Notes from the Trading Desk

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US Indices were mostly higher this past week. The Dow led the way as it climbed 2.30%. The S&P 500 and the Nasdaq were up 1.50% and 1.79%, respectively. The Russell was the laggard as it was down 0.41%. Tech, Industrials, and Consumer Discretionary stocks were all up more than 2%, while more defensive stocks largely sold off — Telecomm and Utilities were both down more than 1% and REITs were not far behind. The long end of the yield curve was essentially flat, though the short end continued its climb higher. The spread between 10s and 2s is currently just a hair above 25 basis points — the smallest spread since mid-2007. Though that is a little misleading, as spreads were actually widening in 2007, having previously inverted in 2006. The spread between 30s and 10s — which are typically seen as less influenced by the Federal Reserve — are a measly 10 bps, a significant drop from the 50 basis point spread at the start of the year. The week was largely devoid of any significant news — the only blip being the Trump administration's proposal to slap a 10% tariff on an additional $200b of Chinese imports. This news momentarily shook the market on Wednesday, though the dip was bought as we closed the week out higher.

A lot of the positive action and discussion this past week seemed to be centered around last Friday's "Goldilocks" jobs number. Per CNBC, Jim Paulsen of Leuthold Group said "the participation rate [went] up, the unemployment rate went up, we had a big job gain and we had weak wages. I think that's about as good as we're gonna get here." Reports like the most recent jobs number certainly beg the question, how much better can the economy get? The unemployment rate was at its lowest level in over 40 years last month. The June number actually ticked higher from 3.8% to 4.0%. However, even the 4% number is still in in the 99th percentile going back 41 years. Consumer confidence is at its highest level since the turn of the century. ISM Manufacturing and Non-Manufacturing are both in their 95th percentiles over the past 40+ years. The yield curve, measured by the spread between 10s and 2s, is in the 73rd percentile — meaning it is at a relatively low spread. Valuations, which we have discussed in depth in previous posts, are historically rich. The Shiller P/E is in its 90th percentile going back 41 years. The only metric that is not at elevated levels is inflation — which is only in its 34th percentile. Taking the average percentile ranking of these 7 economic indicators, we can get a rough gauge of the economy, which currently sits in its 99.7th percentile. The economy is as strong as it has been, as measured by these popularly used metrics, in the last 41 years. The only time the average percentile was higher was March of 2000.

These numbers are not predictive nor are they indicative of anything, other than the fact that the economy is humming along right now. People are working, confidence is high, manufacturing and non-manufacturing activity alike are strong. Corporate earnings are projected to grow nearly 27% for the second straight quarter and are actually projected to accelerate to 29% during Q3 according to Standard and Poor's. The last time we saw earnings growth this strong was in 2009 and 2010. The cost of borrowing as measured by Moody's AAA effective yields, though having recently risen, is still at historically low levels. Even the VIX, which spiked spectacularly earlier this year, is resting near all time lows. The VIX closed on Friday at 12.18, in its 12th percentile over the entirety of the VIX — perceived risk is muted. CNBC and Jim Paulsen are right — this does seem to be as good as it gets. However, caution is always warranted when the party gets this good.

Upgrades/Downgrades & Dividends

ABBV — Initiated hold at Berenberg with a price target of $105 (7/12).

ABT — Removed from Guggenheim's "Best Idea List" (7/13).

CVS — Assumed buy with a target of $81 at Citi (7/9).

NEE — Initiated equal-weight at Barclays with a price target of $182 (7/10).

PYPL — Price target increased from $93 to $105 at Susquehanna (7/11).

PYPL — Initiated buy with a target of $100 at MoffettNathanson (7/11).

SJM — Increased quarterly dividend by 9% to $0.85 from $0.78, payable 9/4 (7/13).

TSCO — Upgraded to overweight from equal-weight at Stephens, target increased to $88 from $70 (7/9).

WBA — Assumed neutral with a target of $69 at Citi (7/9).

WBA — Downgraded to in-line from outperform, though the target was increased from $64 to $67 at Evercore ISI (7/10).

Earnings Calendar

Date	Time	Ticker
7/18	Pre-Market	ABT
7/19	Pre-Market	SBNY
7/19	Post-Market	MSFT

Portfolio News

It was a rather busy week here at Tandem. Earnings season is not quite under way for us here, though that did not stop a number of headlines from rolling in this past week.

JM Smucker announced that they are selling their US baking business to Brynwood Partners in a transaction valued at $375m. Their U.S. Retail channels primarily include Pillsbury, Martha White, Hungry Jack, and a few others, as well as their licensing agreements and manufacturing facilities. Analysts were somewhat mixed on the divestiture. Per FactSet's Street Account, some cited challenges in the packaged goods sector on a more macro basis, rather than SJM specific issues.

On the M&A front, CVS popped briefly intraday on Thursday as news broke that the DOJ was not planning on challenging CVS's acquisition of Aetna. Dominion's acquisition of Scana received FERC approval — though the potential deal still has a few regulatory hurdles to get over before becoming finalized. Lastly, ResMed formed a JV with Alphabet's (formerly Google) Verily. The newly formed JV is set to study the impacts, both financial and health related, of untreated sleep apnea. Ultimately, they are attempting to develop software that will help identify, diagnose, treat, and manage sleep apnea.

Earnings season is set to pick up. We have three names reporting this week, with an additional 13 companies on deck next week. According to FactSet, the average Tandem holding is set to grow its bottom line a little over 12% this quarter, with sales growth just under 9%. For comparative purposes, the S&P is expected to grow its topline a little under 8%, and its Net Income closer to 19%.

	WTD	MTD	QTD	YTD
Dow Jones	2.3%	3.1%	3.1%	1.2%
S&P 500	1.5%	3.1%	3.1%	4.8%
Nasdaq	1.8%	4.2%	4.2%	13.4%
Russell 2000	-0.4%	2.7%	2.7%	9.9%
Con Disc	2.1%	3.0%	3.0%	14.1%
Con Staples	1.0%	2.4%	2.4%	-7.8%
Energy	0.8%	0.5%	0.5%	5.8%
Financials	1.1%	1.5%	1.5%	-3.5%
Health Care	1.6%	4.7%	4.7%	5.8%
Industrials	2.2%	3.0%	3.0%	-2.8%
Info Tech	2.3%	4.7%	4.7%	15.3%
Materials	0.3%	0.9%	0.9%	-3.1%
Utilities	-1.2%	1.2%	1.2%	-0.3%
REITs	-0.9%	0.9%	0.9%	-0.3%

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