Sabal Trust

Investment Environment & Outlook

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TRUST SERVICES | INVESTMENT MANAGEMENT | FAMILY OFFICE | ESTATE SETTLEMENT

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Market & Economic Environment

Investor enthusiasm shifted in August as the markets declined even as the Technology sector rallied +5.1% during the last 5 trading days of the month. Investors should be vigilant as September is historically a weak month for stocks. Since 1923, the S&P has declined on average by -1.1% during September. The upcoming Federal Reserve policy meeting and the G20 economic summit could also fuel potential volatility. Our equity strategy aims to minimize the downside risk against this type of backdrop. The Sabal Dividend Growth portfolio offers reliable and steady income from high-quality companies with track records of increasing their dividends to shareholders.

DEBT DOWNGRADE

Fitch's downgrade of the U.S credit rating reflects increased concerns over growing debt levels. The negative consequences of running persistent deficits are not trivial. Politicians continue to demonstrate their inability to prudently manage our government's finances. Absent a cohesive, long-term strategy to stabilize our nation's financial picture market volatility will remain a reality for investors.

MANUFACTURING

The manufacturing sector, highly correlated to the economy, remains weak and contracted for the 10th. consecutive month. Yet, there are signs of stabilization. Subsiding input costs are bringing relief to companies even as the shortage of workers remains a challenge. During earnings calls, companies discussed the more conservative management of inventory levels, which suggests a degree of uncertainty with the economic outlook.

PUSHING ON A STRING?

The Federal Reserve raised interest rates eleven times in their fight against inflation. Yet, elevated government spending continues to fuel price pressures. Are policy makers pushing on a string as fiscal spending counterbalances the economic impact of higher rates? The issues could become more pronounced as we enter in a highly charged Presidential election campaign process.

CONSUMER CONSUMPTION

Inflation impacts consumer spending. Senior management from Coke and P&G indicated on their recent earnings calls that conscious consumers are bargain hunting and purchasing products in bulk. Target and Home Depot leadership observed that consumers are spending more on essentials and consumables than on more expensive discretionary items. Looking ahead, consumers face challenges from higher energy prices and the resumption of student loan repayments. How consumer consumption changes will determine the economy's path for the balance of the year and into 2024.

HOUSING MARKET

In August, Mortgage rates reached new highs of the current cycle surpassing levels seen last fall. This places further strain on housing affordability as borrowing costs continue to push higher. However, housing prices have not declined due to the low supply of houses. Furthermore, many homeowners are staying in their homes. In part, they refinanced mortgages several years ago when rates were below 3%. Low mobility should benefit Home Depot, as homeowners remain in place and continue to remodel their homes, which was a trend that accelerated during the 2020 COVID lockdowns.

Interest Rate Observations

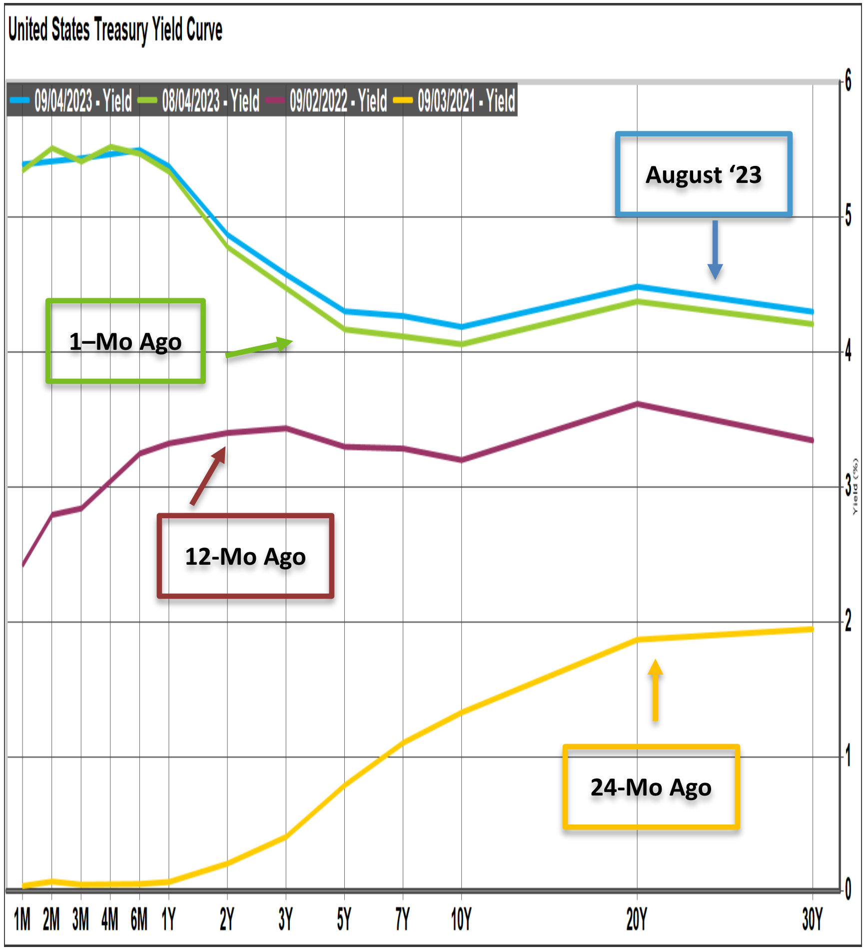
Federal Reserve officials remain committed to fighting inflation with interest rates at their highest levels in 22 years. Policy changes take time to impact the economy. The influence of the eleven rate hikes during the current cycle has not been fully realized. Policy makers expected higher rates to slow economic activity. Yet, persistent economic growth and a stubbornly tight labor market present a conundrum. Chairman Powell warned that more hikes are possible even if they cause economic distress. Investors must embrace the reality of higher rates for longer and the likelihood of unintended consequences as policy makers aggressively fight inflation.

YIELD CURVE

- While investors are not pricing in any policy changes during September's FOMC meeting, Federal Reserve officials continue to retain their optionality for future rate increases. This hawkish tone pushed yields higher across most fixed income assets last month creating downward pricing pressure for bonds. Adding to the uncertainty was Fitch's credit downgrade of U.S. sovereign debt, which highlights the fiscal headwinds that lay ahead.

- The spread between the 2-year and 10-year Treasuries remains deeply inverted. Earlier this year, the inversion touched lows not seen in decades, but has since narrowed. The early part of August saw spread improvement as Treasury issuance pushed longer dated yields higher. Higher long-term Treasury yields reflect investors pricing in higher rates for longer, elevated government bond supply, and concerns around U.S. debt sustainability. We are in the later stages of the rate tightening cycle, but any potential reduction of rates will be part of the 2024 narrative.

- Amid oscillating investor sentiment and yield volatility, we remain conservative in our outlook. We continue to focus on high quality credits across our clients' portfolio as we are able to lock in attractive coupons bolstering their annual income levels. We are also utilizing reviewing duration positioning and preparing for the time when we extend maturities.



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