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MARKET MOVERS & SHAKERS

August has offered a mixed bag for equity investors so far. The Nasdaq and the Russell 2000 both continued their move higher during the first week of August, gaining roughly 2% each. But the Dow and the S&P 500, on the other hand, have taken a bit of a breather after their July ascents. The S&P 500's 9.1% gain in July marked its best month since November of 2020; so perhaps a cooldown was in order. On Friday, the labor market showed resiliency and continued strength as 528,000 jobs were added to the economy in July. Economists were only estimating a gain of 250,000 jobs. In addition, the unemployment rate dropped to 3.5% — matching the unemployment rate prior to COVID. At face value, those numbers sound terrific. The reality though is that the participation rate, which has been improving over the past year, remains at its lowest levels since the late 70s. As a result, only 32,000 jobs have been added to the economy since February of 2020. Yields tracked higher on Friday following the economic surprise as volatility has picked back up a bit more in yields. Broadly speaking, bonds have tumbled as yields have moved higher for so far in August. On the commodity front, oil has continued to drop as the price of WTI crude oil fell below $90 per barrel for the first time since mid-February. This week, markets and yields will undoubtedly be glued to Wednesday's CPI release.

A defining characteristic of equities these past few years has been the outperformance of growth relative to value. That changed for much of 2022. The outperformance of value began around Thanksgiving of last year and continued through most of May. However, over the past few months, the S&P 1500 Value Index has been essentially flat, while the S&P 1500 Growth Index has gained more than 10%. Despite the slight double-digit gain, the S&P 1500 Growth Index's price-to-earnings valuation has increased about 20% over the same time frame and is arguably expensive once more. How has its valuation outstripped its price gain? Earnings have begun deteriorating. Estimates peaked towards the end of June and according to The Wall Street Journal next quarter's estimates fell at their fastest clip in more than two years.

The message from Corporate America after Q1 earnings was pretty consistent – macro headwinds involving the Ukrainian war, inflation, and persistent supply chain issues hampered profitability in the first quarter, but those headwinds should wane into the back half of the year. It seems that can has been kicked out a few more quarters. The supply chain

situation has improved for most companies, but a strong dollar has replaced it as a thorn in the side of multinational corporations. As such, there has been consistency in the idea that these headwinds should now resolve themselves in early 2023.

This earnings season, a new message has appeared. In the dog days of COVID, many economists discussed the K-Shaped recovery. Namely, white collar workers and higher paid workers mostly weathered the COVID economic storm just fine. Lower wage workers faced a much harder time as entire industries like hospitality and tourism, manufacturing, etc. shuddered to a halt. The term K-shaped recovery became commonplace jargon used to describe the recovery occurring for those that were more well off and the absence of a recovery for those that could afford it least. We bring this up because the idea of a k-shaped economy is beginning to occur once more. Visa and Mastercard both reported their earnings within the last few weeks and spending has been incredibly robust for the consumers that they described as "affluent". Travel, entertainment, and restaurant spending has been red hot. Slowdowns, trade downs, and spending shifts have been noted though for lower income folks. Spending for lower income is still strong, but that's because it has to be in an inflationary environment. The lower income earners are spending more money because the cost of food and gas has risen so dramatically. As such, that portion of the consumer economy is spending much more of their income now on gas and groceries and less on things like home furnishings. O'Reilly Automotive made similar remarks. Their DIY customers, who tend to be their most price conscious spenders, have slowed down meaningfully.

Meanwhile, the more affluent consumer base that makes up their Do-It-For-Me base, which pays professionals to do the work, has remained strong. Elsewhere, the usage of private label goods are growing as the consumer trades down. Even McDonald's has made similar comments. On the company's most recent earnings call CFO Kevin Ozan said "We're seeing customers, and specifically lower-income customers, trade-down to value offerings and fewer combo meals." Economic news on Friday was dominated by the jobs number. Much less coverage was given to the fact that the Fed reported that the U.S. consumer borrowing increased at the second fastest rate ever through the end of June. When inflation comes down, a lot of these issues should subside. If the labor market slows down before inflation subsides, the deceleration in the economy should quickly pick up steam. If the labor market remains strong and inflation is slowed, then this economy will continue humming right along.

TRANSITION UPDATES & NEWS **

Transition activity slowed further last week with the only opportunities coinciding with a few earnings-related selloffs. Speaking of earnings, the thick of earnings season is now in the rearview. According to FactSet, the year-over-year earnings growth for Tandem's core holdings has outpaced the year-over-year growth for the S&P 500 by more than 9 percentage points so far. Couple that with the fact that the S&P 500's revenue growth is

outpacing the average Tandem holding by more than 5% and it is clear that Tandem's holdings have demonstrated their earnings power in a tough macro environment in a way that the broader market has not.

Despite the slowdown in transition activity, we have had a few strategy changes to note. We have recently trimmed our position in ADP in Equity and LCC, as well as ResMed and Republic Services in all three strategies. All three stocks continue to meet our fundamental criteria and will continue to be held in the portfolio. However, our quantitative process has begun to suggest that these three names have become sustainably overvalued. As a result, our process dictates that we must trim the position size to mitigate the exposure to the overvalued names.

***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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