Commentary
Cash

October 2021

Monthly Cash Review
State Street GBP Liquidity LVNAV Fund

There was no Bank of England Monetary Policy Committee (MPC) meeting in October, but market rate hike expectations spiraled. CPI inflation dipped from a nine-year high in September and the benchmark 10-year Gilt yield continued to trade above 100 basis points throughout October.

Policy

With no Bank of England (BoE) monetary policy committee (MPC) meeting in October, all policy settings remained unchanged with the bank rate at 0.10% and the stock of quantitative easing at £895 billion. Market expectations for rate hikes, however, spiraled upwards with the meeting on 4 November becoming live for a first hike of at least 0.15%.

Outlook

The September MPC meeting placed more weight on the mounting upside risks to inflation, which seemingly did not change in October — as a result, several MPC members became more hawkish around inflation and yields. The aggressive upward re-pricing of the sterling yield curve was in relation to these comments. BoE chief economist Huw Pill said, “the current strength of inflation looks set to prove more long lasting than originally anticipated” and that the “November meeting was live”. Michael Saunders said, “it is appropriate that the markets have moved to pricing in a significantly earlier path of tightening” and Governor Andrew Bailey commented that the BoE needed to act. All of these contributed to a strengthened case for earlier action. At the end of October, markets were pricing for a potential base rate of 50 basis points by the end of the year and a policy rate of 100 basis points by June 2022. Although rate action by the BoE looks a certainty this year, many economists think the market has gone too far in terms of the number of hikes now priced in before the end of 2022 and that the BoE could send a message in November to push back on this outlook.

Data

The latest data saw a 0.2% month-on-month fall in retail sales volumes in September (consensus 0.5%). Retail sales volumes have now fallen for six months in a row, marking the longest period of consecutive monthly falls since the series began in February 1996. The dip in CPI inflation from 3.2% in August to 3.1% in September (versus consensus expectations of 3.2%) still left inflation above the 3.0% rate the BoE forecast back in August. Core inflation dropped from 3.1% to 2.9%. The distortions from the furlough scheme and the change in the composition of employment that have boosted average earnings growth have now started to ease. The three-month year-on-year rate fell from 8.3% in July to 7.3% in August. The Office of National Statistics said that, excluding those distortions, underlying wage growth accelerated from a range of 3.6%-to-5.1% in July to 4.1%-to-5.6%. The unemployment rate edged down to 4.5% in the three months to August from 4.6% in the May-July period, as expected by economists in a Reuters poll. That’s the lowest rate since the peak of 5.2% last December. The services PMI registered 58.0 for October from 55.4 in September and the manufacturing PMI for October improved to 57.8 from 57.7 prior, leaving the composite PMI for October at 56.8 versus 54.9 in the prior month — readings above 50 are indicative of expanding activity.

Markets

With market rate hike expectations moving higher and the 4 November meeting date edging closer, issuers had little choice but to increase short-term yields to price for a potential rate hike in November. There was still a large gap between longer-end rates that priced for a series of rate hikes and the shorter-end rates (sub three-month), but the increase away from overnight levels was welcomed. This saw the yield curve move to: overnight 0.05%; one-month 0.10%+; three-month 0.20%+; six-month 0.45%+; and 12-month 0.70%+. GBP LIBOR also continued to see a marked increase across the curve, moving to new highs in October: one-month 0.14%; three-month 0.25%; six-month 0.48%; and 12-month 0.85%. UK Treasury Bill weekly auctions saw yields remain low at around 0.01/0.02% across the one and three-month tenors, but the six-month issue traded close to and above 0.30% in the final two auctions of the month. Outside the money market space, the benchmark 10-year Gilt yield traded above 100 basis points throughout the month, hitting a high of 120 basis points on 21 October.

Fund

At the fund level, the weighted average maturity (WAM) maintained an average high 40-day and low 50-day level during October. Investments were mainly added into shorter dated investments due to WAM constraints and now that value could be found in investing close to the November meeting date with the curve having moved higher over this period. High majority of investments were kept overnight to support liquidity ratios. Liquidity requirements were exceeded throughout and well in excess of minimum requirements. Fund liquidity was covered with a combination of government and supranational holdings, gilt repo and bank deposits. The fund always maintains the highest credit quality.

Source: SSGA/Bloomberg, 31 October 2021.
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* Pensions & Investments Research Center, as of December 31, 2020.
† This figure is presented as of September 30, 2021 and includes approximately $59.84 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.

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