Munis weaken as Powell testimony stirs interest rate concerns

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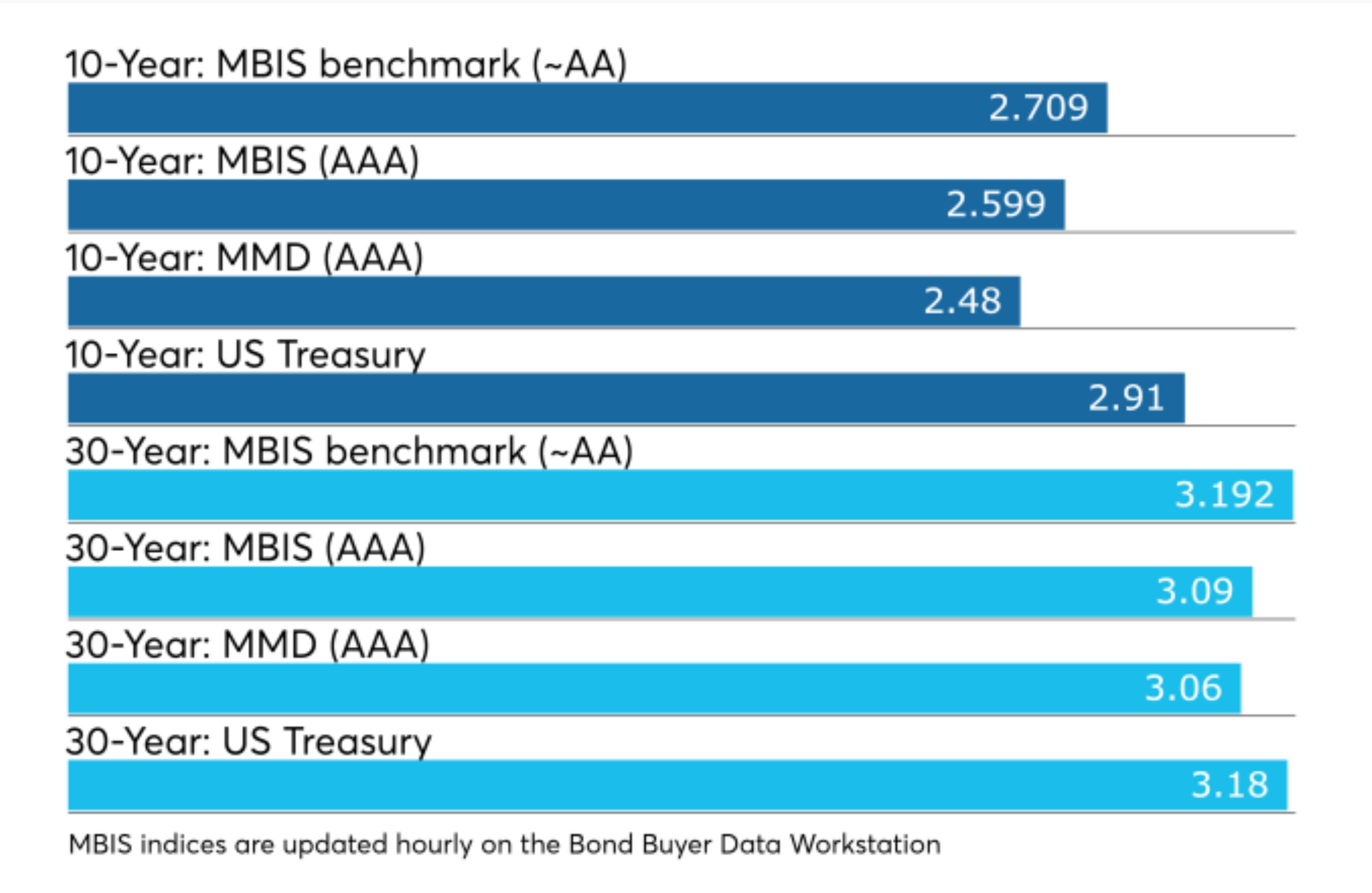
Published February 27 2018, 3:33pm EST



Municipal bonds weakened in subdued activity on Tuesday as new Federal Reserve Board

Chair Jerome Powell's testimony before Congress was perceived by market participants as increasing the possibility of tighter monetary policy.

Rep. Carolyn Maloney, D-N.Y., asked Powell after his testimony before the House Financial Services Committee what it would take to speed up Fed rate hikes. While he refused to comment about the exact number of times the Federal Open Market Committee might raise rates this year, he noted that his view of the economic outlook for the U.S. was stronger following the tax reform and the budget deal. Markets interpreted the response as hawkish.

"Investors paid particular attention to that question/answer, reading it as raising the risk of more than three rates hikes in 2018 and continued rate hikes in 2019," said Jeffrey Cleveland, chief economist at Payden & Rygel.

Trading remained modest throughout the day.

"The backdrop of the market digesting the comments of newly installed Fed Chief Powell has apparently tempered near-term tactical activity in the municipal market through the noon hour," said Jim Colby, senior municipal strategist and portfolio manager at Van Eck Associates. "Current snapshots of adjustments to the MMD scale reflect only modest gains beyond five years."

James Colby

Even with some high quality issuers coming to market — Virginia Beach, New York State Mortgage Authority and New York State Thruway Authority — the new issuance will present "no impediments to price discovery," Colby said. "As investors have come to recalibrate their notion of value along with slight changes in spreads and ratios, decent activity in the secondary market reflects some opportunity to seek and find value for platform investors."

Larger institutional asset allocators, however, may be pointing to next week' $2 billion California deal as the next vehicle where some value and structure is worthy of attention, he said.

"Still, a 30-day visible supply of only $8 plus billion will not, alone, disrupt current notions of where spread valuations should be in high grades," Colby said. "One key and inescapable metric of the market's current and potential for future performance is this comparative: The supply/demand ratio still favors near-term performance, as flows remain positive and supply — from a year-over-year perspective — is down some 40%."

Primary Market

Volume is estimated by Ipreo at $4.76 billion, comprised of $3.12 billion of negotiated deals and $1.64 billion of competitive sales.

On Tuesday, Barclays Capital premarketed the Los Angeles Department of Airports $375.88 million of Series 2018A subordinate revenue bonds subject to the alternative minimum tax for the Los Angeles International Airport.

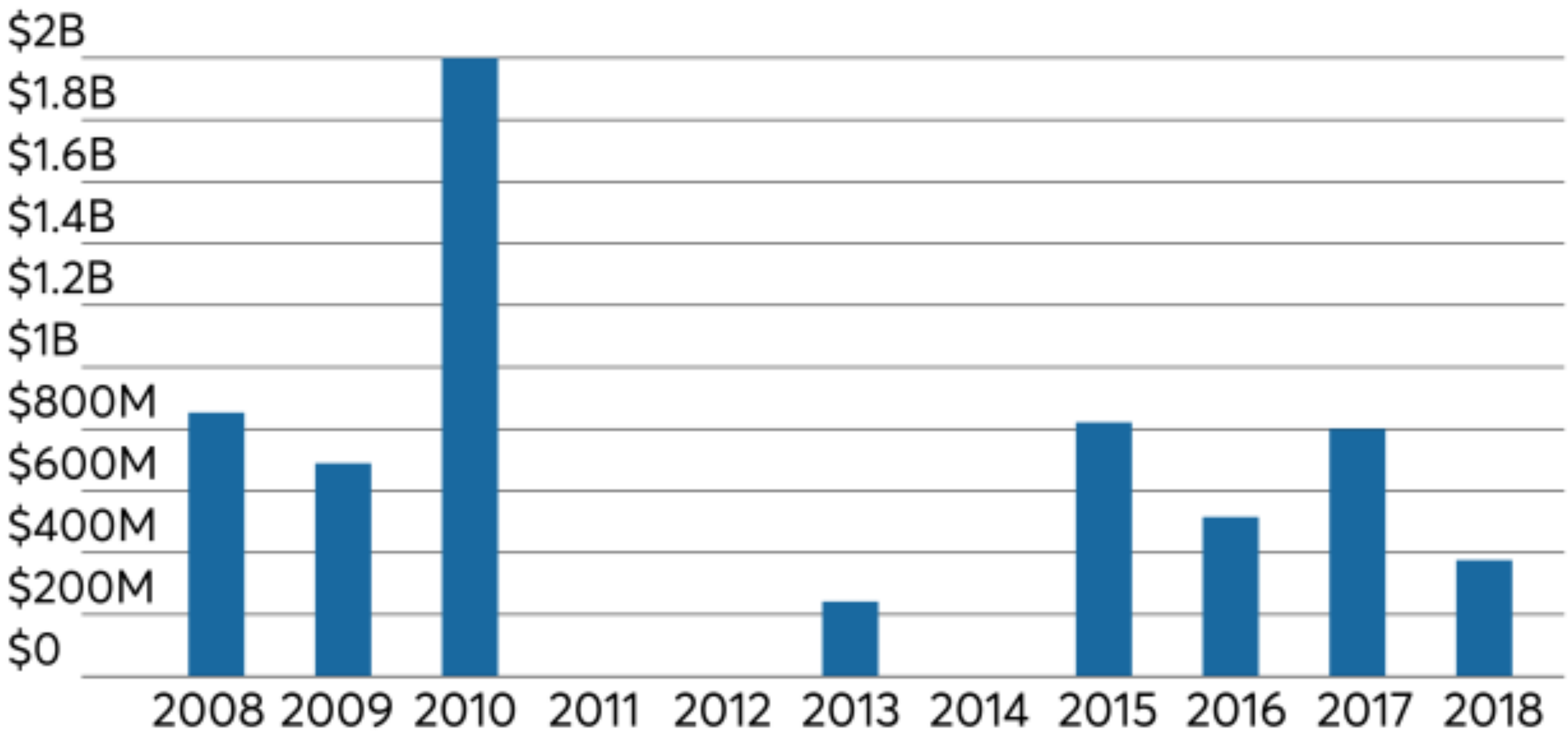
The deal was being premarketed at spreads of 11 basis points to 49 basis points over the MMD scale and 50 basis points over the MMD in 2043 and 85 basis points and 42 basis points over the MMD in a split 2048 maturity. The deal is slated to be priced on Wednesday.

The issue is rated A1 by Moody's Investors Service and AA-minus by S&P Ratings and Fitch Ratings. All three assign a stable outlook to the bonds.

Since 2008, the airport department has issued about $6 billion of bonds, with the most issuance occurring in 2010 when it sold $2 billion of bonds. The department did not come to market in 2011, 2012 or 2014.

Back in the air

Los Angeles Dept. of Airports municipal bond issuance



Source: Thomson Reuters

On Thursday, Baltimore County, Md., will competitively sell about $837 million of bonds and notes in four offerings.

The county will sell $225 million of general obligation metropolitan district bonds, 80th issue, and $121 million of 2018 GO consolidated public improvement bonds. Also on Thursday, the county will sell $246 million of Series 2018 consolidated public improvement general obligation bond anticipation notes and $245 million of Series 2018 metropolitan district general bond anticipation notes.

On Wednesday, Wisconsin will competitively sell $286.84 million of Series 2018A GOs

Also this week, Goldman Sachs will price Alabama's Black Belt Energy Gas District's $653 million of gas prepay revenue bonds for Project No. 3.

RBC Capital Markets will price the New York State Thruway Authority's $600 million of Series L general revenue refunding bonds. The deal is slated to be priced on Thursday.

And Bank of America Merrill Lynch is set to price Houston, Texas' $417 million of airport system subordinate lien revenue and refunding bonds consisting of Series 2918A bonds subject to the alternative minimum tax and Series 2018B non-AMT bonds. The deal is slated to be priced on Thursday.

Previous session's activity

The Municipal Securities Rulemaking Board reported 41,359 trades on Monday on volume of $7.87 billion.

California, Texas and New York were the states with the most trades, with the Golden State taking 15.799% of the market, the Empire State taking 13.339% and the Lone Star State taking 10.749%.

Treasury sells one-year and 4-week bills

The Treasury Department on Tuesday auctioned $22 billion of 364-day bills at a 2.020% high yield, a price of 97.957556. The coupon equivalent was 2.080%. The bid-to-cover ratio was 3.00. Tenders at the high rate were allotted 96.77%. The median yield was 1.990%. The low yield was 1.960%.

Treasury also auctioned $60 billion of four-week bills at a 1.495% high yield, a price of 99.883722. The coupon equivalent was 1.518%. The bid-to-cover ratio was 2.80. Tenders at the high rate were allotted 20.24%. The median rate was 1.440%. The low rate was 1.400%.

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Christine Albano is a reporter in the Investor's & Investing beat, which she has covered for

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Comment