Florida LGIP Strategy Update

Q3 2023

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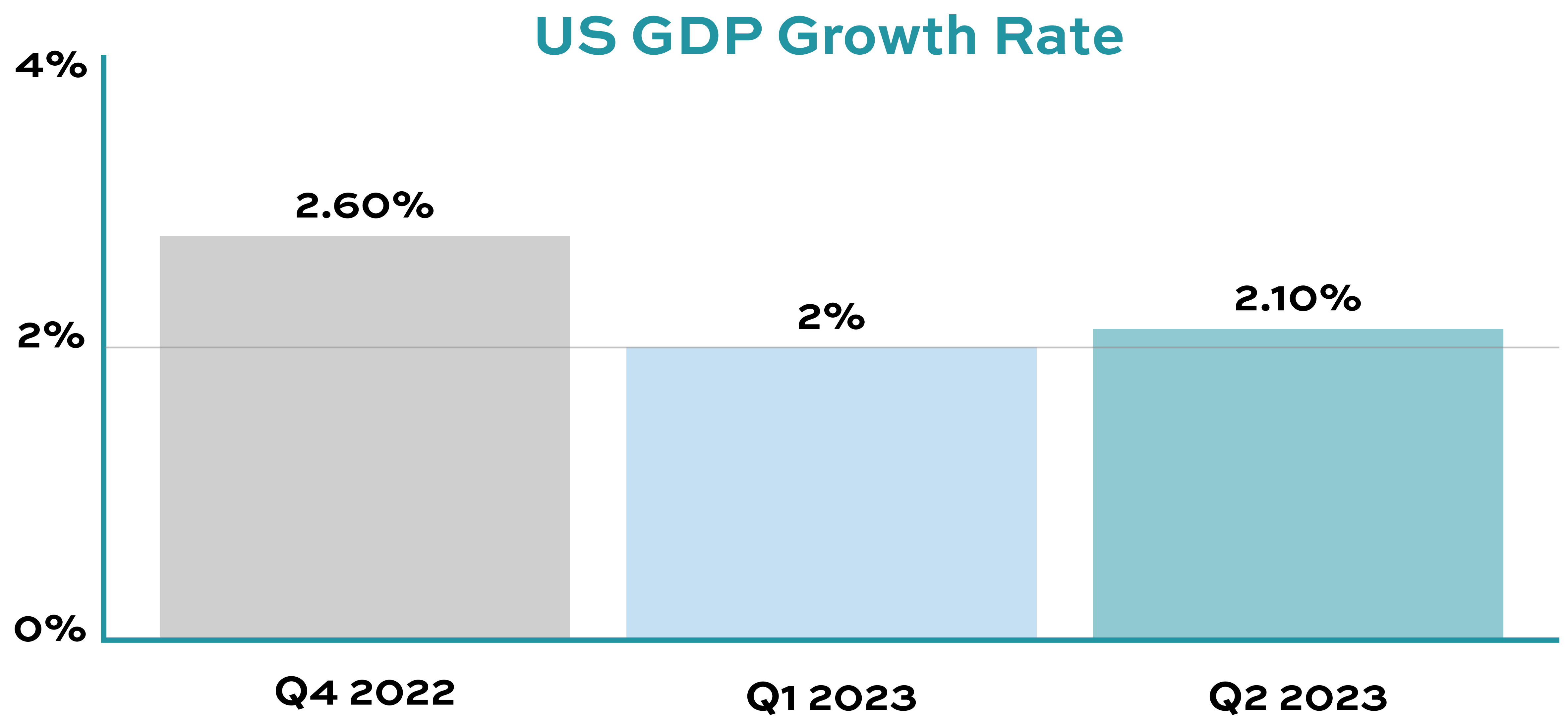
Economic Update

Real U.S. Gross Domestic Product (GDP) for Q2 arrived at 2.1%, continuing a trend of more normalized growth in the post-COVID era. Of course, the most important aspect of the number is that it is positive, refuting any claims of an imminent recession after March's bank failures. As per usual, the U.S. consumer continues to spend, helping bolster a domestic economy that is heavily reliant on consumption. Further aiding the headline number were increases in imports, accelerating business investment, as well as an uptick in local and federal government spending.

The Federal Reserve remains steadfast on its mandate to get inflation back to 2%, even if it must keep rates "higher for longer". Economists surveyed by Bloomberg put the probability of a recession over the next twelve months at 60%, down slightly from the last survey.

Inflationary pressures have moderated from their recent 40-year highs but are anticipated to remain elevated throughout 2023 and into 2024. The Federal Reserve has maintained its hawkish stance (higher interest rates) with a commitment to keep rates at or near current levels until inflation hits their 2% goal. Unemployment remains near the lowest levels since the 1950s, providing an ongoing opportunity for the Fed to pursue tighter monetary policy.



KEY TAKEAWAY

Markets now expect the upper range for federal funds rate to hit ~5.75% by year-end and to slowly decline to ~4.75% over the next 12 months.

*Bureau of Economic Analysis | https://www.bea.gov/data/gdp/gross-domestic-product

Economic Update (cont.)

The Treasury curve is flattening as longer-term rates begin to move higher. Much of the recent move in longer rates is due to the latest Fed press conference where the committee upgraded their projection for the U.S. economy and reiterated that rates will stay high.

Volatility is expected to persist as investors balance ongoing inflationary pressures amid unexpectedly positive economic figures leading to uncertainty in both bond and equity markets.

> **Financial markets are pricing in approximately one 25-basis-point rate hike for the fed funds rate in either November or December of 2023. After this, a long pause is expected well into 2024.**

US Treasury Yields

Date & Yield

Tenor	6/30/22	7/28/23	8/30/23	9/29/23
1M	5.24	5.47	5.55	5.55
3M	5.43	5.52	5.56	5.55
6M	5.47	5.54	5.51	5.53
1Y	5.40	5.37	5.39	5.46
2Y	4.87	4.87	4.90	5.03
3Y	4.49	4.52	4.57	4.80
5Y	4.13	4.18	4.27	4.60

US Department of the Treasury
https://home.treasury.gov/resource-center/data-chart-center/interest-rates/TextView?type=daily_treasury_yield_curve&field_tdr_date_value=2023

LGIP Investment Strategy

We believe the Fed will do everything in its power to fulfill its mandate of "stable prices" (aka 2% inflation goal) by raising short-term rates and keeping them high until CPI is convincingly low.

During Q3 the goal was to slowly reduce floating-rate exposure in the FL-FIT Cash Pool in favor of more fixed-rate positions. However, there will be a mixture of the two through year-end. We are keeping a close eye on the relative value between floating- and fixed-rate instruments as market opportunities are presented.

Bank deposit rates are steadily increasing alongside of Fed rate hikes, but not all are moving in lockstep. We continue to negotiate rates with our depository institutions to provide additional spread over the effective federal funds rate. In the state of Florida, all deposits are FDIC-insured or QPD programs.

KEY TAKEAWAY

During Q3 we found particular value in fixed-rate instruments, especially in the four to six-month maturity range.

STRATEGY

Focus on quality: Short-term U.S. Treasuries provide excellent relative value given the increasing supply available. Additionally, we continue to see value in high-quality municipal bonds and tier-one (highest-rated) commercial paper (where appropriate).

Florida LGIP Comments

FL FIT Preferred Deposit Pool:

Qualified Public Deposits (QPD) and FDIC-insured deposit yields continued to move up alongside the federal funds rate, providing a direct benefit for pool participants. The FL-FIT PDP pool remains a competitive alternative for Florida municipalities seeking yield away from any credit exposure. We expect this pool to closely track the effective federal funds rate, which finished the month at 5.33%.

QTD/YTD return: +1.31%, 3.68%

End of month yield: 5.27%

FL FIT Cash Pool:

Strategically, we are focused on balancing floating-rate exposure with traditional fixed-rate positions as we near the end of the rate hiking cycle. We're targeting a blended average life of around 5-6 months as we add fixed-rate positions to help lock in yield. Additionally, there will always be ample liquidity from prime money markets, ultra-short bond funds, and bank deposits. We expect the pool to continue to outpace the S&P 30-day LGIP index.

QTD/YTD return: +1.36%, +3.84%

End of month yield: 5.50%

FL FIT Enhanced Cash Pool (floating NAV, total return focus):

We continue to focus on balancing liquidity while opportunistically taking advantage of heightened rates. Currently, we are extending the pool's average duration as we look to lock-in yield for the long haul. We see ample opportunities in fixed-rate securities, especially as the yield curve flattens (longer rates moving higher). The pool has closely tracked its benchmark over the last twelve months, and we expect the performance of this pool to be in line with its 0-1 year benchmark moving forward. See below for further details.

FL FIT Select Cash Pool (floating NAV, total return focus):

During Q1, we decided to remove the portfolio insurance (interest rate futures) as we were nearing the latter stages of the rate cycle. In Q2 and Q3 the pool sought to purchase longer duration instruments to align the pool closer to the benchmark, while simultaneously balancing the need for liquidity. Like our Enhanced Cash pool, the strategy is to utilize both floating and fixed coupon structures with high credit quality, sufficient diversification, and an eye toward liquidity. We are targeting a duration near the benchmark of ~1.75 years while also providing some flexibility should rates unexpectedly continue to move higher (floating-rate instruments). The pool continues to outpace its 1-3 year benchmark over the longer term and has outpaced its benchmark by ~50 basis points over the last year. See below for further details.

Florida Floating NAV Pool Details†

As of 9/30/23, all return figures are %

FL Enhanced Cash:

PERFORMANCE

Benchmark: 75/25 split of ICE 0-1y US Treasury and 0-1y AAA-A Corporate

- September 2023 QTD/YTD %: (+1.17, +3.31)
- Benchmark: (+1.32, +3.54)

STRATEGY

Focus on increasing credit quality gradually and reducing corporate bond exposure over time.

Pool yield continues to rise through reinvestment opportunities and resets on floating-rate securities.

- Yield at end of the quarter: 4.98%
- Focus on total return for floating-nav pools

Targeted duration band of 0.40 to 0.65 years

- Continue to target an average duration close to 0.50 years (currently ~0.56)
- Decrease floating-rate instruments over time (currently ~47% of portfolio) in favor of fixed.

FL Select Cash:

PERFORMANCE

Benchmark: 75/25 split of ICE 1-3y US Treasury and 1-3y AAA-A Corporate & Gov't Index

- September 2023 QTD/YTD: (+0.74, +2.33)
- Benchmark: (+0.74, +1.75)

STRATEGY

Continue to focus on high-quality instruments with call protection to lock-in/maintain yield for years to come.

- The inverted yield curve, where longer-term rates are shorter than overnight rates, provides some challenges in providing comparable yield today versus cash.

Pool yield continues to rise, but focused on yield maintenance for the long-term.

- Yield at end of the quarter: 4.18%
- Focus on total return for floating-nav pools.

Targeted duration band of 1.00 to 2.00 years, currently 1.90 years.

- Increased duration as we extend maturities and lock-in yield.
- Continue to increase allocation to fixed-rate securities (~67% of portfolio)

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