Texas LGIP Strategy Update

Q2 2026

PREPARED BY

Dan Marro, CFA
Portfolio Manager

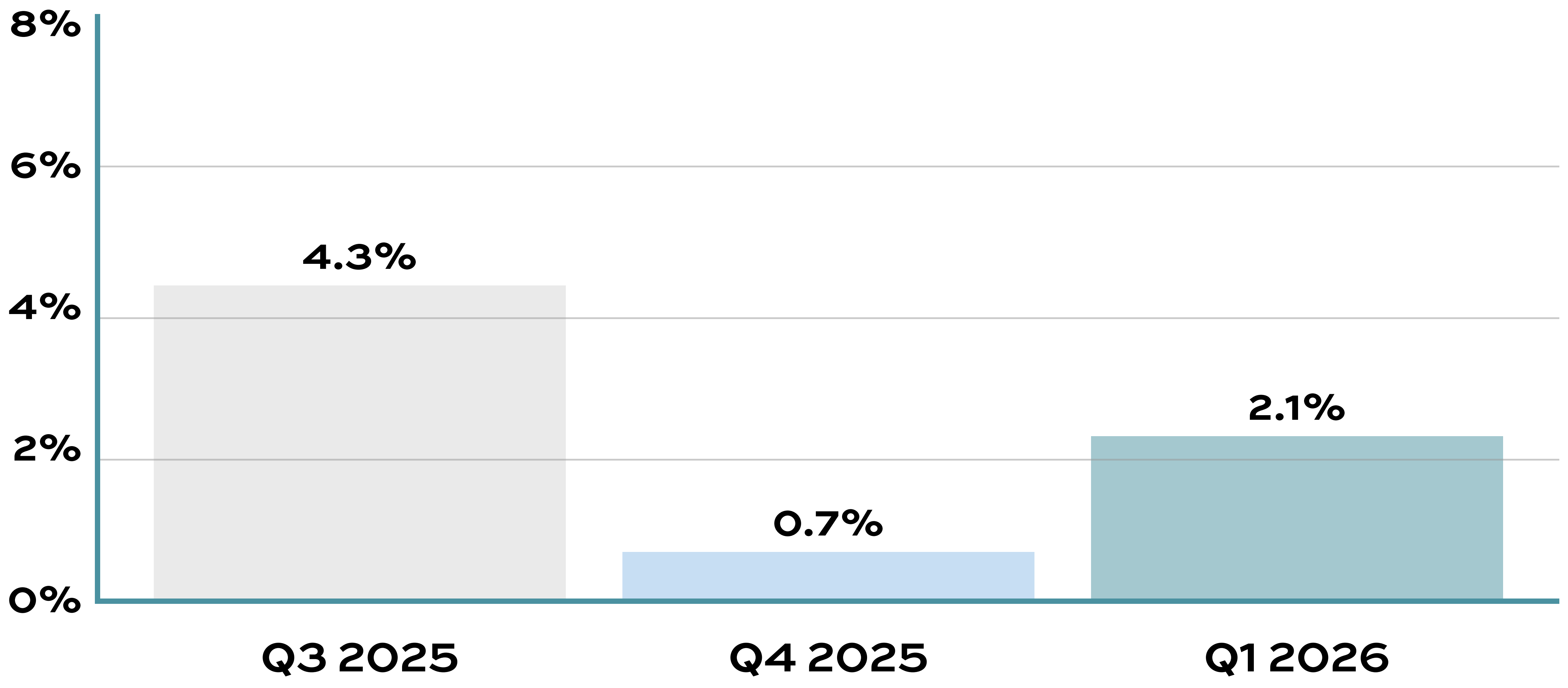
Vito Resciniti
Investment Strategist

Economic Update

The economy grew in the 1st quarter, with the third and final estimate of GDP coming in at 2.1% annualized, revised higher from the prior estimate of 1.6%. GDP growth was driven by sectors such as information, durable goods manufacturing, and related investment activity. A big part of the growth in the information / technology sector continues to be powered by investment in Artificial Intelligence, which has helped drive spending in software, research and development, and related infrastructure.

Nonfarm payrolls had come off a string of a few decent reports in a row, but for June, payrolls came in at just 57k, versus expectations of 113k, down from the May report. Nonfarm payrolls have been mixed overall this year, but the three-month average remains above 100k jobs per month. The unemployment rate, already near historic lows, actually dropped from 4.3% to 4.2% in June.

US GDP Growth Rate



Consumer and business spending continues to power the economy, supported by a resilient labor market and sustained investment from the ongoing AI buildout.

KEY TAKEAWAY

Growth remains positive. Q1's 2.1% marks a rebound from a Q4's 0.7% that was held down by the six-week government shutdown - a sign the underlying expansion remains intact.

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

DEEP BLUE
INVESTMENT ADVISORS

Economic Update (cont.)

The June 16–17 FOMC meeting was the first for new Fed Chairman Kevin Warsh. As expected, the Fed held rates steady at a 3.50%–3.75% range. However, the 2-year Treasury, a leading indicator for future Fed Funds rate movements, moved sharply higher following the meeting. What moved the market was not the rate decision itself, but the Fed's more hawkish messaging, as more officials indicated that rate hikes may be possible in the future. While the decision to hold rates was broadly expected, the shift in future rate projections and less clear forward guidance may lead to more market volatility.

In June, the May CPI report came in at 4.2%, in line with expectations but above the prior print of 3.8% and trending higher. What may be more notable is the move in PPI, or business input prices, which came in at 6.5%, above expectations of 6.4% and well above the prior print of 5.7%. PPI can be a useful signal of pipeline inflation pressure, indicating that higher CPI prints may be possible going forward. Time will tell how much of those higher input costs companies will pass on to consumers.

> **Inflation remains well above the Fed's 2% target - and with officials signaling higher-for-longer,** even possible hikes, the market has repriced yields higher.

US Treasury Yields

Date & Yield

Tenor	6/30/25	4/30/26	5/31/26	6/30/26
1M	4.28	3.72	3.72	3.70
3M	4.41	3.68	3.69	3.87
6M	4.29	3.71	3.78	4.01
1Y	3.96	3.72	3.79	3.98
2Y	3.72	3.88	3.98	4.14
3Y	3.68	3.91	4.06	4.15
5Y	3.79	4.02	4.13	4.19

Source: Treasury.gov, DBIA

LGIP Investment Strategy

The Federal Reserve swore in a new chairman, Kevin Warsh, who conducted his first FOMC meeting in June. Immediately, Fed officials shifted to a more hawkish tone as the market began pricing in the possibility of future rate hikes.

Due to the hawkish Fed pivot, the rate-cutting cycle appears to be over for now. This is reflected in the rapid advance of the 2-year Treasury, which moved from roughly 3.40% to 4.10% since March. With inflation still elevated and the labor market remaining resilient, the 2-year yield, which tends to lead expectations for the Federal Funds rate, has widened by approximately 34 basis points relative to the 3-month Treasury bill.

The widening spread between the Federal Funds rate / 3-month Treasury bill and the 2-year Treasury has created more attractive yields in the part of the curve where the duration of our pools generally falls. Our core strategy of anchoring portfolios with liquidity gives us the flexibility to add strategically in environments like this. Once safety and liquidity priorities are met, we can incrementally take advantage of current market dynamics.

Securities we continue to tactically add include Ginnie Mae floating-rate securities, fixed-to-floating corporate bonds with short expected final maturities, and callable agencies. By adding incrementally, or layering in transactions, we avoid the pitfalls of trying to forecast exactly where interest rates will move next.

KEY TAKEAWAY

The 2-year Treasury has surged past the Fed Funds rate — roughly 3.40% to 4.10% since March - signaling the market is now pricing in the possibility of future rate hikes rather than cuts.

STRATEGY

Our barbell approach anchors portfolios in high-quality, liquid securities while opportunistically adding relative value in cheaper sectors - layering in incrementally rather than forecasting the Fed's next move.

Texas LGIP Comments

TX-FIT Government Pool:

The performance remains anchored by FDIC Insured overnight deposits, alongside laddered securities in US Treasuries and Agencies, both fixed and floating rate. We continue to allocate to agency MBS with final maturities within one year, capitalizing on their yield pickup relative to comparable Treasuries and non-callable agencies. We expect this pool to continue to track the S&P LGIP 30-day index.

YTD net return: 1.75%.

End of quarter net yield: 3.58%.

TX-FIT Cash Pool:

The Cash Pool is composed of a diversified mix of high quality, short duration securities with a strong emphasis on liquidity sources. This high liquidity enables us to strategically allocate to longer duration opportunities such as short-dated agency MBS, floating rate MBS, callable agencies, and asset-backed commercial paper, that should continue to benefit the pool in a falling rate environment.
We expect the pool to track the S&P 30-day LGIP Index over time.

YTD net return: 1.95%.

End of quarter net yield: 3.89%.

Disclaimer

Contact Us

Ken Couch
ken.couch@deepblue-inv.com
(210) 240-9464

Ed Polansky
ed.polansky@deepblue-inv.com
(813) 992-3145