Notes from the Trading Desk

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Markets were rather choppy for much of the week. The S&P 500 traded in a 53 point range — the largest band since the start of the quarter. The Dow turned in a good week, as it was up 1.41%. The S&P 500 was up 0.59%, while the Russell 2000 was up 0.36%. The Nasdaq was the laggard amongst the major indices, as it fell 0.29%. Defensive sectors firmly led the way as Telecomm, Consumer Staples, REITs, and Utilities all rallied more than 2.50%. Energy, Materials, Consumer Discretionary, and Tech stocks all traded lower. The yield curve continued to flatten as 10s to 2s reached a 25 bps spread again. However, much of the weeks intriguing action stemmed from commodities. Gold fell another 3% last week and the precious metal is now down 12.55% from its 52 week high set back in January. WTI also stumbled 2.5% lower. It currently sits $10 off its July high of $75 per barrel.

The weakness in commodities clearly seeped into the market place as the commodity dependent Energy and Material sectors were the worst performers last week. Commodities have surely been hit by the stronger dollar — typically a stronger dollar will act as a headwind for many commodities. We make no bones about it, we certainly are not commodity traders. Yet, the recent 20% drop in copper has started to gain the attention of analysts and journalists alike due to the potential reasons for the drastic drop. Much of the recent fall has been attributed to a Chinese slowdown, who is the largest consumer of the industrial metal.

According to a recent New York Times article, the trade war is starting to take a toll on the world's second largest economy. Nonperforming loans at Chinese banks and Chinese corporate defaults are both on the rise, while investment growth has hit its lowest level since the late 90s. Further exacerbating the Chinese troubles is the renminbi's 9% drop against the dollar over the last 6 months. It has been almost three years exactly since weakness in the Chinese currency spooked our own markets, which in turn fell nearly 11% in 6 trading sessions. However, the Chinese slowdown has yet to put the brakes on our indices this year. The S&P 500 is currently less than one percent away from its January high while the China Shanghai Composite is down 25% during the same period.

The Wall Street Journal wrote a fascinating article focusing on the swift deterioration in the quality of leveraged loans. The market, in an insatiable quest for yield, has absorbed record amounts of junk-rated corporate loans. According to Thomson Reuters LPC and Nasdaq.com, more than 70% of syndicated US leveraged loans are now covenant-lite, compared to just 25% during 2006-2007. The lack of loan holder protections is leaving some to estimate lower recovery rates going forward in the event of a default. As *The Journal* pointed out, Moody's recently estimated that the recovery on leveraged loans would likely be 61% during a downturn, rather than historically stronger average of 70%. Second lien loan recovery rates are estimated to fall even more dramatically to 14% from a 43% historical recovery rate. In April, Guggenheim stated that they believe the next recession will be traced back to the corporate debt market, not the household debt market — à la 2007/2008. This should be a non-issue so long as companies can continue to roll over debt at low interest rates. As an aside, the Fed is set to meet again in September — the market currently is pricing in a 94% chance of a 25 bps point hike and a 64% chance of another 25 bps in December. The cost of borrowing appears to be continuing higher.

Upgrades/Downgrades & Dividends

CTSH — downgraded to neutral from overweight at JPMorgan, however the price target was increased to $87 from $86 (8/14).

DLTR — upgraded to overweight at Atlantic Equities, price target of $110 (8/13).

FISV — downgraded to underweight from neutral at JPMorgan, however the price target was increased to $82 from $77 (8/14).

NEE — Initiated buy with a price target of $184 at Mizuho Securities USA (8/13).

SYK — Initiated buy at BTIG with a price target of $187 (8/16).

YUMC — downgraded to perform from outperform at Oppenheimer (8/17).

Earnings Calendar

Date	Time	Ticker
8/21	Pre-Market	SJM
8/21	Pre-Market	TJX
8/23	Pre-Market	HRL
8/23	Post-Market	ROST

Portfolio News

As far as headlines were concerned, it was a slow week for Tandem holdings. Signature Bank popped nicely earlier in the week following the announcement that their board approved up to $500m in stock buybacks, on top of their dividend that was announced last month. A few of our names also got caught in the flurry of 13-F filings. Einhorn and co. took a stake in TJX, Dollar Tree, and Dollar General, while they liquidated Greenlight's stake in PayPal. The multi-billion dollar Jana Partners initiated a stake in Microsoft. Notably, Berkshire liquidated its position in Verisk Analytics — a holding of ours in both Equity and Mid Cap. While these announcements have absolutely ZERO impact on the way we manage money, it is always interesting to keep track of where large swaths of money are being parked.

While earnings season is mostly behind us, we have one last little surge in the next two weeks. JM Smucker, TJX Companies, Hormel Foods, and Ross Stores are all set to report throughout this week. Dollar Tree, Dollar General, and Brown-Forman are on tap for the following week.

	WTD	MTD	QTD	YTD
Dow Jones	1.4%	1.0%	5.8%	3.8%
S&P 500	0.6%	1.2%	4.8%	6.6%
Nasdaq	-0.3%	1.9%	4.1%	13.2%
Russell 2000	0.4%	1.3%	3.0%	10.3%
Con Disc	-0.2%	1.1%	2.8%	13.9%
Con Staples	3.2%	2.6%	6.6%	-4.0%
Energy	-3.6%	-6.1%	-4.9%	0.2%
Financials	0.6%	0.6%	5.8%	0.6%
Health Care	1.6%	2.4%	9.0%	10.1%
Industrials	1.4%	-0.9%	6.2%	0.3%
Info Tech	-0.2%	2.9%	5.0%	15.6%
Materials	-0.5%	-2.2%	0.7%	-3.4%
Utilities	2.5%	2.6%	4.5%	2.9%
REITs	2.9%	2.6%	3.6%	2.3%