Economic and Market Commentary – February 2024

During February, the market repriced expectations for the timing of the first Fed rate cut in 2024, pushing expectations out from March to June, resulting in a rise in yields. In the US, the yield on the 2-year Treasury note rose 41 basis points ("bps") to 4.62% in February. The yield on the benchmark 10-year Treasury rose 34 bps to 4.25% and the yield on the 30-year Treasury rose 21 bps to 4.38% during the month.

Since the last FOMC meeting in January, economic releases have signaled stronger-than-expected labor market conditions and higher inflation readings. Reflecting on the data surprises received in February, Fed Board Governor Chris Waller remarked that the Fed is in "no rush to begin cutting interest rates to normalize monetary policy" as policymakers "need to verify that the progress on inflation in the last half of 2023 will continue." In addition, Waller emphasized that "the risk of waiting a little longer to ease policy is lower than the risk of acting too soon and possibly halting or reversing the progress we've made on inflation." As it became clear that policymakers will need to see a few more months of data to gain more confidence that core inflation is slowing, bond investors dialed back their rate cut expectations. The market is now expecting around three 25-basis point rate cuts by year-end, compared to the seven cuts priced in at the start of the year. Given the backdrop of elevated wage growth and strong consumer spending, we won't be surprised if policymakers enact just two 25-basis point rate cuts this year if inflation resumes its progress toward 2% by Q4.

The U.S. labor market remained strong in February while core inflation picked up. Total employment on nonfarm payrolls surged by 353,000 in January; the strong jobs growth kept the unemployment rate stable at 3.7%. Meanwhile, inflation measures increased considerably in January, halting the recent softening trends. Specifically, the core Personal Consumption Expenditures (PCE) Price Index, which excludes volatile food and energy prices, rose 0.4% month-over-month, led by a sharp increase in non-housing services prices. While the possibility of inflation hovering above 2.5% year-over-year has increased, it is too soon to tell whether the January inflation readings indicate a stall in overall inflation progress or only a bump along the path to the Fed's 2% target.

Short-Term Bond Fund ("STBF")

As a result of yield curve repricing during the month, the STBF had a -0.20% total return[1] for February compared to the benchmark ICE BofA 1-3 Year US Treasury index of -0.41%. The fiscal year-to-date total return for the STBF is +2.84% compared to +2.46% for the benchmark. The net 30-Day SEC Yield for the Short-Term Bond Fund was 4.46% on 2/29, compared to 4.61% as of 2023-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 emphasize quality and diversification in our credit positioning. We currently favor AAA-rated asset-backed securities (ABS) over corporates, as spread potential over similar maturity Treasuries is more attractive in the former. The sector has benefited from significant issuance early in the year and fundamentals remain strong in the current economic environment. The fund has a headline duration of 1.61 years, versus the index duration of 1.85. The fund holds a 12% allocation to floating rate securities. These bonds enhance the overall yield of the fund – these positions have an average yield over 7%, but do not contribute to duration / interest rate risk. With credit spreads trading toward the lower band of their historical spread levels, we are not reaching for yield nor are we rushing to sell. We continue to opportunistically add, and trim positions based on specific security valuations.

The change in messaging from the Fed starting in December 2023, making it clear we should expect rate cuts in 2024, helps determine positioning for the fund. Current duration (interest rate risk) positioning should help the fund outperform the Treasury benchmark as the Fed starts cutting rates likely later this year. In addition, the still-inverted yield curve means shorter Treasury securities are currently more attractive, yield-wise, versus longer options. Still, as we consider reinvestment risk – rates may stay higher for some time, but lower rates are on the horizon - investing in non-Treasury sectors can offer comparable or higher yields.

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 28% of funds invested in Treasuries and government related securities. There was a $5 million deposit in the fund during February.

[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 +0.44% in February, in line with the benchmark ICE BofA Three-Month Treasury Index return of +0.41%. Fiscal year-to-date, the fund has returned +2.30% compared to +2.22% for the benchmark. The net 7-day SEC yield of the Day to Day Fund was 5.49%, compared to 5.50% at 2023-year end. Comparable prime institutional government funds had an average yield of 5.04%[3] on 2/29. 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 as we search to maximize yield without adding volatility or sacrificing liquidity. As Treasury bill issuance has been met with strong demand due to reduced usage of the Federal Research Repurchase Program facility, we rotate into bills from repo and agency discount notes, and position Treasury holdings to take advantage of the yield curve inversion. While short floating rate securities are difficult to source, the fund holds a 24% allocation to floating rate notes, averaging a 5.6% yield collectively.

The fund remains highly liquid with approximately 48% of the portfolio invested in overnight and short-term securities. Additionally, 35% of the portfolio is invested in government or government guaranteed securities, also enhancing liquidity. The weighted-average maturity of the portfolio is currently 20 days. The fund processed about $33 million in net outflows in February. 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