

General Commentary

Treasuries bounced around throughout the week, ultimately ending significantly better after a flight to quality and a mild inflation reading. On Tuesday, rates rallied 4-8bps after December's retail sales report unexpectedly saw no growth from November despite the holiday shopping season. However, a portion of this was unwound the next day after the delayed released of the Nonfarm Payrolls report showed the US added more jobs in January than any month since December 2024, while the household survey of the unemployment rate unexpectedly fell by 0.1%. The back-and-forth continued Thursday after equity markets plummeted, causing investors to rush to the safety of treasuries. The momentum was carried into the week's close after January's CPI report showed core inflation ticked down to 2.5%. While this shouldn't materially change the Fed's near-term stance, traders are betting that the tamer inflation reading may accelerate rate cuts in the back half of the year with odds of 3 cuts in 2026 jumping to over 50%. The Fed-sensitive 2y saw yields drop by 9bps, while the rest of the curve rallied 16-17bps.

IG Munis

The strong start to the year for the muni market continued to live on another week. However, with MMD/UST ratios at aggressive levels, it was unsurprising to see the muni market underperform the strong rate rally. The benchmark AAA curve still gained but only saw yields lowered by 3-7bps. The long end was the laggard again, though by the end of the week ratios had risen to above 90% which seemed to spark broader interest and the curve to finally adjust lower. Lipper reported another strong week of inflows, with \$1.343bn flowing into IG funds helping to prop up demand. In the primary, the heavy new issue calendar was well received, with most negotiated deals being oversubscribed, bumped, and trading up a few bps on the break. Competitive deals were bid very strongly and most had good follow through. Earlier in the week, there were some residual balances lingering in the longer parts of the curve, but dealers began cleaning those up as the week wore on and the value proposition grew.

Next week's calendar will dip due to the holiday-shortened week, but the pace of issuance should pick right back up thereafter. While the heavy inflows coinciding with seasonally strong reinvestment cash have been extremely supportive, the technical backdrop will likely shift as we head into tax season in March and April. Oftentimes we see accounts tap their muni portfolios to fund tax payments, while reinvestment cash in the Spring tends to be some of the lowest of the year. If 2026 will offer a 3rd consecutive year of record issuance, then we may see some better entry points as the market struggles to maintain the current level of stretched valuations when supply picks up amidst a less favorable demand environment.

HY Munis

The HY market exhibited two distinct personalities this week. In the secondary market, high beta names traded unchanged to a few bps better, matching or even lagging IGs. Buckeye Tobacco and Cofina closed 3-4bps better, while mid-grades like GA SR400 and JFK NTOs traded roughly unchanged on the week. Inquiry seemed very specific, with better prints on select names, especially in NY and CA charter schools. Other "different names" mirrored the benchmarks with a block of Atlanta's nonrated Westside Gulch development trading flat Thursday to Thursday, before Friday's MMD bumps.

The primary market was a completely different story. After last week's NY senior living deal signaled that risk appetite was back, underwriters saw robust interest in this week's slate of issuance. Even previously hung deals like a \$168mm BB rated NY charter school that had first tried to come last Fall saw 10x+ subscriptions and then bonds trading up another 9bps on the break. Similarly, a \$240mm nonrated FL student housing deal that didn't get done a few weeks ago was restructured to 10y puts and traded up 45bps on the break. Mid-grades fared similarly. A BBB- healthcare energy deal saw \$1.7bn in orders for a \$162mm deal and its longest tranche in 2047 was 17x oversubscribed. After being bumped 22bps in the repricing, it traded up another 22bps on Friday. A \$90mm Baa2 rated healthcare foundation was bumped 25bps and then traded up 40bps on the break.

With this level of demand out there, we expect HY issuance may finally pick up this year as speculative transactions find it easier and easier to clear the market. There likely will be value in participating in these new issues as funds receive fractions of their desired allotments and chase bonds on the break, but we suspect this environment will also lead to many overlooked credits in the secondary that discerning investors can choose from.

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Market Commentary

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