

FLORIDA TRUST

Economic and Market Commentary - June 2024

In the U.S., the yield on the US 2-year Treasury note fell 12 basis points (bps) over the month to end at 4.75%. The yield on the benchmark 10-year Treasury fell 10 bps to 4.40%, down from 4.50% at the end of May. The yield on the 30-year Treasury fell nine bps to 4.56%.

In June, the U.S. economy saw modest progress on inflation while the labor market remained healthy. The core Personal Consumption Expenditures (PCE) Price Index, which excludes food and energy prices, registered a soft monthly reading of 0.08% in May, led by a sharp slowdown in non-housing core services prices (0.1%) and a decrease in goods prices (-0.2%). However, housing-related services prices continued to increase above trend at 0.4%. Consequently, the year-over-year core inflation rate slowed to 2.6%. Meanwhile, although the unemployment rate increased to 4% in May and job openings fell, the payroll job growth of +272,000 was stellar. The June unemployment rate increased to 4.1%, and nonfarm payroll employment growth continued to exceed expectations, gaining 206,000 net jobs in June, which suggests that the labor market remains resilient while moving into better balance.

In June, the Federal Reserve maintained the fed funds rate at 5.25% - 5.50%, as higher-than-expected inflation prints in the first quarter of 2024 did not give policymakers confidence to reduce rates. Even with May's softer inflation data, Fed Chair Powell emphasized that policymakers need to see several months of target-consistent inflation data to be comfortable with rate cuts and that it will "probably take longer to get the confidence needed to begin loosening policy." Moreover, the June Summary of Economic Projections (SEP) release shows policymakers continue to expect at-trend growth and a tight labor market for the latter half of the year. However, committee members increased expectations for the year-end core PCE rate from 2.6% to 2.8%. Consequently, the median FOMC member expects just one cut by the end of 2024, down from March's projection of three. While bond investors continue to expect close to two rate cuts in 2024, we think the balance of risks still tilts toward stickier core inflation that could finish the year above 2.8% year-over-year, and, therefore, we anticipate fewer rate cuts.

Short-Term Bond Fund (“STBF”)

The STBF posted a +0.58% total return¹ for June compared to the benchmark ICE BofA 1-3 Year US Treasury index of +0.58%. Short-fixed income returns were again positive across all sectors in June though credit spreads widened; total returns and excess returns year-to-date remain strong. The fiscal year-to-date total return for the STBF is +4.43% compared to +3.76% for the benchmark. The net 30-Day SEC Yield for the Short-Term Bond Fund was 4.67% on 6/30, compared to 4.61% as of 2023-year end.

The STBF remains well-positioned as we favor a high-quality tilt in credit positioning, with ample liquidity. The trend of heavy supply continued throughout the second quarter as issuance of both investment grade (IG) corporates and securitized products exceeded expectations. Supply has been met by healthy investor demand, so credit premiums remained relatively stable throughout the quarter and lower for the year. We anticipate a potential seasonal decline in supply as the year progresses, in part due to the heavy issuance we’ve already experienced, as well as the potential for increased volatility as we approach the presidential election cycle. While risk premiums have come off their lows, they remain close to their lowest levels over the past two years.

The fund has a headline duration of 1.51 years, versus the index duration of 1.84. The fund holds a 11% allocation to floating rate securities. These bonds enhance the overall yield of the fund – these positions have an average yield of 6.7%, but do not contribute to duration / interest rate risk. The timing and pace of rate cuts will be our primary focus over the next six months. Timing turning points, such as the beginning of monetary policy easing, is difficult to assess since markets often move very quickly in response to a change in policy. Hence, more prudent positioning is warranted. We don’t see any imminent risks catalyzing a risk-off move, but we also do not view current credit premiums as an attractive starting place to increase credit exposure.

Messaging from the Federal Reserve indicates a rate cut in late 2024 remains possible. Current yield curve positioning and planned duration extension should help the fund outperform the Treasury benchmark when the Fed starts cutting rates. In addition, the still-inverted yield curve

¹ Net Asset Value calculated by custodian UMB. Net of fees.

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 32% of funds invested in Treasuries and government related securities. There were no participant flows in or out of the fund in June.

Day to Day Fund (“DtD Fund”)

The Florida Trust Day to Day Fund posted a total return² of +0.45% in June, compared to the benchmark ICE BofA Three-Month Treasury Index return of +0.41%. Fiscal year-to-date, the fund has returned +4.27% compared to +4.04% for the benchmark. The net 7-day SEC yield of the Day to Day Fund was 5.46%, compared to 5.50% at 2023-year end. Comparable prime institutional government funds had an average yield of 5.04% on 6/30. 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. Within corporates, we continue to actively participate in favored large US and Yankee banks as financials supply has been robust. 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 position Treasury holdings to take advantage of the yield curve inversion. While short floating rate securities are difficult to source, the fund holds a 33% allocation to floating rate notes, averaging a 5.6% yield collectively.

² Net of fee return calculated by custodian UMB.

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The fund remains highly liquid with approximately 38% of the portfolio invested in overnight and short-term securities. Additionally, 34% of the portfolio is invested in government or government guaranteed securities, also enhancing liquidity. The weighted-average maturity of the portfolio is currently 22 days. The fund processed about \$3 million in net outflows in June. The fund is assigned Fitch rating agency's highest Money Market Fund Rating of AAA mmf.