

# MUNIWATCH

## FIXED INCOME MARKET UPDATE



**Our monthly report is delayed this month so we could incorporate the results of the State and National elections. We have added a “State of the States” section to track spreads on individual State GOs and will highlight material spread narrowing or tightening.**

In October, Muni yields crept higher, rising by 6-9 bps across the curve, echoing the move higher in US Treasury yields. Muni Mutual funds recovered from a single week of outflows and took in over \$5 billion for the month. After the election results were announced, how-ever, both Muni and U.S. Treasury yields fell dramatically as expected gridlock in the split legislature diminished the prospects of a massive stimulus package and higher inflation. The main story in Munis was record monthly supply in October as issuers rushed to market prior to the election.

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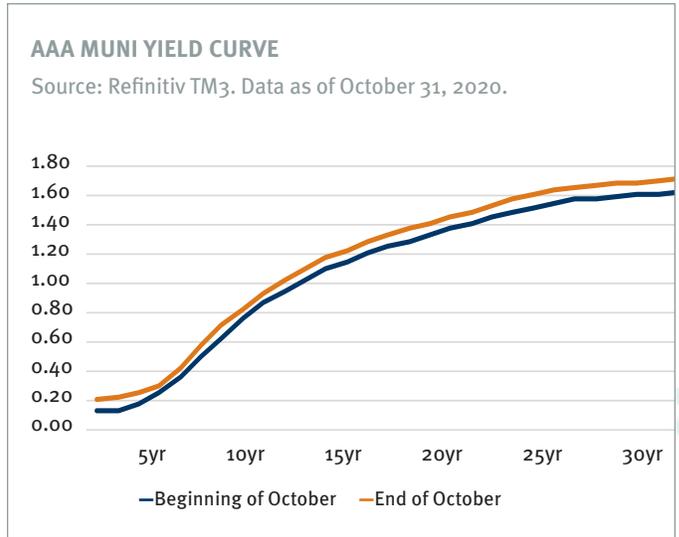
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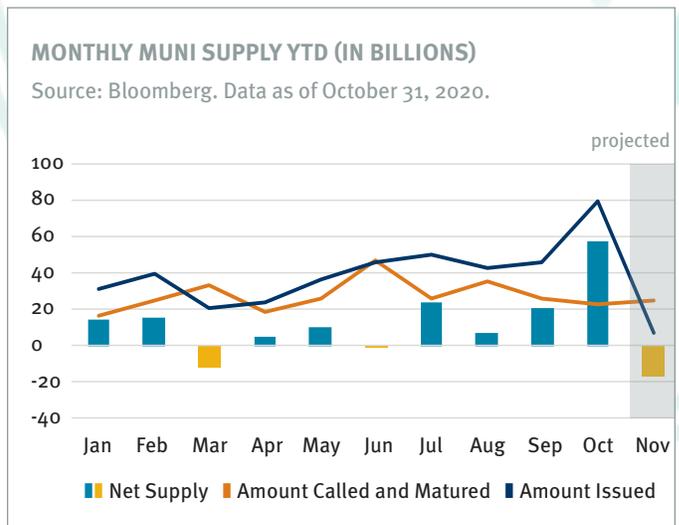
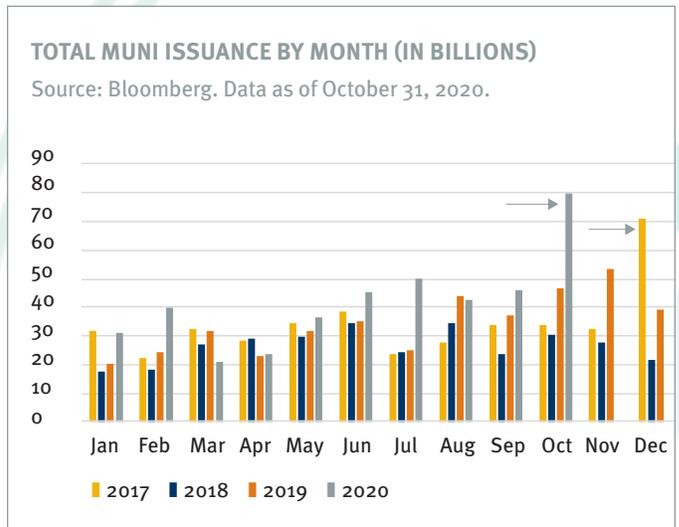
**Muni Yields Rise**

Muni yields rose by 6-9 bps in October (graph, top-right), a parallel shift of 8-9 bps in all but the 5-year area of the curve. After the House and Senate elections appear to result in a split legislature, the market has rallied as the fading likelihood of a massive stimulus package eased inflationary pressures and turned the focus to the Federal Reserve (Fed) for economic action. The expected gridlock decreases the ability of either party to enact significant regulatory changes.



**Muni Supply Surges**

Muni issuance in October was the highest ever at \$79 billion, beating the prior record in December 2017 of \$71 billion (graph, middle-right). Issuers rushed to market prior to the election to lock in low rates before potential changes in tax policy can be put into place and while economic uncertainty remains high. Net supply (amount called or matured subtracted from amount issued) exploded in October to +\$57 billion but as issuance decreases in November, net supply is expected to fall to -\$18 billion. (graph, lower-right). As we mentioned in our previous report, the increased supply in October presented an attractive opportunity, to invest in Munis. Also recognizing this opportunity, investors added over \$5 billion to Muni Mutual Funds in October, recovering from a single week of reported outflows at the end of September, according to Lipper. With rates at such low levels, we remain cautious and continue to emphasize careful sector and individual credit selection.



## STATE OF THE STATES



### Highlights

Since starting the year at historic lows, credit spreads hit extreme highs during the pandemic-driven market dislocation in March and April, and have since returned to more normal levels. Seemingly all Muni credits have experienced spread widening year-to-date but States who entered the crisis with strong fiscal management have been able to so far make their way through.

**Illinois:** While Illinois was in questionable fiscal shape prior to the pandemic, its finances have declined further and it has been the only State to access the Fed's Municipal Liquidity Facility. Illinois' prospects were looking up in October, however, as the State priced a new issue at spreads roughly 100 bps narrower than recent trades in the secondary market. After the State voted down a proposed graduated income tax, which would have increased income tax revenue over the current flat tax, spreads widened about 50 bps due to the perceived increase in credit risk. We expect spreads to remain elevated until more definite fiscal plans are presented.

**New Jersey:** Another "problem state" even prior to the pandemic, New Jersey's economy was hit hard during the first wave of shutdowns. The state has been proactive in making budget cuts to alleviate some credit concerns but its first test of the market since the start of the pandemic, a \$3 billion new issue this week, will provide better price clarity. While this new issue should have strong demand in the market, we expect spreads to widen further given its size as one of the largest deals of the year.

\* Proxy Issuer used.

States with insufficient GO debt or lack of Proxy Issuer: MO, AL, IA, AR, NM, WV, AK, ME, ND, ID, SD, MT, VT, WY

### STATE GO 10YR YIELD AND SPREAD TO AAA (In Order of Outstanding GO Debt)

Source: Bloomberg. Data as of October 31, 2020.

State	Yield on 10yr Maturity (%)	Current Spread to 10yr AAA Muni (bps)	3-Mo Change in Spread (bps)	YTD Change in Spread (bps)
CA	0.68	5	16	17
NY	0.75	13	-6	11
TX	0.76	14	1	3
IL	2.82	220	56	146
FL	0.69	7	-3	-5
PA	1.03	41	-5	7
NJ	1.47	85	5	40
OH	0.71	8	1	-2
MA	0.75	13	2	8
WA	0.74	12	5	2
MI	0.85	23	-2	13
CO*	0.77	15	0	10
VA	0.62	0	2	-1
GA	0.67	5	2	5
MD	0.68	6	5	3
WI	0.66	4	5	0
MN	0.70	8	2	4
AZ*	0.69	7	7	-3
CT	1.15	52	0	6
NC	0.68	5	-4	0
OR	0.72	10	-7	-6
IN*	0.79	17	4	10
TN	0.67	5	8	13
SC	0.73	11	-3	3
LA	0.93	31	-6	7
KY*	0.92	30	1	5
DC	0.75	13	-1	-1
NV	0.92	29	4	15
UT	0.62	0	7	-1
KS*	0.87	25	-2	13
NE*	0.81	19	13	24
OK*	0.74	12	6	6
HI	0.83	21	6	14
MS	0.80	18	-5	-3
RI	0.90	28	-14	-10
DE	0.71	9	-2	6
NH	0.65	2	12	8

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