

Municipal Market Statistics

June 2024

	06-01-24	05-01-24	06-01-23	06-01-21	06-01-19
10-Year AAA BVAL Municipal	2.78%	2.78%	2.61%	0.96%	1.64%
10-Year US Treasury	4.67%	4.68%	3.65%	1.60%	2.13%
10-Year Muni vs. Treasury Ratio	60%	59%	71%	60%	75%
IG Fund Flows YTD	\$5.4B	\$6.0B	(\$7.5B)	\$37.3B	\$26.9B
HY Fund Flows YTD	\$4.9B	\$4.1B	(\$0.2B)	\$11.1B	\$7.9B
IG (LMBITR) Total Return YTD	(1.94%)	(1.62%)	1.65%	0.78%	4.71%
HY (LMHYTR) Total Return YTD	1.63%	0.89%	2.61%	4.79%	6.11%
New Issue Calendar YTD	\$185B	\$139B	\$135B	\$176B	\$131B

Lind Capital Partners Municipal Market Commentary

- Municipal Market Performance:** The divergence between high-grade and high-yield municipal performance widened in May as the Bloomberg Municipal Bond Index (LMBITR) posted a loss of (0.29%), while the Bloomberg Municipal High Yield Index (LMHYTR) recorded a positive return of 0.76%. Year-to-date, the divergence is more pronounced as high-yield is outperforming high-grades by 356 basis points (+1.65% vs -1.91%).
- AAA Municipal Benchmark Rates:** High grade municipals bear flattened in May as the 5 and 10yr maturities rose by over 30bps while the long end of the curve ended the month 2bps lower. The US Treasury market outperformed, particularly on the front end, as rates were essentially unchanged month over month across every tenor.
- Mutual Fund Flows:** After a string of weekly inflows, open-end municipal mutual funds hit a snag in May, experiencing outflows 3-straight weeks to close out the month. Flows in high-yield mutual funds have been much more constructive, seeing inflows 6-straight weeks and 20 out of the last 21 weeks. Year-to-date flows remain firmly positive for both high-grade and high-yield mutual funds, totaling over \$5.4B and \$4.9B, respectively.
- Primary Market Supply:** Municipal supply is slated to finish the month totaling over \$43bn. That figure is up roughly 33% YoY. Non-rated and lower rated new issue supply has been anemic—varying drastically week to week (the forward calendar is encouraging). From a high level, higher yield new issue supply is depressed year-to-date. This, coupled with steady and robust demand (inflows), has led to a primary market that continues to see deals significantly oversubscribed resulting in substantial price tightening. The supply/demand imbalance in high yield has certainly contributed to the outperformance vs high-grades year-to-date. With that said, the entry point for non-rated municipals remains attractive.

Lind Capital Partners Municipal Non-Rated Market Commentary

While our 8 target revenue bond sectors in the non-rated municipal market are always a topic of conversation with clients and prospects, we also focus attention to the sectors in which **we typically do not invest**, most notably tobacco securitization bonds. For those unfamiliar with the sector, tobacco securitization bonds were a product created following the Master Settlement Agreement (MSA) between participating tobacco companies and 46 individual states. In 1998, the major tobacco agreed to make annual payments (in perpetuity) to the states in exchange for release from future legal claims. The annual payments were based on a formula incorporating annual cigarette sales and inflation.

Following the signing of the MSA, states and municipalities sought to monetize the future MSA cash flows by securitizing the future income stream. It is estimated that \$100 billion in tobacco securitization has been issued in the municipal bond market. Today, tobacco securitization constitutes nearly 8% of the Bloomberg Barclays High Yield Municipal Bond Index (LMHYTR)¹. From a sector perspective, tobacco constitutes one of the larger sectors among most high yield funds. It tends to serve as a proxy for high yield mutual fund flows, the most actively bought bond when flows are positive and most actively sold when fund flows are negative. Perhaps the most extreme example of this phenomenon was Buckeye Tobacco 5.00% due in 2055 (NR/NR), a \$3.4 billion maturity in a \$5.4 billion bond issue. At the onset of COVID in early March 2020, these bonds went from a high price of \$115,948 (3.15%) to \$69,500 (7.46%) over a 22-day period. **A whopping 40% price decline in 3 weeks.** In our view, the price volatility was due to the ubiquitous nature of the bond across most high yield funds. As retail investors sought to redeem out of mutual funds, portfolio managers looked for their "*most liquid*" holding to sell and raise cash to meet redemptions. Tobacco bonds generally, and Buckeye Tobacco 5s referenced above, were bonds for which the portfolio managers could obtain a bid, albeit at increasing lower levels each day.

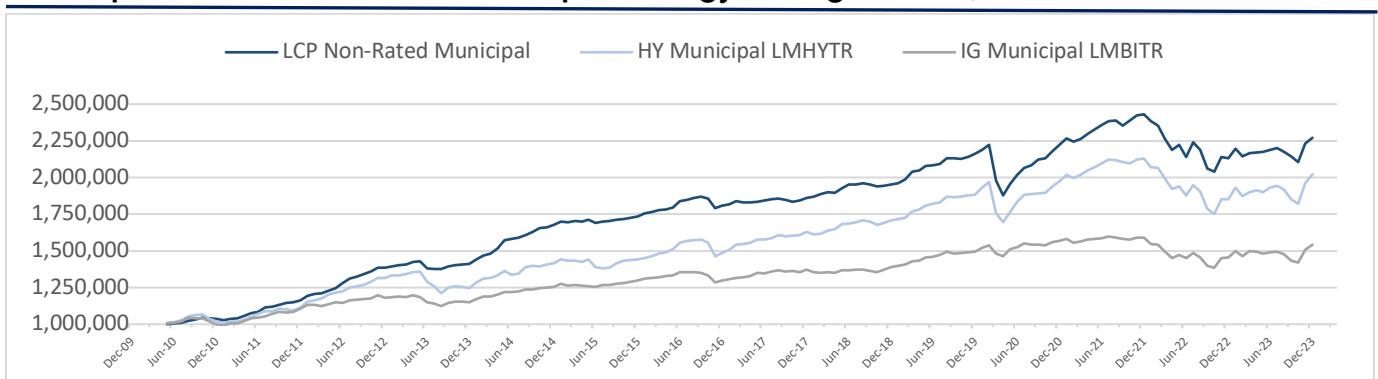
The above example is one of the many reasons we at LCP do not consider tobacco bonds as a core holding, rather as an opportunistic shorter-term investment. Among our other considerations are:

- While many different entities have securitized their tobacco payments, the underlying source of payment for MSA settlement bonds is the same, the participating tobacco companies.
- Annual payments of based on tobacco sales/consumption and inflation. The assumptions used to model the bond payments can be vastly different from actual consumption. Consumption declines in excess of assumptions can lead to financial stress and/or default
- There can be significant outside influences on consumption that are difficult, if not impossible to effectively forecast. These can include a federal ban on the menthol cigarettes, increases in cigarette and tobacco taxes, development of alternatives to cigarettes that impact consumption
- We would be hard pressed to claim a highly differentiated strategy if our core holdings were similar to most high yield municipal bond strategies.
- Finally, we strongly believe our 8 targeted revenue bond sectors of the municipal bond market offer investors compelling opportunities from both a yield and credit perspective. We prefer to take a contrarian view of tobacco bonds and be a buyer when the funds are all selling, and a seller when they are buying.

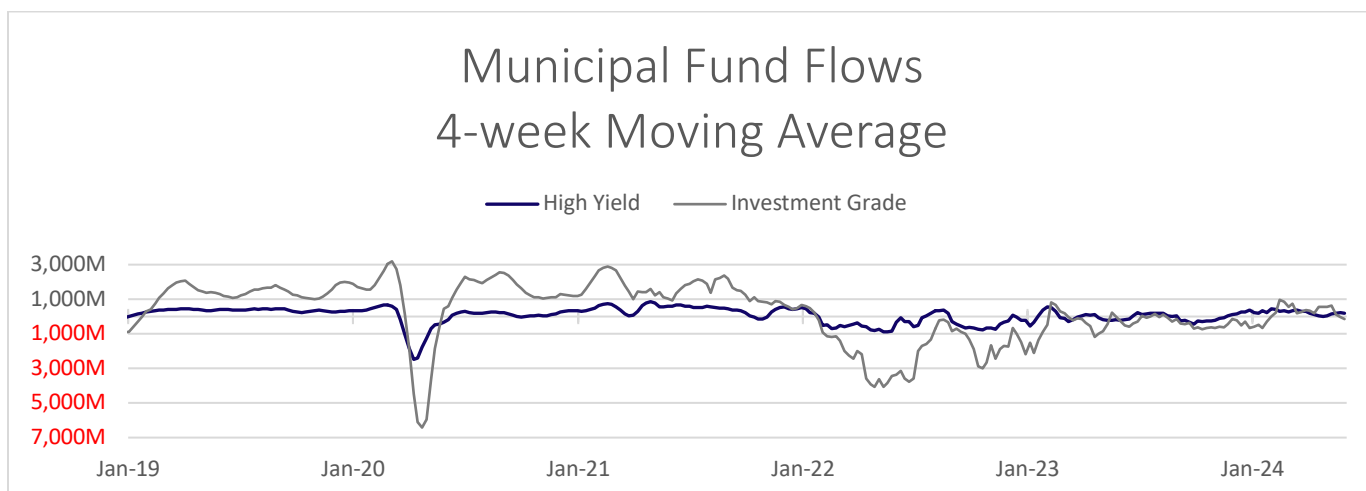
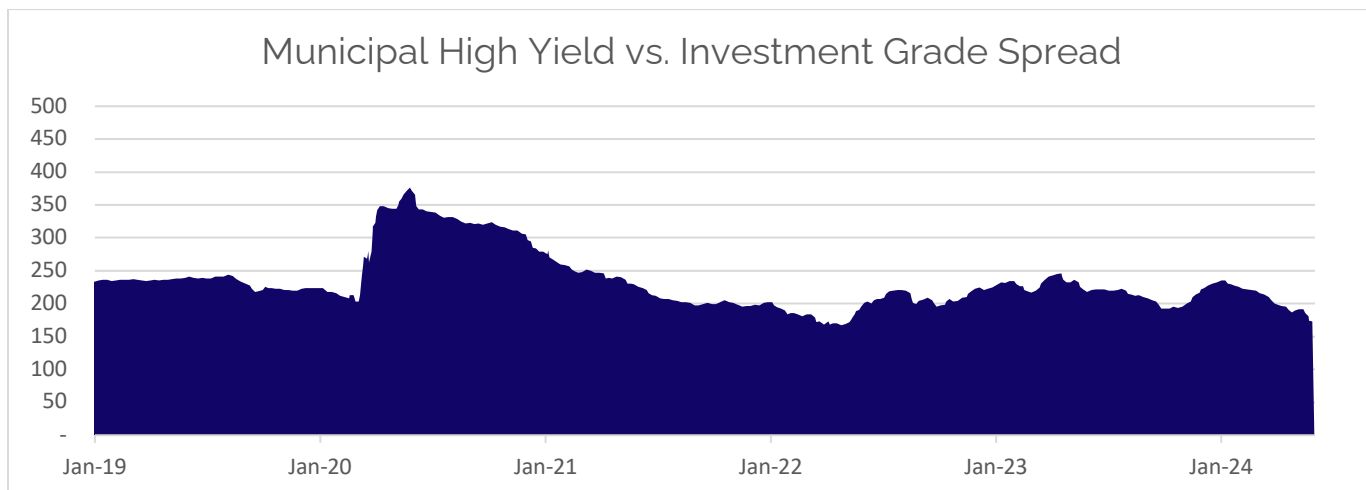
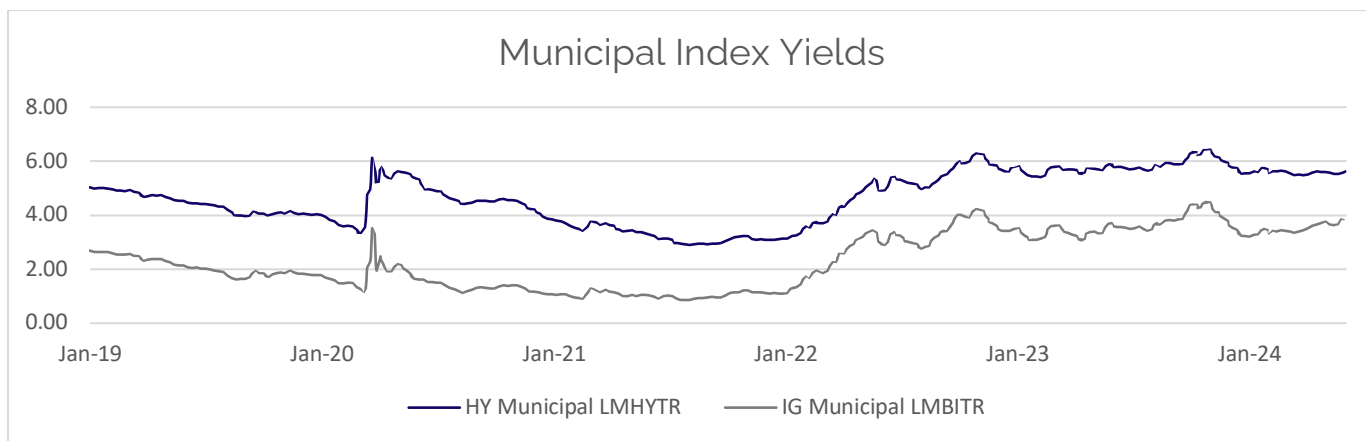
The tobacco securitization market is interesting for the role it plays in the municipal bond market. Portfolio managers seem to claim "diversification" due to different issuers although the source of payment is singular. Tobacco bonds may be easy to buy or sell, but that "*liquidity*" comes at a cost and may not be in the best interests of investors.

¹Bloomberg, LP

Lind Capital Partners Non-Rated Municipal Strategy (through March 31, 2024)



The chart above shows the increase in value of \$1,000,000 invested in the LCP composite at inception (net of management fees and expenses) vs. the benchmark, the Bloomberg High Yield Muni (LMHYTR) as well as the Bloomberg Muni (LMBITR) indices (it is not possible to invest in either Bloomberg Index). Please contact us with questions regarding credit profile, returns, taxable equivalent yields or further portfolio information. Past performance is not indicative of future results.



Sources: Refinitiv and Bloomberg LP

Disclosure

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