General Market

Fixed income markets rallied this week after signs of weakness emerged in both inflation and the labor market. Consumer inflation rose less than forecast in May with the core CPI advancing just 0.1% on the month. PPI Inflation followed suit, also surprising to the downside with a 0.1% increase. Employment data showed further cracks as Initial Jobless Claims continued to climb, causing the 4-week moving average to rapidly approach the post-pandemic highs. With signs of a slowdown, traders increased their wagers on the timing of Fed rate cuts, with an 85% probability now assumed for the September Fed meeting and a 2nd cut before year-end fully priced in.

IG Munis

The muni market underperformed with 3 straight days of an unchanged benchmark curve and only modest bumps thereafter despite USTs rallying most days. That said, dealers reported a stronger tone than the curve implied, with many trades happening 2-4bps better than prior days. The positive performance was impressive considering tax-exempt issuance over the past two weeks each registered in the top 4 of all-time. Usually, we'd expect to see a surge in BWICs to make room for new deals with fresh calls and higher book yields, but JPM only reported a 5% increase in customer BWICs. Supporting the demand were continued fund inflows and seasonally strong reinvestment cash, with Lipper reporting the 7th consecutive week of positive figures at +$523mm. After many accounts built up cash buffers and sat idly by as volatility surged earlier this year, it seems that investors are fully embracing munis again. Especially after the House tax bill made no mention of the muni tax-exemption and the harshest of tariffs have been walked back, investors have been eager to lock in the high absolute yields still on offer. Next week will see a drop off in issuance given the FOMC meeting and Juneteenth holiday so we expect investors will refocus on the secondary market and look to scoop up any value left behind in the wake of the issuance onslaught.

HY Munis

Generic HY names were mostly unchanged to slightly wider on the week despite a small calendar. Perhaps the lack of deals trading up 30bps+ on a break kept the animal spirits at bay. That said, several dealers reported strong inquiries for non-generic names, with buyers looking to fill needs in a variety of sectors. A fund liquidation helped supply a plethora of unique credits, however, a large portion were distressed which limited the buyer pool. Interestingly, many of these bonds traded at massive discounts to their evals, underscoring the risk involved in investing in the most speculative projects. While this portion of the market may unearth rare opportunities for outsized returns, we believe this is best left for firms that have deep expertise in distressed credits and complex workouts.

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