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**KATIE GREIFELD, BLOOMBERG:**

Well, let's switch from some of these individual stock stories to the Treasury market because you're seeing yields fall, the market overall extending its advance towards the best month since March. And that's continuing after a $16 billion sale of 20-year treasuries posted some solid demand. Joining us now to help break it down is Jerome Schneider. He is PIMCO Managing Director and Head of Short-Term Portfolio Management and Funding. And I know you're a short-term guy. But let's talk about some of these long-end auctions because, again, a strong showing at today's 20-year sale. You reminded me in the break it was just two weeks ago that we had that very sloppy 30-year sale and the narrative there was that there's all this concern about how much treasury supply there is. What changed in two weeks?

**JEROME SCHNEIDER, PIMCO:**

Well, investors are basically focused on two things at this point in time. Number one, they're focused on continuing data and evolution of inflation. And then the second component, which is actually related, is the term premiums in the market. And the second component of that term premium aside from inflation is the supply to come. And so a few weeks back when the 30-year came, it was unsettling because of the notion that they tailed in the auction and that was, quote, indicative of lack of demand for those auctions. But today, we actually saw a good result of those auctions, the 20-year point, which is, again, out the longer end of the curve, came quite through and was very strong. It was a very high grade from our marks, and came through the auction by a little less than a basis point. But it's indicative of the wavering sentiments within the broader marketplace, with regard to how supply is going to come into the market, be reconciled with ongoing inflation expectations or lack thereof. And then ultimately, what is the shape of the curve and how is it derived from that term premium again? So it's a bit circular in nature. And ultimately, this is not something that the market is going to react to in any one data point, and nor should we suggest that. But overall, look to the recalibration to come with a growing supply that the treasury has announced in addition to the evolving inflation dynamics to come. Those two things are really most important other than just simply one bespoke print within an auction as we saw today.

**GREIFELD:**

So Jerome, that's the picture at the long end. It's a fairly turbulent one, but let's take it to the very front end of the treasury curve, because there's also been an increase when we think about some of those bill sales as well. How has that been received by the marketplace, that increased supply?

**SCHNEIDER:**

Quite well. In fact, we've seen that supply really get digested as a replacement for the high number of assets that were in the Federal Reserve's reverse repo facility. Right now, that reverse repo facility is about $1 trillion. It came down from about $2.5 trillion, and really was suppressed by moving from that reverse repo facility into bills. Not a lot of friction. In fact, bills have outperformed in the microcosm of late, but I think what's more important, Katie, is to take a moment here. And in fact, tomorrow has a bit of a menu to be presented by the Federal Reserve with an upcoming Minutes. And really what we're going to be focused on on the front end is the evolving situation with regard to how the Fed is determining the next steps. In fact, hopefully what we're trying to glean from the Fed Minutes tomorrow is the fact that what was it that changed their course to going from expecting another rate hike in the September dot plots to perhaps putting it on hold. And in fact, that's what is going to be driving front end rates in the near term. And effectively, if the Fed is on hold and what the Fed foresees is going to be sort of a recalibration, was it tightening financial conditions, was it an outlook for inflation, how does that reconcile? And ultimately, it's going to be something which might or may not portend to the very dovish outlook for the market at this point in the form of rate cuts in 2024.

**ROMAINE BOSTICK, BLOOMBERG:**

I'm curious as to how hard it's going to be to get a read on that, Jerome, because we talk about this idea of how data dependent the Fed was. And we saw the market really trying to front-run the Fed with every economic news release. And Jay Powell and quite a few others, including Neel Kashkari, have kind of made it clear that they're to a certain extent operating from the gut at this stage of the cycle.

**SCHNEIDER:**

Well, what's interesting, and you're exactly right, Romaine, what we basically learned from the last Fed press conference, was that the Fed shifted from a data dependent mode to one of relying upon tightening financial conditions. Oddly and perhaps unsettlingly to the Fed, those financial conditions have actually eased through the form of lowering rates and tightening credit spreads as well as equity markets that are rallying. And so what they relied upon to sort of give themselves a pause and not necessarily suggest future rate hikes has actually reversed itself in the near term. And so we might actually find that we might hope for inclinations that the Fed is still open-minded to some data dependency on a go-all-forward basis. And more importantly, understand that the market's calculus of a dovish-reaction function in the near term, specifically in the second and third quarter of next year, where the Fed rate cuts are priced in, might actually be a little bit more aggressive than actually the Fed wants at this point in time. So reading the tea leaves, reading between the lines is going to be remarkably important in the Fed minutes tomorrow. And then on a go-forward basis, clearly the inflation discussion is ongoing. Here at PIMCO, we think we should be focused on those wage pressures that will continue to be a little bit more persistent on a go-forward basis than most expect.

**BOSTICK:**

This raises the question, Jerome, about heading into 2024 and whether we kind of see a repeat of investor sentiment and investor positioning that we saw in 2023. What changes that, if at all?

**SCHNEIDER:**

The calculus has changed. I think a few things have ultimately changed. Number one, the cost of capital is higher. That's the main purpose of the calculus changing. The second one is, I think, from a practical perspective, the liquidity conditions were relatively benign in 2023. The outlook for 2024 might be a little bit more unsettled perhaps. And I think part of that comes to do with the fact that we have a decreasing amount of excess dollar reserves in the marketplace. We're currently at $3 trillion of excess reserves. And as that declines, we might find that there's a more competitive nature to finding dollar liquidity along the way. And that can be reflected through asset prices, risk premiums, et cetera. And so as a result, the outlook, which was clearly focused on a rising rate environment, but ultimately proved to be a hardy risk-taking environment in 2023, might be a little bit more unsettled for 2024, hence warranting the defensive posture that we have here at PIMCO for the outlook at this point in time. Again, not suggesting a hard landing, but suggesting that the probabilities of recession are a bit higher than the market's expecting at this point in time as portrayed by the calculus of the soft landing discussion. So it's something that we continue to need to reconcile, and perhaps investors need to be thinking about how to be more practical about being defensive. Clearly the front of the yield curve is attractive from those rate perspectives, but we could be in a situation of higher rates longer than the market expects at this point in time.

**GREIFELD:**

Well, Jerome, 30 seconds. You mentioned the very front end of the yield curve, you take a look at money market funds, $5.7 trillion, it seems like nothing has been able to stop that flood of cash. When does it finally maybe start to cool off a little bit, that demand?

**SCHNEIDER:**

Well, that demand has actually become very robust simply because of the risk-off uncertainty outlook. And what we were basically suggesting is investors look at the totality of fixed income within that zero to five-year space, the front end of the yield curve, for a little bit of safety, understand that there could be a little bit more recalibration in the term premiums in the long run. But in general, that fixed income opportunity remains a highly competitive, more important income-producing opportunity as we approach 2024.

**GREIFELD:**

All right, Jerome. It's great to catch up with you. That is Jerome Schneider, of course, of PIMCO. Thank you so much.