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Market Movers & Shakers

Markets were slightly lower through the first two weeks of September. Tech was the worst performing sector, which has led to some underperformance of the Nasdaq relative to its peers. The weakness within the Nasdaq has not been a total surprise. For starters, it had been on an absolute tear to start the year. Secondly, yields have continued to trudge higher – which as we have noted in the past, can be a headwind for growthier stocks. Throughout the month, the 10-year U.S. Treasury has moved higher as its begun retesting its cycle high of 4.35%. The 2-year has also cracked 5% once more, while a 6-month Treasury Bill has recently been yielding more than 5.5%. Higher rates have long been considered a headwind for growth names – but now, higher rates are certainly a headwind for all asset classes, including equities more broadly, as Treasuries may now be attracting more dollars for investment at these higher yields. Given the move in yields, it has been somewhat surprising to see the outperformance of utilities month-to-date. The yield sensitive sector typically does not prefer a market with rising yields. Lastly, the Dollar Index has continued to move higher. After finding a bottom in mid-July, the ICE US Dollar Index surged more than 5% – a strong move for the greenback. Luckily for those going to the Ryder Cup in a week's time, the EUR/USD has fallen to a multi-month low of 1.07. Go Team USA!

Despite the bit of weakness throughout the month of September, the S&P 500 is just 7.5% away from its all-time high. This year's rally was initially met with a lot of skepticism – especially from institutional investors. According to Bank of America's Fund Manager Survey, institutional investors started the year off the most bearish they had been regarding global equities since the turn of the century. Retail, on the other hand, never got quite as gloomy, at least according to AAII's survey of individual investors. Despite the initial divergence between institutional investors and their retail counterparts, both have been steadily increasing their allocation to equities over the past few months as the market has continued to rally. As both investor types have been increasing their allocations towards equities, mega cap growth has continued to be a winner. For much of the year, but especially in August, and even into the first week of September, the market cap weighted S&P 500 has outperformed its equal weighted counterpart. In other words, the largest names were also seemingly the best performing ones. That changed just a bit last week as the equal weighted index outperformed the S&P 500 for the first time since early August. We previously saw a little bit of broadening out of the market throughout July as more names began participating in the rally. However, over the past ~6 weeks, the rallies within the market had become narrow once more.

On the economic front, the August print on CPI was a little hotter than expected and it ticked marginally higher. But the Fed will likely still stand pat at its September FOMC meeting. August PPI also ran a little hot, but one of the main culprits was energy. Over the last month or so, oil has zoomed higher leaving prices at the pump consistently around year-to-date highs. Inflation remains the hot topic and oft-discussed economic datapoint. Perhaps it is understandably so after inflation was mistakenly thought to be “transitory” in 2021 only to show a little bit more persistence than anticipated through 2022. However, it does seem like inflation is generally heading lower. Something that is maybe not being discussed enough though is the labor market. The labor market, which has been incredibly resilient, likely remains the linchpin for this economy. So far, the labor market has been great. Although, there have been a few cracks over the past few weeks and months – which need not mean bad news. The cracks could be shored up, if they do spread through, it could portend some economic uncertainty. First, the unemployment rate has been rising – just marginally so. At the end of January, the unemployment rate was 3.4%. In August, it had risen to 3.8%. Job openings have also steadily been declining. Nonfarm payrolls have also been decelerating. None of those three things necessitate doom. They are all just simply something to monitor.

– Ben Carew, CFA

Transition Updates & News*

PayPal Holdings, Inc. and **Laboratory Corporation of America Holdings** have fully exited since our last update. **PayPal** resided in our Equity Strategy while **Lab Corp** appeared in Equity and Mid Cap. As mentioned in a previous edition of Notes, **PayPal’s** second consecutive outside hire to the CEO position left the company in violation of our requirement that holdings demonstrate consistency and depth in management. LabCorp initiated a quarterly dividend in May 2022 and has since failed to grow consistently, whether it be earnings or dividends. Both needed to be liquidated as a result of those violations.

Dollar General, a discount retailer, is also on its way out the door. We have reduced its position size in Equity and Large Cap twice in the past few weeks. The growth that we value and require to be positive has turned negative, which means Dollar General had to go. Management noted that its customer base feels financially constrained. The company has also not seen the typical trade downs that accompany a slowdown. This is contributing to a decrease in same store sales and negative customer traffic rates. On a macro note, shrinkage is plaguing the entire retail field. Shrinkage is when inventory levels fall due to clerical errors, theft, or damage. **Dollar General** had been teetering on the brink of negative growth for some time. Recently, analysts' estimates have confirmed those negative forward growth rates.

On a sweeter note, **JM Smucker Company** has announced the acquisition of Hostess Brands for $34.25 per share. The total enterprise value will be around $5.6 billion, according to FactSet. Twinkies, HoHos, and Dingdongs will soon fatten Tandem's portfolio. Management noted that the acquisition will help Smucker expedite its penetration into the convenience store. **Smucker** has traditionally operated through grocery outlets, but this acquisition should add a new distribution channel. Hostess, which is already comfortably in the convenience store channel, also has a reputation for strong margins due to its efficient warehouse distribution model. The acquisition should boost **Smucker's** operating margins as overlapping synergies can be utilized between the businesses. The transaction is expected to close in Q3 of its fiscal year (April 2024) and should be immediately accretive.

Terreno Realty Corporation, an industrial REIT, recently announced the purchase of a property in Santa Ana, CA for $14.8M. This nearly 5-acre property consists of 3 multitenant office buildings, which the company plans to level. When redeveloped (ETA 2025), the property will consist of a 92,000 square foot industrial building for loading purposes. **Terreno** functions in six coastal US markets: Los Angeles, New Jersey/NYC, San Francisco, Seattle, Miami, and the DC area.

Mastercard and **Visa** are set to raise merchant fees soon. The change is to take effect in October and April, with an emphasis on online purchases. The Wall Street Journal reported that this could result in capturing $502 million in additional revenue. The fee can be broken down into two categories: network and interchange. When fees go up, it may only be a matter of time before this is felt by the consumer in the form of higher priced goods. There have been talks in the House and Senate to pass legislation that would allow merchants to process charges over alternative networks, however talks are still pending. The intent is to allow more competitors into the card network territory.

– 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.*

Benjamin “Ben” Carew, CFA

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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