

U.S. Municipal Bond Market

REVISED: Our 2022 Municipal Bond Issuance Forecast

- We lowered our 2022 municipal bond issuance forecast to \$410 billion from \$495 billion (Nov. 2021.)
- Higher interest rates and lower economic growth are key reasons for the revision.
- Investors pulled about \$2.1 billion from municipal funds last week. But, we continue to believe taxable and tax-exempt municipal bonds are very investable right now.
- The HilltopSecurities Debt Capital Markets Group’s June 2022 survey results show opinions have evolved in favor of a green bond designation since December 2021.

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We are Now Expecting \$410 billion, Not \$495 billion of Issuance in 2022

We revised our 2022 municipal bond outlook in February, please see [REVISED: The Municipal Market in 2022, Due to the COVID-19 Paradigm Shift \(Feb 7, 2022\)](#), and we are modifying our 2022 issuance forecast as well. Our 2022 municipal bond issuance forecast was stale once the calendar turned to 2022 and factors kept building since the beginning of the year arguing in favor of lower bond activity. In November 2021, we published a forecast that would have been a record of \$495 billion. Please see [Our 2022 Municipal Bond Issuance Forecast \(Nov. 22, 2021.\)](#) Now, we are expecting municipal bond market primary issuance to come in at \$410 billion. Incidentally, \$410 billion is just below the \$436 billion 5-year average and right on top of the \$410 billion 9-year average we have seen the public finance community produce in recent years.

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What Changed? Lower Growth and Higher Interest Rates, Inflation

Rising interest rates since the beginning of the year created barriers to new money and refunding activity. On the new money side, public finance entities experienced a price-shock dynamic because of the steady increase in rates since January. We think that reality is setting in on the new money side however, and issuers will now realize that interest rates are in fact going higher and are likely to stay relatively elevated. The higher interest rate environment suppressed refunding activity this year on the taxable and tax-exempt side. Refundings are not likely to make a comeback, especially if the Fed increases the

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	2022 Revised Forecast (in \$)	2022 Revised Forecast (%)	2021 Actual (in \$)	2021 Actual (%)
New Money	\$348.500	85%	\$345.399	72%
Refunding	\$61.500	15%	136.213	28%
Total	\$410.000	100%	\$481.612	100%
Tax-Exempt	\$352.600	86%	\$353.828	73%
Taxable	\$57.400	14%	\$127.784	27%
Total	\$410.000	100%	\$481.612	100%

Sources: Refinitiv, The Bond Buyer and HilltopSecurities. (\$ in billions)

pace at which they raise their target rate. As of now, most are expecting that the Fed is going to elevate its target rate by 50 basis points during the Wednesday, June 15 meeting ([see Fed meeting calendar here.](#))

Most were also expecting another 50 basis point hike on July 27. Many forecasters were uncertain about what was likely to occur on Sept. 21, and last week's CPI release (see below) raised that level of uncertainty. Either way, it seems the path of U.S. interest rates is going higher, not lower. Another 50 basis point increase is very likely this week and additional 50 basis point increases in July and September are very likely as well. In coming weeks we will be listening to Fed comments to see if they signal that increases in July and/or in September could be even higher than 50 basis points.

The reality of lower economic growth is setting in as well. One of the key reasons we expected record issuance for 2022 initially back in November was because growth forecasts from many economists were coming in at 4.0% or higher. Now forecasts for 2022 U.S. GDP growth are mostly lower. The Organization for Economic Cooperation and Development published one of the latest revisions indicating U.S. growth is likely to come in at 2.5% (versus 3.7%) in 2022 and 1.2% in 2023 (versus 2.4%.) Please see [The Price of War by the OECD, \(June 2022.\)](#)

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Inflation is also a leading theme now, especially compared to the end of 2021. Inflation is accelerating and if you listen and or agree [with those arguing that it has not peaked](#), then inflation numbers might look messy in coming months and the Fed may in fact have to increase their response in September and perhaps maybe in July. Overall yields moved higher Thursday of last week after the [European Central Bank announced it would raise rates](#). Then on Friday markets reacted mostly negatively after [the May consumer price index \(CPI\) number came in at a 40 year high](#).

What Could Issuance Look Like for the Rest of the Year?

Total issuance in 2022 so far has trailed 2021 by almost 10%. It will not surprise us to see this gap widen by the end of the year mostly driven by lower refunding activity. April 2022 was the only month that came close year-over-year to 2021. We are not expecting issuance in any month for the rest of this year to beat out 2021 as you can see from our month-to-month forecast below. Some months may come close, and we expect activity to pick up again toward the end of the summer as it usually does, but again it is important to reinforce that we are not expecting activity in any one month to surpass last year or even surpass most recent averages. It is worth noting that we are expecting issuance to tail off by the end of the year because of the aggressive stance of the Fed. What is also possible is that this tail comes sooner, rather than closer to the end of the year. If we see much more aggressive Fed action it is possible that we could revise our issuance forecast again lower sometime during the third quarter of 2022.

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2021 Actual vs Our 2022 Revision

Month	2021 Actual	2022 Actual/ Forecast
January	\$28.183	\$26.104
February	37.052	30.535
March	47.768	44.141
April	37.105	36.721
May	35.358	32.167
June	50.364	40.000
July	37.601	35.000
August	43.885	40.000
September	44.604	40.000
October	41.811	35.000
November	37.042	25.000
December	40.840	25.332
	\$481.612	\$410.000

Sources: Refinitiv, The Bond Buyer, HilltopSecurities. (\$ in billions)

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We Only Expect Pockets of Strength in Municipal Demand

Investors pulled \$2.1 billion from municipal mutual funds per Lipper data reported Thursday (June 9) last week. Outflows slowed during the week ending May 26 when only \$1 billion flowed out of municipal funds and then \$1.2 billion flowed into municipal funds during the week ending June 2. This was the first time since Feb. 10 of this year that we saw inflows. So far, only four weeks out of 23 this year have seen inflows to municipal funds.

We continue to expect there could be some pockets, or very small pockets of strength in demand. [Our municipal bond analyst survey \(April 2022\)](#) reported that 76% of analysts expect that the trend of negative fund flows is likely to continue, and a little less than half of analysts are expecting net flows to be negative in all of 2022.

Although the overall attractiveness of municipals has decreased slightly since we wrote [Municipal Bonds are an Exceedingly Appealing Fixed Income Option Right Now \(May 11\)](#), we continue to be bullish on absolute tax-exempt and taxable municipal interest rates, and many relative value indicators. Taxable and tax-exempt municipal bonds remain very investable right now.

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How Important is the Green Bond Designation to Your Investment in a High Yield Credit?

There are some very compelling results in the [High Yield Impact Survey – 2022 Update](#) published by the HilltopSecurities Debt Capital Markets Group on June 3, 2022. It was an update to the group's [High Yield Impact Survey](#) published on Dec. 27, 2021.

Many of those directly involved in, and many observers of the municipal bond market are trying to figure out how to value a green bond designation during a primary market sale and how such a designation could support secondary trading activity. The HilltopSecurities Debt Capital Markets Group's survey results show that opinions on this topic have evolved in favor of a green bond designation since December. Those surveyed, and it is important to reinforce that this question was focused on high yield credits, in May reported:

In 2022, almost 60% responded that the designation is nice to have, 10% responded that the designation has a tangible value of 1-4 basis points and 2% said the designation is critical and worth 1-5 basis points. To compare, in the 2021 survey, 45% of responders stated that they do not consider the Green bond designation in their decisions, 45% said it is nice to have, and no respondent reported that it was critical to their investment decision. As we reflect upon this change in sentiment, the cause could be attributed to the proliferation of bonds with an ESG designation or the widening of spread that we have seen over the last six months which has allowed for better investor economics.

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This is a notable change between only about five months and it will be interesting to see how these results evolve in future HilltopSecurities Debt Capital Markets surveys.

Recent HilltopSecurities Municipal Commentary

- [School District Credit Quality is Strong, Former Mayor Bloomberg is Overreaching](#), June 2, 2022
- [Voters Want Normalcy – This is Not It – More Political Change is Likely](#), May 31, 2022
- [Municipal Bonds are an Exceedingly Appealing Fixed Income Opportunity Right Now](#), May 11, 2022

Readers may view all of the HilltopSecurities Municipal Commentary [here](#).

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