



## Castle Tandem Fund Update

As the Q4 earnings season draws to a close, the uncertainty surrounding corporate earnings growth has seemingly become murkier. With 99% of S&P 500 companies having reported so far, it is evident that reported earnings growth will be worse than expected. Coming into the quarter, analysts were forecasting earnings to contract by 3.3% and the final tally will likely show a decline closer to 5%. The million dollar question now is whether or not estimates for the remainder of 2023 have come down enough, because that will likely be a key factor going forward.

Six months ago, analysts were expecting S&P 500 earnings to grow by 10.4% in CY2023. By the start of this year, CY2023 growth was essentially slashed in half as estimates were brought down to 5.7%. Today, estimates for CY2023 are for 1.7%. That is a significant reset of expectations over such a short time period; however, the hope is that the bar has been lowered enough for companies to surprise to the upside. If they can surpass estimates, then that would go a long way in justifying current valuation levels.

It's been extremely quiet on the transaction front within the Castle Tandem Fund over the past few weeks. Given how active we've been over the past 15 months, it feels a bit odd to report that nothing much has changed since last month. There will be times when we are aggressively buying; times when we are aggressively selling; and, other times, like now, where we monitor the portfolio, but no transactions are made. Broadly speaking, our quantitative model is signaling that the vast majority of the Fund's holdings and those companies on our watch list are fairly valued, which explains the lack of activity.

## Financial Markets Review

Interest rates and the future path of monetary policy was the theme of the month in February. As we've discussed numerous times since short-term rates began to rise off the zero bound in late 2021, the direction and speed of change in short-term rates matter a lot for the equity market. In February, as interest rates soared, all major U.S. equity indices gave back some of January's gains. The S&P 500, Nasdaq Composite and Russell 2000 declined 2.44%, 1.01% and 1.69%, respectively.

February began with the FOMC raising the Fed funds rate by an expected 0.25% to a range of 4.50% to 4.75%. During Fed Chair Powell's press conference, he remarked how the disinflation process had started, which sent yields lower and equities higher. The market took his message as a sign that the Fed may not only put an end to their aggressive rate hiking campaign, but that they would be cutting rates by the end of the year.

To the Fed's credit, Jay Powell and the rest of the FOMC have been pretty consistent with their messaging – the Fed funds rate is unlikely to be cut this year and interest rates will remain higher for longer. It wasn't more than 48 hours after the Fed concluded their meeting that the market finally took heed. The non-farm payrolls report was a blowout showing over half a million jobs were created in January, as the unemployment rate sank to its lowest level in over 50 years. There was absolutely nothing in the report that supported the notion of an interest rate cut later this year.

Since the January employment hit the tape, several other economic reports have supported the Fed's message of "higher for longer". Multiple inflation readings have shown that prices have remained stickier than originally thought. In addition, economic growth has remained fairly resilient, which also gives the Fed more leeway to further hike rates and make sure inflation does not become entrenched. All of this has led the yield curve to shift dramatically higher. The 2-year Treasury yield rose from a low of 4.03% on February 2nd to 4.97% on March 2nd. That is a massive move in just a month's time! And for the first time in over 15 years, there is a spot on the Treasury curve with yields greater than 5%, as the 6-month and 1-year Treasury bills both yield roughly 5.1%.

For the time being, the reaction in equity markets has been extremely muted and resilient given the nature of the move in short-term interest rates. Now that there is an alternative, at some point, a 5%+ Treasury bill is going to weigh on financial assets and spark volatility in riskier securities. The good news is that you finally get paid to be patient, which is certainly a welcomed change from the "cash is trash" mantra of the past 15 years.



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18 Years of Investment Experience

Billy Little is a shareholder, Senior 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 oversees Tandem's corporate financials, including business planning, budgeting, and vendor negotiations. Mr. Little also 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 Russell 2000 Index measures the performance of the small-cap segment of the US equity universe. The Nasdaq Composite Index measures all Nasdaq domestic and international based common type stocks listed on The Nasdaq Stock Market.*

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### **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.*

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