NOTES FROM THE TRADING DESK

TANDEM INVESTMENT ADVISORS | BEN CAREW, CFA

January 4, 2021

MARKET MOVERS & SHAKERS

The holiday shortened trading week saw very light volume as most major indices drifted higher. The S&P 500 gained the most among its peers, up 1.43%. The Dow was not too far off, as it was 1.35% higher. The Nasdaq was up modestly, adding 65 bps in positive performance. Finally, the Russell Mid Cap was down slightly, dropping 6 bps, while the Russell 2000 saw a more meaningful decline of 1.45%. Among sectors, performance was evenly distributed. Communication Services, Consumer Discretionary, Consumer Staples, Financials, Health Care, Utilities, and REITs were all up more than 1.8%. Energy was the laggard, closing the week down 0.43%. Elsewhere, Gold continued its recent rally. It has now closed higher four of the last five weeks — a feat it has not accomplished since July. The bond market was quiet as action within Treasuries was muted. However, the ICE US Dollar Index (DXY) fell once more as the dollar continued to weaken against the basket of world currencies within the index.

The DXY has continued to slide lower since it spiked higher in mid-March, closing the year out a hair below $90. The depreciation of the U.S. Dollar against the Index's basket of world currencies has been its worst drop since late 2017 and early 2018. However, the Index is now beginning to approach some technical levels of support. The DXY bottomed around $88 in Q1 of 2018. The $88 level was also strong resistance in 2008, 2009, and again in 2010. Meanwhile, the relationship between the U.S. Dollar and the Chinese Renminbi has become a bit more stable over the past month. The Dollar had slid precipitously relative to the Chinese reserve currency since the start of the summer. But, the exchange rate was essentially flat for the month of December — perhaps signaling a change in the U.S. Dollar's global depreciation. The main driver behind the DXY's slide has been the relationship between the Euro and Dollar. The Euro has appreciated more than 5% relative to the Dollar since the election. The last move of this magnitude was in early September, which preceded the S&P 500 dropping nearly 10% intramonth. The Dollar seems to be at an interesting inflection point. At first glance, it looks like the Dollar could weaken further given the policy backdrop. The U.S. appears set to continue its loose monetary policy and there continues to be hope of fiscal policy support. If loose fiscal and monetary policy should continue, it could provide a further headwind for the Dollar. Of late, a weaker dollar has been beneficial for the larger multinationals and market leaders. On the other hand, as Bloomberg recently pointed out, speculators' short positions in the Dollar have hit their highest levels since March 2011. The Dollar bottomed not long after that and proceeded to rally shortly thereafter.

One thing worth keeping an eye on as we enter 2021 is the Treasury market. JPMorgan estimates that the Treasury Department will likely have to issue $1.8T in Treasuries with a maturity greater than one year. Some are beginning to suspect that this could lead to a supply imbalance that could force rates higher due to insufficient demand in the marketplace. One potential fix would be for the Fed to focus their purchase program on longer-dated maturities to artificially manipulate rates lower. A quick move higher in rates could spell bad news for the Equity market. Many of the market leaders have been inversely correlated with interest rates for the past few years. As rates drop lower, indicating the possibility of a future low growth environment, a premium is placed upon companies that can grow. This relationship is responsible for the historical dispersion in performance between growth and value stocks. While some are questioning the market's ability to digest the immense supply of Treasuries due to hit the market this coming year, credit spreads have shown no indication of deeper financial trouble. High Yield spreads are at pre-COVID levels. Similarly, Investment Grade Spreads and the Yield Curve are seemingly giving the greenlight as well.

However, one thing that could certainly propel rates higher is inflation. According to Bloomberg, Money Supply (M2) has surged at its quickest pace since 1960. While some argue that printing dollars will almost certainly lead to inflation, others counter that the velocity of money has completely dropped off a cliff. Velocity of money is an important measure for how quickly money is passed around the economy. Think of it this way: Person A buys a TV from Person B for $100; Person B then takes that $100 and buys dinner from Person C; Person C then takes the $100

Continued on Page 2

and pays their rent. $100 was all that was available in that scenario, yet it helped cover $300 in transactions. Velocity of money peaked in 1997. At that time, $1 of M2 Growth led to a $2.20 growth in GDP. This rate has plummeted to $1.15 through Q3 2020. The drop in the velocity of money can be argued away to a certain extent by highlighting the fact that velocity of money is merely a function of money supply and GDP. Increasing money supply while keeping GDP constant will lead to a natural drop in the velocity. So, part of the two-decade slide in the Velocity of Money can be attributed to the fact that the Fed's printing press is working faster than the U.S. Economy. In other words, growth of Money Supply has far outpaced the growth of GDP over the past two decades.

Anyway, back to inflation, commodities can often be a great place to spot inflation. Unfortunately, it can oftentimes be hard to discern what is signaling inflation and what is signaling growth. The cost of food is certainly higher. It has risen nearly 4% on a year over year basis since April — the largest change in food prices in nearly a decade. The surge in food prices is also evident in agricultural commodities. Corn futures are up 56% since August. Corn has not moved like that since 2010. Wheat is up 35% since July. Meanwhile, soybeans are up 55%, lean hogs are up 59%, and live cattle are up 42% since March!

Metals like copper and palladium, often indicative of economic growth, can also serve as inflationary hedges. Copper is up nearly 70% from its 2020 lows, while palladium is up nearly 60%. The spot price of iron has nearly doubled off its lows. Oil is even trading close to $50 per barrel after its epic collapse and negative print back in April.

Even the housing market has been seemingly red hot depending on where you live. The S&P CoreLogic Case-Shiller National Home Price Index rose 8.4% in its most recent reading. That is the biggest jump for the index since 2014. Some cities such as Seattle and Phoenix even reported double digit year over year growth. If that is not enough to convince you of the housing craze, lumber is up more than 225% since March. That massive advance even includes a 45% pullback from August to November before rallying once more.

Clearly, between the hot housing market and food prices heading higher, costs for Americans are rising. What is more, the Fed has made it quite clear that they are intent on hitting their 2% inflation target. They have even signaled that they are willing to let inflation run hot to ensure that it holds their magical 2% level. According to the Federal Reserve's preferred metrics, the U.S. economy has been devoid of sustained inflation since the mid-2000s. However, the cost of healthcare and education have been rising at a steep pace for years now. Couple that with the recently accelerating costs of food and housing, and throw in the Fed's desire to push inflation higher and it could spell bad news for some – especially those living on a fixed income.

Since the Fed implemented its first round of Quantitative Easing in November 2008, its balance sheet has grown more than 250%. This buying spree has coincided with S&P 500 earnings growth of roughly 120% -- thanks in no small part to share buybacks as sales have only grown 68%. Meanwhile, the S&P 500 is up 319% and the Nasdaq is up an even more astounding 500%. If we have learned anything from the Federal Reserve's decade long experiment with Zero Interest Rate Policy (ZIRP), Quantitative Easing (QE), and its ever-growing balance sheet, it is that it has paid to be an owner of financial assets.

TRANSITION UPDATES & NEWS **

The end of the year came quietly for Tandem stocks. No major news crossed the tape for any core holdings. As such, it was fairly slow in terms of transitioning new accounts following the Christmas Holiday. I will save the earnings preview for another few weeks. Instead, I wish everyone a Happy New Year! 2020 was a year to remember in so many different ways. Cheers to 2021!

***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.*

BEN CAREW, CFA

Ben Carew is a shareholder and Portfolio Manager for Tandem Investment Advisors, Inc. Mr. Carew joined Tandem in 2013. His duties include quantitative and fundamental research and portfolio management. Mr. Carew also oversees Tandem's internship program. 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.

DISCLAIMER

This writing is for informational purposes only. The information contained in this writing should not be construed as financial or investment advice on any subject matter. Tandem Investment Advisors, Inc. does not represent that the securities, products, or services discussed on, or accessible through, this site are suitable for any particular investor. You acknowledge that your requests for information are unsolicited, and the provision of any information through this site shall not constitute or be considered investment advice, or an offer to sell, or a solicitation of an offer to buy any product, service, or security.

Past performance is no guarantee of future results. Indices are unmanaged and not available for direct investment. They are shown or referred to for illustrative purposes only and do not represent the performance of any specific investment. No data in this writing should be construed in any way as performance of any Tandem investment product. For complete performance information and disclosures, please contact John Carew at jcarew@tandemadvisors.com.

From time to time Tandem may discuss select purchases and/or sales within this report. All past portfolio purchases and sales are available upon request. Any portfolio transaction discussed here does not constitute advice or a recommendation. Please consult your financial advisor before making any investment decisions.

KEY MARKET DATA

	WTD	MTD	QTD	YTD
Dow Jones	1.35%	3.27%	10.17%	7.25%
S&P 500	1.43%	3.71%	11.69%	16.26%
Nasdaq	0.65%	5.65%	15.41%	43.64%
Russell Mid Cap	-0.06%	4.52%	19.47%	15.16%
Russell 2000	-1.45%	8.52%	30.99%	18.36%

	WTD	MTD	QTD	YTD
Comm. Svcs	1.94%	3.07%	13.52%	22.18%
Con Disc	1.98%	2.45%	7.86%	32.07%
Con Staples	1.25%	1.45%	5.64%	7.63%
Energy	-0.43%	4.27%	25.78%	-37.31%
Financials	1.89%	6.05%	22.52%	-4.10%
Health Care	1.86%	3.74%	7.55%	11.43%
Industrials	0.73%	1.12%	15.19%	9.01%
Info Tech	0.91%	5.68%	11.52%	42.21%
Materials	1.17%	2.31%	13.92%	18.10%
Utilities	2.50%	0.42%	5.70%	-2.83%
REITs	1.84%	0.88%	3.45%	-5.36%