

The current weakness in GBP Sterling What should pension scheme trustees do?

By the end of June this year, GBP Sterling was already down circa 10% against the US Dollar year to date, due to safe haven capital flows. Since the beginning of July it has fallen in value another 3%. This is likely due to an impending gas supply crisis which the Bank of England predicts will push the country into a recession which will last into 2024. This will place the BOE in a tough position with inflation remaining high at the same time that economic growth slows.



Source: {Refinitiv}

In such an environment the Bank may not feel it appropriate to raise interest rates very aggressively to control inflation. The most likely outcome given this stagflationary scenario, could be short term real interest rates will fall further into negative territory. This economic outlook may be what has been priced into the GBP/USD exchange rate.

This means that GBP Sterling is trading at its weakest level in history versus the US Dollar except for brief periods during the coal miners' strike in 1985 and the COVID crises in 2020. A similar but less extreme situation applies to other major currencies such as the Euro and Japanese Yen.

It may therefore be a good time for Trustees to review their currency hedging policy. In particular, if a scheme has unhedged overseas assets then the scheme should have benefitted from weaker GBP Sterling. Putting currency hedges in place now would lock in any currency gains that have been made on those assets.

Trustees of UK pension schemes with an overseas parent who are seeking additional funding from the employer will note that the cost to the parent in local currency will have fallen.

If you would like to discuss any of these matters further, please get in touch with your contact at Cartwright.

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