

THE TANDEM REPORT

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"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 superior investment performance. 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 informative.

Respectfully,

John B. Carew
President,
Chief Investment Officer

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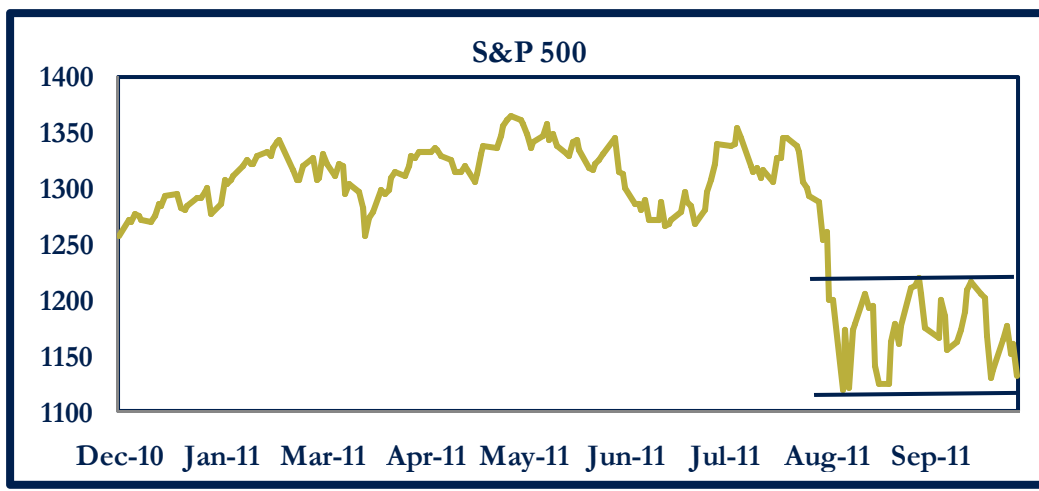
MARKET COMMENTARY: INVESTOR ANXIETY OVER NEWS OF THE DAY LEADS TO DRAMATIC MARKET VOLATILITY

Stock market volatility continues to be the story of the day. After registering a post-crisis high in early May, stock indices nearly entered bear market territory (defined as a 20% decline) in August. In fact, over a span of only 13 trading days from July 22nd to August 10th, the S&P 500 plunged 16%. It then took only 3 days to climb 7.5% and 4 days to return to the August 10th low. For the rest of August and September, the market traded

back and forth between a narrow band on the S&P between roughly 1,120 and 1,220, making several round trips and leaving investors bewildered.

The chart below illustrates the steep drop followed by the volatile swings within the well-defined band. Investor uncertainty has been apparent as evidenced by the sense of gloom as the market tests the lower end of

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COMMENTARY: MANAGING PORTFOLIOS THROUGH VOLATILITY

Managing portfolios through the current stock market volatility is not for the faint of heart. We are often asked how we approach a market like this, and frankly, the answer is that we approach this market the way we would approach any other - by staying true to what we do best. Fortunately, our clients have fared better than most.

Much has been made of the importance of the global economy and the associated risks to growth. We have always focused

on companies that do not rely on economic tailwinds for growth, preferring instead to own companies that grow their earnings through any economic environment.

We regularly use these pages to offer evidence that consistent earnings and dividend growth lead stock prices higher regardless of what the market does. When markets are roaring higher, economically sensitive companies typically perform bet-

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COMMENTARY (CONTINUED)

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ter in the excitement. Conversely, when markets stumble, those companies with sound fundamental growth perform better. While at the end of the day both types of stocks may end up in the same place, we prefer the smoother experience our companies provide to the wild rides of the more economically sensitive.

To illustrate, we update the comparison of J.M. Smucker and Caterpillar introduced in the March, 2011 issue of *The TANDEM Report*. You may recall that our clients own J.M. Smucker and not Caterpillar. While both are excellent companies, Caterpillar does not meet our requirements.

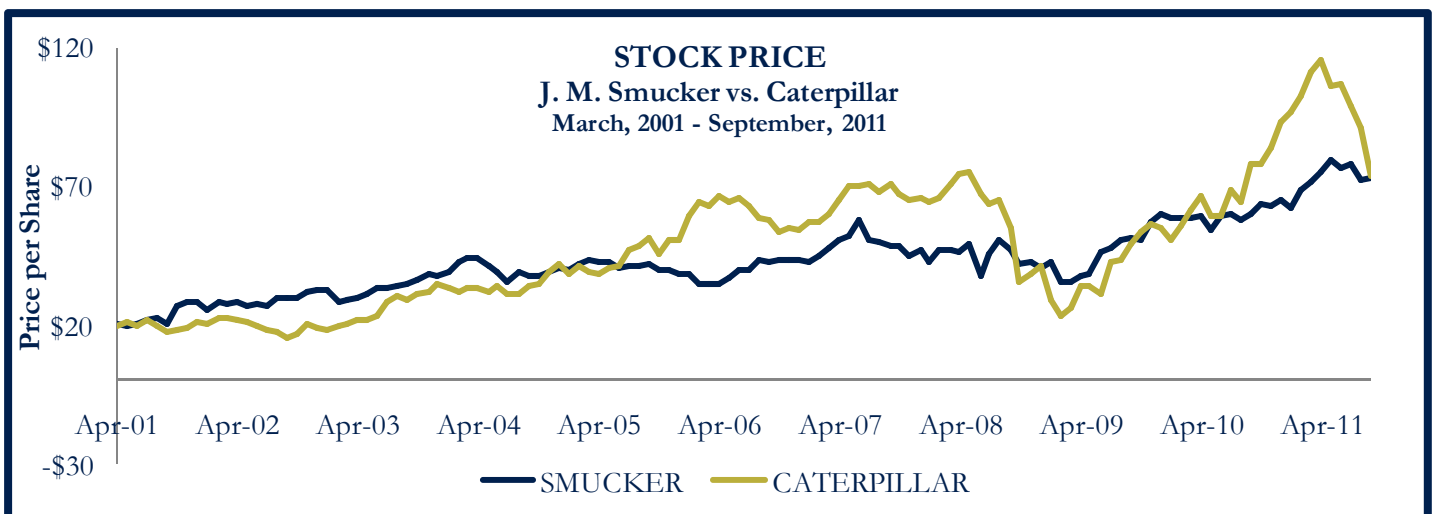
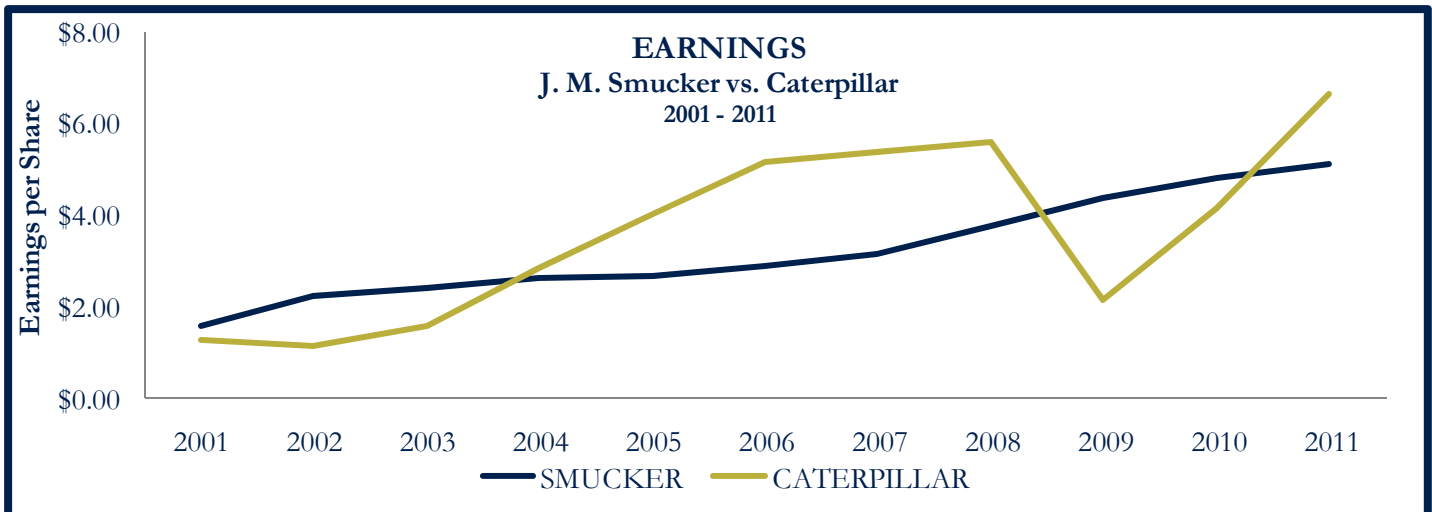
The first chart below shows earnings growth for both companies since 2001. Caterpillar's earnings have outstripped those of Smucker. Yet they have done so with many fits and starts while Smucker has experienced a smooth upward ascent. The result of Smucker's ability to deliver consistent earnings growth independent of the economic turmoil is a much steadier price appreciation. The second chart below reflects that the stock price for both companies begin and end in virtually the same place, but Caterpillar has experi-

enced much greater swings both up and down.

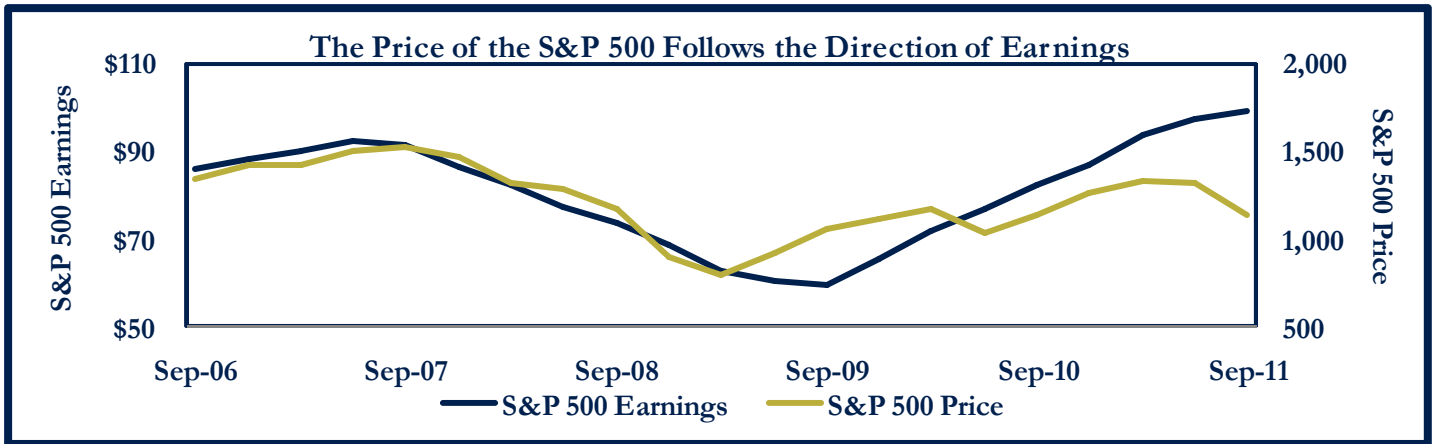
There is a financial term that addresses this smoothness of price movement called beta. The stock market has a beta of 1. A stock or portfolio with a beta greater than 1 can be expected to change in value at a rate greater than the change in value of the market. Similarly, a stock or portfolio with a beta less than 1 can be expected to move at a rate of change less than that of the market. Caterpillar has a beta of 1.44 while Smucker has a beta of 0.54.

The stock portfolios we manage enjoy betas that range roughly from 0.60 to 0.75. To us, this means that our clients' stocks and overall portfolios will not experience the violent swings of the stock market, changing in value more for their own merits than for the direction of the market.

There are many ways to skin a cat. Some great money managers seek more beta and volatility in order to achieve greater returns in rising markets. However, our 20 year history of a lower beta approach has managed to outperform many different types of markets and appears to be well-suited for the current one. After all, the first rule of making money is to not lose it!



MARKET COMMENTARY (CONTINUED)



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the range and the near euphoria as it approaches the upper end. Headline news receives much of the blame for the turbulence. The crisis in the Euro Zone, a China slowdown and fears of recession all rightly concern investors.

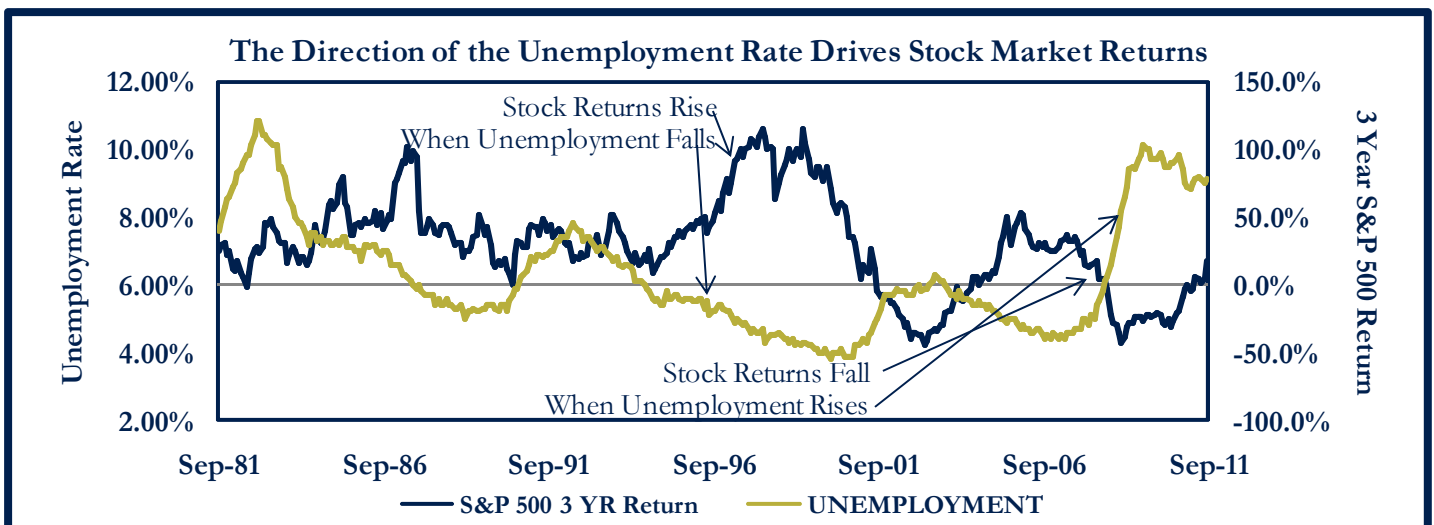
But we believe the real issues are receiving less attention than they deserve. The most important data to focus upon is corporate earnings in the near term and the direction of unemployment in the intermediate term. Certainly external factors like Europe and China will influence these, but excessive concern can distort reality.

The chart above illustrates clearly that the price of the S&P 500 follows the direction of earnings. Until recently, the correlation has been remarkable. As we enter the heart of corporate earnings reporting season in October, it appears that the stock market is forecasting lower earnings as the price dips well below earnings. And the market is in fact a leading indicator of future earnings. However, evidence to date suggests that U.S. companies appear to be healthy and reporting profits in line with expectations. This is welcome news and should provide a floor to the market. Corporations are telling us that it appears the stock market has it

wrong in the short run.

The basically sideways direction (albeit with plenty of volatility) of the S&P indicates that the market has it right in the intermediate term. The chart below shows the inverse correlation between the 3-year return of the S&P 500 and the direction (not the rate) of unemployment. Stable unemployment levels leave the market directionless. But as unemployment either rises or falls, the market does the opposite. Until unemployment begins to move in one direction or another, the market is likely to remain in its sideways pattern.

The news of the day makes investors anxious and this anxiety is manifested in dramatic volatility and oversized short-term swings. Yet evidence suggests that the real drivers of the market's direction are earnings and unemployment. We are not likely to have answers to Europe, China or anything else in the near term, which probably leaves us to enjoy more of this crazy market. But at the end of the day, it really hasn't gone anywhere. Much like a roller coaster, today's market takes us for gut wrenching rides, yet we begin and end in the same place. Let's see what trends may begin to emerge in earnings and unemployment before we commit to gloom or euphoria. Until then, sit back and enjoy the ride. It will be over soon enough.



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YIELD TABLE				KEY MARKET DATA				
					9/30/11 Close	% Change 1 Year	% Change 5 Years	% Change 10 Years
	Current	3 months ago	1 year ago	S&P 500	1,131.42	-0.86%	-15.30%	8.69%
3-month Treasury Bill	0.01%	0.02%	0.15%	Dow Jones Industrial	10,913.38	1.16%	-6.56%	23.35%
5-year Treasury Note	0.95%	1.76%	1.41%	NASDAQ	2,415.40	1.97%	6.95%	61.16%
10-year Treasury Bond	1.92%	3.16%	2.65%	Russell 2000	644.16	-4.73%	-11.22%	59.10%
30-year Treasury Bond	2.91%	4.37%	3.77%	German Xetra DAX	5,502.02	-11.67%	-8.37%	27.71%
Prime Rate	3.25%	3.25%	3.25%	London FTSE 100	5,128.48	-7.57%	-13.96%	4.59%
Federal Funds Rate	0.08%	0.04%	0-0.25%	Shanghai Composite	2,359.22	-11.16%	34.63%	33.68%
Discount Rate	0.75%	0.75%	0.75%	Crude Oil	\$79.20	-0.96%	25.89%	238.17%
3-Month LIBOR	0.37%	0.25%	0.29%	Gold	\$1,620.00	23.95%	170.36%	452.71%
				CRB Index	298.15	3.94%	-2.43%	56.52%
				U.S. Dollar Index	78.79	-0.04%	-8.42%	-30.52%
				Dollar/Euro*	133.84	-1.75%	5.73%	46.96%

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.