Goldman Sachs Exchanges: The Markets

Are higher rates the new normal?

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Sam Grobart: According to some observers, markets are currently priced for perfection. What factors into that? And perhaps more importantly, what might be missing? This is The Markets.

Hi. I'm Sam Grobart. Today I'm joined by Greg Tuorto, a portfolio manager on the Fundamental Equity team at Goldman Sachs Asset Management. And we're going to talk about that perfection, the latest from the Fed, and the new normal of higher rates.

Greg, thanks so much for joining us today.

Greg Tuorto: Thank you for having me.

Sam Grobart: Greg, let's start with some news that came out just a little bit earlier this week. We got the minutes from the latest Fed meeting. They were a bit more hawkish than maybe some people expected. What's your take on them?

Greg Tuorto: Yeah, I think it's been a challenge for the Fed as there are some slightly more hot readings on the economy, especially retail sales most recently, that they're having to deal with. And I think that as you go back and look at the minutes, and there's some dissension in the ranks in terms of some people think we're not done yet, some people think we are done, it set the stage for a little bit more volatility as we move forward in the rest of the year.

Sam Grobart: I want to talk to you for a minute about bond yields. Long-term yields are at their highest in 14 years. And to quote our colleague Tony Pasquariello, he's asking the question, have we entered a new regime for global interest rates or not? What's your answer?

Greg Tuorto: You know, I think about them more as they relate to the companies that we own in our portfolios. And I don't think that the companies themselves think that they're, you know, in a new regime yet. I do think as a consumer, and looking at interest rates where they are, we're definitely in a new world order as it relates to interest rates and what people are willing to do with their money.

You see a lot more headlines about people being "trapped," quote/unquote, in low-rate mortgages. And what that will mean for mobility in the future. But I think more importantly, as you think about the consumer going forward and some news today about savings rates being completely drawn down, the credit card usage will also be a big thing to watch in the back half of the year because credit card rates will follow that. And they will go significantly higher.

So, watching the consumer is probably more important to kind of see how they feel about this new regime going forward.

Sam Grobart: I'd like to take a step back and take a more macro view of things. We've seen better than expected inflation data alongside stronger earnings. And it now appears that markets have fully bought into the soft-landing narrative. But I'd like to address at least one topic here that may be underestimated, which is China. That country has been undergoing a period of economic downturn and deflation. How are you thinking about that?

Greg Tuorto: Yeah. I think the thing we would worry about is if China starts to do the thing that everybody worries is exporting deflation. And that would be something that you would see in terms of making things in the United States, especially for US-focused companies, significantly less competitive based on a price umbrella that they all started to live with when we had higher inflation 12 months ago. So, I think that's the thing we're worried about primarily.

Secondarily, I do think that China as an engine for growth for the rest of the world, which tends to kind of rise all boats in many situations, may be less apt to be a consumer-based economy than they had been in the past. And I do think that some of the employment stuff out of China is a little bit less positive. Some of the housing stuff is, obviously, less positive. So, it's a wait and see mode.

I do think that they have a lot more levers to pull within their economy than we do. I think they have no choice but to listen to their Fed whereas corporate executives do not listen to our Fed in lockstep like they may have done in 1987. But, you know, it's something you have to watch, especially on the exporting deflation front.

Sam Grobart: You mentioned employment data out China. I just wanted to touch upon a smaller point there. China has decided to stop reporting youth unemployment figures after it reached an all time high of 23.1 percent. What does that mean for markets to be getting less transparent data? Are you concerned about that?

Greg Tuorto: I do think it'll add to the volatility mix, which is something that, you know, I think we'd all like to do without. And I do also think it's a bit more emblematic of the fact that they are trying to change their economy in a lot of ways. Many of the youth employment statistics had been coming from some of the manufacturing economy. Maybe as you get deeper and deeper into the center of the country, some of those things aren't as active as they once were. Consumer electronics is pretty weak. I think semiconductors has changed from a China focus to more of a global focus.

Sam Grobart: There's a geopolitical angle there as well now.

Greg Tuorto: Yeah. So, I do think that there are some things there that if they're not trying to hide them, I think that they are trying to figure out where to reallocate some of these, you know, kind of idle hands.

Sam Grobart: Greg, I want to talk more about what you do on a day-to-day basis. You run the small cap business in Asset Management. What are you seeing in that part of the US market right now?

Greg Tuorto: Yeah, I think it's been interesting because we really kind of take our cue from the earnings reports from the companies we talk to. And we spend a lot of time following up with them. And, you know, I think as I mentioned earlier, it's a wait and see.

So far, the consumer portion of the economy is actually doing quite well. The consumers are spending money at restaurants and at retailers. And that's been a bit better than expected. I also think that in the beginning of the year you had a significant negative tilt towards things like the industrial part of the economy and the technology portion of the economy. And I think that has come full circle.

You know, I think that the people who had been expecting recession for the industrial companies have had to take that off of their watchlist. And technology, and many people had been worried about AI or where was AI going to be a beneficiary to these things, are realizing that it's not as impactful for as many companies as they had seen.

Sam Grobart: Greg, last question, what's going to be on your mind next week?

Greg Tuorto: Hoping to get some quiet time at the end of the summer and go on vacation. It's been a much busier August. And I think it's good in a lot of ways because deal flow has been a bit better. I do think that, you know, activity, travel has continued to be quite strong. And I think that as we look into next week, some more corporate earnings are coming out. I think we're going to start to see some people make some bets on whether there's going to be a September hike from the Fed or not. That rhetoric will definitely be ratcheted up, especially as you mentioned in light of the recent rise in rates. And I also think that, you know, as we kind of head into the end of the summer, that back-to-school season, especially for the markets, tends to be very, very fast and furious. Lots of conferences. Lots of company meetings. So, I think you have a lot more to chew on in terms of realistic results from companies.

Sam Grobart: Greg, thank you so much.

Greg Tuorto: Thank you for having me.

Sam Grobart: That does it for another episode of The Markets. Subscribe to our feed on Apple Podcasts, Spotify, or wherever you get your podcasts.

We'll be back on September 8th. Until then, I'm Sam Grobart. Thanks so much for listening. Have a great rest of August.