

General Commentary

Fed Chair Powell's speech on Tuesday discussing the economic outlook noted both the upside risks to inflation and downside risks to employment. However, he reiterated that he expects the inflationary impact of tariffs would be limited to a one-time effect, which market participants took to mean he may be supportive of further cuts. The bond market optimism quickly faded as economic data released over the rest of the week all came in stronger than expected. The third reading of Q2 GDP saw a significant revision higher from 3.3% to 3.8% while Personal Consumption was revised from 1.7% to 2.5%. Separate reports showed that Durable Goods Orders rebounded in August, while Initial Jobless Claims last week fell to the lowest since mid-July. On Friday, the August Core PCE Index came in flat as expected, while Personal Income and Personal Spending both rose, suggesting consumers are in fine shape despite somewhat elevated inflation. With the economy appearing to be humming along, rates rose as investors pared back expectations for Fed cuts. The front end closed the week off 7-9bps, while 10-30y yields rose by 3-5bps.

IG Munis

After starting the week at aggressive valuations relative to taxables, particularly in the front end of the curve, it was no surprise that the muni market struggled to sustain its outperformance. The benchmark AAA MMD curve saw yields jump by as much as 13bps up front, while the 30y kept pace with treasuries after rising 2bps. The front end of the curve felt heavy all week, with a deluge of BWICs and the week's \$14bn+ primary calendar heavily concentrated in shorter tenors as sellers and issuers alike looked to take advantage of tax-exempt to taxable ratios in the mid 50% range. By Thursday, dealers were reporting they could buy AAA paper in the high teens to mid +20s spreads 5y and in, while odd lots were trading off 20-30bps. Several new issues struggled to clear and dealers were left with balances on both negotiated and competitive deals. Fund flows didn't help the case either as Lipper reported \$145mm in outflows from IG funds, most of which were attributed to ETFs. For the week through Thursday, JPM reported BWICs were up 13%, while customer purchases were down 17%. Next week's lighter primary calendar will offer some relief on the supply side, but ratios still hovering below 60% in the front end leave little to be desired.

HY Munis

The HY market underperformed for the week despite a continued lack of sizable new issue for buyers to choose from. Benchmark names generally traded off 10-15bps as Buckeye Tobacco closed off 11bps, Cofina was weaker by 9bps, and GA SR400 Express Lanes traded 16bps worse than last Wednesday's tights. New issues saw mixed performance. On the one hand, a \$55mm nonrated senior living deal saw its 40y bond tighten by 20bps from

premarketing levels and a \$73mm nonrated senior living transaction was bumped 12bps in its 35y tenor and traded up another 5-10bps on the break. However, deals further down the risk spectrum saw minimal oversubscriptions, while others continued to get hung up and remain on day-to-day status. A \$177mm nonrated healthcare deal saw its 35y tranche price to 15 investors, but yields were left unchanged at almost 7%. HY funds saw \$136mm of inflows this week and if flows remain modest, investors will continue to take a more discerning approach to credit, however, if flows pick up into year-end, we expect stronger risk appetite to emerge.

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Market Commentary

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