August 28, 2023 - Tandem Investment Advisors, Inc.

T tandemadvisors.com/notes-from-the-trading-desk/august-28-2023

August 30, 2023

Market Movers & Shakers

The last few weeks have been largely mixed for equities – though both the S&P 500 and Nasdaq recovered some of the month's losses last week. Both major indices are in the middle of their worst months since December. For the most part, the long end of the yield curve has continued to move higher, though bonds did rally during the back half of last week as yields fell. Though earnings season is largely behind us, earnings still remained key as the tech behemoth Nvidia reported its quarterly results alongside a slew of retailers. In terms of Fedspeak, Chair Powell continued to strike a more hawkish tone during his speech in Jackson Hole. However, there were no grand declarations like last year's statement that U.S. households could feel “some pain”. This year, Powell reiterated that the Fed would hike further if necessary but that the Fed will remain patient and data dependent.

At one point last week, the 30-year was yielding 4.48% and the 10-year yielded 4.38% – its highest yield since November 6, 2007. The 30-year mortgage has risen to a 23-year high, which has coincided with a 28-year low in purchase applications, according to CNBC. Meanwhile Chairman Powell's speech in Jackson Hole reiterated the Fed's stance that rates will be higher for longer. It will take time for the economy to digest these higher rates. The impact of higher rates has clearly hindered new buyers in the housing market. Corporations will feel its impact more slowly, but they will likely still feel the effects. According to Morgan Stanley, U.S. companies have $2.6 trillion in corporate debt coming due between 2023 and 2025. Companies that will refinance the debt will likely be doing so at higher rates, which will lead to higher debt servicing costs. As a result, these companies that are rolling over their debt at higher rates will see an impediment to their profitability. Similar issues are currently impacting the Federal Government as well. A recent Bloomberg article highlighted that the weighted average interest for total outstanding debt has risen to 2.76% – the highest level since 2012 and much higher than the 1.80% from the year before. According to the Treasury Department's website, the cost of maintaining the debt has risen to $726 billion as of July 2023 – which accounts for 14% of the total federal spending.

Elsewhere, earnings were a big driver last week. All eyes were on Nvidia, which reported earnings mid-week and smashed expectations. The stock soared in the afterhours. However, it somewhat surprisingly gave up all its post-earnings move during Thursday's session. At one point in the afterhours, it was up 10+%. By the time trading stopped Thursday afternoon, the move reversed, and the stock closed just 10 bps higher. That is a massive intraday decline, which was met with further decline in Friday's session when the stock closed 2.73% lower. A slew of retailers reported earnings as well. Nordstrom said that they are seeing a "cautious consumer". Nordstrom and Macy's have seen a rise in credit delinquencies. Both companies in turn slashed forward guidance. Meanwhile, the CEO of Dick's Sporting Goods rang the alarm bell on retail thefts. President and CEO Lauren Hobart said that "organized retail crime and theft in general" hampered the company's second quarter results. This echoes a sentiment that has been expressed by the likes of Target, Ulta, Walmart, Home Depot, Lowe's and TJ Maxx. Theft, which retailers refer to as "shrink", has been a larger than anticipated drag on margins – back in May, Target said shrink could cost as much as $500 million in profits for 2023. A slowing consumer, or a thieving consumer, is not a great sign for those of us rooting for "no landing".

– Ben Carew, CFA

Transition Updates & News*

There has been a flurry of strategy activity to note on both the buy and sell side since our last edition of Notes from the Trading Desk. Beginning with the recent activity on the buy side, we increased our position in two existing Tandem holdings, **ResMed (RMD)** and **Nike (NKE)**, by roughly 50 basis points in each. **ResMed** is a medical device company that develops and manufactures equipment for the treatment of sleep apnea and other respiratory disorders. **RMD** is a holding in each of Tandem's three strategies: Large Cap Core, Mid Cap Core, and Equity. **Nike**, of course, needs no introduction as its signature swoosh logo is immediately recognizable by billions of people around the globe. **NKE** is held in Tandem's Large Cap Core strategy.

On the sell side, we began our liquidation of **LabCorp (LH)** and **PayPal (PYPL)** over the past couple of weeks. **LabCorp** initiated a quarterly dividend in May 2022 and has since failed to grow consistently, whether it be earnings or dividends. **LH** is a holding in Tandem's Mid Cap Core and Equity strategies. Digital payment platform and Venmo owner, **PayPal**, recently announced the completion of its search for a new CEO, appointing an individual from outside the company: Intuit executive Alex Chriss. This marks the second consecutive outside hire to this position. Tandem requires that companies demonstrate consistency and depth in management. **PYPL** is a holding in Tandem's Equity strategy.

Outside of strategy activity, **BlackRock**'s latest investment stewardship voting report has gathered the attention of many on Wall Street and in Washington. The report reveals that **BlackRock** CEO, Larry Fink, is steering the world's largest asset manager away from its previously unwavering support of ESG (Environmental, Social, and Governance) initiatives. **BlackRock** only supported 7% of corporate ESG proposals over the past year leading up to

June, marking a significant drop from the same period prior to June 2022 when it supported 22% of ESG proposals and an even larger reduction from 2021 where nearly half of global shareholder ESG initiatives received **BlackRock**'s support. This shift aligns with a broader industry trend, as other asset managers like State Street and Vanguard also reduce their support for ESG resolutions, partly due to changes in SEC regulations that make it harder for companies to dismiss shareholder ESG petitions. In **BlackRock**'s own words, "many [ESG] proposals were over-reaching, lacking economic merit, or simply redundant, [and] were unlikely to help promote long-term shareholder value".

– Jordan Watson, CFA

**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.*

Benjamin "Ben" Carew, CFA
Ben Carew is a shareholder, Vice President, and Portfolio Manager for Tandem Investment Advisors, Inc. Mr. Carew joined Tandem in 2013. Mr. Carew manages Tandem's trading desk, overseeing day-to-day investment operations, including trading, quantitative and fundamental research, and portfolio management. Mr. Carew also oversees Tandem's internship program. Mr. Carew is a regular member of the CFA Institute and the CFA Society South Carolina. Mr. Carew currently serves as the Vice Chair for College of Charleston's School of Business Investment Program, a student program seeking to provide the opportunity for a select group of students to distinguish themselves academically, professionally, and personally. Mr. Carew is a graduate of the College of Charleston's School of Business, earning a Bachelor of Arts in Economics with a minor in Finance.

past or future performance.