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Notes from the Trading Desk
- November 8, 2021
by Benjamin “Ben” G. Carew, CFA

MARKET MOVERS & SHAKERS

Financial markets have turned into a bit of an everything rally as bonds, stocks, gold and the US Dollar have all recently risen together. The Russell 2000’s gain of 6.1% last week led all of the major U.S. indices. Its impressive move was followed by the Nasdaq, up 3.1%, then the S&P 500 and the Dow Jones Industrial Average – which were up 2% and 1.4%, respectively. It was a week in which growth stocks and cyclical stocks outperformed. Consumer Discretionary and Tech were the two best performing sectors led by the likes of retail, cruise lines, and semis. Through Friday, the Nasdaq had closed higher for 10 straight days and the S&P 500 had been up for 16 of its 18 previous days. The S&P 500 has also moved at least 1% higher the last four weeks, while the Nasdaq is up nearly 11% this quarter, and the quarter started just five weeks ago. These are not common occurrences. With that being said, these occurrences have not historically been indicative of anything in and of itself. Rather, it serves to show just how hot equities have been since their late September/early October dip.

In terms of news, there was plenty. The FOMC announced the widely anticipated tapering of Quantitative Easing last week, which fueled a mid-week bond rally. The 10-year, which topped out at 1.7% in late October, closed the week around 1.45%. This drop in yields made its way through the rest of the financial markets and helped fuel the aforementioned growth rally. Healthcare stocks, specifically those that are COVID related, had a tough time on Friday following Pfizer’s reported high efficacy in a pill designed to treat COVID-19 patients. The pill reportedly reduced the risk of hospitalization and death by 89% in mild-to-moderate patients that took the pill within three days of their COVID diagnosis. Breakthroughs such as this should continue to make COVID increasingly manageable. More good news came on Friday in the form of a positive jobs report, which showed the unemployment rate dropping to 4.6%. However, the labor force participation rate still remains stubbornly low. There was hope that this would tick higher given the positive trends in COVID and the expiration of unemployment benefits, both of which helped aid the strong jobs number. Alas, that was not the case and the participation rate remains well below its pre-COVID levels. Next, if the CEO of GXO, the world's largest contract logistics provider, is to be believed, the supply chain issues may finally be reaching their zenith. In an interview with Bloomberg, CEO Malcolm Wilson said "We're through the worst of it. I think we've reached the peak." Finally, the House approved a $1.2 trillion infrastructure bill Friday night. According to The Wall Street Journal, the bill includes $110 billion in funding for roads, bridges, other major projects, as well as a $66b investment in rail maintenance and modernization – most of which will go to Amtrak.

Of note, despite the mostly positive news that broke throughout the week, the VIX remained determinedly above 15. This is somewhat surprising given the recent surge in equities. Typically, the VIX and the S&P 500 share an inverse relationship. As markets soar, the VIX will drop. From October 2007 to February 2020 – the market cycle preceding COVID – the average price of the VIX when the S&P 500 was at an all-time high was 12. Clearly, some market participants remain a little distrusting of the current environment and are using options to hedge accordingly. This positioning leads to a more elevated VIX. Similar trends are seen in both the Nasdaq and the Russell 2000's respective volatility indices as well. A drop in these various volatility gauges could very well lead to a surge in their Equity Index counterparts. However, it would also seem that it is likely indicative of a market that some would be quick to sell. In other words, the market currently seems positioned to compound and extend the move in either direction, rather than just chop and stand still.

TRANSITION UPDATES & NEWS **

Earnings season is now mostly wrapped up. According to FactSet, of the 505 stocks in the S&P 500, more than 450 have reported their Q3 results. Year-over-year earnings growth is expected to be 39.2%, while year-over-year sales growth is expected to be closer to 17.4%. Despite the terrific quarter, companies have been a bit more ominous on their calls. For their fourth quarter guidance, 41 companies have issued negative EPS guidance versus 26 companies that have issued positive guidance. 82% of Tandem's holdings have reported their quarterly results. It has been another solid quarter, by and large, as sales growth is expected to be above 14% when it is all said and done. Margin expansion has also clearly been present as earnings are expected to have reported growth of 19% by the end of the quarter as well.

Last week saw the addition of a new name across all three Tandem strategies, Jack Henry & Associates (JKHY). Jack Henry is a fintech company that assists small to mid-sized banks and credit unions process their financial transactions. About 1/3 of their revenue comes from providing technology that helps with core banking – mostly the technology to assist the processing of deposits, loans, transactions, etc. They also have a Payments segment, which helps process payments and helps facilitates ATM, debit and credit card processing as well. ACH origination and remote deposit processing is also a part of this line of business. The $12b firm has a long history of consistently growing their dividend and other key financial metrics.

***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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