

General Market

In a week full of major data releases and market moving events, bond markets were relatively tame until Friday's mega miss on the Non-Farm Payrolls report. On Wednesday, after Q2 GDP came in stronger than expected, the Fed left rates unchanged, but two committee members dissented for the first time since 1993, adding to speculation that the Fed would cut in September. However, Chair Powell's press conference was more hawkish than expected after he downplayed talks about September and argued it was still too early to be thinking about cuts, which caused treasury yields to rise. Markets sharply reversed course on Friday after payrolls only increased by 73k in July while the prior two months were revised down by 258k jobs. The front end rallied as much as 25bps intraday on Friday as participants rushed to re-price in a September cut. Additionally, President Trump revealed new tariff rates on US trading partners, which would bring the country's overall levy on goods up to 15.2% from just 2.3% last year, risking further economic deterioration.

IG Munis

The muni market tone continued to improve, especially in the long end where dealers reported strong interest from crossover accounts for clean blocks of high-grade paper withing +/- 15bps of a 5% yield. Lipper reported the second consecutive week of mutual fund inflows and the 13th week of inflows out of the last 14, which helped demand. However, with underwriters continuing to hammer the market with deal after deal, we saw an uptick in sale lists, with JPM reporting +17% relative to the previous 5-week average. Dealers also reported sparse demand from SMA accounts in the front end of the curve from 2-20 years. Due to Friday's massive treasury rally, the muni market underperformed as the benchmark curve was only bumped 7bps. If the narrative takes hold that the Fed is behind the eight ball and will need to cut rates several times in the coming months to catch up to the realities of a weaker economy, we expect muni yields will drift lower alongside treasuries. However, with the record pace of new issue supply seeing no end in sight, ratios may remain more elevated relative to its historical averages. While August reinvestment capital will be the highest of the year, next week's \$17bn+ of issuance is the 4th highest on record.

HY Munis

Similar to last week, the HY market continued its recovery from July's early under-performance, albeit at a measured pace. Benchmark names mostly kept pace with high grades, with bellwether Buckeye Tobacco bonds rallying 8bps to 6.38%. Accounts were somewhat cautious as they waited to see the result of the \$3.4bn Baa3 rated Georgia SR 400 Express Lanes transaction with all maturities in long duration of 35 and 40y. The two 6.5%

coupon tranches ended up being ~3x oversubscribed and the underwriter was only left with a small balance of the discount 2060s, with all bonds coming in above a 6% yield. As reads came in that the deal would clear, many accounts breathed a sigh of relief. In addition, a \$269mm Baa3 Guam Business Privilege Tax deal saw 16-17x oversubscriptions on its longest bonds out to 15y and was bumped 17-18bps. Despite rates selling off between the final pricing and when bonds freed, the Georgia toll road deal traded up 20bps on Thursday's break and rallied a further 7bps alongside the broader muni market on Friday. Overall, while the tone improved in the later part of the week, investors still seem somewhat cautious to allocate capital to high yield muni funds with Lipper reporting just +\$44mm this week vs +\$893mm for IGs (coming on the heels of two consecutive weeks of HY outflows). Given tight credit spreads and high absolute yields in the investment grade market, we remain cautious on generic HY risk especially in light of a cloudy economic outlook. That said, active credit managers who have the capacity to perform in-depth due diligence on less frequently traded names are likely going to be able to find some diamonds in the rough, especially if the broader market widens and funds are faced with investor redemptions.

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Market Commentary

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