



# INTERMEDIATE MATURITY MUNI



## COMMENTARY – FIRST QUARTER 2019

### MACRO OVERVIEW

Following a tumultuous end to 2018, U.S. equities rebounded in Q1 2019 on more resilient domestic economic activity. Globally however, growth slowed more meaningfully, especially in China and the Eurozone, where lingering trade disputes and political uncertainty (Brexit) have exacerbated already weaker economic environments. Bond market performance was strong during the quarter as rates rallied across the curve. Yields on benchmark USTs were down 22bps, 28bps and 20bps in the 2yr, 10yr, and 30yr portions of the curve, respectively. The primary driver of lower yields was a stark reversal of policy expectations from the Federal Reserve. Entering the year the Fed was still signaling two interest rate hikes in 2019, however, following its March meeting, expectations were revised substantially lower, and language within the FOMC minutes now depicts a more dovish outlook for the U.S. economy.

- Our current economic outlook for the U.S. supports moderating performance for 2019. GDP estimates hover right above 2.0%, lower than 2018’s 2.9% but certainly not recessionary.
- The bond market, as evidenced by the UST Forwards Curve, has also dovishly tilted its outlook. Forwards are now pricing an interest rate cut in late 2019.
- The spread between the 3 month T-Bill and 10yr Treasury turned slightly negative in late March and was arguably the most significant inversion so far in this cycle. This was short-lived and we believe calls for a recession based on this relationship have been pre-mature.
- Little tangible evidence of a genuine trade deal with China has emerged. However, should a deal be struck, it would likely help alleviate some near-term concerns regarding the health of the global economy.

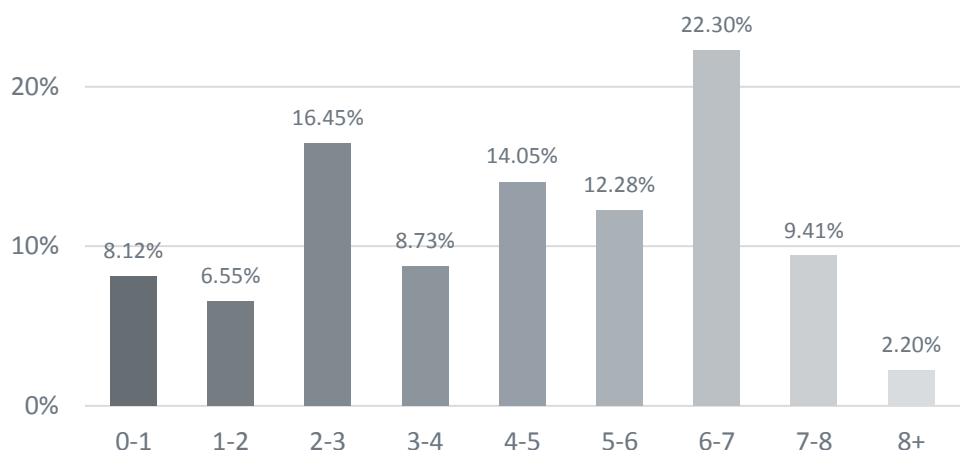
### MARKET DYNAMICS

Municipals ended the first quarter in very strong fashion. For the period, yields on the benchmark AAA MMD Index were lower by 27bps, 35bps, 41bps and 39bps in the 2yr, 5yr, 10yr and 30yr portions of the curve, respectively, and outperformed their Treasury counterparts. Demand was the primary driver as record inflows poured into Munis. Lipper reported 12 consecutive weeks of fund inflows totaling \$22.5B, marking the best yearly start since the series began in 1992. The insatiable vs demand for Munis was seen most prominently in high-tax states where the \$10,000 SALT cap heightened the appeal for tax-exempt income. Although supply was down modestly, it’s the demand side of the equation that forced Muni/UST ratios to some of their richest levels on record and we expect this trend to continue over the near-term.

### DURATION PROFILE

#### COMPOSITE CHARACTERISTICS

Duration: 4.38 yrs  
 Yield-to-Worst: 1.91 %  
 Yield-to-Maturity: 2.14 %  
 Maturity: 6.73 yrs





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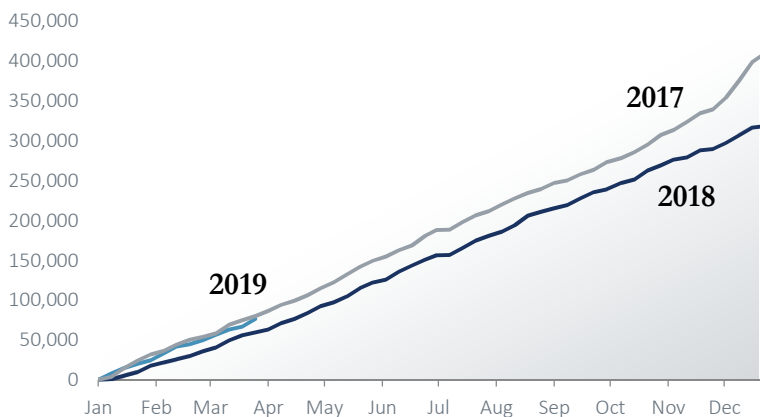
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### PERFORMANCE NOTES

After ending 2018 on a strong note, Municipals continued to perform well through the first quarter. Strategy performance was in-line with the benchmark with longer duration assets generally posting higher total returns. Our decision to modestly extend portfolios earlier in the year helped capture some of the better returns in maturities past 10 years. As mentioned above, demand, especially from retail investors, was the primary driver of Municipal outperformance. The Bloomberg Barclays 1-15 YR Muni Index returned 2.51% during the quarter with Transportation and Higher Education as the best performing sectors. While current ratios suggest Munis may be overbought, we still think there could be some further tightening on front-end maturities as retail demand should remain steady and issuance continues on the lighter side over the near-to-medium-term.

#### TOTAL MUNICIPAL ISSUANCE YOY (\$BLN)

SOURCE: BLOOMBERG



“Near-term technicals appear strong and with the Fed seemingly on pause ...

**risks to meaningfully higher rates appear low**

... making it a reasonable time to add to Muni positions.”

#### 10 YR MMD YIELD (%)

SOURCE: BLOOMBERG



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