

General Commentary

Geopolitics took center stage this week after the US and Israel began striking Iran over the weekend. Oil surged with Brent Crude up 32% from last Thursday's close before reports surfaced of the potential strike. Countries such as Iraq and Kuwait began cutting oil production after oil fields began running out of storage due to tankers being unable to enter or exit the Strait of Hormuz. With inflation fears rising due to energy shortages, treasury yields jumped with the front end and belly off 19-23bps, while the long end rose 15bps. On the data front, the ISM Manufacturing report showed an expansion in February, while Prices Paid jumped to the highest level since June 2022, further exacerbating inflation concerns. However, Friday's Nonfarm Payrolls report dialed down the temperature after a surprisingly weak reading. The US lost 92k jobs in February whereas economists had predicted a 55k gain. The 2-month revision took another 69k jobs off, while the household survey of the unemployment rate jumped to 4.44%.

IG Munis

The sudden about face in the treasury market and uncertainty over how long lasting the incursion would be kept many muni participants on the sidelines to kick off the week. Not wanting to make any brash decisions, customer buys and sells were down 15-22% on Monday, according to JPM Research. BWICs rose 32%, but the hit ratio plummeted 26% as liquidity dried up quickly. The benchmark AAA MMD curve was cut 3-5bps but one trader thought they should have gone 7-10bps more in the 5-10y space, citing multiple AA+ to AAA GO prints trading +15-20 that normally would trade very close to the scale. As the new issue market began opening for orders on Tuesday, a similar theme emerged. With ratios compressed in the short to intermediate tenors, investors found comfort in a barbell approach where they could hide out in the front end, while taking advantage of the steepness of the curve by moving out to longer maturities where valuations are the most compelling. A \$786mm AA+ AZ Trans deal was 1-2x oversubscribed out to 6y, had balances from 7-15y, but was then 4-5x over in the longest maturities offered in 18-20y. Similarly, a \$299mm AA+ NC Housing deal had balances 6-10y but was 3-5x oversubscribed out long. In the secondary, BWIC volumes began to normalize, but the hit rate continued to be poor, at -15%. MMD got cut 10bps out to 15y, its biggest selloff since the April tariff tantrum.

As investors came to terms with the "new normal", the tone improved throughout the week, leading to two straight days of an unchanged MMD curve before Friday's modest 1-2bp cuts in 8-21y. The focus shifted back to the supply/demand imbalance due to heavy inflows and pent-up cash that needed to be invested as inquiries built to try to take advantage of a suddenly cheaper market. Lipper reported the 15th consecutive week of inflows, with IG

funds taking in \$1.175bn. By the end of the week, JPM reported that while BWICs rose 21%, hit rates ended up being about average and customer purchases rose 15%. The 8bp outperformance of the muni market relative to treasuries up front and 6bps out long pushed the market back into relatively rich territory. As we enter a typically weak Spring environment due to lower reinvestment cash, increased supply, and tax-related withdrawals, investors will likely remain somewhat cautious over the coming weeks. To get off the sidelines, we suspect the focus will be on new issues priced at a concession and volatile days where liquidity providers can pick up bonds 10bps+ cheaper than prior levels.

HY Munis

The HY market fared similarly, with early uncertainty leading to very wide bid/asks, but as calm was restored throughout the week, the market ultimately outperformed. Very few HY trades printed on Monday and benchmark names were off just 3-4bps, however, by Tuesday, things started to get sloppy. A morning BWIC with BBB rated senior living names saw bonds trade 8-10bps behind evals, which helped set the tone for the day. There was a customer order 15bps behind where a FL student housing deal had traded up to on the break two weeks ago and a dealer showing stock bids on select customer offerings in the senior living and development district space anywhere from 30-40bps behind evals.

Despite what would normally be a rotation into safety, HY funds continued to receive inflows, with Lipper showing +266mm, driving accounts to use the opportunity to deploy cash at higher yields than they've seen in a few weeks. As the market firmed up, JPM Research reported HY customer purchases fell 21% relative to recent averages, reflecting the ongoing lack of a true need for sellers to capitulate. Benchmark names like Cofina, Buckeye Tobacco, and Chicago BOE all finished the week off just 7-8bps, slightly better than the IG market and only widening about half as much as treasuries. It remains to be seen how long this conflict will last and what the read-through will be to economic activity and risk appetite, but it's clear that the HY market remains well funded and will need to undergo a longer period of instability before spreads can truly widen.

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Market Commentary

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