Increase in the Federal Reserve Rate

Commentary by Payden and Rygel

The Federal Reserve increased the overnight lending rate in December for the first time since 2006. Short-term rates rose as the FOMC unanimously agreed to raise the Federal Funds rate from 0% to 0.25%, and indicated the potential for four additional rate hikes in 2016. The committee's actions effectively set a floor for short-term yields of 0.25%. Consequently, 3-month maturity Treasury bill yields increased to 0.17% from -0.02% at the end of the third quarter. The Fed's decision to move rates higher by 0.25% in December was based on strength in the labor market and improvements in household spending, business investment, and housing market conditions. The yield curve flattened with shorter-maturity bond yields increasing more than longer-maturity bond yields.

Credit markets were able to absorb higher rates and robust new issuance with spreads tightening modestly. Demand for short-maturity assets remains high which should act to limit the increase in short-term yields. Additionally, market participants are less optimistic about the strength of the US economy and are expecting only two rate hikes in 2016. We think the Federal Reserve Board will move slowly and gradually. The much-anticipated rate hike was just ¼ of 1%. The US economy is not in perfect condition and inflation is still low, so there is no urgency for the Fed to move quickly. The broad consensus view is that short-term interest rates will end 2016 around 1%. In addition, other global economies face a range of economic and political challenges and global central banks seem in no rush to raise interest rates. As a result, we think low-interest rates will continue to be a dominant global theme in 2016.

STRATEGY – Florida Trust Day to Day Fund

The Day to Day Fund holds US Government securities (US Treasuries, agencies and repos) as well as short-term corporates and commercial paper and seeks to provide a stable and positive overall yield. In anticipation of higher interest rates before year-end, we invested a large portion of the portfolio in overnight government money market instruments. After the December rate hike, we invested in higher yielding securities, increasing the portfolio's overall yield. The 7-Day "SEC" Yield* of the Day to Day Fund has risen from 0.18% on 11/30/15 to 0.27% on 12/31/15, and is expected to rise further as securities mature and funds are reinvested at higher market rates, moving toward 1% by year end if the Fed continues on its path of raising interest rates.

*calculated in accordance with the yield methodology set forth by SEC Rule 2a-7 for money-market funds

STRATEGY – Florida Trust Short Term Bond Fund

The Florida Trust Short Term Bond Fund holds a diversified mix of sectors for income generation and was positioned in anticipation of rising short-term interest rates, including our expectation of a hike in the Federal Funds rate before year-end. After the mid-December rate hike, we began to extend the portfolio duration. We will continue to move maturities out the yield curve to capture the higher yields now available. Corporate bonds remain attractive, and we anticipate maintaining our exposure through the purchase of bonds in the new issue market. Within the corporate sector, we kept our floating-rate exposure to help mitigate interest rate risk. We maintain our allocation to high-quality asset-backed and mortgage-backed securities (ABS/MBS) with short duration profiles for their yield and diversification benefits.

The market yield of the Short Term Bond Fund rose from 1.14% on 11/30/15 to 1.25% on 12/31/15, and is expected to rise further as maturing securities are reinvested at higher rates, which will enhance the income component of the fund's return, as active management is employed to seek positive total returns.