

Central Banks Cautious Amid Rising COVID-19 Cases

LIQUIDITY | GLOBAL LIQUIDITY TEAM | INVESTMENT INSIGHT | OCTOBER 2020

Federal Reserve Board¹

As expected, the Federal Open Market Committee (FOMC) kept the target range for the federal funds rate unchanged at 0.00% to 0.25% at the conclusion of its November 5th meeting. The press release was relatively in line with prior months.

European Central Bank¹

At the European Central Bank's (ECB) policy meeting on October 29th, President Lagarde and the policy committee kept the ECB deposit rate unchanged at -0.50%, as expected. While the committee kept the total size of the Pandemic Emergency Purchase Program at €1.35 trillion and left the Asset Purchase Program unchanged, it implied further stimulus measures were likely. In response to national lockdowns and economic risks, the release noted, "the Governing Council will recalibrate its instruments, as appropriate, to respond to the unfolding situation and to ensure that financing conditions remain favorable to support the economic recovery and counteract the negative impact of the pandemic on the projected inflation path." While no changes were made to monetary policy in October, investors will be paying close attention for any new policy announcements during the next ECB meeting on December 10th.

Bank of England¹

The Bank of England Monetary Policy Committee (MPC) voted unanimously to maintain the Bank Rate at 0.10% at its November 5th meeting. The MPC also voted unanimously at its meeting to increase its target purchase of U.K. government bonds by an additional £150 billion, bringing the

total to £875 billion. Economic forecasts have been cut as England entered into a full four-week lockdown in an attempt to reduce the spread of COVID-19. With Brexit uncertainty still on the horizon, the MPC believes it still has more it can do, but for now asset purchases remain the preferred monetary policy tool. Going forward, the MPC will continue to monitor economic and inflation data while standing ready to take "whatever additional action is necessary to achieve its remit."

Portfolio Strategy

MSLF EURO LIQUIDITY FUND (LVNAV)

With the eurozone economic recovery stalling as renewed restrictions and lockdowns are reimposed throughout much of central Europe, the ECB has prepared the market for additional stimulus in the December meeting. With excess liquidity already at record highs, this is likely to have further dampening effects on short-term rates. The yield curve is already very flat and little pick up in yield is available for longer-dated investments. Indeed, the year-end pressures are already starting to be reflected in maturities over the turn of the year with much lower yields. Again, the Fund's assets under management continued to grow, exceeding €8 billion intra-month before month-end flows caused the Fund to finish the month up €700 million at €7.7 billion.

MSLF STERLING LIQUIDITY FUND (LVNAV)

MPC members continue to debate the potential use of negative interest rates, and consequently the money market yield curve remains entirely flat or inverted for the sterling market. Given the low

¹ Source: Bloomberg



DISPLAY 1 Overnight Rates

As of 31/10/20

	SONIA (%)	EONIA (%)	OBFR (%)
Overnight	0.05	-0.47	0.08

Source: Bloomberg

yields, we have limited our trading to shorter-dated money market assets to limit the amount of overnight being carried and complemented this with opportunistic trading in tail-end bonds and floating-rate notes. This has seen the WAM of the Fund stay in the high 40 days, with the WAL lengthening to 58 days by month end. Fund growth has continued into the fourth quarter, as assets under management increased in early October prior to the normal month-end outflows.

MSLF U.S. DOLLAR LIQUIDITY FUND (LVNAV)

Minutes from the September FOMC provided more color around the committee's pivot to an average inflation target but added little clarity to their outlook for asset purchases. Third quarter gross domestic product expanded at a record 33.1%, fueled by personal spending growth, after declining in the prior quarter by the most in seven decades of data. As positive economic data continues to hit headlines, and the short end of the curve remains flush with cash, 3-month LIBOR touched all-time lows on October 19, setting at 0.20863%.

With spreads remaining tight and potential market volatility in the near term, we remain conservatively positioned across our funds, maintaining elevated levels of liquidity and keeping the weighted average life (WAL) below 55 days.

MSLF U.S. DOLLAR TREASURY LIQUIDITY FUND (PUBLIC DEBT CNAV)

We continued to have Treasury bill pay-downs during October, which moved yields marginally lower. The debate over another stimulus bill continued all month in Washington and did not result in a plan, pushing the possibility for more bill supply to some time after the presidential election. We continued to favor purchasing Treasury bills up to 6-month tenors and in overnight repurchase agreements collateralized by U.S. Treasuries. The Treasury bill curve remained flat, with only a few basis point spread between 1-month and 1-year bills. We continue to ensure high levels of liquidity and manage the portfolio to be responsive to changes in market conditions and interest rate levels.

DISPLAY 2 LIBOR Rates

As of 31/10/20

	GBP LIBOR (%)	EUR LIBOR (%)	USD LIBOR (%)
Overnight	0.05	-0.58	0.08
1 week	0.04	-0.58	0.10
1 month	0.04	-0.56	0.14
2 months	0.05	-0.53	0.18
3 months	0.04	-0.53	0.22
6 months	0.06	-0.52	0.24
12 months	0.13	-0.47	0.33

Source: Bloomberg

DISPLAY 3 Yield Curves

As of 31/10/20

	U.K. GOVERNMENT BONDS	GERMAN GOVERNMENT BONDS	U.S. GOVERNMENT BONDS
2 year	-0.04	-0.80	0.15
5 year	-0.04	-0.82	0.38
10 year	0.26	-0.63	0.87
30 year	0.83	-0.22	1.66

Source: Bloomberg

12 Month Performance Periods to Latest Month End (%)

MSLF Euro Liquidity Fund (LVNAV)	OCT '19 - OCT '20	OCT '18 - OCT '19	OCT '17 - OCT '18	OCT '16 - OCT '17	OCT '15 - OCT '16
Institutional Accumulation Share Class	-0.55	-0.47	-0.51	-0.50	-0.32
MSLF Sterling Liquidity Fund (LVNAV)	OCT '19 - OCT '20	OCT '18 - OCT '19	OCT '17 - OCT '18	OCT '16 - OCT '17	OCT '15 - OCT '16
Institutional Distributing Share Class	0.32	0.69	0.43	0.21	0.43
MSLF U.S. Dollar Liquidity Fund (LVNAV)	OCT '19 - OCT '20	OCT '18 - OCT '19	OCT '17 - OCT '18	OCT '16 - OCT '17	OCT '15 - OCT '16
Institutional Distributing Share Class	0.82	2.37	1.78	1.01	0.41
MSLF U.S. Dollar Treasury Liquidity Fund (Public Debt CNAV)	OCT '19 - OCT '20	OCT '18 - OCT '19	OCT '17 - OCT '18	OCT '16 - OCT '17	OCT '15 - OCT '16
Institutional Distributing Share Class	0.56	2.14	1.50	0.55	0.14

Past performance is not a reliable indicator of future results. The net performance data shown is calculated net of annual fees. The sources for all performance and Index data is Morgan Stanley Investment Management. Please visit our website www.morganstanley.com/im to see the latest performance returns for the fund's other share classes.

Institutional Distributing and Institutional Accumulation Share Class Risk and Reward Profile



The risk and reward category shown is based on historic data.

- Historic figures are only a guide and may not be a reliable indicator of what may happen in the future.
- As such this category may change in the future.
- The higher the category, the greater the potential reward, but also the greater the risk of losing the investment. Category 1 does not indicate a risk free investment.
- The fund is in this category because it invests in money market securities and the fund's simulated and/or realised return has experienced low rises and falls historically.

This rating does not take into account other risk factors which should be considered before investing, these include:

- The value of bonds are likely to decrease if interest rates rise and vice versa.
- Issuers may not be able to repay their debts, if this happens the value of your investment will decrease. This risk is higher where the fund invests in a bond with a lower credit rating.
- The fund relies on other parties to fulfill certain services, investments or transactions. If these parties become insolvent, it may expose the fund to financial loss.
- While it is intended that the distributing share classes will maintain a share price of €1/\$1/£1 this may not be achieved due to the creditworthiness of the issuers of investments held or changes in interest rates.

Past performance is no guarantee of future results.

Please refer to the Prospectus for full risk disclosures. All data as of 31 October 2020 and subject to change daily.

INDEX INFORMATION

One week Euro LIBID Index – One week London Interbank Bid Rate - The average interest rate which major London banks borrow Eurocurrency deposits from other banks.

One Month Euro LIBID Index – One month London Interbank Bid Rate - The average interest rate which major London banks borrow Eurocurrency deposits from other banks.

Euro Overnight Index Average (EONIA) – the standard interest rate at which banks provide loans to each other with a duration of 1 day within the Eurozone.

FTSE 1 Month Treasury Bill Index – index calculated by FTSE that is an average of the last one month Treasury bill month-end rates.

One Week USD LIBID Index – 1 week London Interbank Bid Rate - The average interest rate which major London banks borrow deposits from other banks.

One Month USD LIBID – 1 month London Interbank Bid Rate - The average interest rate which major London banks borrow deposits from other banks.

FED Funds – excess cash reserves that commercial banks and other financial institutions deposit at regional Federal Reserve banks; these funds can be onward lent to other market participants with insufficient cash on hand to meet their lending and reserve needs.

One Week GBP LIBID Index – 1 week London Interbank Bid Rate - The average interest rate which major London banks borrow deposits from other banks.

One Month GBP LIBID – 1 month London Interbank Bid Rate - The average interest rate which major London banks borrow deposits from other banks.

SONIA – the standard interest rate at which banks provide loans to each other with a duration of 1 day within the Sterling market.

DEFINITIONS

Weighted average maturity (WAM) – measures the weighted average of the maturities of the portfolio's individual holdings, taking into account reset dates for floating rate securities.

Weighted average life (WAL) – measures the weighted average of the maturities of the portfolio's individual holdings.

Public Debt Constant Net Asset Value (CNAV) MMF – a MMF qualifying and authorised as a Public Debt CNAV MMF in accordance with MMF Regulation which seeks to maintain a stable NAV and invests 99.5% of its assets in money market instruments issued or guaranteed by sovereign entities, reverse repurchase agreements secured with government debt and cash.

Low Volatility Net Asset Value (LVNAV) MMF – a MMF qualifying and authorised as a LVNAV MMF in accordance with MMF Regulation which seeks to maintain a stable NAV under the condition that the stable NAV does not deviate from the NAV per Share by more than 20 basis points. In case of a deviation of more than 20 basis points between the stable NAV and the NAV per Share, the following redemption or issue of Shares shall be undertaken at a price that is equal to the NAV per Share.

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