Tortoise QuickTake Podcast

May 23, 2017

Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, a senior member of Tortoise provides a timely update on trending topics in the market.

Hello and welcome to the Tortoise Credit Strategies weekly podcast. I'm Greg Haendel, one of the Senior Portfolio Managers on the investment team at Tortoise Credit Strategies. First, we just want to convey our condolences to the families and those affected by the Manchester event. For today's podcast, we will primarily discuss what one man believes and I quote is "the single greatest witch hunt of a politician in American history." All political views and accuracy of the prior statement aside, we will try to wade through the fake news in U.S. politics and discuss some of the political news currently swirling about, what it could mean for the U.S. financial markets and how we have positioned our portfolios as a result of recent news and in anticipation of what's to come.

First, a brief history: Immediately following the election of President Donald Trump and the Republican sweep in Congress in November 2016, financial market expectations surged higher as a result of an increased probability that the new administration would pass pro-business and pro-spending policies aimed at improving economic growth. Potential policy enhancements include business and consumer tax cuts, decreased financial regulation and increased fiscal stimulus among other policies. Financial markets will typically move in anticipation of future events, discounted by the likelihood and timing of such events occurring. Over the months following the election, many U.S. equities market indices surged over 10%, 10-year U.S. Treasury interest rates increased almost 80 basis points, investment grade corporate bond spreads tightened 23 basis points in the Bloomberg Barclays U.S. Corporate Bond Index and the dollar strengthened more than 5% versus a basket of currencies according to the DXY Index, all from trough to peak. In fairness however, not all of these moves were solely the result of financial market expectations regarding the new administration's potential policies. Although, each was influenced by these expectations to some degree.

Fast forward to today, and we have witnessed market recalibrations to varying degrees, some over the last couple months, some just last week, as a result of the storm of political controversy surrounding President Donald Trump. These controversies (whether fake news or not) include alleged campaign ties to Russia, questionable timing surrounding the firing of former FBI Director Comey, allegations of obstruction of justice, potential leaks of confidential information to Russian officials and most recently, the appointment of former FBI Director Robert Mueller as special counsel investigating the alleged ties between the Russian government and individuals associated with the campaign of President Trump. While words such as "impeachment" have been tossed around, the main impact of this elevated political uncertainty is a higher risk of inaction, which for financial markets presently translates to the possibility of further delays to, and lower likelihood of, pro-growth policy initiatives moving forward. As a result, we have seen 10-year U.S. Treasury rates retrace almost 50% of their post-election move higher, the dollar retrace 100% of its move higher, while equity prices and corporate credit spreads have retraced less than 20% of their post-election move.

Again, in fairness, while not all of the moves higher in various markets were solely the result of the Trump trade, the amount of retracement (or lack thereof) also isn't solely the result of a reversal of the Trump trade. For example, equities and corporate credit spreads have benefited from an improving first quarter earnings season; corporate bonds continue to enjoy strong retail and foreign demand, while interest rates suffer from some softer first quarter hard economic data.

Without implying impeachment is or is not in the cards, it is worth trying to extrapolate what could happen to the markets or what has happened in the limited number of U.S. historical impeachment proceedings, and the likelihood of those proceedings occurring. First, we believe it would take a proverbial smoking gun in the investigation under the Republican-controlled Congress to move forward with impeachment proceedings. However, in 2018, should Congress swing back to Democratic control after the mid-term elections, we believe it would be a much lower bar to move forward with impeachment proceedings. Nevertheless, looking back at historical impeachment proceedings, the market reactions were very muted and minimal in the proceedings in the early 1920s under President Harding and in the late 1990s under President Clinton. While the market certainly behaved very differently and poorly in the 1970s during the Nixon impeachment proceeding, it is difficult to pin the market actions on politics given the dollar devaluation, inflationary pressures, Federal Reserve hiking interest rates and massive insurance fraud at the time. As such, we believe that the economy matters more to the markets than politics. However, as was the case following the recent election, the markets extrapolated strong improvements in the economy and business climate as a result of expected pro-growth policies to come out of the new administration. As such, any interference (whether it be a delay or inability to get some of these policies passed) will cause the markets to recalibrate as we have seen in some markets over the past few months and in other markets over the past week.

At Tortoise Credit Strategies, we remain constructive on U.S. economic growth and corporate earnings irrespective of any potential pro-growth policies boost from the Trump administration, and we further remain moderately bearish on the direction of interest rates as a result of improving growth, tighter Federal Reserve policy and an eventual rise in inflation. However, early in 2017, most major markets had fully priced in the potential boost from President Trump's pro-growth policies with little to no discount for the timing or likelihood of these policies getting passed. As a result, we pared back some risk on the margin since the beginning of the year to reflect this disconnect; although we do remain modestly overweight risk assets, reflecting our continued constructive stance on improving U.S. economic growth. In addition, any significant delays or the elimination of some of these pro-growth policies could be seen as a longer-term positive for the markets as long as it prevents the Federal Reserve from aggressively removing accommodation from what could have been too much economic stimulus from the Trump policies.

Thank you for listening to the Tortoise Credit Strategies podcast and hopefully you will join us for next week's edition.

Thank you for joining us. And stay tuned for our next cast. Have topics you want covered or other feedback to share? Write us at info@tortoiseinvest.com.

The **Bloomberg Barclays U.S. Corporate Bond Index** measures the investment grade, fixed-rate, taxable corporate bond market. It includes U.S. dollar-denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

The **U.S. Dollar Index (USDX, DXY)** is an index (or measure) of the value of the U.S. dollar relative to a basket of foreign currencies, often referred to as a basket of U.S. trade partners' currencies.