expiration for the June contract, it would not be crazy to think the same nightmare scenario could happen again. The June contract, which expires May 19th, fell more than 40% on Tuesday before settling at \$11.57/barrel. However, the contract ultimately rallied off its lows as it settled on Friday at \$16.94. Oil has long been considered a bellwether for the global economy and last week we watched the decimation of demand in

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WTI Crude Oil (NYM \$/bbl) May 2020 Contract



front of our very eyes. The outlook for the oil and gas sector has become so dire that Secretary Mnuchin announced last Friday that the government is actually considering taking equity stakes in U.S. Energy companies. Per Reuters, President Trump discussed the potential for Russia and the Saudis to make further production cuts while announcing that Texas, Oklahoma, and North Dakota are all cutting production as well.

While Crude undoubtedly captured the market's attention last week, there are additional trends that are worth monitoring. Tech seems to be perceived as a safe haven trade of late. However, the trade runs the risk of becoming overcrowded. According to Bank of America's most recent Fund Manager Survey, investors remain increasingly overweight Tech stocks. Similarly, RBC recently noted that Hedge Funds have added the most to Tech stocks relative to other S&P 500 stocks since March 17th. Volatility of the Nasdaq Index has been markedly lower than its historical positioning relative to the volatility of the S&P 500 as well. Tech has been trading like a defensive pocket. Should Tech roll-over, it could be a bad omen for the market as a whole. We mentioned it briefly last week, but the 5 largest names (Microsoft, Apple, Alphabet, Facebook, and Amazon) now account for more than 20% of the S&P 500 — the largest concentration at the top of the index in decades. However, this narrow breadth is now beginning to be noticed by more market participants. Goldman Sachs' Chief U.S. Equity Strategist, David Kostin, recently noted the growing discrepancy between mega-cap stocks and the rest of the market. In fact, as Kostin noted, the median S&P 500 company was recently trading 28% off its 52-week highs, while the S&P 500 was down only 17%. This 11% difference is a full one standard deviation greater than its average dating back to 1980. In other words, market breadth has narrowed significantly, which has historically been a negative sign for equities. Kostin went on to note that narrow market breadth, while it can continue for a long period of time, ultimately always ends in a pullback. He goes on to note that "the further market concentration rises, the harder it will be for the S&P 500 index to keep rising without more broad-based participation."

TRANSITION UPDATES & NEWS **

Last week, we liquidated two names from our Equity and Large Cap strategies. Carrier and Otis were both spun off from UTX following the merger of Raytheon and United Technologies — which created a newly formed company, Raytheon Technologies. Both CARR and OTIS are in more cyclical businesses than RTX, and both saw a hit to operations during the financial crisis. Each of these businesses cater to the construction industry (residential and commercial), which is in-

herently more cyclical than RTX's defense business. Carrier and OTIS were able to bounce back following the financial crisis — however they also benefitted from the resources of a much larger company to help them navigate those waters. As a result of their cyclicity, we liquidated both positions. Outside of those two names, the week was relatively quiet on the strategy level.

Tyler Technologies, which provides tech and management solutions to local governments, announced that there has been rapid adoption of their virtual court offering. The Virtual Court was released earlier than expected to help conduct court sessions entirely online in response to COVID-19. In other coronavirus news, LabCorp announced that it will expand its serological testing for COVID-19. Many believe that antibody testing is crucial to the reopening of the economy. LabCorp also announced that they received FDA approval for an At-Home Test Kit.

Last week also marked the start of earnings season for us here at Tandem — though the season really hits the ground running this week. O'Reilly Automotive, NextEra Energy, and Signature Bank all reported earnings last week. NextEra beat on the bottom-line and confirmed their full-year guidance. O'Reilly came in below expectations and was going to have a weak quarter regardless of the coronavirus. However, the negative impact of COVID-19 began to hit their business in earnest in mid-March. Management reported that same store sales declined 13% from mid-March to mid-April. Lastly, Signature Bank also reported an impact from COVID-19. They raised their provision for loan losses and their earnings came in well below expectations — which is unsurprising in this environment. However, their CEO found the silver lining in the recent turmoil noting, "our premise for bringing our banking model to the West Coast is certainly bearing fruit where we continue to see significant disruption in the marketplace."

***The transition update describes activity taken by Tandem on the transition level, not the composite or firm-wide level. The transition update is applicable to new accounts and new money. New accounts and new money are not automatically invested on the first day. Rather, they are transitioned into our strategy over a longer time period that is dependent upon market conditions. This update describes that transition.*



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KEY MARKET DATA

	WTD	MTD	QTD	YTD
Dow Jones	-1.93%	8.48%	8.48%	-16.69%
S&P 500	-1.32%	9.76%	9.76%	-12.20%
Nasdaq	-0.18%	12.14%	12.14%	-3.77%
Russell Mid Cap	-1.27%	9.71%	9.71%	-20.37%
Russell 2000	0.32%	6.93%	6.93%	-26.10%

	WTD	MTD	QTD	YTD
Comm. Svcs	-0.04%	9.50%	9.50%	-9.36%
Con Disc	-0.22%	16.25%	16.25%	-6.52%
Con Staples	-3.19%	7.48%	7.48%	-6.91%
Energy	1.67%	18.40%	18.40%	-42.05%
Financials	-3.13%	4.33%	4.33%	-29.41%
Health Care	-0.47%	13.12%	13.12%	-1.66%
Industrials	-2.48%	4.22%	4.22%	-24.35%
Info Tech	-0.80%	10.19%	10.19%	-3.27%
Materials	-0.89%	10.69%	10.69%	-18.75%
Utilities	-3.76%	5.14%	5.14%	-9.77%
REITs	-4.23%	6.47%	6.47%	-14.13%