Investment Environment & Outlook

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Sabal Trust

Market & Economic Environment

The economy is akin to a living breathing entity that continually flexes up and down. Investor sentiment collides with policy influences and economic data to affect market pricing. From a numbers perspective, the 2nd quarter earnings season is almost complete and financial results from companies were nothing short of spectacular. Most companies exceeded revenue and earnings expectations. The rapid spread of the Delta variant poses a real threat and adds a new uncertainty to the investment environment. However, companies and individuals alike have demonstrated a resilience during the pandemic that is likely to be enduring.

CONSUMER CONFIDENCE

Consumer confidence measures the outlook of current economic conditions and future expectations. Confidence directly influences spending and economic activity. Even with continued stock market gains and additional fiscal relief measures, confidence levels plunged last month. The decline was related to concerns about the Delta variant's impact on the economy and higher inflation. Positive consumer sentiment is critical to support the economic recovery.

HIGH FREQUENCY DATA

High frequency data provides a granular look into broader trends and activities. The Delta variant appears to be influencing consumer behavior based on recent data readings. Specifically, the number of airline passengers moving through TSA security checks, OpenTable reservations, and hotel occupancy have trended lower over the last few weeks. Assessing future consumer-related data will provide additional signals into the sustainability of the economic recovery.

LABOR SHORTAGE

Even as unemployment levels remain elevated, the struggle to find qualified workers continues. These pressures could dissipate over time. However, labor shortages could result in wage inflation because tight labor markets force companies to increase compensation and benefits to attract job seekers. Labor costs represent ¾ of all input costs and a sustained move higher could signal a potential change in monetary policy.

INFLATION

July's core inflation (ex food and energy) slowed after surging +5.4% y/y in June which could signal a moderation of supply chain shortages. This would be consistent with the Federal Reserve's transitory inflation outlook. During the 2Q21 earnings season, companies across a wide range of industries and sectors reported materially higher costs. Only time will tell if these pressures are permanent or not. Future interest rates depend on the answer.

RETAIL SALES

Earlier this year, the $1,400 stimulus checks distributed by the Administration fueled broad-based sales. However, July's retail sales fell -1.1% as consumers pulled back spending on services and experiences. This spending softness along with the recent plunge in consumer confidence indicates clouds could be building on the horizon. The effect of the Delta variant on future consumer confidence and behavior will be important to monitor because consumer spending is a dominant influence of economic growth.

GEOPOLITICAL RISKS

Geopolitical risks can lay dormant for long periods of time. When and where they resurface is unpredictable. The unfolding tragedy in Afghanistan is a fluid situation and could serve as the spark to destabilize an already volatile region of the world. If tensions continue to escalate in the Middle East, the markets will take notice, especially if the region's energy complex is impacted.

Fixed Income Observations

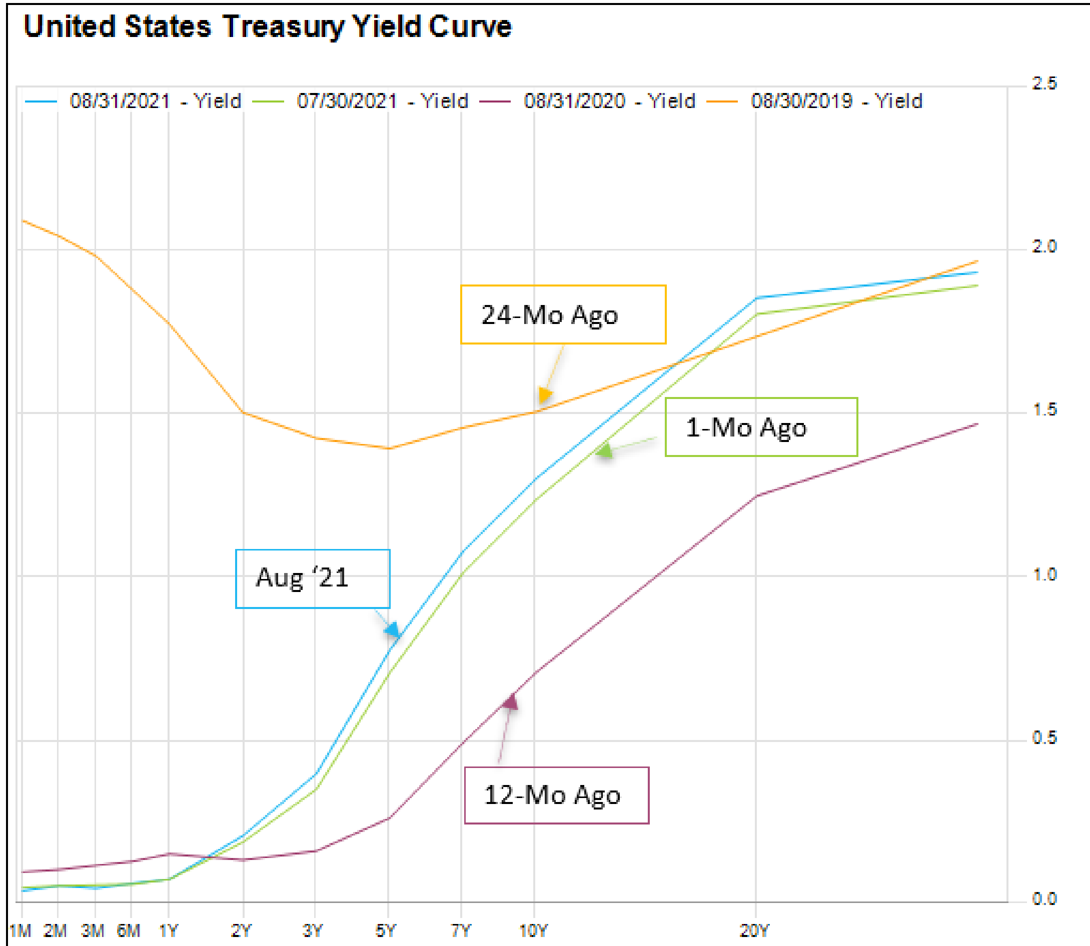
The Federal Reserve's Jackson Hole Symposium pivoted at the last minute and went virtual because of the surging Delta variant. Even as Chairman Powell reiterated continued progress toward their inflation mandate and recently expanded inclusionary employment goals, Delta was on everyone's mind. Markets continue to search for direction on rate policy and policy makers offered no timeline for asset tapering at the Symposium. It is important to note that reducing bond purchasing activity is not the same policy shift as raising interest rates. More time is required as market participants digest upcoming economic data and the true impact of the Delta COVID variant becomes apparent.

YIELD CURVE

- While corporate spreads continued to widen gradually throughout the month, the direction changed after the Jackson Hole Symposium. With interest rates hikes off the table for now, confidence returned to the credit markets. Investors, who were nervous before, rushed back into the corporate bond markets creating demand for Investment Grade as well as High Yield debt, pushing spreads to their tightest levels in almost two months.

- In August, Treasuries curve bear steepened, for the first time since March. The belly of the curve climbed 9 bps while the long end was up ~3-5bps. 30-yr yields closed the month at ~1.93% while the 10-yr yield rose to ~1.31%.

- The Tax-Exempt Muni curve also shifted higher like most other asset classes. AAA TE Muni's, currently yielding 72% of comparable treasuries, still remain expensive by historic standards.



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