

The TANDEM Report

Volume XXI, Issue 3, July 2020



"It requires a great deal of boldness and a great deal of caution to make a great fortune, and when you have it, it requires ten times as much skill to keep it."

~ Ralph Waldo Emerson

Dear Clients,

Tandem is committed to the preservation of your wealth by minimizing risk while adding value through consistent and superior investment performance over time. This issue of **The TANDEM Report** provides a summary of our views pertaining to the investment landscape and subjects that influence our decision making. More information about our firm, including our investment style and process, is available at www.tandemadvisors.com or upon request. We hope you find this report useful.

Respectfully,

John B. Carew
President

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All performance figures, charts and graphs contained in this report are derived from publicly available sources believed to be reliable. Tandem makes no representation as to the accuracy of these numbers, nor should they be construed as any representation of past or future performance.

Market Commentary: The Market Rebounds Sharply on Hope and Stimulus

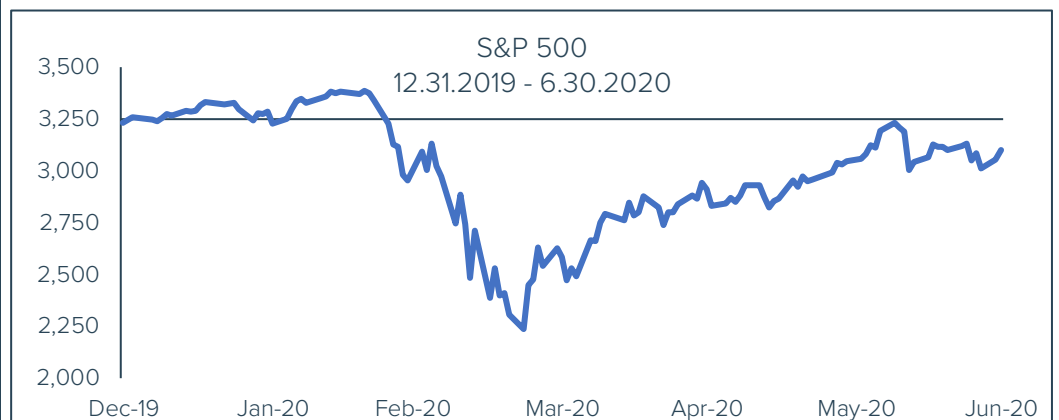
Much has changed since we last visited. At that time, it appeared that stocks had bottomed and were off to the races, but we couldn't be certain. Now we can be. In fact, the S&P 500 bottomed on March 23rd, declining almost 34% from its all-time high on February 19th. The ensuing rally, which stalled out a bit in early June, has been nothing short of spectacular. At its June 8th peak, the index was up over 44% from its bottom, nearly recovering all that was lost.

For the 2nd quarter, the S&P advanced nearly 20%. That paled in comparison to the NASDAQ, which was up more

than 30%. The divergence between the two is meaningful. The NASDAQ is more heavily influenced by large Technology companies like Amazon, Apple, Microsoft and Tesla, all of which were up more than 20%.

Big Tech companies have clearly been COVID-19 stock market winners. Some argue that their stock price out-performance is justified, given their positioning in this new economy. Perhaps this is so, but likely not to this extent. Signs of excess speculation are emerging, and it is possible these high fliers return to earth in the 3rd

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Commentary: The Fox and the Hedgehog

The ancient Greek poet Archilochus wrote, "the fox knows many things, but the hedgehog knows one big thing." The fox has clever ways to ensnare the hedgehog. Each time, the little hedgehog rolls up into a prickly ball, creating an impenetrable defense to the fox's nefarious efforts.

Philosopher Isaiah Berlin used this parable as the basis for the title of his essay *The Hedgehog and the Fox*,

published in 1953. In this work, Berlin divides writers and thinkers into two groups - those possessed of a single defining idea (hedgehogs) and those influenced by multiple notions with room for nuance (foxes).

Noted business author Jim Collins later applied the concept to business in his book *Good to Great*. Collins developed the notion that organizations

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COMMENTARY (CONTINUED)

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are more likely to succeed if they can identify the one thing that they do best – their "Hedgehog Concept."

The story was also loosely adapted into a cartoon in the 1960s as **The Road Runner Show**. Any reader that watched Saturday morning cartoons no doubt recalls this interpretation of the parable. In the series, Wile E. Coyote devises elaborate schemes to capture the speedy Road Runner. Mr. Coyote's business card even lists his title as Genius. While the many methods of entrapment he devises could be considered ingenious, they never manage to ensnare Road Runner, for Road Runner's one big thing (his speed) is mightier than the many things Mr. Coyote employs.

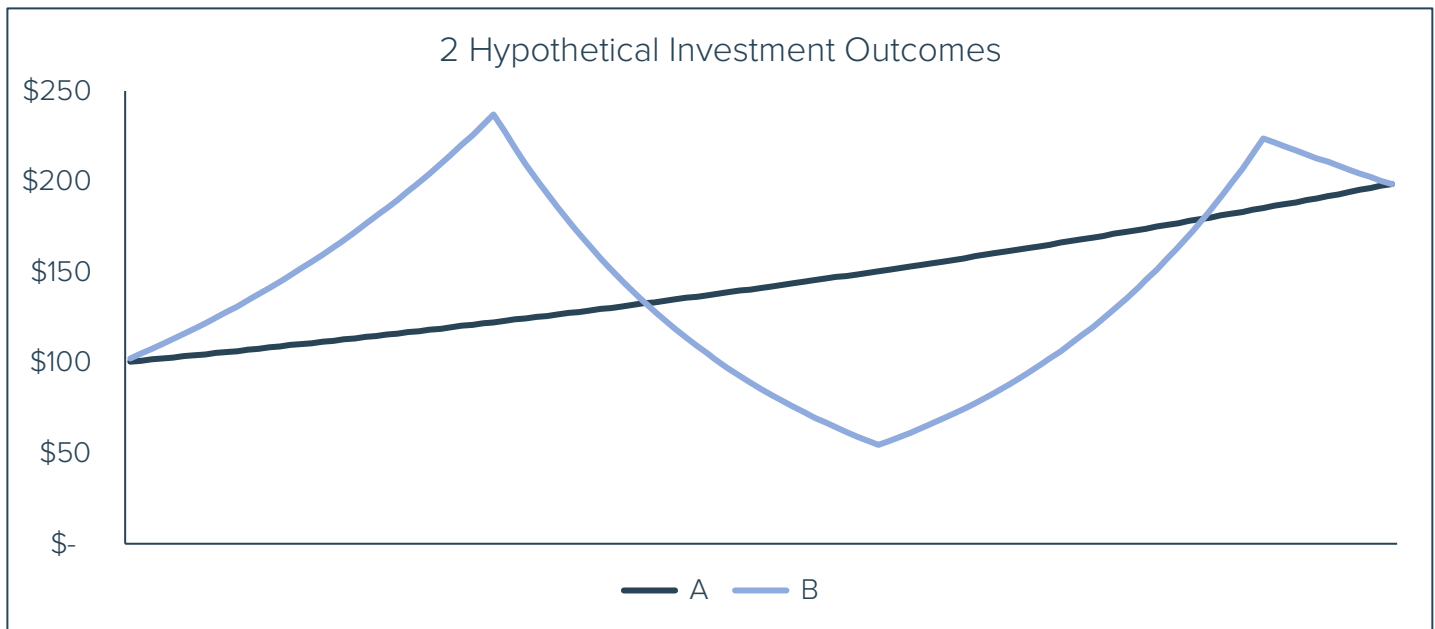
Tandem is a hedgehog. Our one big thing is to be the best in the world at providing market-like or better returns over a complete market cycle with a less volatile, more consistent experience for investors. We

late, most investors perceive risk to be declining. The reasoning apparently is that the market has it right, prices are rising, so risk is declining. This false sense of security causes investors to buy when prices are high.

Conversely, risk is perceived to be increasing when prices are falling. Obviously there is a reason prices fall, but generally speaking, the same company at a higher price carries more risk, not less.

Think of a market cycle. As prices soar and continue to hit new highs, enthusiasm for stocks increases. This can be measured by the amount of money flowing into the stock market. Historically, inflows increase at or near market tops. In other words, the market is at its riskiest the last day it hits a new high.

And then prices fall. Investors begin to sell stocks, and the selling accelerates with the steepening of the decline. Perceived risk has increased. Real risk has not.



seek to reduce risk when the odds appear to be against us, and add to risk when the odds seem in our favor. We will leave it to those we serve to determine whether we have attained our goal. But it remains our primary motivator and our one big thing.

Our hope is that this approach limits the stock market's impact on our clients' portfolios during turbulent times, allowing our clients to stay invested through a market cycle. We believe that if we can achieve this, then our clients have a better chance at investment success. As we wrote in our *January Commentary*, staying invested is the key to investment success, and limiting volatility is the key to staying invested.

Volatility in the market makes investors want to do the wrong thing at the wrong time for the wrong reason. When prices are high and rising, as they have been of

Yet outflows are their greatest at or near market bottoms.

Market volatility can create false perceptions of risk. This causes investors to ultimately buy high and sell low, never experiencing the true returns of the market. The foxes in the stock market have many tricks to employ to try to do better next time. But they are commonly reduced to trend following and timing. Neither of these appears to us to be repeatable or sustainable.

For reference, let us consider the hypothetical investments charted above, noted as A and B. Both investments have identical beginning and ending values. They start with \$100 and finish with \$200. Similar to the tortoise and the hare (not to mix parables), A runs

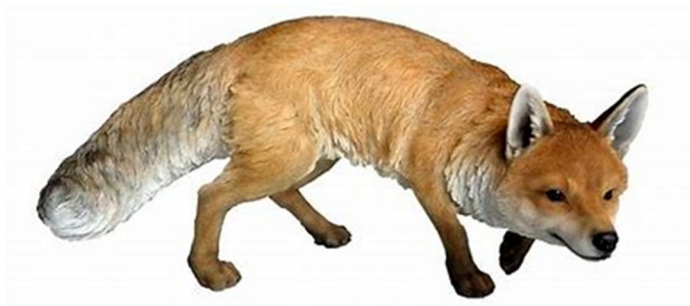
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COMMENTARY (CONTINUED)

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the steady race while B zips out ahead, falls behind and finally catches up in the end. If you were told with certainty that you could double your money, would you care which investment you chose? Of course not! They result in the same return. Unless, of course, you actually pay attention to the investments.

Imagine that you split \$200 equally between A and B. If you did nothing, you would end up with \$400. However, as the value of B rises dramatically faster than that of A, aren't you at least a little tempted to want to move some money out of A and into B? And when B's decline begins to steepen, don't you wish you hadn't done that, and aren't you tempted to move some money out of B and back to A? Your temptation, with the benefit of hindsight, is to buy high and sell low. This is the exact opposite of what you know to be sound - buy low and sell high. But the volatility gets in the way and clouds your vision. You are not alone! There are many foxes out there.



The Hedgehog knows one big thing. By maintaining focus on the one big thing, the Hedgehog is only interested in buying low and selling high. She is content to be different from all the foxes, if she is even aware of them. Buy low, sell high, have patience, be willing to hold cash when no alternatives present themselves, reduce volatility, stay invested, repeat.

Tandem's hedgehog philosophy allows us to focus solely on what we believe to be important. You may not agree with us as to what is important, and that is fine. There is more than one way to skin a cat. But for us, we are not interested in timing the market, following trends or investing in momentum. We simply identify companies that meet our criteria, buy the stock of any that we consider to be unsustainably inexpensive and reduce our ownership in any that we view to be unsustainably expensive. We eliminate any companies from the portfolio that cease to meet our investment criteria.

When prices are low, we often see this as an opportunity to add some risk to the portfolio. We do so by investing some of a portfolio's cash reserves into the stock of a company that meets our criteria and has a valuation that our math tells us is unsustainably low.

We perform this discipline one stock at a time, without a view of the market that informs us. We are merely making an unemotional, unbiased decision on a company, based upon our math.



The reverse is true when we believe a company's valuation reaches an unsustainably high level. We reduce portfolio risk by taking profit in overvalued securities while the prices are high. We invest the proceeds in the portfolio's cash reserves until better opportunities present themselves. Thus, we hopefully succeed in selling high, having patience, and buying low - just as it is supposed to be.

We take these actions proactively, not in response to market events. Our decisions are informed by the specifics of a company, not an opinion or an emotion. We are not following trends or public opinion. Those things have no place in our methodology. In fact, we often find ourselves at odds with 'prevailing wisdom'.

A client once observed that Tandem is both aggressive and defensive. To that we say emphatically - Exactly! Risk is fine when the odds are in our favor. Risk should be reduced when the odds are not.

Most investors measure return only on an absolute basis. Your returns are better than mine, so you win. It shouldn't be that simplistic. If your returns were achieved with a high degree of risk, are the returns commensurate with that level of risk? Winning the lottery produces a tremendous payoff. Yet the likelihood of a successful outcome when "investing" in lottery tickets is limited. If you buy \$50 worth of lottery tickets every week for 50 weeks you will "invest" \$2,500. Winning \$1,000 might provide a thrill, but not a reasonable return when adjusted for the level of risk you assumed.

In short, while most market participants rely upon varying metrics, Tandem's notion of investing is to rely upon the simple notion of reversion to the mean. If valuations are high, risk is rising and this trend will ultimately result in reverting back to a more normalized valuation. Sell when prices are high. If valuations are low, buy and capture the price rise as valuation becomes normalized over time. It is that simple. We know one big thing. And hopefully it produces consistent, repeatable, less volatile results for our clients.

MARKET COMMENTARY (CONTINUED)

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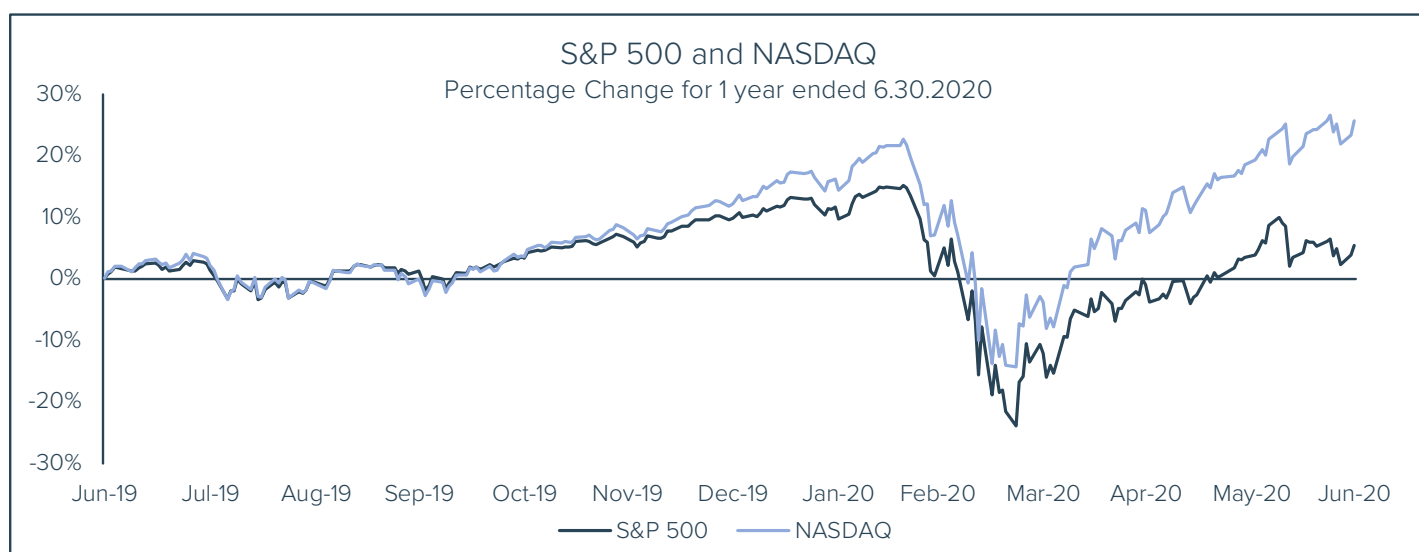
quarter. You should note that these companies are not in your Tandem portfolio. These are tremendous companies, but absent a global pandemic they do not represent appropriate value (in our view) for their level of risk (see *Commentary* on page 1). It is worth noting that the Information Technology sector now comprises 27.5% of the S&P 500, while Energy and Financials together only account for 12.9%. In 2010, they combined to represent 27% of the S&P while Technology was only 18.7%. It is reasonable to ask how long this outperformance can last. The chart below illustrates the NASDAQ's consistent outperformance relative to the S&P for the last year. The NASDAQ is up over 25% while the S&P is up only a little more than 5%.

Beyond Tech, much of the market's recovery has been fueled by hope for an end to the pandemic and by stimulus. On the hope front, we are clearly in a bet-

ter place today than we were 3 months ago. Testing has been greatly expanded and progress is being made on both the vaccine and treatment fronts. It does seem that it is simply a matter of time before we can be inoculated or cured. How much time is hard to say. But when we can all return to normal activity without fear, economic activity will return to normal. How long it takes to get there will determine how much of the economy survives until then.

On the stimulus front, the Federal Reserve's actions have been unprecedented in terms of both speed and size. They acted quickly to calm financial markets. Backstopping corporate debt has allowed companies like Boeing, which at one point appeared headed for bankruptcy, to access credit markets without requiring a direct government bailout. The Fed has added roughly \$2 Trillion to its balance sheet this year, Congress has allocated another \$3 Trillion or so, and

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TANDEM NOTES

Tandem's communications team is really upping its game of late. Under the skillful direction of Elaine Natoli, our publications, materials and web site have all been revamped. Further, we have begun a series of recorded conversations called **TANDEM TALK**. All of our publications, which include **Notes from the Trading Desk**, **Observations** and **The TANDEM Report**, are archived on our web site. Some of them are available as audio.

Speaking of audio, we are thrilled to welcome Margaret White to the Communications team. She is the voice of all Tandem audio products. Margaret joined us in April as Marketing Specialist. With an extensive background in communications, Margaret has been an invaluable addition as we have rolled out new ways for you to consume our message. Her posts on LinkedIn, her editing skills (both the written and recorded word), and her voice have been impactful and appreciated.

We must also acknowledge the insane contributions of both Allison Cianci and Billy Little. Both have school-aged children forced to learn from home. Somehow these two have managed to do the impossible through this pandemic - work full-time, parent, teach and babysit simultaneously. We hope schools can re-open soon, for all of you working parents.

We also need to send out a hearty thank you to Ben Carew and Jordan Watson for helping us perform for you as well as we have, while keeping us all well informed and laughing. Our trading room hasn't missed a beat. Our office never closed, and these two have been here every day, working 12 - 14 hours a day many times.

We are blessed to have a tremendous team here at Tandem. Thank you for allowing us to do what we love as we serve you.

MARKET COMMENTARY (CONTINUED)

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globally total stimulus is roughly \$18 Trillion. It is not hard to see why there is now such a disconnect between the stock market and the real economy.

For comments about specific stocks in your Tandem portfolio, please visit our website to read *Observations* and *Notes from the Trading Desk*. We did have a few companies succumb to the virus, as uncertainty regarding the future forced such Tandem stal-

warts as TJX and Ross Stores to suspend their dividends to preserve cash until more clarity emerges. We similarly had to part company with Disney, which we had just purchased in the 1st quarter.

For the most part, your portfolio companies weathered the storm in admirable fashion. We were very fortunate to have no direct exposure to the travel and leisure sector and the energy sector. Our process has served us well.

5 Year Annualized Dividend Growth for Tandem's Holdings by Strategy from Q2 2015 to Q2 2020

Tandem's average dividend-paying holding has increased its dividend by 9.70% on an annualized basis for the last 5 years. This growth is the result of strong and growing earnings, cash flow and revenue.

Large Cap Core 5Yr. Annualized Dividend Growth		Equity 5 Yr. Annualized Dividend Growth		Mid Cap Core 5 Yr. Annualized Dividend Growth	
Company	Dividend Growth	Company	Dividend Growth	Company	Dividend Growth
Abbott Laboratories	8.45%	Abbott Laboratories	8.45%	Becton, Dickinson	5.66%
AbbVie, Inc.	18.27%	AbbVie, Inc.	18.27%	Brown & Brown	9.10%
Accenture Plc	9.42%	Accenture Plc	9.42%	Brown-Forman CI B	6.70%
Automatic Data Processing	13.18%	Becton, Dickinson	5.66%	C. H. Robinson Worldwide	6.06%
Becton, Dickinson	5.66%	BlackRock	10.74%	CBOE Global Markets	11.38%
BlackRock	10.74%	Brown & Brown	9.10%	Check Point Software Tech	NA
Brown & Brown	9.10%	Brown-Forman CI B	6.70%	Ecolab Inc.	7.33%
Brown-Forman CI B	6.70%	C. H. Robinson Worldwide	6.06%	Essential Utilities	7.26%
C. H. Robinson Worldwide	6.06%	Check Point Software Tech	NA	Euronet Worldwide	NA
CBOE Global Markets	11.38%	Comcast	12.97%	ExlService Holdings	NA
Comcast	12.97%	Costco	11.84%	Expeditors International	7.63%
Costco	11.84%	Dollar General	10.35%	FactSet Research	11.84%
Dollar General	10.35%	Dominion Energy	7.74%	Fiserv	NA
Dominion Energy	7.74%	Ecolab Inc.	7.33%	Henry Schein	NA
Ecolab Inc.	7.33%	Essential Utilities	7.26%	Hormel Foods	13.21%
Essential Utilities	7.26%	Euronet Worldwide	NA	Laboratory Corp of America	NA
Expeditors International	7.63%	Expeditors International	7.63%	National Retail Properties	4.16%
FactSet Research	11.84%	FactSet Research	11.84%	NV5 Global Inc.	NA
Hormel Foods	13.21%	Fiserv	NA	O'Reilly Automotive	NA
Intercontinental Exchange	14.87%	Henry Schein	NA	T. Rowe Price	11.60%
Johnson & Johnson	6.13%	Hormel Foods	13.21%	Republic Services	7.66%
Microsoft	10.47%	Intercontinental Exchange	14.87%	ResMed	6.85%
National Retail Properties	4.16%	Johnson & Johnson	6.13%	Signature Bank NY	NA
NextEra Energy	12.70%	Laboratory Corp of America	NA	J.M. Smucker	6.58%
T. Rowe Price	11.60%	Microsoft	10.47%	Stryker	10.76%
Raytheon Technologies	NA	NextEra Energy	12.70%	Tyler Technologies	NA
Republic Services	7.66%	O'Reilly Automotive	NA	UMB Financial Corp	5.70%
ResMed	6.85%	PayPal Holdings	NA	Verisk Analytics	NA
Signature Bank NY	NA	T. Rowe Price	11.60%	Waste Connections	16.29%
J.M. Smucker	6.58%	Raytheon Technologies	NA	Yum! Brands, Inc.	NA
Stryker	10.76%	Republic Services	7.66%		
Walgreens Boots Alliance	6.27%	ResMed	6.85%		
Waste Connections	16.29%	Signature Bank NY	NA		
		J.M. Smucker	6.58%		
		Stryker	10.76%		
		Tyler Technologies	NA		
		Verisk Analytics	NA		
		Walgreens Boots Alliance	6.27%		
		Waste Connections	16.29%		
Average	9.79%	Average	9.81%	Average	8.65%

Companies not paying a dividend on 06.30.2015, or that have restructured since then, are NA. All companies in Large Cap Core currently pay a dividend.

The list of holdings above for Tandem's 3 strategies are as of 06.30.2020. These lists do not constitute investment advice, nor do they represent performance of any Tandem investment product. FactSet is the data source for the above calculations.

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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.

YIELD TABLE				KEY MARKET DATA				
	Current	3 months ago	1 year ago		6/30/2020 Close	% Change 1 Year	% Change 3 Years	% Change 5 Years
3-month Treasury Bill	0.16%	0.29%	2.17%	S&P 500	3,100.29	5.39%	27.93%	50.27%
2-year Treasury Note	0.19%	0.45%	1.81%	Dow Jones Industrial	25,812.88	-2.96%	20.91%	46.50%
5-year Treasury Note	0.34%	0.59%	1.83%	NASDAQ	10,156.85	32.40%	79.87%	131.01%
10-year Treasury Bond	0.73%	0.87%	2.07%	Russell 2000	1,441.37	-7.99%	1.84%	14.95%
30-year Treasury Bond	1.49%	1.46%	2.57%	German Xetra DAX	12,310.93	-0.71%	-0.12%	12.48%
Prime Rate	3.25%	3.78%	5.50%	London FTSE 100	6,169.74	-16.91%	-15.63%	-5.39%
Federal Funds Rate	0.08%	0.65%	2.38%	Shanghai Composite	2,984.67	0.19%	-6.51%	-30.22%
Discount Rate	0.25%	1.02%	3.00%	Crude Oil	\$39.27	-32.84%	-14.70%	-33.97%
				Gold	\$1,800.50	27.72%	45.12%	53.69%
				CRB Index	137.97	-23.79%	-21.06%	-39.27%
				U.S. Dollar Index	97.35	1.76%	2.02%	1.76%
				Euro/Dollar*	1.12	-1.20%	-1.69%	0.85%

The data used to compile the above tables come from publicly available sources. Tandem believes it to be reliable, but makes no such assertions. Such data is not meant to imply past or future performance for Tandem or any securities market.

* Negative return represents dollar strength, positive return represents dollar weakness. Returns are cumulative, not annualized.