TANDEM
INVESTMENT ADVISORS

Financial Markets Review

Last month, we briefly discussed seasonality as it relates to stock market performance during the months of August and September. Over the past 50 years, August and September have been the two worst months for both the S&P 500 & Nasdaq, and going back to 1928, September has been the weakest month of the year. Without fail, the seasonality trade struck again, as the S&P 500 posted its worst decline since last December, falling 4.77%. Not to be excluded, the Nasdaq Composite and Russell 2000 also had their worst month, declining 5.77% and 5.89%, respectively.

Much of the equity market weakness in September can be directly attributed to the consistent upward pressure on interest rates, specifically at the long end of the curve. Last month, we noted the effect a break above 4% on the 10-year Treasury bond had on equity prices in August. This past month, the equity market weakness was compounded as the 10-year Treasury bond jumped another 57 basis points to 4.57%. And, just a few days into October it climbed an additional 40 basis points as the yield approaches 5%.

For much of this year, we have opined on two topics with both being geared toward interest rates. The first topic has to do with market expectations vs. Fed expectations. It's been over a year now since Fed Chair Jerome Powell first stated that the Fed's plan was to maintain a restrictive policy for some time. His message of interest rates staying "higher for longer" has been repeated at just about every Fed meeting since then, but the market has failed to embrace his words. As much as the Fed has tried to talk interest rates higher, market participants took the other side and bet on premature rate cuts. It wasn't until the September FOMC meeting that the market finally blinked. Even though the Fed paused on hiking rates, the market came around to the Fed's side as the expectation is now for the first rate cut to be in Q4 of 2024 rather than Q2 of next year, which is in line with the Fed's expectation. This change in expectations is vastly different than just six months ago when the market was anticipating rate cuts to begin before the end of 2023.

As the market embraces "higher for longer", it brings us to the second topic we have discussed multiple times this year – the point at which bonds become a formidable competitor to stocks for an investor's incremental dollar. With inflation rates trickling lower and bond yields continuing higher, the interest rate adjusted for inflation, which is referred to as the real rate, has finally reached a level last seen just before and during the recession in 2008. A positive and ever-increasing real rate is attractive for fixed income investors since you are getting compensated in excess of the inflation rate. At the same time, it weighs on equity valuations and increases borrowing costs, which restricts economic growth.

One could argue that higher interest rates have taken their toll on equities. As noted for several months now, if it weren't for the strength of the "Magnificent Seven", the return profile of the cap-weighted S&P 500 would look much different so far this year. To get a better gauge of how the average stock is doing year-to-date, through the end of September the S&P 500 Equal-Weight Index is higher by 1.79%, which pales in comparison to the 13.07% advance in the cap-weighted S&P 500. In fact, only one-third of S&P 500 companies are actually outperforming the index. Higher money market rates and 5%+ yields at the front end of the curve have proven to be competitive against the average stock. The question now is whether or not higher rates on the back end of the curve, which feed into higher borrowing costs for businesses and consumers, prove too much for the economy to handle. Only time will tell.

Castle Tandem Fund Update

There are a few themes in the market right now that have recently given us the opportunity to add to a handful of positions. The first theme is higher rates. We have gone to great lengths discussing the impact of rising rates on stocks and the economy as a whole. As interest rates have taken another leg higher, rate sensitive sectors, such as REITs and utilities, have suffered in kind.

The sell-off in REITs has presented an opportunity for us to add to Terreno Realty (TRNO). As a reminder, TRNO is a real estate company that acquires, owns, and operates industrial properties in six major coastal U.S. markets. The types of properties include warehouse/distribution, flex, research and development and trans-shipment. TRNO's focus is to purchase industrial real estate in areas where there is growing demand but limited or shrinking supply. This strategy has worked well for TRNO since they became public in 2009, as seen by their consistent growth in revenues, earnings, and cash flows. And due to their strong fundamental growth, TRNO has been able to grow their dividend at a compounded annual growth rate of 12% over the past 10 years.

In addition, the decline amongst utilities gave us an opportunity to add to NextEra Energy (NEE). NEE owns Florida Power & Light, which is America's largest electric utility. They are the world's largest generator of renewable energy from the wind and sun and a world leader in battery storage. NEE recently reaffirmed their guidance of 6%-8% earnings growth through 2026 and 10% dividend growth through 2024. This affirmation came on the heels of negative guidance and a cut in the distribution rate for one of their growth-oriented limited partnership subsidiaries – NextEra Energy Partners (NEP). The decline in shares of NEP fed through to the parent company, NEE, which ultimately gave us the ability to add to the Fund's position in NEE at what we believe is an opportunistic valuation level.

The second theme gripping markets at the moment is with the adoption and hype surrounding the new weight loss drugs. As the hype builds, several analysts have come out declaring that several industries will be upended by these drugs as they become widely adopted. ResMed (RMD) was one of those companies that got caught up in the crossfire. RMD provides cloud-connectable medical devices for the treatment of sleep apnea, COPD, and other respiratory conditions. RMD continues to meet all of our growth metrics, while the valuation has been driven back down to a rather attractive level. Thus, we were able to add to our position in the Fund.

Lastly, we were able to incrementally add to the Fund's position in Brown Forman (BF.B). BF.B produces and distributes whiskey, scotch, tequila, vodka, and wine under the following brands – Jack Daniel's, Woodford Reserve, Old Forester, Finlandia, Diplomatico, Herradura, and Korbel. The belief is that these weight-loss drugs could result in less alcohol consumption. The knock-on effects that the weight-loss drugs will have is still up for debate. In the meantime, we view the indiscriminate selling of certain companies as an opportunity to add to our positions at attractive valuations that we have not seen in quite some time.

William "Billy" L. Little, Jr., CFA
Senior Vice President
19 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 S&P 500 Equal Weight Index is the equal-weight version of the S&P 500. 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.

As of September 30, 2023 the Castle Tandem Fund held the following positions mentioned in this report: Terreno Realty Corporation (TRNO, 1.50% of Fund total net assets), NextEra Energy, Inc. (NEE, 2.21% of Fund total net assets), ResMed, Inc. (RMD, 2.11% of Fund total net assets), and Brown-Forman Corporation - Class B (BF.B, 1.76% of Fund total net assets).

The Fund does not have a position in NextEra Energy Partners LP (NEP).

The investment objectives, risks, charges and expenses of Castle mutual funds must be considered carefully before investing. The prospectus for each Fund contains this and other important information about the investment company, and it may be obtained by calling 1-877-743-7820, or visiting www.castleim.com. Read it carefully before investing.

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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