FLORIDA SAFE INVESTMENT POOL

Economic Update

July 28, 2016

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Economic and Market Commentary

Economic Overview

During the second quarter of 2016, global financial markets experienced increased volatility. Investors were concerned about the overall growth of the global economy. Global growth fears sparked wider credit spreads and lower equity prices. In addition, the recent vote by U.K. residents to exit the European Union exacerbated the situation. In the U.S., incoming economic data point to a slow growth economy with fits and starts. The third revision of U.S. GDP growth came in at an annual rate of 1.1%, up from the previous reported 0.8% for the first quarter of 2016. This is below the 1.4% expansion experienced during the fourth quarter of 2015. This performance was largely driven by an increase in consumer spending, notably on housing, utilities and healthcare. Consumer spending which accounts for more than two thirds of the economy rose 1.5% from a prior estimate of 1.9%. Residential investment and state and local government spending also increased while business investment, exports and Federal government spending declined. To measure the pulse of the U.S economic environment, other important economic indicators to look at include inflation, productivity and unemployment.

Inflationary pressures in the U.S generally remain low, anchored down by low energy prices. However recently, prices have increased in certain sectors of the economy. Headline consumer prices as measured by the Consumer Price Index (CPI) rose 0.2% in May and 1.0% over the last 12 months. Core CPI which strips out volatile food and energy items increased 0.2% in May and was up 2.2% on an annual basis. The price increase was spurred by rising housing and medical costs. While both the headline and core CPI measures remain below the 2008 pre-financial crisis levels, we expect an uptick in price pressure if the momentum of economic growth continues and the labor market continues to improve.

Economic and Market Commentary

The labor market continues to improve, although at a slower pace. On average during the first quarter, the U.S economy added 195,000 jobs versus 231,000 jobs per month during the fourth quarter. The unemployment rate fell by 0.3% to 4.7% in May, mostly driven by a decline in the labor participation rate from 62.8% in April to 62.6% in May, the lowest reading in 2016 and close to a four decade low.

Taking a closer look at productivity in the U.S, there has been a steady decline over the past fifteen years. While it is difficult to determine why, it is interesting to note that income inequality has been on a steady climb. These two factors have led to hostility and frustration toward the elite and populist sentiment towards anti-establishment is on the rise. The political environment domestically and internationally is an area to monitor in coming months.

During the month of June, economic data were mixed. As a result, investors were left sitting on the sidelines in a wait-and-see mode awaiting further Fed guidance on timing of future rate hikes and the much anticipated Brexit referendum. At their June 15th meeting, the FOMC left short-term rates unchanged at a range of 0.25 – 0.50%. Speaking before the Senate Banking Committee in Washington on June 21st, Chairwoman Janet Yellen stated that "proceeding cautiously in raising the federal funds rate will allow us to keep the monetary support to economic growth in place while we assess whether growth is returning to a moderate pace, whether the labor market will strengthen further, and whether inflation will continue to make progress toward our 2 percent objective". While the Federal Reserve has a dual mandate of maintaining price stability and full employment, external factors from outside the U.S. continue to pose challenges to Fed's macroeconomic policies. Potential threats include uncertainty related to China's economic expansion and side effects from the recent U.K vote to leave the European Union. Going forward, we think the Fed will postpone their late summer rate hike to sometime later this year or early next year, as fears of weaker global growth have been fueled by the recent Brexit vote.

Economic and Market Commentary

The U.S economy appears strong relative to other developed countries and will likely lead global growth in 2016. Risks to financial markets include political uncertainties related to U.S. presidential elections and geopolitical shocks. Thus far, Brexit culprits include falling global equity markets, which could rattle confidence across the globe and a falling sterling pound against a stronger U.S. dollar. A stronger dollar would make U.S. exports more expensive. Lower exports could take a bigger bite out of economic growth.

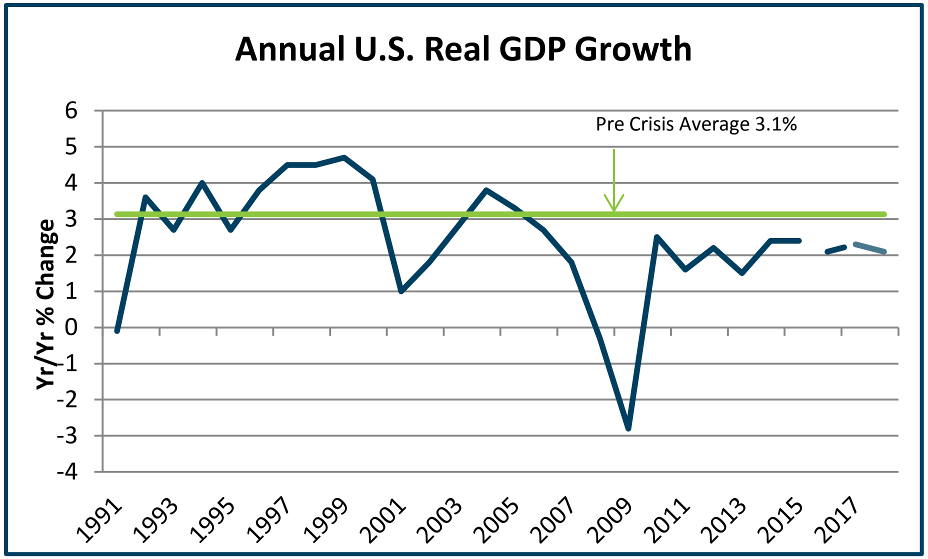
Economic Outlook

Annual GDP Growth

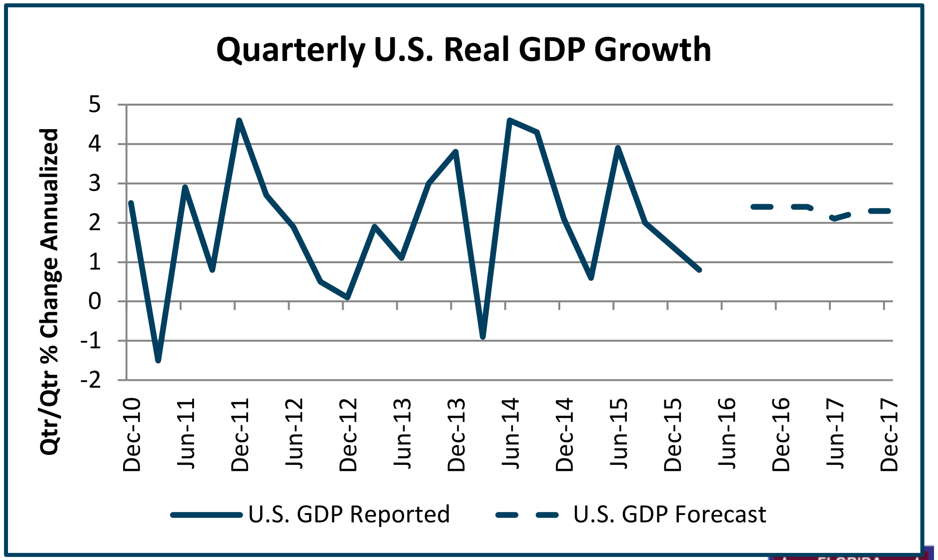
- Full year 2015 2.4%
- Stuck in secular stagnation
- Long term growth expected to remain below 3% average
- Pickup in CPI expected due to a recovery in energy prices and increasing labor costs.
- Global weakness continues despite negative European interest rates.
- Political unrest is surfacing with the rise of nationalism, and anti-establishment populism grows

Quarterly GDP Growth

- Q1 2016 0.8% annual rate
- Revised up from 0.5% preliminary estimate
- Improved personal consumption expenditures, residential fixed investment and government spending at the local and state level
- Non-residential fixed investment, exports and private inventory investments detracted

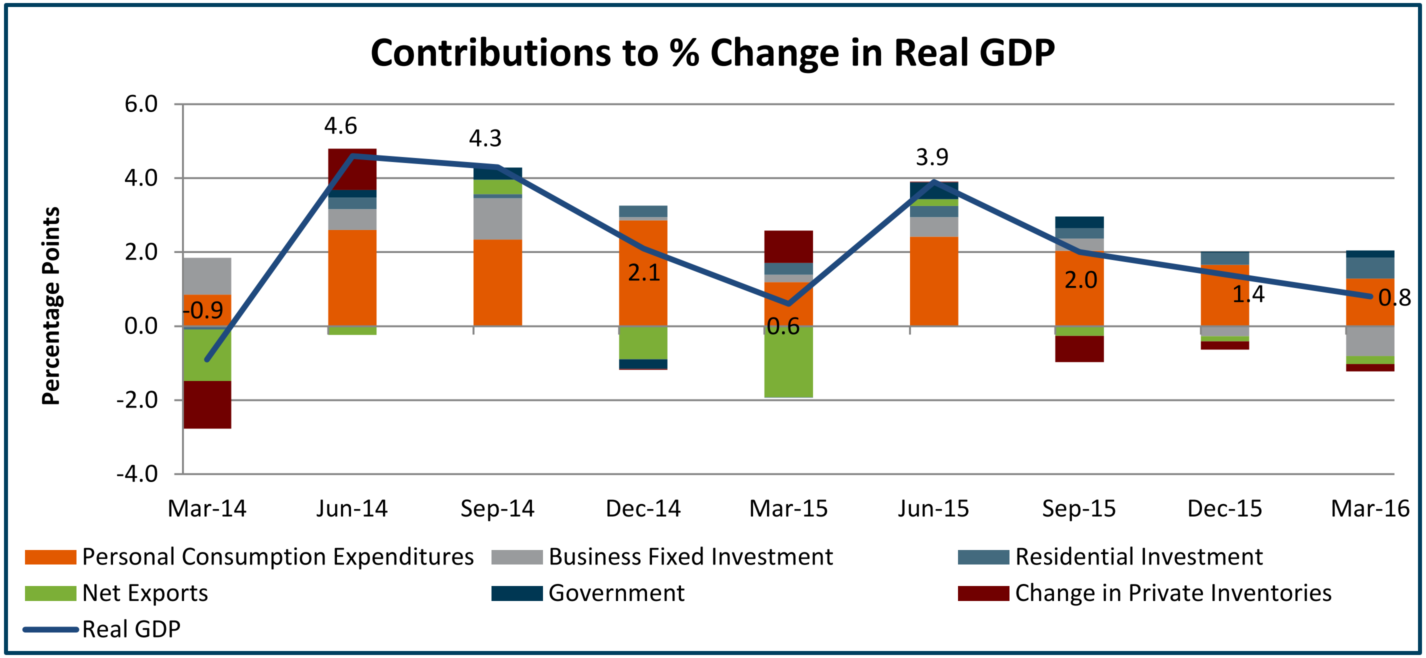


Source: Bloomberg



Source: Bloomberg

Economic Outlook



Source: Bloomberg

Contributing Factors to GDP

- Personal Consumption Expenditures have been declining
- Business Fixed Investment declined significantly in Q1
- Residential Investment is on the rise
- Government Spending has not been a significant contributor
- Exports have detracted less

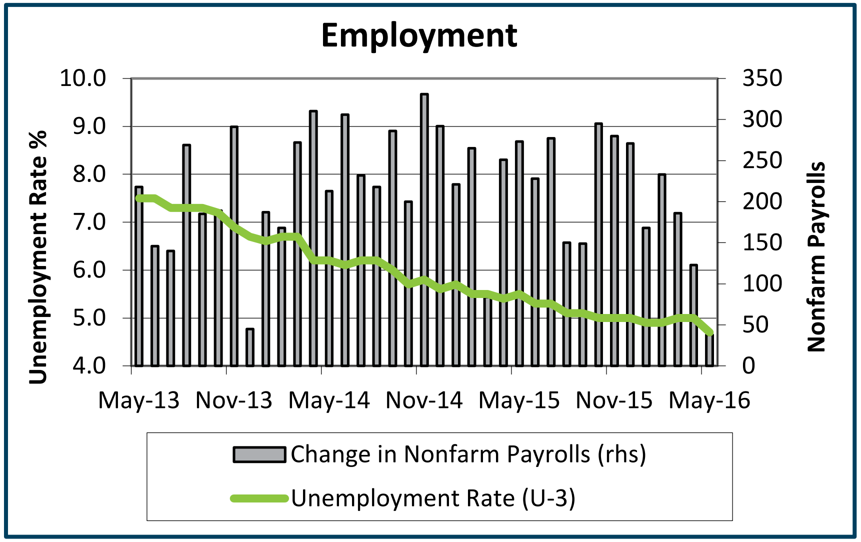
Employment

Employment

- Unemployment at 4.7% in May.
- Payrolls grew a meager 38,000 in May and averaged 195,000 during 1Q 2016 versus 231,000 for 4Q 2015
- Participation rate fell to 63% in May versus 66% pre-crisis.
- Key factor in allowing Fed moves later this year

Wages and Inflation

- Continued healthy wage growth above inflation rate
- TIPS market projects 1.43% inflation over the next 5 years
- Underlying inflation slowly rising supporting future rate increases by the Fed
- Tight job market could contribute to future wage inflation



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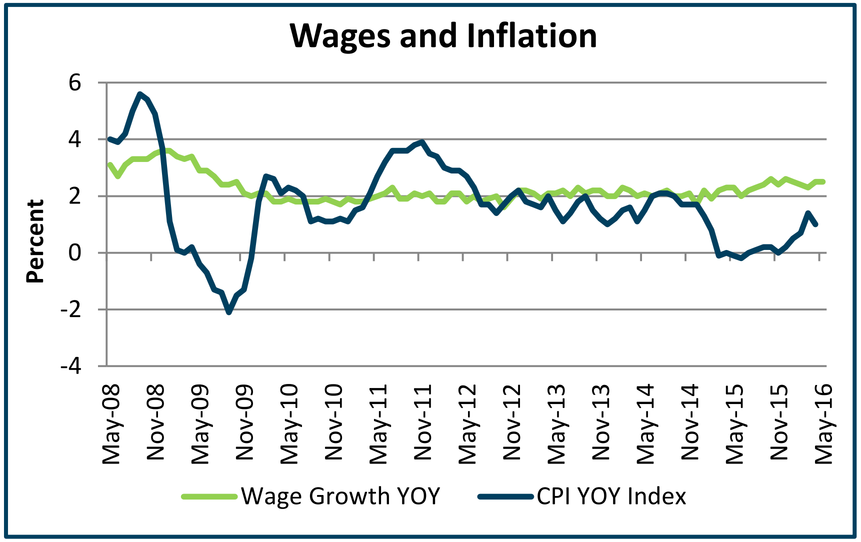

Source: Bloomberg

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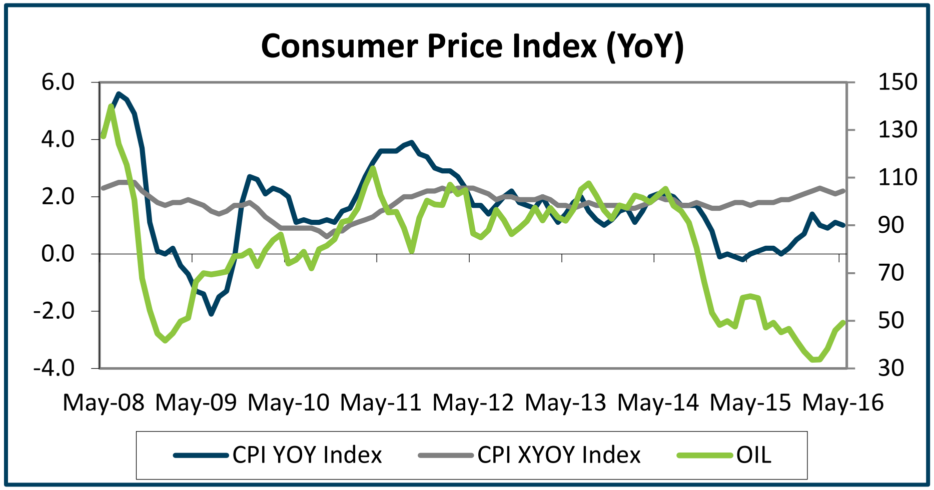
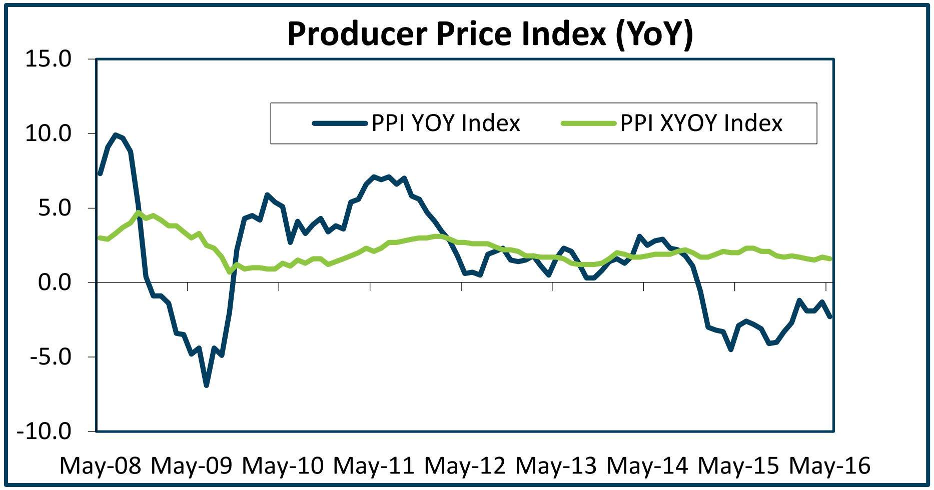
Consumer Price Index (YOY)

- Oil prices have recovered to $50/barrel
- Core CPI 2.2% for the past 12 months ended May
- Food prices have risen 0.7% over the past 12 months
- Energy prices have declined 10.1% over the past 12 months



Source: Bloomberg

- PPI measures prices the producers receive on their goods.
- Difficult to get top line revenue growth
- Core PPI excluding food, energy and trade services rose 1.2% in May year over year
- Gas Utility Index was down 4.7% for the past 12 months



Source: Bloomberg

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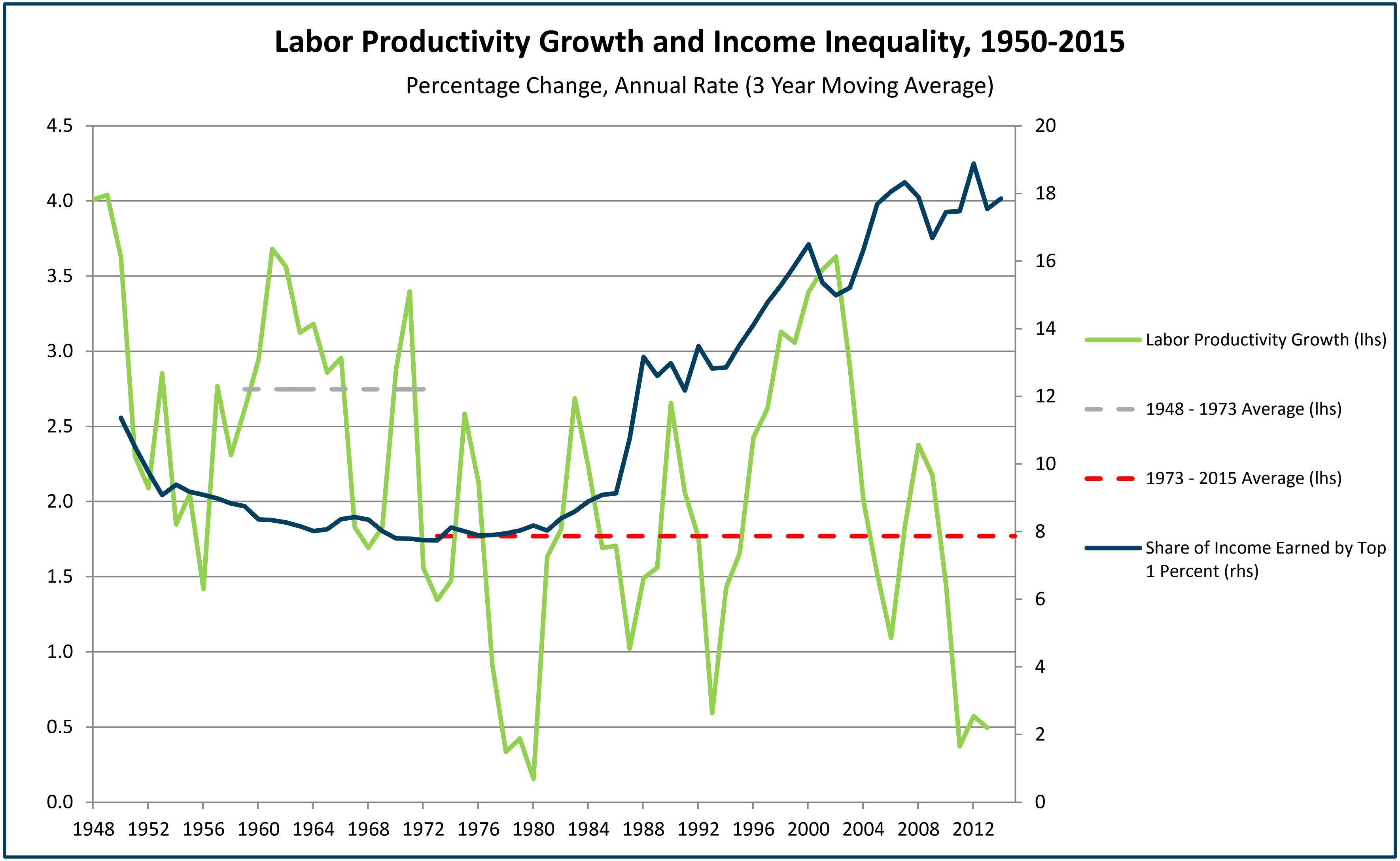
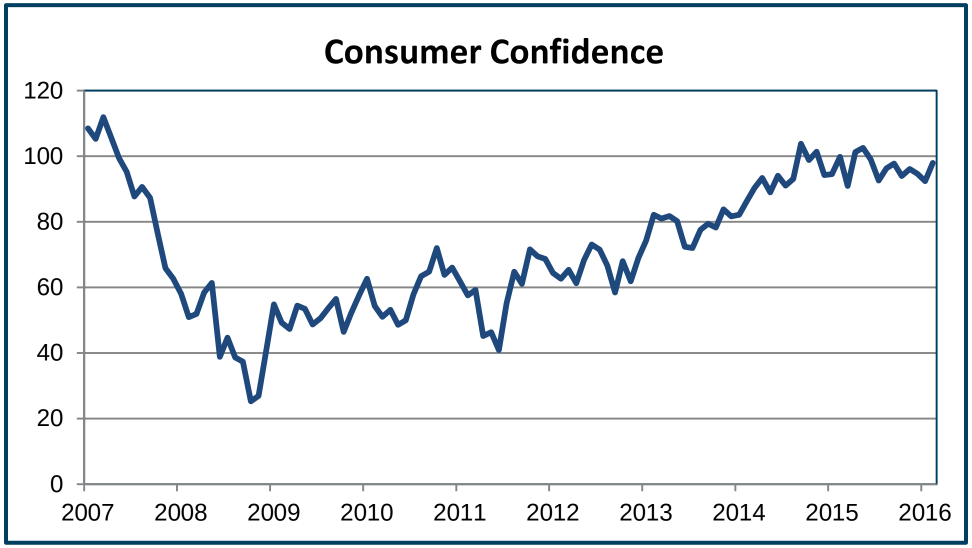
Economic Outlook



Source: St. Louis Federal Reserve, The World Wealth and Income Database

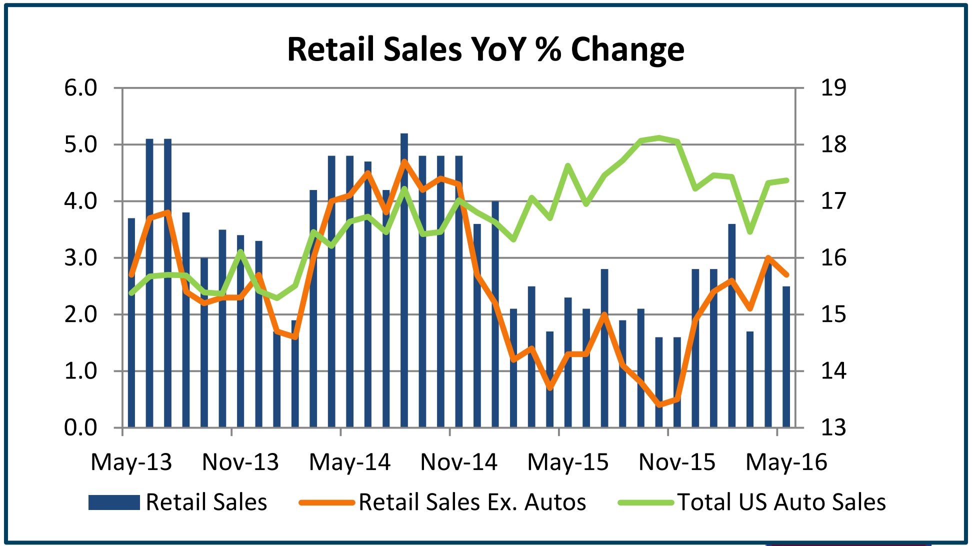
The Consumer

- Consumer sentiment rose to 98 in June from 92.4 in May
- Consumers more upbeat about jobs and income prospects over the next six months
- Remain optimistic about economic growth



Source: Bloomberg

- Retail sales rose 0.5% May following a 1.3% increase in April
- 9 out of 13 index categories showed increases in demand in May vs. April
- Auto sales quite strong
- Steady gains should boost economic growth



Source: Bloomberg

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