**MEDIA: Television**

**STATION: Bloomberg**

**MARKET: National**

**DATE: 2023-12-18**

**TIME: 10:14 AM ET**

**PROGRAM: Bloomberg Markets**

**SUBJECT: Erin Browne - Asset Allocation**

**PAGE COUNT: 4**

**ALIX STEEL, BLOOMBERG:**

Which brings us to the question of the day; is all of this just too good to be true? Is this a peak “Goldilocks scenario"? I want to bring in Erin Browne, PIMCO Portfolio Manager for Multi-Asset Strategies. Okay, we've had a few days as I adjust this, too good to be true?

**ERIN BROWNE, PIMCO:**

I don't think it's too good to be true. We've seen about 125 basis points of financial conditions easing, one of the largest bond market rallies since January of last year about 35 basis points. So the market right now is certainly pricing in a more dovish outcome, but when you look under the surface, there's still certain segments of the equity market like cyclicals, which are really dislocated from this sort of peak optimism. So I don't think it's too good to be true. I do think it's certainly going to be tougher gains ahead. It's not going to be a straight line, but I do think ultimately the significant financial easing that we've seen, is really going to be impactful for equity markets and for risk markets more broadly.

**GUY JOHNSON, BLOOMBERG:**

Too impactful? There is a danger, Erin, that this becomes a positive feedback loop that starts to affect consumption. The economy doesn't actually end up having a significant slow down financial conditions, basically are too loose. As a result of which we're back to where we started, inflation becoming a problem once again. How do we, how do we thread that needle with equity markets looking good, bond markets looking good, but not too good?

**BROWNE:**

So I think that's a really good point, and I do think that ultimately that does lead the Fed to likely hike later than what the market's currently pricing. I don't think that will likely see the optimism that the market's priced it in on the very front end of the fixed income curve. But I do think that once the Fed does start hiking, they'll likely hike for longer and perhaps even faster than what the market's currently pricing. And so it's going to be a longer tail, but maybe more delayed start.

**STEEL:**

So then when it comes to those cuts, is it because they're normalizing or because they're actually easing? Because that's going to really make a difference on how to put that money to work in that environment.

**BROWNE:**

I think that's the key question, and I do think it's because they're normalizing. Rates are still quite restrictive and with inflation coming down, they're even more restrictive and will likely be quite restrictive even towards the tail end of next year. And so I think that what the Fed will ultimately do is normalize rates back into more neutral territory over the course of the next 12 months to 24 months, but they're not going loose in terms of monetary policy. They're just normalizing rates back down to some of the hikes that they put in due to the very excessive inflation that we've experienced over the last three years or so post-pandemic.

**JOHNSON:**

Erin, I'm sitting in cash right now. I'm wondering what to do. I'm trying to decide which assets I want to be buying, if I am going to be pulled out of my money market. Where do I go? What do I look for at the moment? 10 years at 4%, do I buy it at 4% or do I wait potentially for a bounce back to 4.5? Do I buy a dip in the equity market? What do you think? I'm just wanting all those people out there with all that money. What's the strategy? What do you think is going to be the way to play this?

**BROWNE:**

So it's interesting you asked that question because that's probably the number one question that we're getting from investors right now, is when do I move out of cash? Certainly cash has been a really great safe haven over the last couple of years and continues to be so. But I think what's important is when we've looked historically at when you want to move out of cash and into the longer duration assets, typically that point is when you're at peak rates ahead of the Fed rate cutting cycle and we're at that point now. So I think as you move into 2024, it's going to be key for investors to start moving that cash out of cash into longer duration assets, locking in some of those very high rates which you’ll likely not see in six months, 12 months time and now is really the time to do it. Also when you look at fixed income, the return that you can get from fixed income that's guaranteed or nearly guaranteed is very high on a historical basis relative to equities. So I do think you want to be overweight, longer data fixed income in your portfolio, not ignore equities but center your bets within equities really on the US market as opposed to international, EM or even developed market international.

**STEEL:**

So how much of that money then does it belong to US equities? And I guess, where? Because you look at small caps, ripping higher. You're also seeing more and more of the small caps stocks above that 15 day moving average. Like that rally is truly broadening. It's not just the “Magnificent Seven”.

**BROWNE:**

Yeah, and I'm a little bit cautious still on the small cap index. I think that the point of when you want to start getting long the small caps is when the Fed actually starts cutting, not in advance of that. And I still think that right now the small caps are probably moving in excess of what they really ought to. There's still a number of those companies which are negative cash flow, negative earning companies which concerns me in an environment where rates are quite restrictive. Within the US, I think large caps are the key as we move into next year, starting to buy some of the machinery industrial names that are leveraged particularly to the CHIPS Act, to the IJ, the Biden Inflation Reduction Act, and some of the other infrastructure build outs still staying away from the negative cash flow companies like the small caps.

**JOHNSON:**

The market though over the last few days, Erin, has been in a full “dash for trash” mode. High yields have done really well. Small caps at Alix’s point have done really well. Those are the kinds of trades that have been performed. Non-profitable tech has had a great run. How much do you think is left in the tank in those kinds of trades? And is there any interest in those kinds of assets in your portfolio?

**BROWNE:**

No, not in sort of the “dash for trash” names. There is, you know, not. I still think that just given the restrictiveness of rate as we move into 2024, that's going to start to really bite as companies try to refinance their debt. They just are not going to have the capacity to do so to reinvest in their businesses. And so I am concerned, not of a significant default wave, but those companies really having challenges next year, just given some of the lagged effects of the restrictiveness of rates. Remember that January tends to be a reversal month. And so I do think as we move into January, I do think that you're going to see a retracement in some of those names that have materially outperformed this year which, in my view, don't have real fundamental underpinnings for that outperformance. So that would be sort of the pivot that I would be expecting sometime in January with these sort of junkier credits or junkier names. But I do think that those names, you know, even looking at names that are highly leveraged and that have high leverage to, you know, consumer debt like the auto names, I think are going to come under pressure next year as we sort of enter an environment where rates are going to start to bite and refinancing is going to become increasingly more challenging before the Fed actually starts cutting rates.

**JOHNSON:**

It does seem to be a familiar theme, doesn't it, over the last few years, we come into the end of the year, everybody's very exuberant, you get into January, a little bit of a check on that. Erin, have a great holiday. Thank you very much indeed. Erin Browne, PIMCO Portfolio Manager for Multi-Assets Strategies.