

Weekly Municipal Market - A Trader's Insight

16th AMENDMENT  ADVISORS LLC™

A LOOK AHEAD – WEEK OF 2.11.19

COMMENTARY

Municipal bond funds continue to see strong inflow data. This past week municipal bond mutual funds saw inflows of around \$1.15 billion. Long term, high yield and national municipal funds all benefitted from strong inflows. ETF's again saw outflows of around (\$300mm). An interesting note this week was investors pulled some (\$400mm) from municipal money market funds and another (\$170mm) from short term municipal bond funds. We believe this was due to investors wanting to extend duration a bit further out on the curve given the richness of municipals in the 10-year part of the curve.

SPECIAL FOCUS - LOW RATIOS 10 YEAR CURVE

Last week, 10-year municipal/treasury ratios remained in the low 80% range. You will see in **Chart 1** below that according to Bloomberg, 10-year ratios continue to remain near their 5-year lows. We believe the trend to lower ratios directly correlates to the popularity of separately managed accounts (“SMA”), a trend that began following the financial crisis. However, two more recent factors may play a role as well in the recent downward shift in ratios. The combination of the fear of rising rates and new rules requiring brokers to disclose commissions on municipal bond trades has, in our opinion, pushed financial advisors to offer SMAs to clients. Prior to May 2018, many financial advisors could be considered “transactional brokers”- meaning commissions were generated on a “per trade” basis. Not surprisingly, FAs did not have the motivation to recommend SMAs to clients. Subsequent to the May 2018 rule change, financial advisors are now required to show commissions to retail accounts. This change has led many FAs to offer municipal account management with an asset based/fee-based approach. These FAs now choose from a menu of municipal SMA managers approved on the dealer platforms. We wrote about this important rule change in May 2018.

We have observed over the past couple of years that during new issue order periods, specifically retail order periods, many of these SMA managers have been primarily focused on maturities inside of 12-years. The supply/demand imbalance in this area of the curve has been a main driver of this prolonged period of rich ratios in the 10yr area of the municipal market.

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Chart 1



We continue to believe these 10-year ratios will remain relatively rich for the short term and still believe the best area of the curve to pick up value would be in the 15 to 20-year part of the curve.

RATIOS

Municipal (MMD) Treasury Ratios (as of 2/08/2019)

	Muni	Treas	Muni/Treas	Wkly Chg
5 Year	1.70%	2.44%	69.6%	-0.5%
10 Year	2.12%	2.63%	80.5%	-0.1%
30 Year	2.97%	2.98%	99.8%	0.1%

SPOTLIGHT

Last week we highlighted the MA Development Finance Agency (Wellsforce Inc.) **NR/BBB+/BBB+** health care deal. The \$415mm deal saw over \$4bln in orders and was bumped 7 to 15 basis points and continued to trade up once the deal was free to trade.

This week's \$7bln calendar should also be met with solid demand and fund flows continue to be positive. This week our attention will be on benchmark high grade deals such as District of Columbia GO's Aaa/AA+/AA+, NY Dormitory Authority for The State of New York University Aa2/AA- and the State of Oregon GO's Aa1/AA+/AA+. We expect these deals should be met with solid demand.

Data Sources: MMD from TM3 and Treasury data from Bloomberg; Fund Flow data from Lipper from JP Morgan

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