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**MADISON MILLS, BLOOMBERG RADIO:**

We want to get another take now on what this actually is going to mean for the markets, thinking about the policy impact here. Libby Cantrill, Managing Director and Head of Public Policy at PIMCO is joining us now. So Libby, for investors, how should they be thinking about the implications of this given it is narrower now?

**LIBBY CANTRILL, PIMCO:**

Yes, well, good afternoon and happy birthday, Kailey.

**KAILEY LEINZ, BLOOMBERG RADIO:**

Thank you.

**CANTRILL:**

I think this is something that's important to contextualize because this is part of a really broader approach that in many ways was started under the Trump administration, which of course includes tariffs, export controls under the Biden administration on semiconductors and likely other technologies that are forthcoming. And then, of course there's a tighter CFIUS investment process as well for inbound capital investments in the United States from China. So again, this is taken in a broader context. And this is one prong of this multi-prong approach. As you have just discussed, this is quite a bit more limited. I think more limited than it was really originally conceived more than a year ago, more like 18 months ago, because this has been iterated by the various folks in the administration. And I think it's really, in some ways, to be viewed as kind of a beta, because as you noted, the U.S. government has never done anything like this. This is very novel. So I think in some ways, this probably represents a part of a broader approach, but also in many ways, I think probably the beginning of this scrutiny on investors and investment capital from the U.S. to China. Now, not everyone's going to be happy with this. So we can talk about the congressional dynamics. Representative Mike Gallagher, the Chairman of the U.S. House Select Committee on China has already previewed his frustration with this more watered-down approach. But again, I think from an investment perspective, this should be viewed as one prong in a multi-pronged approach. And something that's probably going to be, again, more the beginning than the end in terms of more scrutiny on outbound capital going from the U.S. to China.

**MILLS:**

So in terms of this being the beginning and not the end, Libby, is this something that investors should start to be looking at more closely, maybe getting a little bit concerned about, just how big could the reach get here?

**CANTRILL:**

Well, this is something that we're talking to our U.S.-based clients quite a bit. And what we're seeing from a practical perspective is that there has already been, in many ways, some self-sanctioning behavior. I.e. The political risk of investing in China has now increased to such an extent for some clients, for some investors, that they're just simply withdrawing or at least pairing back what kinds of new investments are in the pipeline. And so I would be surprised that even though the policy might be kind of watered down here, if the practical implication for many investors who just, again, don't want to deal with the political headache here, not to mention, of course, that China may be less of a desirable investment target because of their own economic issues that they're dealing with. But they might just start kind of retreating or at least pairing back some investments. So I think we'll see a change in behavior regardless, even though there will be criticism that this has been significantly watered down.

**LEINZ:**

Libby, when we're thinking about the China policy question, how much should we be paying attention truly to the administration? And how much is this actually a matter of Congress, which seems to be a lot more hawkish on the China issue than the White House does?

**CANTRILL:**

I think this is something that we keep saying to our clients, especially as we think about the 2024 election, that the direction of travel on all of this is relatively clear, and I think it's agnostic in terms of who's actually sitting in the White House to some extent, right? They're going to be different degrees and sort of shades here in terms of approach and style. But it's pretty clear that with Congress, as you note, more hawkish and likely leaning in and trying to put more pressure on whoever is sitting in the White House in 2025, that we'll see more of this. Now, practically from a policy perspective, it really is the administration that holds the pen here because even though much of Congress is more hawkish, Congress can't agree on many things. And they haven't been able to really agree on an approach here. We've talked about this before. There was an amendment to the National Defense Authorization Act, the NDAA, that passed the Senate by a very bipartisan basis. I think it was 91 to 6, most recently. But that was just a disclosure based regime in terms of outbound investment. So even that didn't go as far in some ways as what this EO likely is going to do because it didn't have any blocking or prohibition types of provisions. I think it sort of shows you that while there is a lot of rhetoric from Congress, to really legislate on this stuff is still a relatively high bar. So the administration will still matter. But the hawkishness will kind of continue, again, regardless of who's in the White House, come 2025.

**MILLS:**

Well, Libby, I'm curious when you look at a move like this, how it plays into your overall thinking when it comes to Biden's economic scorecard, where are you thinking and how is your thinking changed on how President Biden has handled the economy when you look at a move like this?

**CANTRILL:**

Yeah, I think in some ways, again, as you all noted, this was so well telegraphed. This is not surprising. In some ways, it's a relief to know when we actually see the details of the EO. It will be a relief because we've been talking about this with our clients for a while. I think broadly in terms of the so-called Bidenomics, I think the administration is really leaning into all the very strong economic data, and for good reason, right? Unemployment is very low, inflation is coming down, growth is sort of remaining robust, and the consumer is hanging in there. I think what we've discussed before, however, is that there are some potential headlines on the horizon that make that strategy somewhat risky. We've talked about the resumption of student loan payments. We've talked about banks pulling back on consumer credit, the fact that a lot of folks actually haven't had to pay their last year's tax bill because they live in these emergency zones, and that's coming on October 1st. So I think it's, again, for good reason, if you just look at the economic data, but as a political strategy, it might be a bit risky if the economy actually does slow down because of some of these headwinds, and then he owns it. So he's owned it on the upside, but he might own it on the downside as well. Clearly, I don't think the administration thinks that there will be a recession, and that's why they have so full heartedly leaned into this rhetoric.

**LEINZ:**

Well, Libby, on the subject of the economy, I know we've spoken with you often on this show about how a shutdown wouldn't necessarily have the same dramatic horrible economic ramifications a potential default would, but it also strikes me that especially in the context of the fact that the economy is still strong, Fitch still downgraded the US and stripped it of its AAA rating last week. And in your research that you put out earlier this week, you said that downgrade actually only increases the chances of a government shutdown this fall. Can you explain that reasoning?

**CANTRILL:**

Yeah, it’s somewhat ironic, right? Because one of the reasons why Fitch downgraded the US from AAA to AA plus was citing the political standoff and the dysfunction around some of these big fiscal inflection points. Now, of course, we have a note that Congress did come to an agreement with relatively low volatility and actually before the X dates. In that way they actually overachieved. But still, the point does stand. Of course, we are just getting used to the debt ceiling fights and government shutdowns and what have you. But ironically, as I did point out in our client note, this actually could increase the chances of a government shutdown. The reason is because what we're already seeing is many House Republicans walking away from the spending limits that were agreed to in part of the debt ceiling resolution. As part of that resolution, just as a reminder, spending limits for 2024 and 2025 were agreed to and of course passed and signed into law. Now some House Republicans want to actually cut those spending costs. They want to actually fund the government at about $100 billion less than that. Now this is all kind of eating around the edges because as we've talked about, discretionary spending is only about a quarter of the federal budget. But still, they feel like now, Fitch downgrading the U.S. just hardens that point of view that the U.S. does need to get a fiscal House in order, so to speak. So I think in some ways this just makes it more likely. We already thought it was actually relatively likely for a shutdown to happen this fall. I think this actually just increases the chances because again, it just hardens that stance for some of these fiscal conservatives to not vote for anything, even though, I think arguably they did agree to some of these spending limits as part of the debt ceiling resolution.

**LEINZ:**

So much to look forward to. Libby Cantrill, Managing Director and Head of Public Policy at PIMCO. Thank you very much for joining us.