THE BOND BUYER

Munis vastly outperform big selloffs in UST, equities

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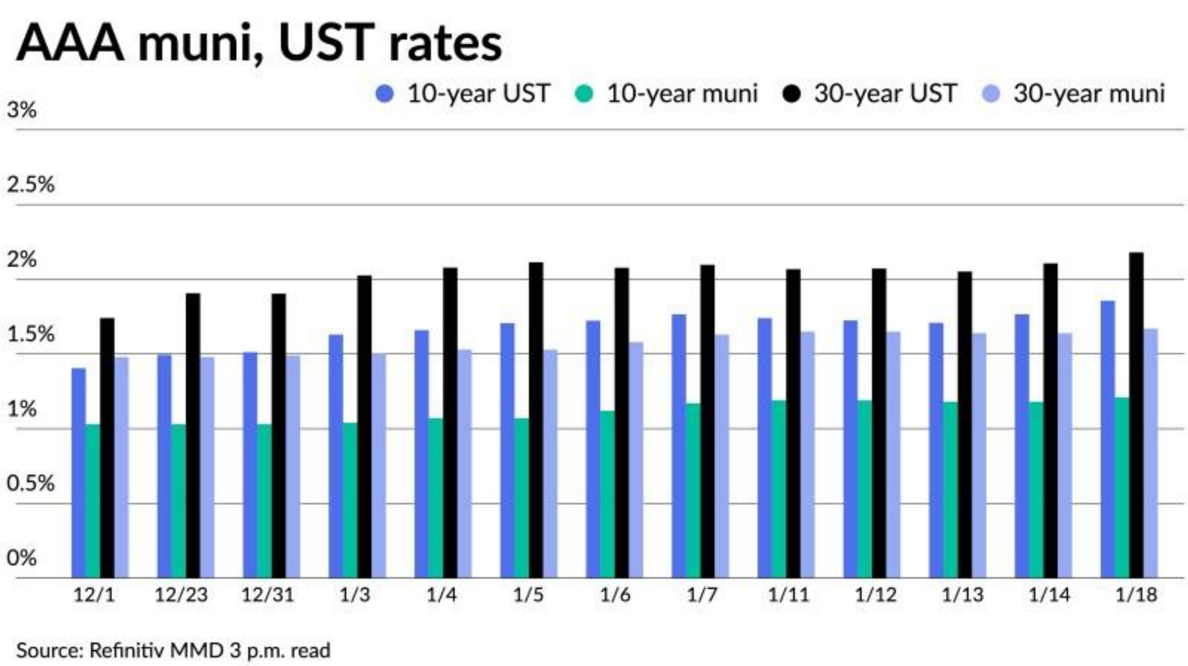
Municipals outperformed another large selloff in U.S. Treasuries that pushed that market to the highest yields since before the pandemic began while equities also saw massive losses as the markets fully digest an expected March rate hike.

Triple-A benchmark yields saw two to four basis point cuts across the curve Tuesday while the 2-, 5- and 10-year UST hit highs that further flattened the taxable curve.

Municipal to UST ratios again fell on the day's moves. The five-year was at 51%, 65% in 10 and 77% in 30, according to Refinitiv MMD's 3 p.m. read. ICE Data Services had the five at 51%, the 10 at 69% and the 30 at 78%.



As short-term rates climb faster than longer-term rates, the UST curve is projected to flatten even more, said Eric Kazatsky of Bloomberg Intelligence, adding that if inflationary pressures remain, the longer end of the curve may even fall.

“The question for investors then becomes, what have munis done during Fed tightening cycles? The answer: They've outperformed,” Kazatsky said.

Municipal ratios have tended to drop during rate hike periods over the last several decades, implying that municipal bond values are richer than similar-duration taxables like U.S. Treasuries. In 2022, this tendency may favor tax-exempts, he said.

With a backdrop of net negative supply, muni reinvestment demands are expected to outnumber available bonds in the remainder of the month, said Jeffrey Lipton, managing director of credit research at Oppenheimer Inc.

“There are still enough days in January to temper the bloodletting, yet admittedly, it would be challenging to finish the month in the green,” he said.

Long-dated muni rates have returned to the zip code of early November 2021, with the 30-year benchmark up as much as 20 basis points on some triple-A scales since the beginning of the year, as U.S. Treasury yields hit levels not seen since pre-pandemic, accompanied by a broad flattening of the Treasury yield curve, according to Lipton

“We are now experiencing the type of market selloff that should offer more compelling entry points for muni investors,” Lipton said. “We are also expanding market exposure to shifting fund flow dynamics with the potential for decelerating inflows and even episodic outflows.”

When it comes to fixed-income performance, Lipton said the move to higher rates has positioned the muni asset class to outperform. Munis tend to outperform Treasuries in weakening markets because of less susceptibility to interest rate changes compared to corporate bonds and better taxable equivalent yields. Other — albeit diluted — variables, such as technicals and even bets on increased taxes, are likely to be help limit the losses in the municipal bond market, he said.

Refinitiv Lipper recorded the first outflow of high-yield muni money since October 2021 last week, although total muni fund flows were positive for the week after 45 weeks of inflows.

“With the tightness of investment grade muni spreads, high-yield would likely demonstrate front-line withdrawals as negative performance ensues for the broader muni market, and investor anxiety emerges within the high-yield space,” Lipton said. “Security selection across the high-yield spectrum should become even more critical to the investment thesis throughout 2022.”

The rise in interest rates will dictate issuer mood in the coming months, and if rates climb quicker than expected, it might have an impact on taxable volume, potentially shelving a number of taxable advance refunding issuances, Lipton said.

The primary this week is essentially crammed into the next two sessions. The Virginia Public School Authority (Aaa/AAA/AAA//) kicked off the week with a competitive sale of $115.11 million of special obligation school financing bonds, Chesterfield County Series 2022, to Raymond James & Associates. Bonds in 1/2023 with a 5% coupon yield 0.35%, 5s of 2027 at 0.9%, 5s of 2032 at 1.28%, 2s of 2037 at 1.97% and 2.25s of 2042 at 2.3%, callable in 1/15/2032.

Secondary trading

New York Urban Development Corporation 5s of 2023 at 0.46%. Ohio 5s of 2023 at 0.48%. Dallas ISD 5s of 2023 at 0.48%-0.45%. Los Angeles Department of Water and Power 5s of 2024 at 0.56%.

Oregon 5s of 2026 at 0.85%. New York City TFA 5s of 2026 at 0.90%-0.89%. New York City waters 5s of 2027 at 0.95%. Louisiana 5s of 2027 at 0.95%. Massachusetts 5s of 2028 at 1.10%

Prince Georges County, Maryland 5s of 2029 at 1.17%. California 5s of 2029 at 1.17%. California 5s of 2031 at 1.32%. Minnesota 5s of 2032 at 1.31%.

DASNY 5s of 2034 at 1.60%. New York City TFA 5s of 2035 at 1.62%. DASNY 5s of 2035 at 1.63%.Washington 5s of 2037 ay 1.54%.

Los Angeles Department of Water and Power 5s of 2034 at 1.39% versus 1.38% original, 5s of 2036 at 1.50% versus 1.48% original.

Los Angeles Department of Water and Power 5s of 2049 at 1.82%. Los Angeles Department of Water and Power 5s of 2051 at 1.90% versus 1.85% original. Massachusetts 5s of 2051 at 1.84%.

AAA scales

Refinitiv MMD's scale was weaker at the 3 p.m. read: the one-year at 0.35% and 0.48% in two years. The 10-year at 1.21% and the 30-year at 1.67%.

The ICE municipal yield curve was cut two to four basis points: 0.33% in 2023 and 0.54% (+2) in 2024. The 10-year was at 1.27% (+3) and the 30-year yield was at 1.69% (+4) in a 4 p.m. read.

The IHS Markit municipal analytics curve was up a basis point: 0.35% (+1) in 2023 and 0.48% (+1) in 2024. The 10-year at 1.2% (+1) and the 30-year at 1.68% (+1) as of a 4 p.m. read.

Bloomberg BVAL was cut two to four basis points: 0.37% (+3) in 2023 and 0.51% (+4) in 2024. The 10-year cut three to 1.24% and the 30-year up three to 1.68% at a 4 p.m. read.

Treasuries and equities sold off.

The two-year UST was yielding 1.045%, the five-year was yielding 1.655%, the 10-year yielding 1.874%, the 20-year at 2.266% and the 30-year Treasury was yielding 2.200% at the close. The Dow Jones Industrial Average lost 543 points or 1.515%, the S&P was down 1.84% while the Nasdaq lost 2.60% at the close.

Omicron impact?

The manufacturing sector in New York took a hit apparently as a result of Omicron, and while this may suggest weak gross domestic product in the first quarter, the economy should rebound quickly, which should the Federal Reserve to liftoff in March, analysts said.

The Empire State manufacturing survey’s general business condition index plunged into contractionary territory, falling to -0.7 in January (its first negative reading since June 2020) from 31.9 in December. Economists polled by IFR Markets expected a drop to 25.0.

The new orders also fell below zero, while shipments fell to 1.0. The price indexes and employment numbers also declined. Respondents were generally optimistic about conditions in six months. However, the future price indexes rose, suggesting continued inflation pressures.

The surprise declines “presumably” resulted from “the uncertainty and disruption generated by the Omicron variant,” said ING Chief International Economist James Knightley. “New York bore the brunt earlier than other parts of the country.”

But, he noted, the report suggests “obvious downside risks for this week’s Richmond, Chicago and Philly Fed survey,” and given “the weak December retail sales figure and the sharp declines in mobility data, [it] indicates a pretty hefty contraction in economic activity at the turn of the year.”

While Omicron is expected to dissipate quickly, Knightley said, “we think we should see much better activity data from mid-Feb onwards, but it looks as though it will be touch and go as to whether we get a positive or negative U.S. GDP reading for Q1.”

But by next quarter, he expects “very strong” readings as long as “COVID case numbers fall meaningfully.”

The report suggests several things, including the continuance of “high, sticky inflation,” said Nancy Tengler, CEO and chief investment officer at Laffer Tengler Investments. “2022 promises to be Mr. Toad’s Wild Ride — mostly not, but maybe, occasionally scary.”

While the “case for peak inflation in December … is somewhat supported by this awful report,” she said, it suggests “growth will be slowing in 2022.”

The report showed shorter delivery times and increasing inventories, as they did in the ISM manufacturing PMI, which supports “our view that the supply chain might be clearing modestly just as demand for goods shifts to services,” Tengler said. “Unexpected that unfilled orders fell as hours worked fell as well but that is likely support for our thesis.”

And while the hope is that this is just one report and it’s skewed by Omicron impacts, she said, it raises the question, “if we are slowing and we know emerging and developed economies around the globe are slowing — how aggressive can the Fed be?”

Also released Tuesday, the National Association of Home Builders said builder confidence dipped in January, with its housing market index slipping to 83 from 84 a month earlier.

Economists expected the level to hold.

The index is based on data from the first half of January, noted NAHB Chief Economist Robert Dietz, and therefore “do not fully reflect the recent jump in mortgage interest rates.”

While demand for homes is “solid,” the industry faces lean inventory of homes for sale, he said, while rising building material costs, labor shortages “and higher mortgage rates point to declines for housing affordability in 2022.”

Primary to come

The New York City Transitional Finance Authority (Aa1/AAA/AAA/) is set to price Thursday $950 million of tax-exempt future tax secured subordinate bonds, Fiscal 2022 Series C, Subseries C-1. J.P. Morgan Securities.

The New Jersey Transportation Trust Fund Authority (Baa1/BBB/BBB+/A-) is set to price Wednesday $750 million of transportation program bonds, 2022 Series BB. J.P. Morgan Securities.

The Metropolitan Washington Airports Authority (A2/AA//) is set to price Thursday $739.815 million of Dulles Toll Road revenue refunding bonds, Series 2022, insured by Assured Guaranty Municipal Corp., consisting of $418.64 million of second senior lien revenue refunding bonds, Series 2022A, serials 2051-2053 and $321.175 million of federally taxable second senior lien revenue refunding bonds, Series 2022B, serials 2025-2037, term 2041. Wells Fargo.

Main Street Natural Gas (/BBB-//) is set to price Wednesday $600 million of gas supply revenue bonds, Series 2022C. J.P. Morgan Securities.

Dallas Independent School District in Texas (Aaa/AAA/AAA/) is set to price Thursday $387.07 million of unlimited tax school building bonds, Series 2022, serials 2023-2052. HilltopSecurities.

WakeMed Health and Hospitals in North Carolina (A2//A+/) is set to price Thursday $300 million of corporate CUSIP taxable bonds, Series 2022A J.P. Morgan Securities.

Claremont McKenna College in California (Aa3///) is set to price Wednesday $300 million of corporate CUSIP taxable bonds, Series 2022. Morgan Stanley & Co.

Hawaii (A1/A+/A+//) is set to price Wednesday $273.655 million of alternative minimum tax airports system revenue bonds, Series 2022A and refunding Series 2022B, consisting of $219.26 million of Series 1 and $54.395 million of Series 2. Morgan Stanley & Co.

Hidalgo County Regional Mobility Authority in Texas (Baa3/BB+///) is set to price Thursday $211.315 million of senior lien toll and vehicle registration fee revenue bonds, Series 2022A and junior lien toll and vehicle registration fee revenue and refunding bonds, Series 2022B, consisting of $69.205 million of Series 1, $79.153 million of Series 2, $30.6 million of Series 3 and $32.358 million of Series 4. Morgan Stanley & Co.

The Texas Department of Housing and Community Affairs (Aaa/AA+//) is set to price Wednesday $190 million of non-alternative minimum tax social residential mortgage revenue bonds, Series 2022A, serials 2023-2033, terms 2037, 2042, 2047 and 2052. RBC Capital Markets.

The village of Skokie, Illinois, (/AA/AA+/) is set to price Thursday $177.335 million, consisting of $151.060 million, Series 2022A, serials 2022-2040 and $26.275 million, Series 2022B, serials 2022-2041. Baird.

The Wisconsin Health And Educational Facilities Authority (Aa3/AA-//) is set to price Thursday $172.085 million of revenue bonds, Series 2022. J.P. Morgan Securities.

Georgetown Independent School District, Texas, (/AAA//) is set to price Wednesday $165.845 million of unlimited tax school building bonds, Series 2022, PSF. FHN Financial Capital Markets. Georgetown ISD is also set to price Wednesday $103.88 million of taxable unlimited tax refunding bonds, Series 2022-A. FHN Financial Capital Markets.

Orange County Health Facilities Authority, Florida, (//A-//) is set to price Thursday $140.64 million of revenue bonds, Series 2023A. Ziegler.

Ohio (Baa1///) is set to price Thursday $105.2 million of higher educational facility revenue bonds, serials 2027-2037, terms 2042, 2047 and 2052. KeyBanc Capital Markets.

Missouri Public Utilities Commission (///) is set to price Thursday $100 million of interim construction notes, Series 2022. D.A. Davidson & Co.

Competitive:

Fairfax County, Virginia, (Aaa/AAA/AAA/) is set to sell $272.255 million of public improvement bonds, Series 2022A at 10:45 a.m. eastern Wednesday.

New York City Transitional Finance Authority (/AAA//) is set to sell $69.005 million of future tax secured taxable subordinate bonds, Fiscal 2022 Subseries C-3 at 11:15 a.m. eastern Thursday.

New York City Transitional Finance Authority (/AAA//) is set to sell $180.995 million of future tax secured taxable subordinate bonds, Fiscal 2022 Subseries C-2 at 10:45 a.m. Thursday.

Cobb County School District in Georgia (MIG1/A-1+//) is set to sell $100 million of short-term construction notes, Series 2022 at 10:30 a.m. Thursday.