BOXWOOD

CAPITAL MANAGEMENT, LLC

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Q1 of ‘21 can be simply summarized by the observation that rates rose and when that happened the core stocks of The Jensen Opportunity Fund declined. Indeed, the Breaking News banner on the CNBC app read, “S&P 500 falls as tech shares come under pressure amid rising bond yields.” That push notification came 2 days before the end of the quarter but just as easily could have captured the essence of many of the trading days since the beginning of the quarter. On the days when the yield on the 10-year Treasury was rising, the accompanying decline in high growth, mega cap tech stocks seemed inevitable. The contrapositive was also true – when those stocks were rising, the 10-year was usually declining in yield – just not as frequently and not at the same level as the declining stock days.

The rising rate environment “caused” (reluctantly used) a general repricing in high growth stock names. The higher yields made the value of the growth stocks’ future earnings less valuable. The so called multiple(P/E) lowered. With rates artificially low, those spectacular earnings were rewarded with a higher stock price, but with higher rates, not so much.

What should a repricing of growth stocks in a rising rate environment mean to a long-term investor? Very little. Rates are rising for all good reasons. Vaccines are being distributed at an accelerating pace, while case counts, hospitalizations and deaths are all decreasing (maybe plateauing, but not rising, as of this April 1stish writing). Life is slowly going back to normal and so should rates. According to the Federal Reserve inflation is in check. The yield on the 10-year at the beginning of the year was held artificially low and now it is not. Normalized rates for the right reasons should be welcomed. Therefore, a repricing in some of the fund’s holdings shouldn’t be alarming.

Despite the downward pressure rising yields put on the share prices of the fund’s stock positions, The Jensen Opportunity Fund still outperformed the S&P 500 index by 43 basis points and finished the quarter 6.20% over the end of the previous year’s value.

As described in previous updates, the fund will occasionally use stock options, for example, to either add leveraged long positions or put on a hedged short position. The outcome of those positions on the performance of the fund depends on the various success of the trades. In the case of Q1, the fund was able to add “alpha” through the use of call options bought on underlying “reopen” stocks. Those call options paid off handsomely and allowed the fund to outperform the S&P yet again.

Until next time,

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