US Municipal Notes

Muni Charts of the Week – Strong Technicals Continue

After two heavy volume months, municipal issuance fell back down to earth in July. While volume was spot on our original $26 billion projection for the month, it was lower than the $30 billion 10-yr average for July. The 10-yr average for August is also $30 billion. With this week’s issuance, volume for the first half of August should approach $20 billion, with two full weeks of production left. Therefore, August 2016 volume is likely to either hit the average, or rival the $32 billion posted in August 2015. This puts the market on a pace to finish the year with total volume in the $400 billion to $425 billion range. With new money issuance flat to slightly higher yr/yr, the key to issuance in the remaining four months of the year will be refundings which, to date, have not kept pace with 2015 issuance.

Municipal bond mutual fund flows continue to be impressive; with the 44th consecutive week of inflows reported by Lipper US Fund Flows in the week ended August 3. The breadth of these inflows remains very strong as all municipal subsectors posted inflows last week (Exhibit 2). Since this string of inflows began in October 2015, municipal funds have seen cumulative inflows of $49 billion. We expect these inflows to continue for the next several weeks, but believe they will begin to moderate as we move past the summer peak in coupon payments. Elsewhere, the July employment report reflected a solid gain in local education payrolls in the month (Exhibit 3). However, since July is typically a month in which local education reduces headcount, the gain was solely a product of the seasonal adjustment the Bureau of Labor Statistics (BLS) applied to the data. Local general government employment was up slightly, but state employment has yet to come off its post-recession bottom. Finally, 1Q2016 state GDP statistics clearly illustrate the impact of lower energy prices on the broader economies of the resource states. North Dakota, for example, reported an 11.4% SAAR decline in its GDP in the first quarter (Exhibit 4).

Exhibit 1: July was the only month thus far in 2016 to post new issue volume lower than its respective 10-yr average with $26 billion issued vs. the $30 billion average for the month. August is shaping up to be an average month as well. Note that the 10-yr average for August is also $30 billion. After this week, August volume will be approximately $20 billion with two solid weeks of production left to go. We continue to expect 2016 full-year volume of between $400 billion and $425 billion.
Exhibit 2: Municipal Funds reported their 44th consecutive week of net inflows last week. The approximately $780 million in net inflows was almost identical to the prior week’s number. The August 1 coupon was a big factor in last week’s results. Consequently, we expect flows over the next few weeks to remain in positive territory, but to diminish somewhat.

Exhibit 3: State and local governments made a positive contribution to last week’s July employment report, adding almost 35,000 employees in the month. This is principally the result of a 21,600 gain in the local government employment sector. We note, however, that this increase is a result of the BLS’ seasonal adjustment. Local education payrolls decline substantially each July as the school year ends. Last month, this sector posted the lowest level of non-seasonally adjusted July payroll reductions since 2005, thereby resulting in a seasonally adjusted gain in education payrolls.
Exhibit 4: The most recent release of quarterly state GDP statistics illustrates the influence that energy and farm prices are exerting on the economies of the resource states. We note that the outsized decline in North Dakota’s GDP was the product of declines in several industries, not just mining and agriculture.

Percent change in real GDP growth by state (SAAR)

Source: US Bureau of Economic Analysis
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