



## May 29, 2023 - Tandem Investment Advisors, Inc.

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May 31, 2023

### MARKET MOVERS & SHAKERS

Large cap growth and tech's outperformance of the broader market continued once more last week. According to FactSet, the NYSE FANG Index was up more than 5.5%. As tech outperformed, the Nasdaq gained more than 2.5% last week. The Russell was down marginally, while the Dow retreated 1% and the S&P 500 gained 32 bps. In a week in which the S&P 500 outgained its equal-weighted counterpart by more than 1.5%, the market's narrow leadership was further exacerbated. Despite this, banks continued to trade markedly better. The SPDR Regional Bank ETF, KRE, is now up nearly 17% from its early May lows – a feat that is a little unsurprising given the high short interest and the negative sentiment surrounding the industry. Elsewhere, yields continue to rise. The 10-year has traded back up to 3.8% for the first time since early March, while the 2-year has gained 80 bps over the past few weeks. As yields have risen, the dollar has continued to strengthen. Those two trends would normally be enough to buck the large cap growth trade's recent momentum. However, that has not been the case these past few weeks. The market is also backing off its bet of Fed rate cuts in the back half of the year. At the end of April, the market was pricing in at least 3 rate cuts by the December meeting. Today, the market is pricing in one more 25 bps hike in June followed by (maybe) one cut in the back half of the year.

Nvidia was one of the week's main contributors to tech's outperformance. The mega cap chip maker saw its market cap balloon more than \$200B following a positive earnings call mid-week. The company, which topped \$1T in pre-market trading earlier this week, noted AI's positive impact on the demand of its chips. The 24% jump on Wednesday may seem significant, but what's an additional 24% to a stock that's up 166+% this year already? The company is being priced for perfection at this point. Earnings growth is currently estimated to grow at a compounded annualized rate of 56% from the end of FY2023 through FY2027, while sales are expected to grow at an annualized rate of more than 34%. The stock now trades at nearly 50x earnings and 21x sales. Both are well above long term averages. It reminds me a bit of Cisco in the late '90s. Cisco was priced for perfection at the time. Valuations were rich, estimates for future growth were high, and the stock was trading at 25x sales. Over the last 15 years, it has traded with an average P/S ratio of 3.2x. Cisco's market cap has never surpassed the high water mark it set during the Tech Bubble. Cisco isn't a bad

company, and it wasn't a bad company coming out of the Tech Bubble. But its valuation got ahead of itself. Long story short, the price one pays for a stock can matter. Maybe this time will be different for Nvidia.

Perhaps the most important news came over the weekend rather than during the week. At the time of writing, it has been reported that an agreement has been reached "in principle" between House Speaker Kevin McCarthy and President Joe Biden. The agreement will suspend the borrowing limit for the next two years. It will also cut some domestic spending while extending limits to some government programs like food assistance. Congress will need to act fast to pass a bill before the government runs out of money – which could prove tough. Progressives and more conservative lawmakers alike expressed displeasure with the negotiated agreement. Republicans sought deeper cuts to government spending, while some progressives were dismayed by the spending limits. As an aside, one interesting thing to note – McCarthy said student loan payments will resume under this agreement. Payments, which had been "paused" since the start of the pandemic, would be expected to resume by late summer/early fall. According to CNBC, the average bill is ~\$400/mo. That's money that is hopefully being saved by most, but given today's low personal savings rate, it's likely that it is being spent. If that is the case, then that is a good chunk of change that will no longer be consumed, further tightening the belt for many consumers as they begin paying student loans once more.

– Ben Carew, CFA

## TRANSITION UPDATES & NEWS \*\*

The back half of May featured noisy headlines, but markets hummed along. With the majority of earnings behind us, benchmarks have fared well. The S&P posted a smidgen of gain for the week while the Nasdaq closed out a couple percentage points higher.

Tandem went to work transitioning new accounts and monies. We have repeatedly purchased names such as **Essential Utilities**, **Hormel**, **Jack Henry**, **MarketAxess**, and **Nike** over the course of May. From utilities to financials, there have been many opportunities to purchase our core holdings, as the broader market has yet to participate in the narrow rally enjoyed by tech names and anything surrounded by the buzz of AI.

**Microsoft** has recently received approval from the EU for their acquisition of Activision Blizzard. This transaction, which was announced in January of 2022, was most recently held up by European regulators. This acquisition is projected to total \$68.7 Billion.

We had two strategy level sales made in the latter half of May. **O'Reilly Auto Parts**, which sells car parts to professionals and DIY customers alike, was trimmed in Equity and Mid Cap. **Verisk**, a provider of data analytics and risk assessment for insurers, was trimmed in Mid Cap. Both stocks were sold for valuation purposes.

**Brown & Brown**, an insurance brokerage firm, will acquire Kentro Capital Limited. Kentro is a London-based insurance group that manages over \$500 million in gross written premium. In addition, BRO will acquire Kentro's subsidiaries Nexus, Xenia, Millstream, Capstone Brokers, and Spectrum Risk Management. All these companies provide specialized product review and underwriting and should help bolster BRO's UK-based business following their 2022 acquisition of Global Risk Partners.

**Costco** reported earnings after the bell on May 25th. Management noted fewer big-ticket discretionary purchases. Healthy margins were reported, and forward-looking discussions were generally positive. Q3 revenue missed estimates, while EPS beat. The report cited the addition of 25+ new warehouses over the next 5 years.

In the Medical realm, **AbbVie** has received FDA approval of their product Skinivive. Skinivive is projected to improve skin smoothness in adults. In addition, Abbott has received FDA approval for their spinal cord stimulation devices to help treat chronic back pain for those not suitable for surgery.

– Annie Klopstock

*\*\*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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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.

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