Tortoise QuickTake
Credit Podcast

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

Welcome to the Tortoise credit weekly podcast. I'm Jeff Brothers, senior portfolio manager for Tortoise. We hope that everyone had a great holiday and are well rested because, judging by the start to the new year, it's going to be a wild one. In today's podcast, we wanted to review the events of the past week and share our takeaways from Chairman Powell's dovish comments on Friday.

The year began with a continuation of December's gloomy and volatile markets. Risk assets fell as investors worried about weaker global economic growth, the government shutdown, trade tariffs and the hawkish Federal Reserve. The much weaker-than-expected ISM manufacturing report on Wednesday increased fears that the U.S. economy might be heading towards a recession. The ISM Index fell from 59.3 to 54.1, the largest decline since 2008. The New Orders Index fell 11 points, indicating potential further weakness in capital expenditures. The ISM report also follows news earlier in the week that China's PMI contracted for the first time in two years. Apple added to the pessimism by lowering revenue estimates, acknowledging weakness in China. By Thursday's close, all signals from the debt markets were flashing red. The 10-year Treasury yield fell to a one-year low of 2.54%, investment grade credit spreads climbed to 157 basis points, the highest since June of 2016 and TIPS breakeven inflation rates were down 50 basis points from the October highs. In addition, the market had completely priced out the probability for rate hikes in 2019 and was now looking for the Fed to start cutting rates in 2020.

Friday's news completely flipped the pessimistic sentiment by relieving the financial markets' worst fears on global growth and Fed policy. We may be in the midst of a slowdown in growth, but Friday's employment report sent a strong signal that the economy remains on very solid footing. The U.S. economy added a much better than expected 312,000 new jobs in December and prior months were revised higher by 58,000. Wages continued the gradual upward trend and hit a new cycle high of 3.2%. The unemployment rate actually increased from 3.7% to 3.9%, but for all the right reasons, as the labor participation rate increased to 63.1%. The markets also positively reacted to China's relaxing policy rates and signs that the trade negotiations were inching forward. The biggest positive news, however, came from Chairman Powell's joint interview with Janet Yellen and Ben Bernanke at the American Economic Association meeting. We have several takeaways from the interview. First, the Powell put option on the markets is back. Powell emphasized that the Fed would "remain patient" and "flexible" and that "policy was not on a preset path." Following the December FOMC meeting, Powell appeared tone deaf to the market sell-off and tightening financial conditions. In the Friday interview, he stressed the Fed was "listening" to market signals. A second important takeaway was the Fed's willingness to adjust the balance sheet strategy if necessary. From the December meeting, Powell characterized the balance sheet runoff as on autopilot with the preferred policy adjustment tool being rates. Powell did not believe the balance sheet was the cause of the recent turmoil, but said the Fed would adjust policy should conditions change. Powell also used the interview to reiterate the Fed's independence and stated he would not resign from the Fed even if Trump asked him to step down. A final takeaway is that the Fed has a communications problem. This was the second "do-over" from Powell. Friday's dovish reversal was reminiscent of how Chairman Powell tried to walk back from his comments of rates being a long way from neutral to now just below.

Our general conclusions from the wild first week of the year are first, volatility is here to stay, next - the markets went too far pricing in a potential recession and lastly, the Fed occasionally needs a Mulligan.

Thank you for listening, we will talk to you again next week

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@tortoiseadvisors.com.

The ISM Index is a monthly composite **index**, released by the Institute for Supply Management that is based on surveys of 300 purchasing managers throughout the United States in 20 industries in the manufacturing area.

The ISM Manufacturing Index monitors employment, production, inventories, new orders and supplier deliveries.

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