Municipal Bond Investor Weekly

High Net Worth Wealth Solutions and Market Strategies // Fixed Income Solutions

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THE WEEK AHEAD

1. Large Treasury auctions will set the tone for the market ahead of Friday's much anticipated CPI number.
2. Mean reversion? The divergence of muni and Treasury yields (muni lower / Treasury higher) has created concern for a muni sell-off, but redemptions and fund flows will provide countervailing pressure.
3. Fed Watchers look for other signals as the Fed blackout goes into effect ahead of next week's meeting.

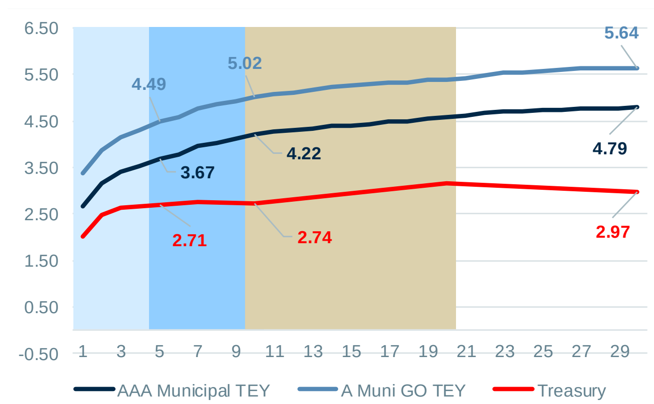
MONDAY'S COMMENTARY

THE NUMBERS THIS WEEK

Treasuries sold off (prices lower, yields higher) fairly sharply, with yields ending the week 14-24 basis points higher across the curve, with intermediate yields (5 to 10 years) all finishing the week +20 basis points higher. Municipal yields diverged from their taxable counterparts last week, as the entire benchmark AAA curve moved lower in yield, from 3 to 8 basis points. The slide lower was not entirely unexpected, as municipal yields are moving back towards a historically normal relationship to taxable yields.

Year		Treasury	Municipal (AAA)	Municipal (A)	Municipal TEY* (AAA)	Municipal TEY* (A)	Muni (AAA)/Tsy Ratio	Muni TEY* (AAA)/Tsy Ratio
1	2023	2.01	1.58	2.00	2.67	3.38	79%	133%
2	2024	2.47	1.86	2.30	3.15	3.88	75%	127%
5	2027	2.71	2.18	2.66	3.67	4.49	80%	136%
10	2032	2.74	2.50	2.97	4.22	5.02	91%	154%
20	2042	3.16	2.71	3.20	4.57	5.40	86%	145%
30	2052	2.97	2.83	3.34	4.79	5.64	95%	161%

**Taxable equivalent yield @ 40.8% tax rate*



Traditional ladder strategies (table on right) highlight opportunities along the curve, based on maturities. Duration focused strategies can extract additional yield available with longer maturities, while potentially mitigating risk with shorter calls. **Yield curve (upper right) highlights taxable equivalent yields.**

Maturity Range	Avg. Maturity	Duration	Yield to Worst	TEY*
1 to 5	3.0	2.78	2.13%	3.60%
5 to 10	7.5	6.33	2.58%	4.36%
10 to 20	15.0	8.03	2.94%	4.96%

**Taxable equivalent yield @ 40.8% tax rate. Assumes a 10-year call.*

JUNE REDEMPTIONS: IN A NEW YORK STATE OF MIND

Last week kicked off the unofficial start to summer with the Memorial Day Holiday, and for the muni market, that poses the question "will we have a drought this year?" The months of **June, July and August are traditionally the largest redemption months** in the muni market. And this year is no exception. Current data suggests approximately $114 billion of municipal bonds will either mature or be called over the three months from June 1 through August 31 – with $45 billion expected to come due in June alone. The summer months have historically seen "negative net supply" as the number of bonds being redeemed outpaced the number of new bonds being issued. In recent years, with 2020 being the exception due to the record breaking issuance and surge in taxable issues, we've seen "deficits" in the ~$20 to ~$40 billion range. Bloomberg forecasts indicate we could see a "deficit" of close to $27 billion – and that could increase as we progress through the summer.

June is traditionally one of the largest debt service payment months for New York municipal bonds. New York issuers rank second in municipal issuance with $449 billion in bonds outstanding and $23 billion issued year-to-date (Bloomberg). **New York, The Empire State**, is the fourth largest state in the country by population (home to ~20 million residents, with ~44% living in NYC, the most populous city in the United States, and another 14% on Long Island) and the 27th largest state by area. The state of New York's credit rating was upgraded by Moody's in April 2022; it is currently rated Aa1/AA+ with a stable outlook by both Moody's and S&P. The state's credit strength comes from its large and diverse economy with high income levels (120% of the US average), a well-funded pension system, and an extensive business environment that attracts a highly educated and global workforce. While the state relies on the financial sector for a higher-than-average proportion of income and continues to face uncertainties from the pandemic regarding the recovery of the office-intensive New York City metropolitan area, the key driver of the state's economy, outmigration trends, and related risks with the financially-strapped and heavily indebted Metropolitan Transportation Authority (MTA), a unit of the state, agile financial management, federal stimulus aid, and strong tax collections have combined to produce a surplus and build the state's reserves, with the state projecting a multi-year period of extremely strong cash balances.

Interestingly, only about 3% of New York State's debt is in the form of general obligations bonds. Instead, New York relies primarily on personal income tax and sales tax backed bonds for its financing needs – common issuers of this debt include the New York State Dormitory Authority and the New York State Urban Development Corporation. Despite the lack of New York state general obligation bonds, these issuers provide investors an opportunity to buy liquid, **high quality New York State bonds**. So how does New York trade compared to other states? One way we measure "cheap/rich" in the muni market is relative to the AAA pricing curve. Currently the Bloomberg Benchmark 10 year yield for generic AAA rated 5% coupon paper is 2.45%. For New York (Aa1/AA+), 10 year paper is 2.56% (per Bloomberg) - 11 basis points "cheaper." (For comparison, Virginia (Aaa/AAA) 10 year paper is the richest, at 3 basis points through the scale at 2.42%; Illinois (Baa1/BBB+) is the cheapest at 122 basis point over the scale, 3.67%.) New York investors in the top tax bracket could benefit even more from purchasing New York munis because they are exempt from both federal **and** state tax – a 2.56% tax-exempt yield equates to a taxable equivalent yield of 5.08%. New York City residents may benefit even more, getting a **"2 for 1"** tax advantage with New York munis – the taxable equivalent yield for 10 year NY munis is 5.50%, more than double the tax-exempt yield! Even more yield can be achieved with "kicker" structures – high coupon callable bonds sold at a premium. Let's look at a current New York offering as an example.

CUSIP Asset	Curr Face	Mdy / S&P (Underlying)	Issue Description	Coupon Maturity	Mkt Px Duration	Px To	Date	Yield	ATY	TEY	Principal Accrued Int	Net Money Settlement
650036CF1 *Muni*	100 *100.00%*	Aa1/- *(Aa1/-)*	NEW YORK ST URBAN DEV CORP REV Callable 09/30@100 - Material Events	5.000% *03/15/2044*	113.200 6.797	*Next Call* *Maturity* *Curr Yield*	09/15/2030 03/15/2044 -	3.172% *(w)* 4.079% 4.417%	3.172% 4.079%	6.296% 8.096%	$113,200 $1,153	$114,353 06/08/2022

ATY/TEY calculations use a Fed Tax rate of 40.80%, a Cap Gains Tax rate of 23.80%, a State of NY, and a State Tax rate of 8.82%.

**Not a recommendation. For illustrative purposes only. Prices and yields are subject to change.*

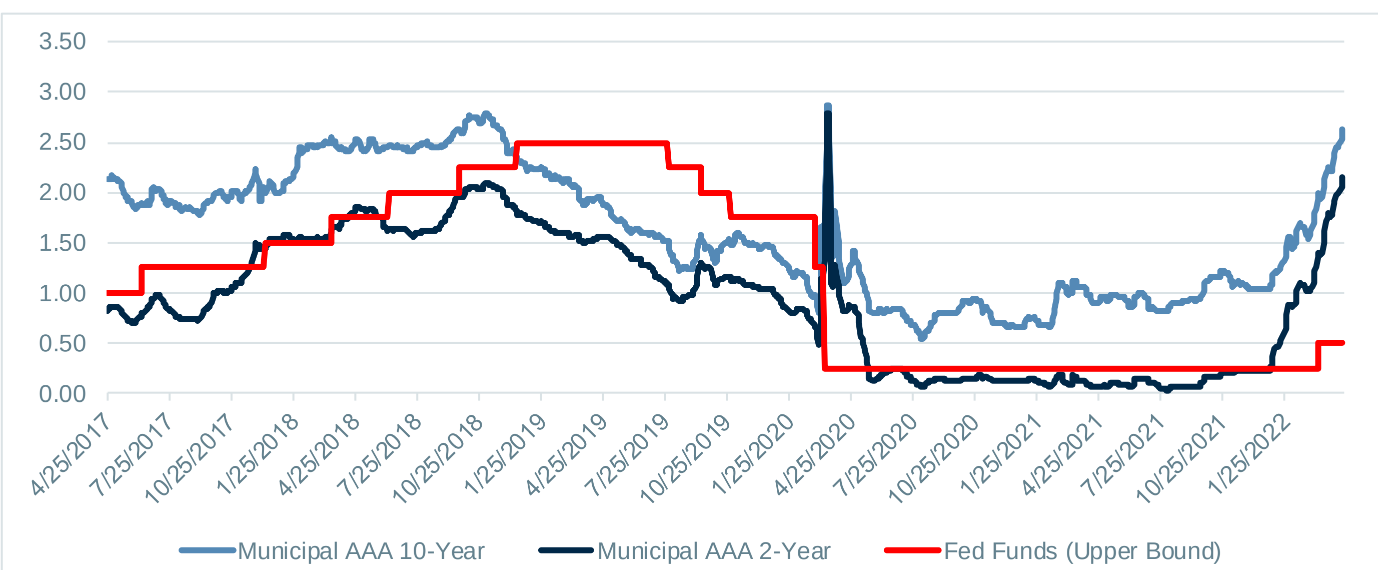
This New York personal income tax revenue “kicker bond” has a 5% coupon with a call date in ~8 years and a final maturity in just under 22 years. The yield to call is 3.17% - that is 84 bp over the AAA scale in 2030; that equates to a taxable equivalent yield of 6.29% (based on a New York state resident in the top tax bracket). Although it’s not likely the bonds will make it to maturity, the yield to maturity is 4.07% - 135 bp over the AAA scale in 2035; that equates to a taxable equivalent yield of 8.09%. As you can see, because of the double tax-exempt benefit residents from high tax states receive when buying municipals from their state, this bond’s taxable equivalent yields would provide New York investors with almost two times the tax-exempt yield.

What does all of this mean for municipal investors? Quite simply, demand (from reinvestment of matured and called bonds) is likely to exceed supply (new issues) and economic fundamentals tell us what that usually means: bond prices rise and bond yields fall. These muni market supply and demand dynamics are not likely to change over the course of the summer. Given these dynamics, we would expect that municipal yields would lag at any movement in Treasuries. When that happens, munis become “more expensive” relative to Treasuries. We measure that by comparing the yield on municipals to the yield on comparable Treasuries. For the past five years, the 10 year ratio has averaged ~88%, however, over the past year that ratio averaged 77% and was as low as 56%. After hitting a recent high of 104% in April, that ratio has declined to 83% – and could likely stay in that range if we have a “drought.” While that ratio is a little “expensive” on a historical basis, it is still above the average over the last year, and munis continue to provide tax-efficient relative value for investors in the top tax bracket, as can be seen in the example above. So when redemption money is available to reinvest, don’t wait - opportunities may be limited. Fixed Income Solutions is available to work with your financial advisor to help you weather any market conditions that may develop this summer!

NAVIGATING TODAY’S MARKET

The Bond Buyer is expecting $6.5 billion in municipal new issuance this week. Some of the larger deals expected include: the State of Maryland (Aaa/AAA/AAA) is selling $1.05 billion in general obligations bonds, including both taxable and tax-exempt series; Atlanta, GA (Aa3/-/AA-) is issuing $578 million of both AMT and non-AMT general revenue airport bonds; the Public Finance Authority, WI (-/AA-/AA) is selling $255 million of Cone Health healthcare system revenue bonds, with both taxable and tax-exempt portions; the Texas Water Development Board (-/AAA/AAA) is bringing a $254 million state revolving fund revenue bond deal to market; the West Valley-Mission Community College District, CA (Aaa/AAA) is bringing a $239 million deal to market; and Harris County, TX (Aa2/-/AA) is selling $201 million of toll road first lien revenue refunding bonds. See table below for additional new issuance.

HISTORICAL YIELDS



Date	Amount	Issuer	ST	Description	Moody's/S&P/Fitch	Maturity
6/6	$16MM	City of Sachse	TX	General Obligation Bonds	Aa2 /AA+ /	2/15/2023-42
6/7	$200MM	Prosper Independent School	TX	Fixed Rate Unlimited Tax School Building	Aaa / / (Aa3 / /AA-) PSF	02/15/2023-53
6/7	$161MM	New York City Housing	NY	Multi-Family Housing Revenue Bonds	Aa2 /AA+ /	05/01/2026-
6/7	$130MM	New Hampshire Municipal Bond	NH	2022 Series C Bonds	NR /AA+ /NR	8/15/23-52
6/7	$40MM	Minnesota Rural Water Finance	MN	Public Projects Construction Notes Series	MIG-1/ /	12/1/2023
6/7	$2MM	Massachusetts Housing Finance	MA	Housing Bonds, 2022 Series A (Non-AMT)	Aa2 /AA /	06/01/2025-34
6/7	$24MM	Massachusetts Housing Finance	MA	Housing Bonds, 2022 Series A (Non_AMT)	Aa2 /AA /	06/01/202434,37,42,
6/7	$49MM	Massachusetts Housing Finance	MA	Housing Bonds, 2022 Series A (Non-AMT)	Aa2 /AA /	06/01/2024-26
6/7	$54MM	Lansing School District (Ingham,	MI	2022 School Building and Site Bonds,	/AA / (/A /)	05/01/2024-47
6/8	$50MM	Warren Consolidated SD (Macomb	MI	2022 School Building and Site Bonds (ULT-	/AA / (/BBB+ /)	05/01/2023-42
6/8	$42MM	Virginia Housing Development	VA	Rental Housing Bonds 2022E	Aa1 /AA+ /	6/1/2025
6/8	$35MM	Pasco County, Florida	FL	Half-Cent Sales Tax Improvement	NR /AA+ /NR	10/1/34-51
6/8	$32MM	Los Rios Community College	CA	2022 Refunding General Obligation Bonds	/AA /	08/01/2022-30
6/8	$147MM	Conroe Independent School	TX	Unlimted Tax School Building Bond	Aaa /AAA / (Aa1 /AA+ /)	02/15/2023-47
6/8	$42MM	Anna Independent School District	TX	Unlimited Tax School Building Bonds	/AAA / (/A+ /) PSF	2/15/2024-52
6/9	$4MM	Schley County School District	GA	General Obligation Bonds, Series 2022	Aa1 / / (A2 / /)	2/1/24-33
6/9	$36MM	Ridley School District, Delaware	PA	General Obligation Bonds, Series of 2022	A1 /AA / (/A- /) BAM	11/15/24-42
6/9	$27MM	Ernest N. Morial New Orleans	LA	Special Tax Refunding Bonds	/ /AA+	7/15/2023-27
6/9	$14MM	Crawford AuSable SD	MI	2022 School Building and Site Bonds ULT	/A+ /	
6/9	$5MM	City of Mesquite	TX	Combination Tax & Limited Surplus	Aa2 /AA /	2/15/2023-42
6/9	$27MM	City of Mesquite	TX	Combination Tax & Limited Surplus	Aa2 /AA /	2/15/2023-42
6/9	$28MM	Bethlehem Authority, Pennsylvania	PA	Guaranteed Water Revenue Bonds, Series	NR /AA /NR (/AA- /) BAM	11/15/29-37

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Sourced from Bloomberg: Treasuries: US Fed H15 CMT Curve - The H15 curve is comprised of the constant maturity treasury rates as published daily by the Federal Reserve in the H15 report. Municipal (AAA): BVAL Municipal AAA Yield Curve (Callable) - The curve is populated with high quality US municipal bonds with an average rating of AAA from Moody's and S&P. The yield curve is built using non-parametric fit of market data obtained from the Municipal Securities Rulemaking Board, new issues, and other proprietary contributed prices. The curve represents 5% couponing. The 3 month to 10 year points are bullet yields, and the 11 year to 30 year points are yields to worst for a 10-year call. Municipal (AA): US General Obligation AA Muni BVAL Yield Curve - The BVAL curve is populated with pricing from uninsured AA General Obligation bonds. Municipal (A): US General Obligation A+ A A- Muni BVAL Yield Curve - The BVAL curve is populated with pricing from uninsured A+, A, and A-rated General Obligation bonds. Fed Funds (Upper Bound): The federal funds rate is the short-term interest rate targeted by the Federal Reserve's Federal Open Market Committee as part of its monetary policy. US Treasury securities are guaranteed by the US government and, if held to maturity, generally offer a fixed rate of return and guaranteed principal value. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance.

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