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**RICK SANTELLI, CNBC:**

I'd like to welcome a special guest on today's important day today and tomorrow, of course, big jobs report. Jerome Schneider, Managing Director of PIMCO. Jerome, welcome and I'm going to start right out, looking at today's data because I disagree with the conventional wisdom out there. All I hear all day is that year over year Core PCE at 4.2% was in line. It might have been in line, but it was one-tenth hotter and the entire year has been above 4.1%. Over half of last year was above 5%, and we haven't been below 4% since September of 2021. Do you think inline’s important or do you think that's awfully sticky looking?

**JEROME SCHNEIDER, PIMCO:**

It's a little sticky looking. In fact, I think we have to caution investors from looking at too much of the minutiae of any one data point, whether it's today's figures with spending an income or tomorrow's figures with jobs. The reality is that the notion of what is inflation is a complex notion. We have the Fed themselves looking at several different indicators favored by the PC indicator, but the one today is actually pushed to be a more subdued level, due to price level indications, which are basically coming off the peak point that we've seen over the past few years. So the goods pricing, the services pricing, those are all moving lower and creating a more, perhaps euphoric marketplace for risk assets. But reality, it's a longer-term equation that's going to have more complex variables, specifically the wage variable that's going to come to play and it's going to create–

**SANTELLI:**

So when we think about the Fed longer term, how much time do they have? I don't think you're going to get this thing under three and a half percent next year, either, do you? Year over year, PCE Core?

**SCHNEIDER:**

Well, one of the things that you have to focus on is that the Fed is perhaps more data dependent, but what they've explicitly stated in the Jackson Hole mission was that inflation is going to remain a focus, which means perhaps in the near term over the next three months, maybe even longer, they’re looking to be less data dependent. So the conquest of inflation is a longer term, frankly, prognostication at this point in time, where you do have some upside propensity for wage pressures to come into the equation as we enter into 2024. That's going to be the outlook as we look at average hourly earnings tomorrow and point at cost indexes, other factors that come into play, despite a very robust economy in terms of growth and growth outlook specifically in this third quarter right now.

**SANTELLI:**

What about the savings rate today, Jerome? Savings rate moved from 4.3% in June to 3.5% in July. That's the lowest savings rate since October of 2022. Is that the nest egg that we see that's been giving some investors and some consumers a little extra horsepower? What do you think about that drop? Is it something to be concerned about?

**SCHNEIDER:**

It's absolutely something to be focused on, not necessarily concerned about at this point in time. It has been the basis of resiliency in risk assets and the market in general. The decrease in income was obviously noteworthy today, but on the flip side, you had the increase in spending, which obviously brings that savings rate down to about 3.5% or so. More specifically though, what it also highlights is that the nest egg; that savings sitting on the sidelines on that private sector balance sheet, the consumers, has been quite robust. And in this outlook, which we remain more conservative at the PIMCO right now, we have to be very mindful of the fact that the private balance sheet, the consumer, is actually in a much healthier spot than what we've seen in other parts of a weakening economy where we're going to be more conservative. Rather, it's the public balance sheets that are basically in focus now.

**SANTELLI:**

Jerome, there's a lot of stories today about a pivoted PIMCO. They're starting to look at mortgages. And one thing I've looked at, if you look at the credit default swaps on investment grade credits, okay? They are at the cheapest levels in 18 months. Year to date on investment grade and year to date on high yield spreads, they've really come in. It's made mortgages look cheap by comparison. Now all of a sudden, everybody seems to be jumping into the mortgage arena. Is this the type of dynamic we should be worried about? Because these spreads are shrinking and investment grade and high yield, they're shrinking on top of treasury rates that are much higher than they were just a few years ago.

**SCHNEIDER:**

It's a key point, Rick. And I think investors should be focused on not necessarily that the spreads are very tight, but the economic outlook which remains more conservative. At PIMCO, we're still thinking that there's at least a possibility of a recession, not a high probability but a possibility. And when you have that environment, you're going to be more conservative with how you're allocating corporate credit. We think agency mortgages are a high quality diversifier to that, that allows you to basically be in the higher income world of the fixed income universe at a lower volatility point that complements your ability to earn the diversified sources of income. So we don't disagree with the fact that corporate bonds, spreads and allocation of corporate bonds is perhaps a slight underweight at this point in time as it has been for the past few quarters, really predicated on a more conservative outlook for the economy. Challenged by increasing funding costs, et cetera.

**SANTELLI:**

Well, we're going to have to leave it there Jerome, but I'll tell you what, with tomorrow's data points, who I’m paying particularly close attention; all the wage components of course, and the notion that on the corporate arena, defaults are up, but investor demand is also up, a very strange brew. Thank you for joining me today.