Florida LGIP Strategy Update

Q4 2023

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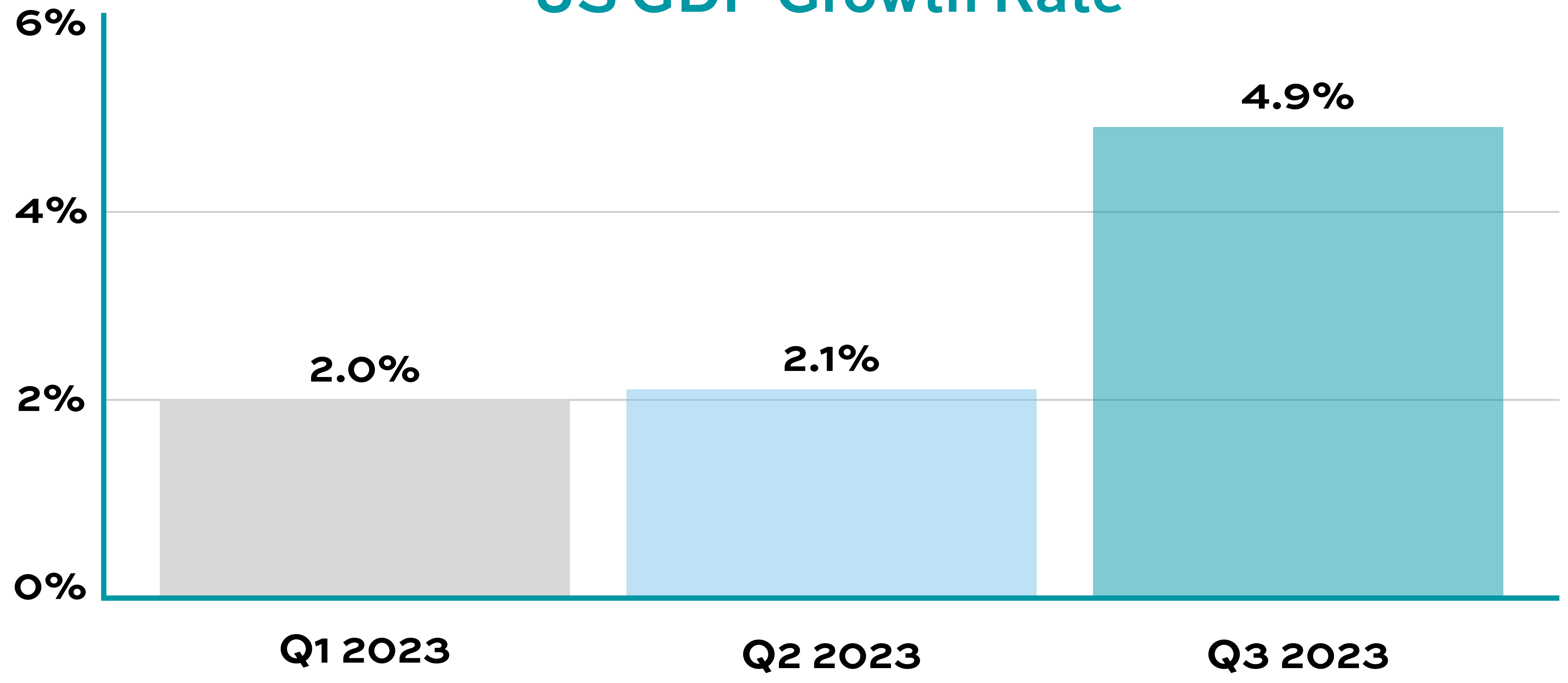
Economic Update

Q3 Real US Gross Domestic Product (GDP), which subtracts out the effects of inflation, arrived at a whopping 4.9% and followed a more "normal" read of 2.1% for Q2. The U.S. economy continues to show signs of strength despite lingering inflationary pressures and high consumer prices. As per usual, the US consumer continues to spend, helping bolster a domestic economy that is heavily reliant on consumption.

Meanwhile, the December jobs report beat expectations: Total nonfarm payroll employment increased by 216,000 in December, and the unemployment rate was unchanged at 3.7%. Employment continued to trend up in government, health care, social assistance, and construction, while transportation and warehousing lost jobs. The United States needs ~100k new jobs per month to maintain existing employment levels.

> **The Federal Reserve** policymakers agreed in December that it would be appropriate to maintain a restrictive stance "for some time," while acknowledging they would likely need to begin cutting rates late in 2024.

US GDP Growth Rate



KEY TAKEAWAY

The U.S. economy continues to show signs of strength despite lingering inflationary pressures and high consumer prices.

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

Economic Update (cont.)

Inflationary pressures have moderated from their recent 40-year highs but are anticipated to remain above the Fed's target of 2% for some time. 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 ongoing opportunity for the Fed to pursue tighter monetary policy.

Markets are pricing in 5–6 quarter-point rate cuts this year (-125 or -150 basis points in total), while the Fed's median projection is for three (-75 basis points in total). Additionally, markets see a ~50% chance of the first rate cut in March, while the Fed itself sees the first cut later in the year, likely in September.

Volatility is expected to persist as investors balance the expectations for rate cuts with generally positive economic data.

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US Treasury Yields

Date & Yield

Tenor	12/30/22	9/29/23	11/30/23	12/29/23
1M	4.12	5.55	5.56	5.60
3M	4.42	5.55	5.45	5.40
6M	4.76	5.53	5.38	5.26
1Y	4.73	5.46	5.16	4.79
2Y	4.41	5.03	4.73	4.23
3Y	4.22	4.80	4.48	4.01
5Y	3.99	4.60	4.31	3.84

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" by holding short-term rates near current levels until CPI gets closer to their 2% goal.

Since early December, fixed-rate bonds appear very expensive, while floating-rate bonds appear unexpectedly cheap.

Focus on quality: We continue to see value in high-quality municipal bonds and tier-one (highest rated) commercial paper (where appropriate). Domestic banks, especially short-term corporate bonds, are an excellent alternative to traditional money market instruments and provide considerable yield pickup to commercial paper.

STRATEGY

At this juncture, we are focused on relative value between fixed and floating-rate instruments.

Florida LGIP Comments

FL FIT Preferred Deposit Pool:

Qualified Public Deposits (QPD) and FDIC-insured deposit yields have stabilized close to the federal funds rate and will closely track any future changes in the benchmark overnight rate. The FL-FIT PDP 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 year at 5.33%.

QTD/YTD return: +1.33%, 5.06%.

End of month yield: 5.28%.

FL FIT Cash Pool:

Strategically, we have added fixed-rate positions to lock in yields during Q4 while also taking advantage of relative value in floating-rate instruments. Geographically, we look to increase exposure to domestic issuers and seek out short-term corporate bonds as an alternative to commercial paper. Additionally, there continues to be ample liquidity from prime money markets, ultra-short-term bond funds and bank deposits. We expect the pool to continue to outpace the S&P 30-day LGIP index.

QTD/YTD return: +1.41%, +5.30%.

End of month yield: 5.57%.

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

We continue to focus on balancing liquidity while opportunistically taking advantage of market opportunities to lock in yields for the coming years. We see ample opportunities in fixed-rate securities but are also taking advantage of mispriced floating-rate instruments that will provide a relatively attractive yield no matter the interest rate environment. 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 Q4, we made the decision to tactically reintroduce the portfolio insurance (interest rate futures) to help insulate the portfolio. During Q2 to Q4, 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 towards 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 ~30 basis points over the last year. See below for further details.

Florida Floating NAV Pool Details†

As of 12/31/23, all return figures are %

FL Enhanced Cash:

PERFORMANCE

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

- December 2023 QTD/YTD %: (+1.77, +5.14).
- Benchmark: (+1.56, +5.16).

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: 5.05%.
- 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 ~0.60).
- Decrease floating-rate instruments over time (currently ~49% 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.

- December 2023 QTD/YTD: (+2.24, +4.62).
- Benchmark: (+2.51, +4.31).

STRATEGY

Continue to focus on high-quality instruments with call protection to protect 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 remains focused on yield maintenance for the long term.

- Yield at end of the quarter: 4.41%.
- Focus on total return for floating-NAV pools.

Targeted duration band of 1.00 to 2.00 years, currently 1.56 years.

- Increased duration as we extend maturities and lock-in yield.
- Continue to increase allocation to fixed-rate securities (~68% of portfolio).

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