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**JOUMANNA BERCETCHE, CNBC:**

Well, 2024 is likely to be the year of U.S. stagflation, according to PIMCO's cyclical outlook report with the country aligning with other developed markets as the economic drag from higher borrowing costs builds. Now, PIMCO says that although central banks have likely finished their hiking cycles, global recession risk remains elevated. Happy to say that Nicola Mai, the Executive Vice President and Portfolio Manager from PIMCO, joins us on the show this morning to talk through the report. Nicola, the commentary that I've read from your research report, your latest update, echoes similar negative bearish sentiment that we had from the World Bank earlier this week. My colleague, Sylvia, on the show this morning, spoke to the World Bank. And I thought it was interesting that for the 3rd year in a row, they have downgraded their expectations or see slower growth prospects for the world, not just individual economies, but globally. And where is this bearishness coming from?

**NICOLA MAI, PIMCO:**

Yeah, thank you so much and good morning. I think we need to recognize, first of all, that the global economy has been very resilient so far, driven by a very strong U.S. consumer. But we do think that this resilience will not last. And the reasons are mainly two. The first one is that we've had a big fiscal sugar rush in 2023 with the U.S. budget deficit widening and with excess savings from the pandemic checks, still sloshing around the system, that's been supporting activity. And secondly, the pass-through of monetary policy has been fairly slow, partly given the long debt maturities in the U.S. think about mortgages, which are 30 years on average. Now, as we look to 2024, I think these effects will change. First of all, fiscal policy looks set to turn contractionary across the globe. In the U.S. The fiscal expansion we had is not expected to continue this year. Secondly, the excess savings, so those pandemic checks that are sloshing around the system will go down in real terms as inflation is eroding the real value of this savings. So that boosts from legacy fiscal policy, legacy fiscal stimulus will also fade. And also, the more time goes by, the more the monetary drag from higher rates will, you know, will bite. And, you know, in Europe, we're seeing a quicker pass-through of monetary policy and we're seeing lesser fiscal stimulus than in the U.S. and you're already seeing a weak economy. And I think looking forward, the U.S. will look more European in our view.

**BERCETCHE:**

So interesting. So reading between the lines of what you're saying, fiscal policy is still in the driving seat, but let's turn to monetary policy and financial conditions because this is a year where most of the central banks are expected to start cutting rates. And markets, obviously, are running ahead of them. But if we do see the beginning of a sustained rate-cutting cycle from the likes of the Fed, ECB, Bank of England, and others, what would that do to financial conditions and then invariably to growth prospects?

**MAI:**

Yeah, I mean, that's a good question. I think the focus is squarely on rate cuts here. I think central banks have reached the peak. We're seeing pretty meaningful disinflation. But I think the markets may have got a little bit ahead of themselves when it comes to rate-cut expectations for 2024. The markets are pricing 140 basis points of cuts by the Fed and the ECB, about 120 for the Bank of England. With rate cuts starting early this year, now, I think that may be a little bit optimistic in the sense that central banks still see high wage inflation. And certainly, central banks that are focused on not being the Arthur Burns, you know, Arthur Burns, making the mistake that Arthur Burns made in the past of easing policy too quickly before beating inflation. So I think actual rate cuts will happen this year, but they could be a little less than the market is anticipating. So you could have a little less monetary support to the global economy than the market anticipates. Now, as you look beyond 2024, actually, I think there is potential for rates to fall more than the market is anticipating. I think about 2025 and beyond. You know, if you look at previous cutting cycles, generally speaking, markets tend to underestimate the depth of the cutting cycles. And we still think that equilibrium rates are low. And so we're cautious on rate cuts for 2024, but we do see meaningful cuts in the cycle as a whole, which is why we tend to like medium-term bonds here, the belly of the curve.

**SILVIA AMARO, CNBC:**

It's Sylvia, joining the conversation here. I would like to ask you about the different speeds of central banks, because one line in your report suggested that while central banks so far have been pretty much synchronized in raising rates, going ahead, their paths could be a little bit more differentiated. So I was just wondering, how is that likely to play in the bond market? How is that likely to affect the different geographies?

**MAI:**

Yeah, I mean, I think there's going to be quite a bit of differentiation. I mean, first of all, going in the opposite direction is going to be the Bank of Japan that, in our mind, will probably raise interest rates. You know, obviously, they haven't hiked so far, but I think the higher inflation trend, weight trend, should support interest rate hikes going forward. Now, when it comes to the major developed market central banks, I think actually there is potentially room for differentiation here with Europe being weaker than the US and seeing potentially a quicker or a deeper cutting cycle going forward. And in that regard, I would actually mention the UK. I mean, if you look at the interest rate forwards in the front end of the curve, you can see that the rate expectations for the UK and the US are pretty much aligned for the next few years, but the UK economy is a lot weaker than the US. And also, arguably, the equilibrium rate in the UK is lower, given lower growth potential. So there could be opportunities, for example, in the UK bond space here.

**AMARO:**

I would also like to draw your attention to the US market more specifically, because one of the main themes for this year is naturally the upcoming US election. So I was just wondering whether you could talk about the fact that we might see a Republican candidate winning the election. What could that mean for US treasuries?

**MAI:**

I mean, first of all, it's too hard to speculate at this point. Who will win this election? You know, I think at this point, the key points to watch will be fiscal policies, so how the different parties will approach fiscal and foreign relations as well will have an impact. So we're obviously very focused on the US election. We'll be watching it closely, but at this point, I think it's too early to speculate on implications.

**BERCETCHE:**

Nicola, we're going to leave it there. Thank you so much for joining us today on the show, fascinating to hear your perspectives on how you think this year is going to play out. Nicola Mai, Executive Vice President, Portfolio Manager from PIMCO.