THE BOND BUYER

Munis ignore FOMC; ICI reports $517M inflows

By

Lynne Funk Gary Siegel

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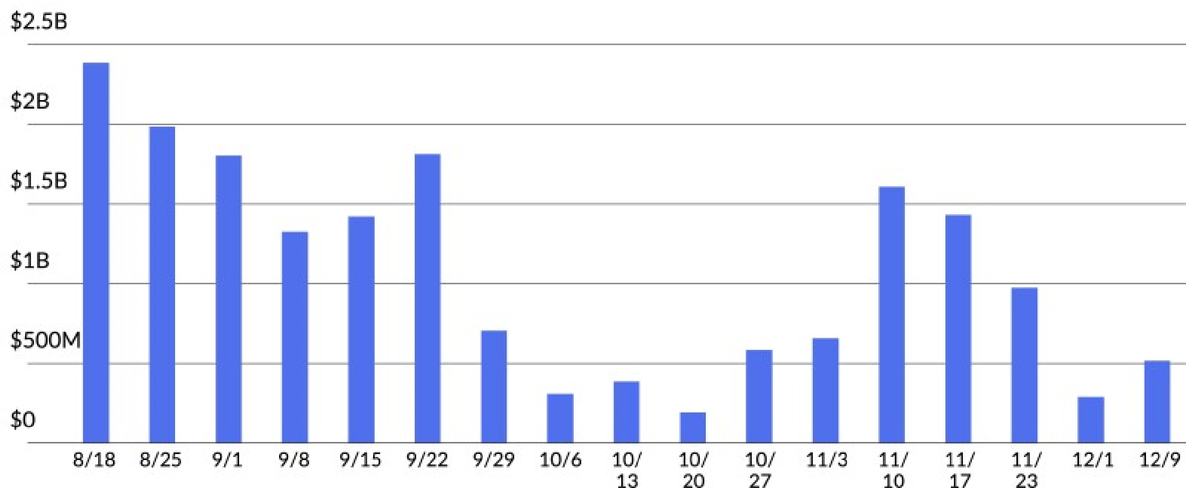
Municipals were lightly traded and ignored moves to higher yields in U.S. Treasuries Wednesday while equities rallied after the Federal Open Market Committee doubled the speed of its taper and projected three rate hikes in 2022.

“It would seem that today’s decision was a first move by the Fed to restore its credibility as an inflation-managing institution,” said Christian Scherrmann, U.S. economist at DWS. “But its more hawkish announcement was also justified by more optimism that progress towards maximum employment has picked up.”

USTs rose while munis were unmoved by the news.

Ratios were slightly lower with the five-year muni-to-UST ratio at 47% in five years, 71% in 10 and 80% in 30, according to Refinitiv MMD's 3 p.m. read. ICE Data Services had the five at 47%, the 10 at 73% and the 30 at 80%.



The Investment Company Institute reported $517 million of inflows into municipal bond mutual funds in the week ending Dec. 8, down from $289 million in the previous week.

It marked the 40th straight week of positive flows into the long-term funds and brought the total inflows for this year near $82 billion.

Exchange-traded funds saw $168 million of inflows after $229 million of inflows the previous week.

Informa: Money market muni funds rise

Tax-exempt municipal money market fund assets rose by $117.1 million, bringing their total up to $86.41 billion for the week ending Dec. 14, according to the Money Fund Report, a publication of Informa Financial Intelligence.

The average seven-day simple yield for the 150 tax-free and municipal money-market funds remained at 0.02% from the previous week.

Taxable money-fund assets lost $1.33 billion, bringing total net assets to $4.476 trillion in the week ended Dec. 14. The average seven-day simple yield for the 779 taxable reporting funds was at 0.01%.

In the primary, Ramirez & Co. priced for the Port Authority of New York and New Jersey (Aa3/A+/A+/) $420 million of taxable consolidated bonds. Bonds priced at par: 0.767% in 2/2023, 1.595% in 2026, 2.225% in 2031, 2.795% in 2036 and 2.925% in 2051, callable in 8/15/2031.

Secondary trading

Maryland 5s of 2022 at 0.18% and 5s of 2023 at 0.25%-0.24%. Washington Suburban Sanitation District 5s of 2025 at 0.58%.

New York City TFA 5s of 2026 at 0.66%. Connecticut 5s of 2027 at 0.81%.

Washington 5s of 2034 at 1.19%. Ohio 5s of 2034 at 1.20%. Los Angeles DWP 5s of 2039 at 1.36%.

AAA scales

Refinitiv MMD's scale was unchanged: the one-year at 0.15% and 0.25% in 2023. The 10-year sat at 1.03% and at 1.48% in 30.

The ICE municipal yield curve showed yields were unchanged at 0.17% in 2022, 0.28% in 2023 and 1.05% in 2031. The 30-year yield steady at 1.49%.

The IHS Markit municipal analytics curve was steady: 0.17% in 2022 and at 0.26% in 2023. The 10-year was at 1.02% and the 30-year at 1.49% as of a 3 p.m. read.

Bloomberg BVAL was steady at 0.17% in 2022 and 0.23% in 2023. The 10-year at 1.04% and the 30-year at 1.49%.

Treasuries were weaker and equities rallied.

The five-year UST was yielding 1.244%, the 10-year yielding 1.459%, the 20-year at 1.895% and the 30-year Treasury was yielding 1.856% at the close. The Dow Jones Industrial Average rose 369 points, or 1.04%, the S&P was up 1.52% while the Nasdaq gained 2.03% near the close.

FOMC

The Fed will taper monthly purchases of Treasury securities by $20 billion in January and agency mortgage-backed securities by $10 billion, with similar cuts expected every month, "but it is prepared to adjust the pace of purchases if warranted by changes in the economic outlook." In January, the Fed will buy $40 billion of Treasury securities and $20 billion mortgage-backeds.

The dot plot shows 10 participants expect three rate hikes next year, five see two, two project four increases and one forecaster sees a lone 25 basis point increase.

"This is a major pivot from the Fed, prompted by clearer evidence that inflation is broadening," said Brian Coulton, Fitch Ratings' chief economist. "By signaling that asset purchases will now cease in March 2022 they are paving the way for an interest rate hike late next summer."

The way the panel describes inflation, he said, "has changed markedly. Supply-demand imbalances related to the pandemic are now described as contributing to elevated 'inflation' rather than to 'price increases in some sectors.'"

Moving forward, there is less consensus, with three expecting rates to climb to a range between 2.0% and 2.25%, five expecting the fed funds rate target between 1.75% and 2%, three projecting a 1.50% to 1.75% range, five at 1.25% to 1.50% and two at 1.00% to 1.25%. In 2024, five officials see rates between 1.75% and 2.0%, five see them at 2.0% to 2.25%, one expects a 2.25% level, two see rates between 2.25% and 2.50%, four expect the target between 2.75% and 3% and one sees a 3.0% to 3.25% range.

The long-term view by most is a 2.5% target, with outliers at 2.0% and 3.0% and others sprinkled between 2.25% and 2.5%.

The Summary of Economic Projections shows the panel believes GDP growth will slow to 4.0% next year, 2.2% in 2023 and 2.0% in 2024, with unemployment at 4.3% this year (down from September's 4.8% projection) and 3.5% in ensuing

years. In September the 2022 median rate for unemployment was 3.8%. In the post meeting statement, the FOMC said it will not raise rates from the current zero to 0.25% range until maximum employment has been achieved.

The inflation expectations were raised, with the median for PCE this year at 5.3% (up from 4.2% in the prior SEP), 2.6% next year (up from 2.2%) and 2.3% in 2023 (up from 2.2%). Core PCE expectations were: 4.4% (up from 3.7% in the prior SEP), 2.7% next year (up from 2.3%) and 2.3% in 2023 (up from 2.2%).

“The bar for rate hikes now rests squarely on the labor market, with the statement indicating that the inflation threshold even under the Fed's new flexible regime has been met,” Wells Fargo Securities Senior Economist Sarah House and Economist Michael Pugliese said.

Powell said the Fed will take many factors into consideration in determining maximum employment, including the labor force participation rate, wages, job openings and the quits rate.

“What the Fed sees as maximum employment might be a situation in which the labor force participation rate remains below pre-pandemic levels,” said DWS' Scherrmann. “This, however, implies a higher level of wages and therefore a somewhat higher level of inflation — which is not what we are seeing in the updated forecasts looking beyond 2022.”

Powell said determining when maximum employment is reached is a judgment the committee will make, although in his opinion the economy has made “rapid progress” toward that goal.

While he wouldn't be pinned down on when rate hikes would start, Powell said there would “not be a very extended wait” after taper ends. Additionally, the markets move based on announcements of what the Fed plans to do, he said.

When the employment cost index came in higher than expected right before the FOMC's November meeting, Powell said he understood tapering would have to be accelerated and considered whether to do it at that meeting.

While Omicron poses “a risk” to the economy, it's uncertain at this point what its impact will ultimately be, Powell said.

Data
Retail sales gained 0.3% in November and were 18.2% higher than a year ago. Economists polled by IFR Markets expected a 0.8% rise.

“Sales contracted after adjusting for the surge in the consumer price index (CPI) for the month,” said Grant Thornton Chief Economist Diane Swonk. “The winter

Delta wave is now upon us. That surge coupled with the unknown threat posed by Omicron has already overwhelmed hospitals in some areas and taken a toll on reservations at restaurants. The bulk of the weakness associated with the current wave of infections is expected to show up in the first quarter data."

Although holiday sales continue at a record pace, “consumers are no longer the price-takers they were when they were flush with cash from stimulus checks,” said Wells Fargo Securities Senior Economist Tim Quinlan and Economist Shannon Seery. “Higher prices for gas and food is taking away wallet share from other spending categories.”

Despite the miss, ING Chief International Economist James Knightley said, “we shouldn’t get too down about these figures. The numbers for October were revised up a touch and we need to remember that retail sales are actually 21.6% higher than they were before the pandemic struck.”

In other data released Wednesday, manufacturing activity in the New York State showed strength, with the Empire State Manufacturing Survey’s general business conditions index climbing to 31.9 in December from 30.9 in November.

Economists expected a 27.3 read.

The price indexes moderated somewhat, but still suggested “ongoing substantial increases in both input prices and selling prices,” the report said. Employment data showed a “solid increase in employment.”

Also released, import prices grew 0.7% in November after a 1.5% gain in October, while export prices were 1.0% higher in November after a 1.6% jump in October.

Economists expected imports to rise 0.7% and exports 0.5%.

Separately, business inventories rose 1.2% in October after a 0.8% increase in September. Economists expected a 1.1% increase.

Also, the National Association of Home Builders/Wells Fargo Housing Market Index gained to 84 in December from 83 a month earlier. Economists expected the index to hold at 83.

Lynne Funk Innovation Editor, The Bond Buyer

Gary Siegel Managing Editor, The Bond Buyer