Notes from the Trading Desk

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Major domestic indices finished with their third straight strong week. The S&P 500 was up 2.54%, while the Dow, Nasdaq, and Russell 2000 were up 2.40%, 3.45%, and 4.83%, respectively. Since the disastrous Christmas Eve trading session, the S&P 500 is up nearly 10.5%. The Nasdaq Composite is up an impressive 12.6% during the same time frame. The Russell 2000 has put them all to shame as it has rallied 14.3%. Crude was up an additional 7.5% last week and has recaptured $50+ per barrel. Yields remain suppressed as the long end of the curve remains near 52–week lows.

Before celebrating the slaughter of the bear market of 2018, and as we previously discussed in the December 3rd edition of *Notes*, large rallies in Bear markets are in fact quite common. At the end of the day, neither we, nor anyone else, have any idea whether or not the "bottom" is in. However, we can take a look at some of the data. In the very short run, the rally appears to be tapering off as the S&P has run into prior support around the 2,600 level. The S&P is up 10.43% in its last 12 trading sessions since its Christmas Eve selloff. That gain is good for the largest 12-day gain since October 2011.

Whether or not the bottom is in should most likely come down to the upcoming earnings season. More specifically, the forward guidance given by companies will be paramount. According to Standard and Poor's, Q1 earnings estimates for the S&P 500 have declined 4.3% since their October peak, while CY2019 estimates have fallen 3.5%. Earnings and price action have historically been highly correlated (see chart below). A slowdown in earnings, or worse — a decline in earnings — would certainly portend tougher times ahead for the market.

Again, as we discussed in the December 3rd *Notes*, these blowout rallies tend to occur either in the midst of bear markets or they cluster around the bottoms. As Bespoke Investment Group recently pointed out, there have been 12 instances since 1945 where the S&P 500 has dropped 15%+ in a 3-month period, followed by a 10% pop in 10 days. And, 50% of the time, we have made a lower low. However, the average one-year return in those twelve instances following the 10% pop is 13.86%. Whether or not the bottom is in seems to be a coinflip. A recent CNBC article highlighted the duration of bear markets since 1945, There have been 12 bear markets since World War II, as defined by a 20% drop in the S&P 500. The average duration of a bear market is 13 months — though it certainly feels much worse than that given the last two were 31 and 17 months respectively.

Lastly, it does not seem entirely coincidental that the slide in Crude and the slide in stocks have occurred simultaneously. Both Crude and the broader stock market began their sharp falls on October 3rd and bottomed out on December 24th. Crude currently seems to be in the driver's seat as the two asset classes have become highly correlated in the short-run. Similar to the S&P 500, Crude also seems to be running into some short term resistance.

Source: Standard & Poor's

Upgrades/Downgrades & Dividends

ACN — Upgraded to buy from neutral at BoAML, though their price target remains $166 (1/8).

BF.B — Downgraded to sell from neutral at Goldman Sachs, price target cut to $43 from $48 (1/9).

D — Downgraded to underperform from neutral at BoAML, target cut to $69 from $72 (1/11).

DG — Upgraded to overweight from sector weight with a target of $125 at KeyBanc (1/7).

DG — Initiated outperform with a price target of $126 at BMO Capital Markets (1/10).

DLTR — Initiated market perform with a price target of $98 at BMO Capital Markets (1/10).

DLTR — Upgraded to accumulate from hold at Gordon Haskett, price target of $110 (1/7).

DLTR — Upgraded to buy from neutral at Buckingham, their price target increased from $92 to $116 (1/8).

DLTR — Downgraded to perform from market outperform at Oppenheimer, though their price target increased from $92 to $104 (1/10).

NKE — downgraded to neutral from outperform at RW Baird, target cut to $82 from $87 (1/9).

NKE — Upgraded to buy from hold at Needham target is $85 (1/10).

NKE — Upgraded to buy from hold at HSBC, target increased to $95 from $92 (1/9).

NNN — Upgraded to outperform from market perform at Raymond James with a $53 price target (1/8).

RSG — Downgraded to neutral from buy at UBS, price target cut from $83 to $77 (1/10).

YUM — Downgraded to neutral from buy at Goldman Sachs, target cut to $76 from $83 (1/11).

Portfolio News

Earnings season is about to begin for the broader market, though we still have a little bit more time here until the busy work begins for us. Comcast (CMCSA) kicks off earnings season for us on January 23rd, followed by a slew of names over the ensuing two weeks. According to FactSet Research, Tandem's core holdings, on average, should grow their EPS by 13.5% and their revenues by 10.2%. Meanwhile, the S&P's EPS growth should be 10.5% with their 5.6% topline growth.

Part of the discrepancy in estimates could be attributed to a more diverse geographic revenue base in the S&P 500 than Tandem's average holding. Again, per FactSet's data, roughly 63% of the S&P 500's revenue is derived domestically. The average Tandem holding has more than 75% of their revenue coming from the United States. While the rest of the world appears to be slowing down, with Europe potentially headed for a recession, combined with the ever-present threat of trade war escalations, a more domestic-focused revenue base seems to provide a little more certainty.

	WTD	MTD	QTD	YTD
Dow Jones	2.4%	2.9%	2.9%	2.9%
S&P 500	2.5%	3.6%	3.6%	3.6%
Nasdaq	3.5%	5.1%	5.1%	5.1%
Russell 2000	4.8%	7.3%	7.3%	7.3%
Comm. Svcs	2.1%	6.0%	6.0%	6.0%
Con Disc	3.7%	6.0%	6.0%	6.0%
Con Staples	0.6%	1.6%	1.6%	1.6%
Energy	3.4%	8.1%	8.1%	8.1%
Financials	1.0%	2.7%	2.7%	2.7%
Health Care	2.3%	1.6%	1.6%	1.6%
Industrials	4.1%	5.4%	5.4%	5.4%
Info Tech	3.4%	2.5%	2.5%	2.5%
Materials	1.9%	3.4%	3.4%	3.4%
Utilities	0.8%	0.6%	0.6%	0.6%
REITs	3.9%	3.1%	3.1%	3.1%