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MUNICIPAL MARKET WEEKLY UPDATE

Wednesday December 23, 2020

Primary and Secondary Market Recap

By John Kozak, Managing Director and Head of Municipal Sales and Trading

DIVERGENT VIEWS

As we wind down the year, there are headlines that are indicative of larger themes in play that will drive the municipal market in 2021:

- Virus mutation expanding lockdowns globally
- $2.3 trillion stimulus & spending package approved by Congress

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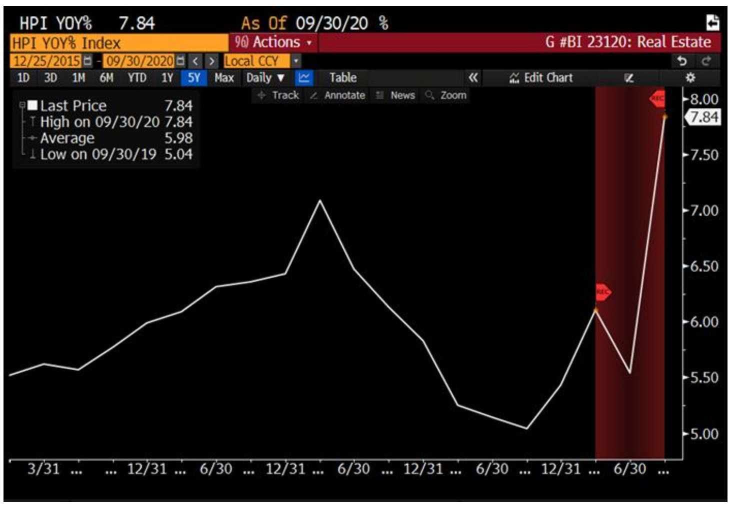
News stories like these summarize the two main driving larger economic questions. The lag effect of economies being shuttered has yet to be fully realized. This has suggested a muted recovery yet to come and has pushed global interest rates to low absolute levels as governments try to protect their economies. The unkowns as to the timing of worldwide immunization goes hand in hand with governments opening up the channels of commerce. One can easily argue that low rates and slow growth are here for the forseeable future.

More recently, some analysts have taken a differing view based on massive global stimulus. With a $2.3 trillion year-end spending bill and stimulus package on its way to the Oval Office, a US economic recovery in 2021 could drive up interest rates. In a twist on recent concerns, some feel that rising rates are a greater near-term challenge to munis rather than fundamental credit risk. While the recently approved spending/stimulus package is behing held up by the President, it is likely this bill (or one very similar) will get passed by December 28th. Furhtermore, President-Elect Biden told reporters on Tuesday that he will ask Congress for yet another stimulus package once he takes office in late January.

Housing Rebound Could Spur Economic Growth



This massive influx of stimulus could lead to rising interest rates in the form of a steeper yield curve. As rates rise, mutual funds could begin to see redemptions, which would add further pressure on the market. When investors see negative returns, outflow risks rise as forced selling due to mutual fund redemptions can often trigger a cycle of additional liquidations spread out across the broader market.

RATIOS AND THE RELUCTANT BUYER

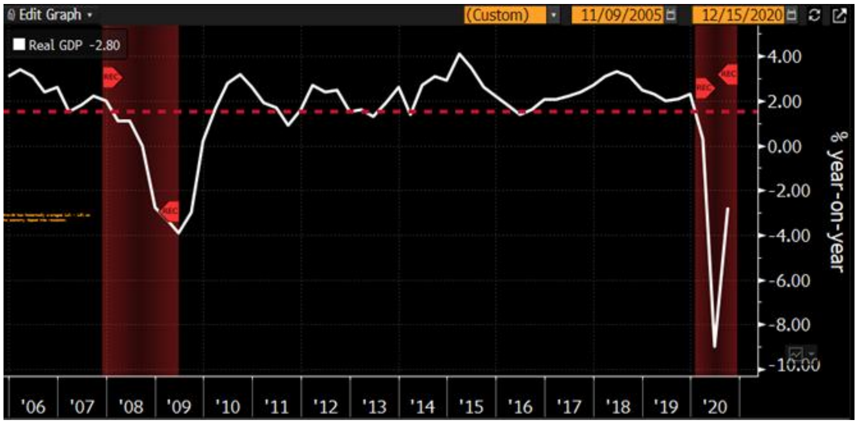
The municipal market has embraced this low interest rate environment with massive issuance. Yet rather than spur weakness in the market due to heavy supply, investors have poured money into the market creating a strong technical imbalance with even stronger demand. As we discussed last week, this technical imbalance has made munis at (or very near) their "richest" valuation as measuered against the US TRSYs. Many investors are reluctant buyers of municipal debt at these valuations. With ratios pointing to low relative value in munis and the possiblility of a quick economic rebound, one could argue there is an underlying sense of fragility in the market.

Muni Ratios are Extremely Rich

MUNI/TREAS	CURR %	AVG %
1yr/1yr	144.4	133.0
2yr/2yr	116.7	107.9
3yr/3yr	94.1	87.4
5yr/5yr	60.3	72.0
7yr/7yr	64.1	83.5
10yr/10yr	77.2	99.3
15yr/10yr	105.4	136.6
20yr/10yr	127.2	161.1
30yr/10yr	151.1	187.3
15yr/30yr	58.6	70.8
20yr/30yr	70.7	83.6

Something along the lines of inflows turning into outflows, a rapid and successful deployment of the vaccine, or surprsingly strong economic data cold be the trigger to a rapid rise in a very short time-period.

Real GDP Snapping Back



This will be our last market commentary of 2020. We will return with trade data beginning January 4th and with commentary on January 14th. Have a safe and merry holiday season!

NOTABLE AWAY PRINTS

Size ($m)	Issuer	Coupon	Maturity	Yield	Spread	Call Date	Insurance
Illinois							
265	RANTOUL IL GO	4.00	01/01/2026	0.90	68	01/01/2025	
California							
2050	LOS ANGELES CA DEPT	5.00	07/01/2045	1.21	-13	07/01/2030	
500	SANTA CLARA CNTY CA	5.00	08/01/2028	0.43	-8	08/01/2027	
1735	CA VAR PURP GO BDS	5.00	11/01/2031	0.88	10	11/01/2030	
Transportation							
500	ORANGE CNTY CA ARPT	5.00	07/01/2025	0.47	27	Non-Callable	
900	CHARLOTTE NC ARPT	5.00	07/01/2049	1.69	31	07/01/2029	
810	PA TPK COM TPK	5.00	06/01/2037	1.47	42	06/01/2027	

*Only includes bonds with call dates greater than or equal to 5 years from today