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**JONATHAN FERRO, BLOOMBERG:**

PIMCO’s Tiffany Wilding, looking ahead to the rest of this year, writing this: “Markets appear priced for a benign economic outcome that would be a historical rarity given current conditions. Higher bond yields offer resilience amid increasing risk to the global economy.” Tiffany, I'm pleased to say, join us now for more. Tiffany, wonderful to catch up with you. It always is. You think both growth and inflation have likely peaked. What are the sources of demand, Tiffany, that you and the team think are fading?

**TIFFANY WILDING, PIMCO:**

Yeah, so this is something that's obviously been discussed quite a bit. But we had just amazingly large transfers from the government sector to the households and businesses for that matter during the pandemic. And that created just a very large positive economic overhang, that I think we're just still working through. So Milton Friedman famously said that “monetary policy works through long and variable lags.” Well, in this case, fiscal policy is also working through long and variable lags. But the thing is, that higher inflation and price levels is eroding the real value of those positive excess overhangs. And we think that they are diminishing. And the resilience that you're seeing in economies, that's set to fade. So we would be careful about over extrapolating that. And we think the markets maybe have. And they're just not pricing in a high enough probability of recession.

**FERRO:**

Tiffany, as you indicated, that positive excess overhang was a consequence of a major fiscal transfer from the sovereign balance sheet over to the consumer. Is that leaving the sovereign balance sheet in a precarious position?

**WILDING:**

Yeah, well, obviously government debt levels are much higher. That's not only in the U.S., that's everywhere. And that's going to impact policy moving forward. And what that's meant to us is just that there's going to be less room and less capacity, less willingness to implement more if in the future as the economy goes into a downturn. And by the way, it's not only the federal government balance sheet or debt that's more elevated now, but of course central banks also have larger balance sheets. And we think there's probably going to be some fatigue there as well. So you're not going to see the type of policy response that we've seen from the past two crises; The Great Financial Crisis as well as The Pandemic. You're just not going to see that in our minds moving forward.

**FERRO:**

So going forward, what do you think is the new reality? What are we going back to, Tiffany?

**WILDING:**

Yeah. So we've discussed for several years now that this new reality that we're moving into is somewhere different from what economists called “The Great Moderation” prior to that. So we think we're just going into a more volatile world. And that's also being exacerbated by the fact that there are just secular transformations that are happening. We've obviously all talked a lot about the transformation towards renewable energy. But there's also transformations that are happening geopolitically as well. And that's just creating a more volatile environment overall. So this is something that we're going to have to deal with, unfortunately, moving forward.

**FERRO:**

The Federal Reserve might have to try and deal with some of these issues as well. For the Fed, Tiffany, what we've heard so far from speaker after speaker is they're comfortable allowing the bond market to do the work for them. Does that mean November's no longer a live meeting for you and the team?

**WILDING:**

Well, I think it's a close call, quite frankly. The data that we've seen more recently has just been stronger. The labor market report obviously was very strong. And the more recent inflation report that we got yesterday just kind of showed the underlying trends, these super core measures that the Federal Reserve is very focused on. They're just not going in the right direction, unfortunately. It's right that the bond market adjustment that we've seen over the last several months is tightening financial conditions. And that is doing the work for the Fed. But I think it's possible that the Fed might just want to take out some insurance and might want to try to lock in some of these additional financial conditions tightening with another rate hike. So we think it's ultimately a very close call at this point. But I think the broader issue here is at what level of rates and financial conditions do we really need here to start to really cool economic activity and ensure that inflation is back to target? I think the bond market and the Fed is still searching for that level.

**FERRO:**

Tiffany, it's interesting you say that because all indications we get from the Federal Reserve are that they believe we are sufficiently restricted. And if we’re not, we're only 25 basis points or something like that away from it. Would you push back against that?

**WILDING:**

I think there's just a lot of uncertainty right now in general. And as I said, there's a lot of economic volatility. The pandemic situation was obviously very unique as was the war in Ukraine for example. And just the traditional economic models are just not set up for that kind of supply shock. So I think there's a lot of uncertainty. We agree monetary policy is restrictive. As I said, we think the probability of recession here is quite elevated. But there's some uncertainty around that obviously. The Federal Reserve is dealing with that uncertainty by treading lightly, by going slowly now that policies in restrictive territory, they're trying to probe for those levels of restriction that bring the economy more into balance. But again, we're not exactly sure where that is. And it's certainly possible that we haven't hit it yet. But on the other side of that, it's possible that we're already there. Monetary policy works through lags. And certainly we could come to a point where the economy is slowing more than Federal Reserve officials expect. And it looks like the policy is too tight.

**FERRO:**

Tiffany, thanks for the update from you and the team. Tiffany Wilding there, out of PIMCO on the latest on the bond market and what we can expect from the Federal Reserve and the US economy.