Economic and Market Commentary – August 2023

The July U.S. Consumer Price Index (CPI) showed a second month of easing price pressures. Core CPI, which excludes food and energy prices, rose by just 0.16% but remains well above the Fed's 2% target at 4.7% year-over-year. Declining commodity prices helped bring down headline inflation while services prices remained elevated. U.S. labor markets continued to exhibit resilience, with the unemployment rate declining to 3.5%. Stellar consumer spending data topped expectations following another rate hike in July, with retail sales rising by 0.7% in August, compared to 0.3% in July. Although cooling inflation and tight labor markets are fueling the possibility of a "soft landing" soon, in his much-anticipated remarks at the Jackson Hole Economic Symposium, Fed Chair Powell reinforced that there is still a long way to go to bring inflation down to the 2% target. Globally, economic data from other countries has not reflected the same resilience.

The 2-year US Treasury fell two basis points ("bps") to 4.86%. The 10-year Treasury rose 15 bps to 4.11%, and the 30-year rose 20 bps to 4.21%. The 10-year yield rose to highs not seen since 2007 as market participants digested strong economic news, managed more Treasury issuance needed to finance the deficit, and grappled with Japan's Yield Curve Control strategy. An auction of two-year Treasury notes drew the highest yield since 2006 after the bond market yield surge that intensified in anticipation of another Federal Reserve rate hike. The $45 billion was awarded at 5.02% and was the highest yield since before the financial crisis.

At the annual Jackson Hole Economic Symposium, Jerome Powell expressed that the Fed was seeing progress, but its job remained unfinished. Powell lit a fire under the bond market last August. This year, his speech was longer and acknowledged the progress made on inflation. Headline inflation was 7% a year ago and is "3.3% as of July." He also noted improvement in core inflation, dividing underlying inflation into three parts: core goods, housing, and non-housing services. He's hopeful for the continued progress on all three. However, core goods prices remain above pre-COVID levels, housing may cool with a lag but is still excessively high, and non-housing services are in lockstep with the unemployment rate near cycle lows. As Chair Powell framed it, policymakers' choice is to hold or hike, NOT to hold or cut, as many bond investors now anticipate.

Short-Term Bond Fund ("STBF")

The STBF had a 0.44% total return[1] for August compared to the benchmark ICE BofA 1-3 Year US Treasury index of 0.39%. The fiscal year-to-date total return for the STBF was +3.46% compared to +2.48% for the benchmark. The net 30-Day SEC Yield for the Short-Term Bond Fund was 4.77% on 8/31, up from 3.93% as of the 2022-year end.

The STBF remains well-positioned with ample liquidity and an up-in-quality diversified mix of credit sectors for income generation. We continue to favor a healthy allocation to liquidity as well as corporates and securitized bonds, and floating rate securities where available. The fund has a headline duration of 1.4 years, versus the index duration of 1.8. The fund holds a 14% allocation to floating rate securities. These bonds enhance the overall yield of the fund – these positions average a near 8% yield - but do not contribute to duration. Over the coming months, we will look to move closer to a neutral headline duration, focusing on corporate credit purchases in the 2-3-year space. In addition, the inverted yield curve means shorter Treasury securities are currently more attractive, yield-wise, versus longer options.

Given recent volatility, we are keeping a focus on liquidity. In our view, the Fed Funds rate is closer to the terminal rate (ending level for this cycle) and will remain near current levels for longer than current market expectations. In addition, the Fed has signaled their appetite for maintaining higher policy rates as inflation, though improved, is still high, and the labor market still strong, though with the beginnings of strain. This backdrop is likely to result in continued market volatility as the investors continue to parse the impact of modestly tighter financial conditions, growth pressures, and continued restrictive monetary policy.

The STBF is assigned Fitch rating agency's highest Fund Credit Quality Rating and Fund Market Risk Sensitivity Rating of AAAf/S1. The liquidity of the fund is very strong, with 31% of funds invested in Treasuries and government related securities. There were ~$18 million in withdrawals in August.

[1] *Net Asset Value calculated by custodian UMB. Net of fees.*

Day to Day Fund ("DtD Fund")

The Florida Trust Day to Day Fund posted a total return[2] of +0.45% in August, versus the benchmark ICE BofA Three-Month Treasury Index return of +0.45%. Fiscal 2023 year-to-date, the fund returned +4.19% compared to +4.00% for the benchmark. The net 7-day SEC yield of the Day to Day Fund was 5.29%, compared to 4.16% at 2022-year end. Comparable prime institutional government funds had an average yield of 5.05%[3] on 8/31. The Fund continues to provide safety, income, and liquidity of investments in a stable, $1 NAV Fund.

We continue to diversify credit exposure by investing in high-quality commercial paper ("CP"), and money market tranches of ABS, to build yield over Treasury bills in the Day to Day Fund, to maximize yield without adding volatility or sacrificing liquidity. Recently we have sold municipal variable-demand-notes ("VRDNs") in favor of overnight repurchase agreements and Treasury bill exposure. As inflation accelerated in 2022 and the market began pricing in more aggressive moves by the central bank, front end rates increased, and ultra-short rates diverged. As a result, the fund benefited from purchasing money market securities including repo, VRDNs, short term ABS, agency discount notes, and CP for higher yields while maintaining limited volatility. Now, short Treasury bills yield more, and we have rotated positioning accordingly. In addition, the fund holds a 13% allocation to floating rate notes, averaging near a 6% yield collectively.

The fund remains highly liquid with approximately 36% of the portfolio invested in overnight and short-term securities. Additionally, 41% of the portfolio is invested in government or government guaranteed securities, also enhancing liquidity. The weighted-average maturity of the portfolio is currently 42 days. The fund experienced $12 million in net withdrawals in August. The fund is assigned Fitch rating agency's highest Money Market Fund Rating of AAA mmf.

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[2] *Net of fee return calculated by custodian UMB.*

3 Crane Institutional Government 7-Day Yield