Commentary
Cash

August 2020

Monthly Cash Review

The Federal Open Market Committee (FOMC) extended the expiration of liquidity programs and left rates unchanged. Although this came as no surprise, knowledge that FOMC programs remain in place boost sentiment should the markets go awry.

The FOMC left rates unchanged at their July 29th meeting, surprising no one. They extended the expiration of the various liquidity programs, including the corporate credit facilities and the money market facilities, although at this point the market is far from needing this type of support. Nonetheless, the knowledge that the programs are in place should things go awry provides a boost in sentiment.

US gross domestic product recorded the largest decline since the 1940's, -32.9%, highlighting the ongoing impact of Covid-19.

The US Treasury announced their quarterly refunding (how much debt they will issue at each of their auctions). As expected the Treasury increased the size of all note auctions (2-, 3-, 5-, 7- and 10-year), bond auctions (20- and 30-year), inflation note auctions (TIPS) and floating rate debt auctions (2-year). The bill auction (1-, 2-, 3-, 6-month and 1-year) sizes remained steady through the month but are lower from the extraordinary sizes we saw in April, May and June. It is expected that Treasury bill issuance could increase once the second Covid-19 relief package is approved coupled with anticipation of the seasonal need we often see in the fourth quarter. Bill yields held steady over the course of the month.

Consumer Price Index (CPI) data for July came in at 1.6% ex-Food and Energy and 1% for headline, which was higher than expectations. Core Personal Consumption Expenditures (PCE) came in at 1.25% and remains under the 2% target the Federal Reserve (Fed) is looking for. Fed Chairman Powell's speech at the Jackson Hole Symposium outlined how the Fed's monetary policy framework would be updated including how the Fed will now be targeting an average inflation rate of 2% over time, thus allowing inflation to run over 2% at times. He highlighted four key economic developments that motivated the update:

- First, the potential, or longer run, growth rate of the economy has declined. Some slowing could be expected as our population growth slows and ages, but more troubling is productivity growth which is the primary driver of improved living standards.

- Second, the general level of interest rates has fallen both in the US and globally. Estimates of the neutral Fed funds rate have fallen substantially. This rate is not affected by the monetary policy rate but driven by fundamental factors in the economy. The median estimate from FOMC participants of the neutral Fed funds rate has fallen from 4.25% in 2012 to 2.5% today. This has profound implications for monetary policy as the Fed has less room to cut rates to stimulate growth and maintain price stability.

- Third, the record-long expansion that ended earlier this year led to the best labor market seen in some time. Labor force participation was increasingly undoing what some had thought was permanent damage to the labor market. Moreover, the gains were felt across demographics, including job gains among Black and Hispanic populations. Chairman Powell highlighted the benefit of these gains to families and communities.

- Fourth, these record gains in employment did not trigger a significant rise in inflation. As the unemployment rate moved below the neutral rate — which in 2010 was 5.5% — Fed officials expected a rise in inflation. However, after inflation remained subdued, officials revised their estimate lower and at present it stands at 4.1%, ultimately contributing to lower inflation outcomes. Chairman Powell noted that global disinflationary pressures could also be accountable for low levels of inflation as the labor market tightened.

Chairman Powell went on to explain why these low levels of inflation could be problematic for an economy. Because expected inflation leads to general levels of interest rates and lower expectations, the Fed has limited ability to lower interest rates in order to promote growth and boost employment. Furthermore, lower inflation expectation or deflation can create lasting damage on an economy. The Fed's new statement explicitly acknowledges the challenges posed by the proximity of interest rates to the effective lower bound (0.00%). To counter these risks, they are prepared to use their full range of tools to support the economy. This appears to be highlighting the fact the Fed will use various forms of quantitative easing on a perpetual basis.

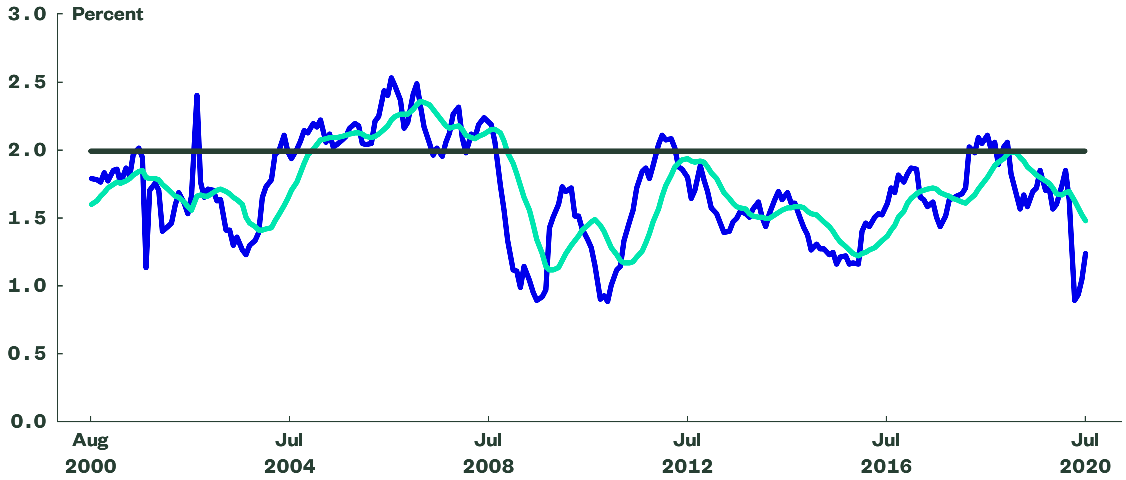
The Fed expressed that maximum employment is a broad based and an inclusive goal, noting their appreciation of a strong labor market in many low- and moderate-income communities. They will be informed by the shortfalls of employment from its maximum level rather than deviations from its maximum level. Such a change should reflect a robust job market can be sustained without causing an outbreak in inflation.

Importantly, Chairman Powell notes they are not tying themselves to a specific inflation average. Their approach is viewed as a flexible form of average inflation targeting with plenty of room to maneuver.

With this new understanding of the Fed's Monetary Policy framework, it would be easy to expect interest rates to remain at the lower bound for considerably longer than they had through the economic recovery period of 2008 to 2015. Over the last 20 years, Core PCE has averaged 1.73%. As noted by the FOMC, demographic trends are in place in the US, across developed markets as well as the move towards globalized economies. And while our current administration can try to stop the trend, it appears to be too late and would be hard to imagine Core PCE rising above 2% for a prolonged period of time long enough to warrant a FOMC rate hike. Therefore it could be expected that the FOMC will not raise their target rate range above zero for a decade or more.

Figure 1
Personal Consumption Expenditures — 20 years

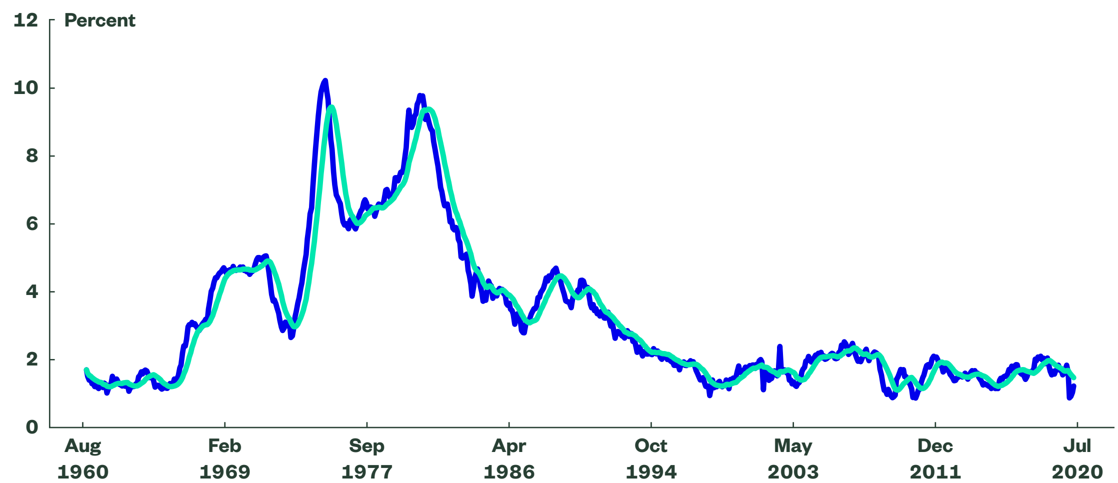
PCE Core YOY %
1 Year Average



Source: Bureau of Labor Statistics, Bloomberg as of August 31 2020.

Figure 2
Personal Consumption Expenditures — 60 years

PCE Core YOY %
1 Year Average



Source: Bureau of Labor Statistics, Bloomberg as of August 31 2020.

About State Street Global Advisors

Our clients are the world's governments, institutions and financial advisors. To help them achieve their financial goals we live our guiding principles each and every day:

Start with rigor We take a highly disciplined and risk-aware approach built on exhaustive research, careful analysis and market-tested experience to meet client needs. Rigor is behind every decision we make.

Build from breadth Today's investment problems demand a breadth of capabilities. We build from a universe of active and index strategies to create cost-effective solutions.

Invest as stewards We help our portfolio companies see that what is fair for people and sustain-able for the planet can deliver long-term performance. As fiduciaries, we believe good stewardship is good investing.

Invent the future We created the first ETF in the US and are pioneers in index, active, and ESG investing. Using data, insights and investment skill, we are always inventing new ways to invest.

For four decades, these principles have helped us be the quiet power in a tumultuous investing world. Helping millions of people secure their financial futures. This takes each of our employees in 28 offices around the world, and a firm-wide conviction that we can always do it better. As a result, we are the world's third-largest asset manager with US $3.05 trillion* under our care..

* This figure is presented as of June 30, 2020 and includes approximately $69.52 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.

ssga.com

State Street Global Advisors Worldwide Entities

Abu Dhabi: State Street Global Advisors Limited, ADGM Branch, Al Khatem Tower, Suite 42801, Level 28, ADGM Square, Al Maryah Island, P.O Box 76404, Abu Dhabi, United Arab Emirates. Regulated by the ADGM Financial Services Regulatory Authority. T: +971 2 245 9000. **Australia:** State Street Global Advisors, Australia, Limited (ABN 42 003 914 225) is the holder of an Australian Financial Services License (AFSL Number 238276). Registered office: Level 14, 420 George Street, Sydney, NSW 2000, Australia. T: +612 9240-7600. F: +612 9240-7611. **Belgium:** State Street Global Advisors Belgium, Chaussée de La Hulpe 120, 1000 Brussels, Belgium. T: 32 2 663 2036. F: 32 2 672 2077. SSGA Belgium is a branch office of State Street Global Advisors Ireland Limited. State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. **Canada:** State Street Global Advisors, Ltd., 1981 McGill College Avenue, Suite 500 , Montreal, Qc, H3A 3A8, T: +514 282 2400 and 30 Adelaide Street East Suite 800, Toronto, Ontario M5C 3G6. T: +647 775 5900. **France:** State Street Global Advisors Ireland Limited, Paris branch is a branch of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. State Street Global Advisors Ireland Limited, Paris Branch, is registered in France with company number RCS Nanterre 832 734 602 and whose office is at Immeuble Défense Plaza, 23-25 rue Delarivière-Lefoullon, 92064 Paris La Défense Cedex, France. T: (+33) 1 44 45 40 00. F: (+33) 1 44 45 41 92. **Germany:** State Street Global Advisors GmbH, Brienner Strasse 59, D-80333 Munich. Authorised and regulated by the Bundesanstalt für Finanzdienstleistungsaufsicht ("BaFin"). Registered with the Register of Commerce Munich HRB 121381. T: +49 (0)89-55878-400. F: +49 (0)89-55878-440. **Hong Kong:** State Street Global Advisors Asia Limited, 68/F, Two International Finance Centre, 8 Finance Street, Central, Hong Kong. T: +852 2103-0288. F: +852 2103-0200. **Ireland:** State Street Global Advisors Ireland Limited is regulated by the Central Bank of Ireland. Registered office address 78 Sir John Rogerson's Quay, Dublin 2. Registered Number: 145221. T: +353 (0)1 776 3000. F: +353 (0)1 776 3300. **Italy:** State Street Global Advisors Ireland Limited, Milan Branch (Sede Secondaria di Milano) is a branch of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. State Street Global Advisors Ireland Limited, Milan Branch (Sede Secondaria di Milano), is registered in Italy with company number 10495250960 - R.E.A. 2535585 and VAT number 10495250960 and whose office is at Via Ferrante Aporti, 10 - 20125 Milano, Italy. T: +39 02 32066 100. F: +39 02 32066 155. **Japan:** State Street Global Advisors (Japan) Co., Ltd., Toranomon Hills Mori Tower 25F 1-23-1 Toranomon, Minato-ku, Tokyo 105-6325 Japan. T: +81-3-4530-7380. Financial Instruments Business Operator, Kanto Local Financial Bureau (Kinsho #345), Membership: Japan Investment Advisers Association, The Investment Trust Association, Japan, Japan Securities Dealers' Association. **Netherlands:** State Street Global Advisors Netherlands, Apollo Building, 7th floor Herikerbergweg 29 1101 CN Amsterdam, Netherlands. Telephone: 31 20 7181701. SSGA Netherlands is a branch office of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. **Singapore:** State Street Global Advisors Singapore Limited, 168, Robinson Road, #33-01 Capital Tower, Singapore 068912 (Company Reg. No: 200002719D, regulated by the Monetary Authority of Singapore). T: +65 6826-7555. F: +65 6826-7501. **Switzerland:** State Street Global Advisors AG, Beethovenstr. 19, CH-8027 Zurich. Authorised and regulated by the Eidgenössische Finanzmarktaufsicht ("FINMA"). Registered with the Register of Commerce Zurich CHE-105.078.458. T: +41 (0)44 245 70 00. F: +41 (0)44 245 70 16. **United Kingdom:** State Street Global Advisors Limited. Authorised and regulated by the Financial Conduct Authority. Registered in England. Registered No. 2509928. VAT No. 5776591 81. Registered office: 20 Churchill Place, Canary Wharf, London, E14 5HJ. T: 020 3395 6000. F: 020 3395 6350. **United States:** State Street Global Advisors, One Iron Street, Boston, MA 02210-1641. T: +1 617 786 3000.

Important Information

Investing involves risk including the risk of loss of principal.

The whole or any part of this work may not be reproduced, copied or transmitted or any of its contents disclosed to third parties without SSGA's express written consent.

The information provided does not constitute investment advice and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It does not take into account any investor's particular investment objectives, strategies, tax status or investment horizon. You should consult your tax and financial advisor. All material has been obtained from sources believed to be reliable. There is no representation or warranty as to the accuracy of the information and State Street shall have no liability for decisions based on such information.

ID293475-3230014.1.1.GBL.RTL 0920
Exp. Date: 09/30/2021