

Muni Fortnightly

FOMC Dot Plot and ending of “talking about talking about” tapering surprised markets and left real-yields substantially higher and the Treasury Curve flatter. Muni yields ended higher.

PWM Fixed Income Research

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Bottom Line:

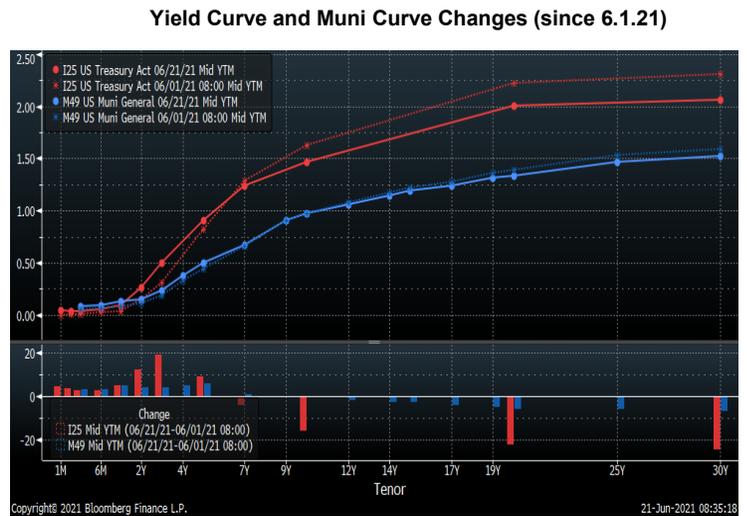
- Treasury yields become volatile post-FOMC meeting which was interpreted as relatively hawkish.
- State tax-supported debt rose 2.5% in fiscal 2021.
- Very positive state and local pension plan investment returns will allow for lower pension plan net liabilities to fall, cash outflows for funding pressure to be alleviated amidst low interest rates.

What Happened in the Bond Markets Last Week?

- The FOMC met and the fireworks punk has been lit. On Wednesday, the meeting concluded with the surprising revelation on Fed Funds expectations. Going into the meeting many thought that an incremental dot or two (on the Dot Plot) might indicate that one rate hike for 2023 was the central expectation but markets were surprised with two rate hikes for 2023 placed onto the plot's central expectation. Also, Chair Powell said that the FOMC seems to be done talking about talking about tapering and are now about ready to talk about tapering. You may think that this is silly semantics, but the Fed wants markets to know well in advance of when they will kick off their monetary stimulus tapering process so as not to shock markets. The Treasury market's reaction was a) very significant real-yield escalation (the inflation trade was if not busted, seriously bruised) with 5yr real yields lifting +25 bps (and 10yr real yields +~15 bps) mostly in one day and b) a significant Treasury curve flattening – with the 30yr dropping below 2.00% and the 10yr sliding below 1.4% all the while the 2yr Note has come back into play, lifting +10 bps.
- Municipal bonds' yields were higher, trailing Treasury yields by a noticeable margin. The 10yr AAA GO Ratio rose to 67.2.

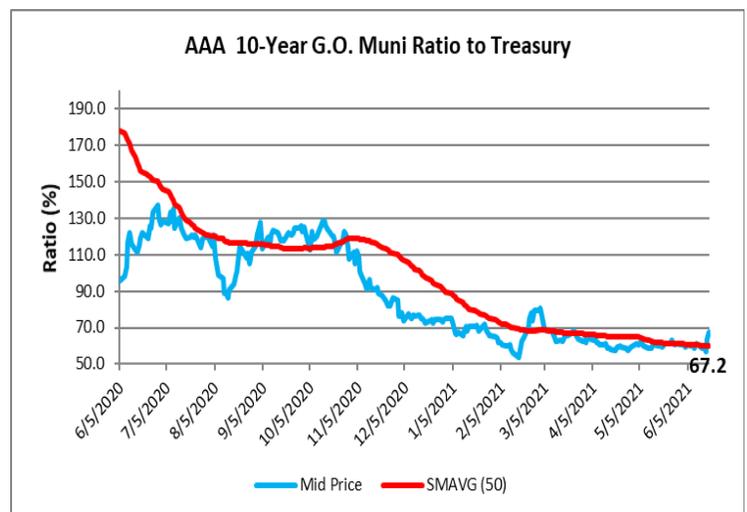
(Since 6/1/21)	Treasuries		Munis (Bloomberg AAA GO Index)		
	Tenor	Change (bps) - MTD	Yield (%)	Change (bps) - MTD	Yield (%)
3 mos.	+1.3	0.03%			
1 year	+3.5	0.05%	+4		0.13%
2 year	+10.5	0.25%	+4		0.13%
5 year	+13.1	0.88%	+8		0.47%
10 year	-1.5	1.44%	+8		0.96%
30 year	-12.9	2.01%	+6		1.52%

One can observe these changes by looking at how rates have changed along the curve for both the Treasury curve and for the AAA-rated G.O. Index since last week. The top panel shows four yield curves; two for the Treasury curve - one for the most current date and one from last week and two for the AAA-rated G.O. - current and last week. The bottom panel of the graph shows changes in the rates along both curves for the week for both Treasuries and the AAA G.O. Index.



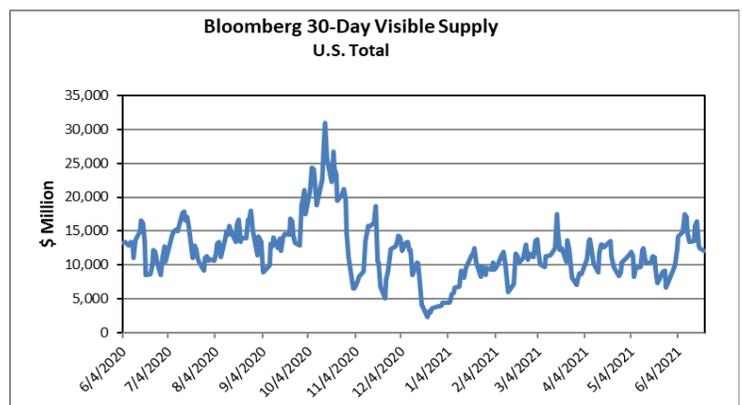
Data Source: Bloomberg

The line graph to the right shows the ratio of 10-year AAA-rated muni yields to the 10-year Treasury yield over the last year.



Data Source: Bloomberg

The Bloomberg 30-Day Visible Supply currently stands at \$12.0 billion. The year-to-date average is 10.8 billion and the 12-mo average is \$12.2 billion.



Data Source: Bloomberg

Articles of Interest

Muni Fund Flows: According to Refinitiv Lipper, muni funds had net inflows of \$1.85 billion last week. ETFs and high-yield funds had net inflows for the week.

State Government Debt Medians 2020 (Moody's): Moody's issued a Sector Profile report of the State Government sector noting the 2.5% increase in net tax supported bonded debt in 2020. The highlights of the report include: 1) most of the increase in the debt came from the states of New York, New Jersey and Illinois (already top ten in debt burden), 2) net tax-supported debt to personal income actually fell as income was bolstered by federal aid but unaided capacity to pay debt fell, 3) GO debt no accounts for 51% of state's outstanding debt, 4) pent up investment need for infrastructure could lead to more debt issued in the future.

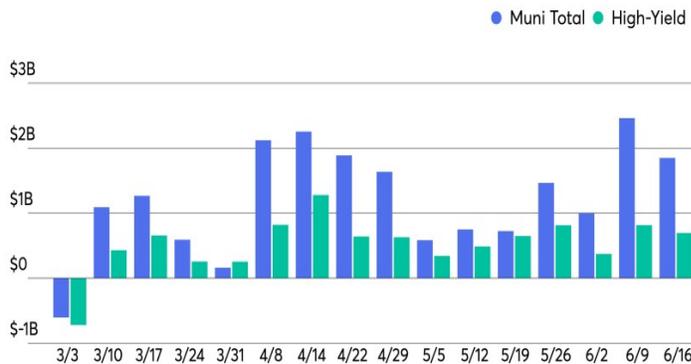
State and Local Pensions Benefit Investment Returns (Moody's): Moody's issued a *State and Local Government Sector Comment* discussing the "exceptional and potentially record-setting investment returns" the public pension system has enjoyed for fiscal year 2021. Investment returns will approach 25% to 30% if market conditions are maintained through the end of the fiscal year. The strength of the returns will improve near-term funding requirements and necessary cash outflows and will provide some relief to adjusted net pension liabilities. However, liabilities will remain elevated due to low interest rates.

Illinois Public School Funding Credit Positive (Moody's): Illinois K-12 public school districts received a boost from a Governor-signed budget which materially increases funding for education. Moody's calls this act a credit positive and will primarily benefit school districts classified as Tier 1 and 2 – including Ba3-rated Chicago Public Schools. The funding to date for Chicago Public Schools has helped to materially improve its financial position.

Puerto Rico:

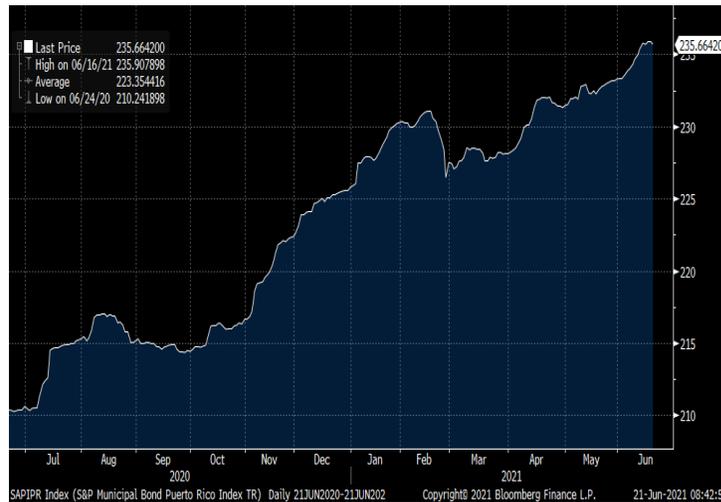
The S&P Municipal Bond Puerto Rico Index: finished at 235.7 vs. 233.3 at the beginning of June; +1.0%, +4.4% YTD

Refinitiv Lipper reports continued inflows



Source: Refinitiv Lipper (Includes ETFs)

S&P Municipal Bond Puerto Rico Index Level (1-year)



Source: Bloomberg

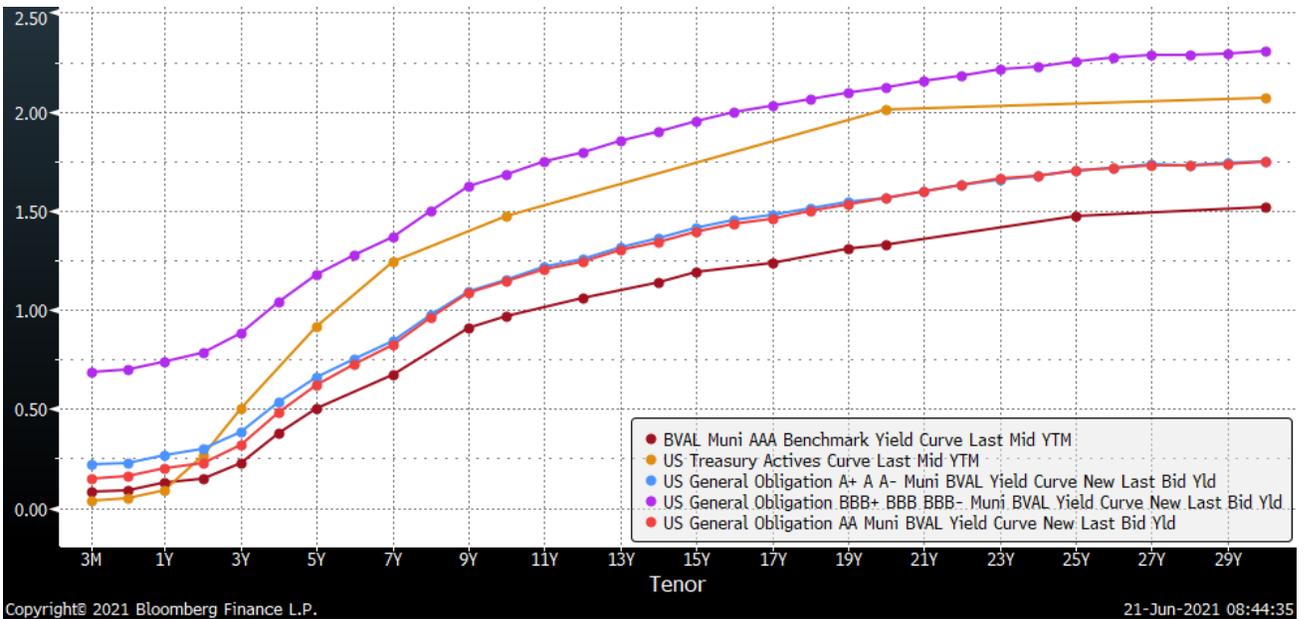
Relative Value by Maturity

AAA Muni Ratios and Spreads by Maturity - Data Source: Bloomberg

6/21/2021 Maturity (yrs.)	Yield-to-worst (%)		0% Tax Rate		35% Tax Equivalent	
	AAA Gen. Oblig.	Treasury	Spread (bps)	Ratio (%)	Spread (bps)	Ratio (%)
1	0.13	0.09	11.8	154.2	11.8	237.3
2	0.16	0.27	-2.3	59.3	-2.3	91.2
3	0.24	0.50	-12.8	48.2	-12.8	74.2
4	0.38	0.72	-13.3	53.0	-13.3	81.5
5	0.50	0.91	-13.6	55.2	-13.6	84.9
7	0.68	1.24	-19.9	54.6	-19.9	84.0
10	0.97	1.47	2.2	66.0	2.2	101.5
15	1.19	1.69	14.3	70.5	14.3	108.5
20	1.34	2.00	5.6	66.8	5.6	102.8
25	1.47	2.03	23.4	72.5	23.4	111.5
30	1.52	2.06	28.6	74.0	28.6	113.9

Relative Value by Rating

Muni Index Yield Curve by Credit Rating – Data Source: Bloomberg



For more information please contact your Financial Advisor.

Appendix – Important Disclosures

Some of the potential risks associated with fixed income investments include call risk, reinvestment risk, default risk and inflation risk. Additionally, it is important that an investor is familiar with the inverse relationship between a bond's price and its yield. Bond prices will fall as interest rates rise and vice versa.

When considering a potential investment, investors should compare the credit qualities of available bond issues before they invest. The two most recognized rating agencies that assign credit ratings to bond issuers are Moody's Investors Service ("Moody's") and Standard & Poor's Corporation ("S&P"). Moody's lowest investment-grade rating for a bond is Baa3 and S&P's lowest investment-grade rating for a bond is BBB-. Ratings are measured on a scale that ranges from AAA or Aaa (highest) to D or C (lowest).

The Bond Buyer 20-Bond Index consists of 20 general obligation bonds that mature in 20 years. The average rating of the 20 bonds is roughly equivalent to Moody's Investors Service's Aa2 rating and Standard & Poor's Corp.'s AA. The Bond Buyer 11-Bond Index uses a select group of 11 bonds in the 20-Bond Index. The average rating of the 11 bonds is roughly equivalent to Moody's Aa1 and S&P's AA-plus. The Bond Buyer Revenue Bond Index consists of 25 various revenue bonds that mature in 30 years. The average rating is roughly equivalent to Moody's A1 and S&P's A-plus. The indexes represent theoretical yields rather than actual price or yield quotations. Municipal bond traders are asked to estimate what a current-coupon bond for each issuer in the indexes would yield if the bond was sold at par value. The indexes are simple averages of the average estimated yields of the bonds, are unmanaged and a direct investment cannot be made in them.

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