



## Financial Markets Review

The volatility in financial markets that began a little more than 3 months ago took another leg higher in the back half of February and into the first week of March. The swings in equity prices have not been for the faint of heart. Just in the first 2 months of the year, the S&P 500 has declined 12%, risen 8%, declined 10% and risen 7%. Through all of the ups and downs, the S&P 500, Nasdaq, and Russell 2000 have fallen 9%, 15% and 11%, respectively, since the start of the year.

Over the past couple of weeks, the news headlines have rightfully been dominated by the Russian invasion of Ukraine. And one would naturally think that the weakness in equities is the result of this tragedy. However, the uncertain geopolitical landscape is just another catalyst rather than the cause of the heightened volatility and decline in equity prices.

As we have discussed for several months now, U.S. equities entered a new volatility regime in November of last year. It was then that Federal Reserve Chairman Jerome Powell hinted for the first time that the Federal Reserve was possibly behind the curve on reining in inflation. The tapering of Quantitative Easing ("QE") had just started and no more than a couple of weeks later it was announced that the tapering schedule would need to be accelerated. From that point forward, the tapering of QE has accelerated, the idea of Quantitative Tightening ("QT") or reducing the size of the Fed's balance sheet has been tossed around and the market's expectations for future Fed rate hikes has soared. At one point, market participants were banking on a 50-basis point rate hike in March with another six 25-basis point rate hikes throughout the year. The shift in expected Fed policy has done a complete 180 since only six months ago when the majority of market participants expected, at most, a single 25-basis point rate hike in 2022. The cause of the decline in equity prices and rise in volatility is due to the actual and perceived reduction in monetary and fiscal liquidity. Record valuations across numerous financial assets and the hostile actions of Russia have been catalysts to rising volatility and falling stock prices, but certainly, they are not the cause.

So, what could stem the tide of falling equities? In the short run, any reprieve in the Russia/Ukraine headlines or backing down by Putin would certainly be applauded by markets. Investor sentiment, as measured by the CNN Fear & Greed Index, is flashing an "extreme fear" reading. And bears are currently outpacing bulls in the most recent Investors Intelligence survey. As investors brace for more downside, any positive development on the geopolitical front could usher in a massive relief rally in equities. However, this type of rally in equity prices would likely be short-lived as it wouldn't alter the path of monetary and fiscal policy.

The issues we face today are the same, if not worse, than what initially set off the volatility in equities. Inflation is stubbornly high, which is forcing the Fed to tighten monetary policy at the same time asset valuations are elevated. The Russian/Ukrainian conflict has caused commodities to spike, which is certainly not going to help the inflation picture. Just last week, commodities, as measured by the S&P GSCI Index, experienced its largest weekly increase in more than 50 years. The sharp rise in energy, food and metals caused the 5-year breakeven inflation rate to take another leg higher and pass the rate in November of last year when the Fed pivoted to a faster pace of tightening. At the same time, expectations for future growth are declining as real interest rates fall, the yield curve continues to flatten with the spread between 2s and 10s at only 25-basis points and the Atlanta Fed's GDPNow model estimating 0% real GDP growth for Q1'2022. The market environment we find ourselves in today is the one we discussed a few months ago.

*"An economic growth scare coupled with a faster than expected reduction in liquidity is a recipe for financial asset volatility."*

– Observations, December 2021

The wildcard in everything continues to be inflation and the market's expectations for future inflation. As long as inflation expectations remain elevated, the Federal Reserve will be forced to act aggressively. Considering the median S&P 500 stock is trading at a forward P/E of 19x, which according to Morgan Stanley is in the 94th percentile of historical levels, valuations are still not all that supportive. Until inflation expectations or equity valuations come down, the volatility story will continue to be much of the same.

## Castle Tandem Fund Update

Most of what I have written thus far has been based around the broader equity markets. However, as most of you know, we are an active, bottom-up manager, which means the equity indices have no bearing on how we manage our strategies. The S&P 500 might still be considered overvalued with enough reason to fall further before valuations begin to make more sense, but that does not mean every company within the index needs to decline further.

It is our job to block out the noise and act on opportunities. Ultimately, we are looking to add to or establish positions in companies that are capable of growing through any economic environment. The underlying volatility allows us to be opportunistic to buy what should be bought and sell what should be sold. The S&P 500 trading 10% off its all-time high is not a signal that guides our decision making. Rather, we look for opportunity in individual companies, which also means that our purchases and sales do not happen all at once. Many companies will provide the opportunity to buy or sell well before the market bottoms or tops.

Over the past few months, we have become net buyers after being net sellers for much of the prior 12 months. At the end of Q3'2021, the Fund held 28.32% in cash and cash equivalents<sup>1</sup>. As of March 9, 2022, that cash position has dropped to 18.42%. The volatility has given us the opportunity to add to our existing holdings in T. Rowe Price (TROW), and Comcast (CMCSA). We have also been able to establish new positions in Jack Henry (JKHY), MarketAxess (MKTX), and Visa (V). Until the root cause of this volatility regime ebbs, there will continue to be opportunities to deploy cash for those who are patient.

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1 Represents cash equivalents and other assets less liabilities



Billy Little, CFA  
Portfolio Manager  
Castle Tandem Fund

Billy Little is a shareholder, Vice President and Portfolio Manager for Tandem Investment Advisors, Inc. Mr. Little began his career in the investment industry in 2004, as a Financial Advisor with Ameriprise Financial in Baltimore, Maryland. Mr. Little joined Tandem in 2006. Mr. Little directs Tandem's quantitative and fundamental research. He is a regular member of the CFA Institute and past President of the CFA Society South Carolina. Mr. Little graduated from the College of Charleston with a Bachelor of Arts in Business Administration with a concentration in Finance.

*The opinions expressed are those of the Fund's Sub-Adviser and are not a recommendation for the purchase or sale of any security.*

*The Standard & Poors 500 Index (S&P 500) is an index of 500 stocks. The Nasdaq Composite Index is a market-cap weighted index of more than 2,500 companies listed on the Nasdaq stock exchange. The Russell 2000 index measures the performance of the small-cap segment of the US equity universe. The S&P GSCI is a broad-based commodity index.*

*As of December 31, 2021 The Castle Tandem Fund held the following positions mentioned in this report: T. Rowe Price Group, Inc. (TROW, 3.05% of Fund total net assets); Comcast Corp (CMCSA, 2.26% of Fund total net assets); Jack Henry & Associates, Inc. (JKHY, 2.09% of Fund total net assets); MarketAxess Holdings, Inc. (MKTX, 1.65% of Fund total net assets). Visa, Inc. was added to the Fund's portfolio after December 31, 2021. As of March 9, 2022 Visa represented 2.01% of the Fund's total net assets.*

**The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the Fund, and it may be obtained by calling 1-877-743-7820 or visiting [www.castleim.com](http://www.castleim.com). Read it carefully before investing. Distributed by Rafferty Capital Markets, LLC Garden City, NY 11530.**

## Important Risk Information

*The risks associated with the Fund are detailed in the Fund's Prospectus. Investments in the Fund are subject to common stock risk, sector risk, and investment management risk. The Fund's focus on large-capitalization companies subjects the Fund to the risks that larger companies may not be able to attain the high growth rates of smaller companies. Because the Fund may invest in companies of any size, its share price could be more volatile than a fund that invests only in large-capitalization companies. Fund holdings and asset allocations are subject to change and are not recommendations to buy or sell any security.*