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 provides a timely update on trending topics in the market.

Welcome to this week's Tortoise credit podcast. I'm John Heitkemper, portfolio manager for high yield bonds and leveraged loans at Tortoise.

It's probably not advisable to divulge too many personal details on a podcast, but I'm going to take a risk this time. In a day and age when we get less and less correspondence by snail mail, I think a highly anticipated delivery can still make your day. For some, this might be a big tax refund check or a certain issue of Sports Illustrated. For me, and here comes the secret, I really look forward to getting my annual Pocket Edition of the *World in Figures* from *The Economist* magazine. I'll pause here so you can make fun of me, but in my defense, its arrival over the weekend turned out to be pretty timely. Right there on page 32, titled "Trading Places", is the reason behind last week's major financial market hiccup. According to The Economist, the U.S. and China together account for nearly a quarter of all global exports. But after last week's tit-for-tat tariff skirmish between the Trump administration and its Chinese counterparts, investors are now rightfully concerned that trade between the two economic powers may be at risk.

In case you missed the details, last Thursday the U.S. announced that it would impose tariffs on $50-$60 billion worth of Chinese exports to the U.S. in an attempt to address our country's $375 billion deficit in traded goods with China, a move that's also viewed as retaliation for supposed Chinese theft of U.S. intellectual property. The announcement comes just a month after the U.S. imposed tariffs on imported steel and aluminum under the guise of national security. In response a day later, the Chinese slapped their own tariffs on $3 billion worth of goods that we ship to China. Now, according to most economists, who literally maxed out my email inbox by the end of the week with research notes, the $50 billion figure is just over 10% of its exports to the U.S., which shouldn't be large enough to harm China's economy and certainly not of a magnitude to impact the global economic expansion. Closer to home, for U.S. consumers, the tariffs on Chinese imports could be modestly inflationary – JP Morgan estimates the impact at a quarter of a percentage point, to the extent producers don't absorb them with a hit to their margins.

But markets are forward looking – or maybe forward panicking in the case of last week – and the important question is what comes next. According to the *Wall Street Journal*, the two countries are already engaged in behind the scenes negotiations to settle this brewing trade spat. If we had to guess, last week's pronouncement from the U.S. will end up being a headline grabbing volley that serves as an initial bargaining position as the two countries hammer out new trade arrangements. If anything is predictable about the Trump administration, it's that they like to make a splash and then attempt to cut a deal.

As the metaphorical sausage gets made, however, we're watching for fallout - whether real or just headline risk - to specific sectors in the U.S. economy. Should a trade war escalate, the industries that appear on paper to be particularly vulnerable include transportation equipment (think airplanes), chemicals, machinery, computer-related products and agricultural goods, namely soybeans. Those industries cut across wide swaths of the U.S. economy, but is China really in a position to go after them? Our gut says that China has much more to lose than gain by targeting products made by the likes of Boeing, Deere or Intel. But that's probably not much comfort if you're the CEO of one of these companies; both management teams and investors detest uncertainty. And despite what the economists' data suggest, there's plenty of uncertainty in this brewing tariff battle.

Speaking of economists, I'd be remiss if I didn't say at least a few words about our new Fed Chair Powell's first FOMC meeting and post-game press conference, which dominated the week's financial news prior to Thursday. As anticipated, the FOMC raised its Fed Funds target by 25 basis points to a range of 1.50-1.75%. More interestingly, the accompanying statement included a new phrase about the strengthening outlook for the U.S. economy, and those infamous dot plots showed the potential for more aggressive rate increases after 2018. While many thought the forecast would climb to four rate hikes in 2018, the median remained at three, leading to a small rally in the short end of the U.S. Treasury curve. In his augural press conference, Powell pointed out that the markets pay too much attention to the dot plots and emphasized that the Phillips curve relationship between low unemployment and higher inflation has weakened. This last comment suggests that as a non-PhD economist, Powell may be less adherent to economic theories and models than his predecessors. A more pragmatic approach to monetary policy might just be in order given the uncertainties around trade that emerged later in the week. In fact, maybe next year's Economist Pocket Edition can include a translation of Presidential tweets to Fed dot plots; I think financial markets would really appreciate that help.

Thanks for listening and please tune in for future Tortoise credit podcasts.

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.