Municipal Bond Market Monitor

Municipal Bond Group

Q1 2023

Q1 2023 Municipal Market Review

A volatile, but encouraging start to the year

- Muni bond Index: +2.78% | HY Muni Index: +2.73% | Taxable Muni Index: +5.21%
- US Treasury Index: +3.01% | IG Corporate Index: +3.50%

Yields decreased across the curve (AAA Muni Yields):

- 2-Year 2.60% → 2.38% -22 bps
- 5-Year 2.52% → 2.22% -30 bps
- 10-Year 2.63% → 2.27% -36 bps
- 30-Year 3.58% → 3.30% -28 bps

Muni Fund flows modestly negative & supply continues to be low

- -$1.7 billion in outflows from muni mutual funds in Q1 and tax exempt supply of $73bn, down 25% Y/Y

Muni/Treasury ratios remain rich, particularly at the front end of the curve

- 2 year AAA Muni / UST ratio at 59%.
- 10 year AAA Muni / UST ratio at 65%.

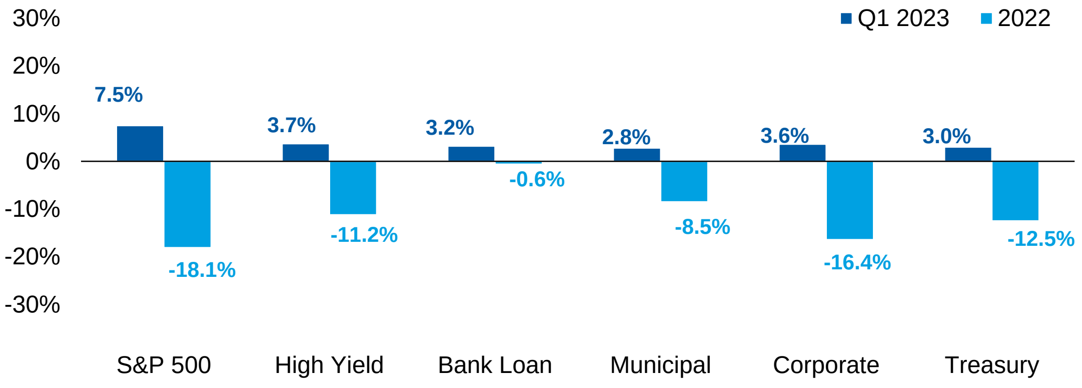
Past performance is no guarantee of future results. It is not possible to invest directly in an index. See end of report for important additional information. This commentary may contain statements that are not historical fats, referred to as “forward looking statements”. Actual future results may differ significantly from those stated in any forward-looking statement, depending on factors such as changes in securities or financial markets or general economic conditions.

Source: Index Performance: Bloomberg, AAA YTD changes as of 3/31/2023. Fund Flows: Lipper, Ratios: Bloomberg

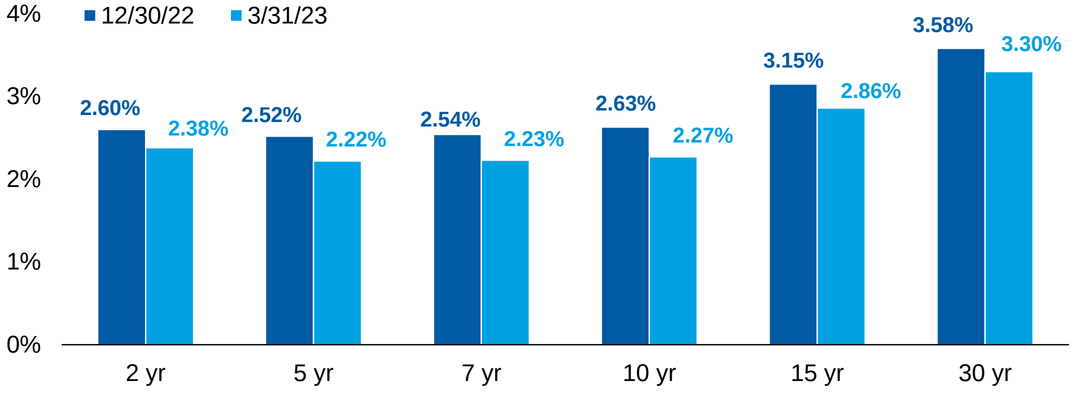
Municipal Yield Changes

- It was a volatile start to the year as inflation data was mixed, unemployment remained low and debate around an economic 'hard', 'soft' or 'no' landing continued on.
- After raising federal funds 425 bps in 2022, the FOMC lifted rates 25bps in February and another 25bps in March despite the emergence of the regional bank crisis.
- Treasury yields displayed significant volatility and finished the quarter 30-40bps lower. Most of the move occurred in March with the 2-year yield declining 76bps, while the 30-year yield moved 23bps lower.
- Though not quite as volatile, municipal yields decreased 22-36bps across the curve.

Major Asset Class Returns



AAA Municipal Yields (%)

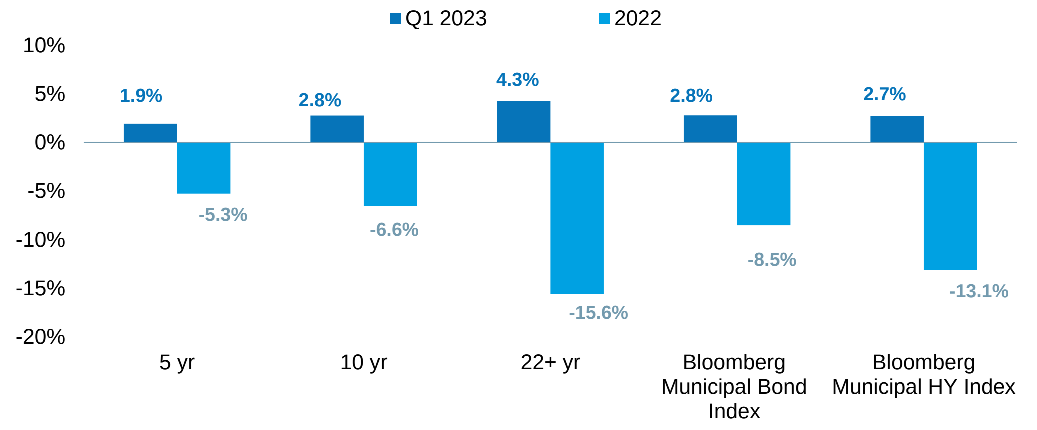


Source: Bloomberg and Thomson Reuters as of 3/31/2. Past performance is no guarantee of future results. It is not possible to invest directly in an index. See end of report for important additional information. *Basis points (BPS) is a unit that is equal to 1/100th of 1% and is used to denote the change in a financial instrument.

Index Returns

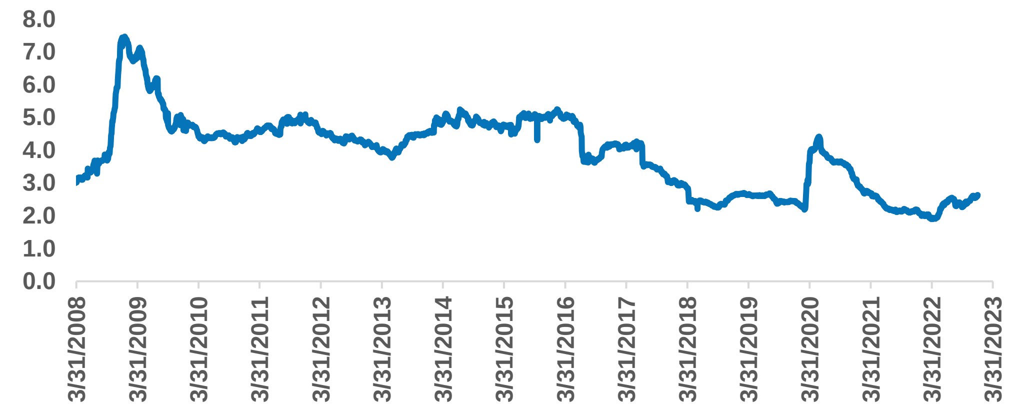
- Consistent with Q4 ‘22, high quality muni returns were positive across the curve with long duration outperforming.
- Up 3.7%, BBB’s outperformed, while high yield municipals performed in line with the investment grade benchmark.

Index Returns



- High yield spreads widened 12bps during the quarter and finished the quarter at +275bps to the AAA Index.
- Though high yield spreads remain relatively neutral, we believe absolute yields and value in certain high yield sectors and issuers continue to be attractive.

High Yield Index vs AAA Index Yield to Worst Spread

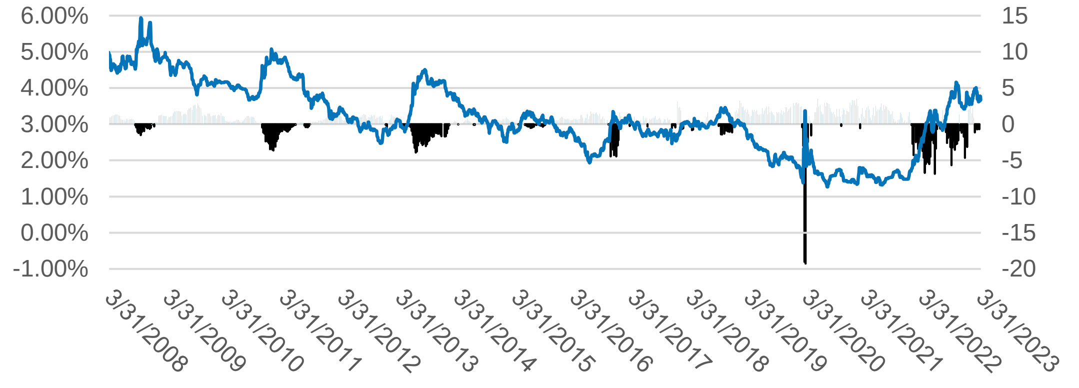


Source: Bloomberg, MMA and Morningstar Direct as of 3/31/23. Past performance is no guarantee of future results. Performance less than one year is cumulative. It is not possible to invest directly in an index. See end of report for important additional information.

Flows and Issuance

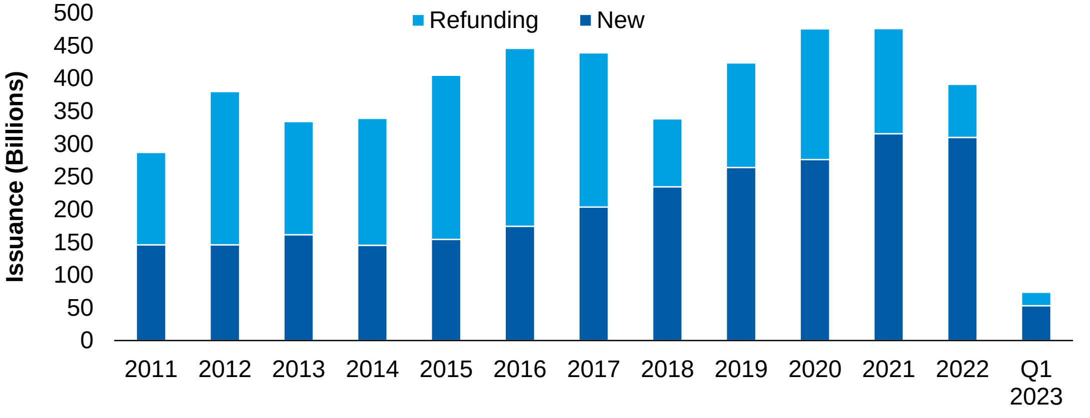
- Though muni funds enjoyed net positive flows early in the quarter, they experienced net outflows for the final six weeks of the quarter.
- Overall, net outflows finished at a modest -$1.7billion, according to Lipper.

Muni Mutual Fund Flows



- At $73bn, municipal issuance was down 25% vs Q1 ‘22. 81% of issuance was new money and 19% was refunding deals.
- Taxable municipal issuance remained low as higher rates slowed advance refunding deals. For the quarter, taxable muni issuance was down 29%, at approximately $12.0 billion.

Municipal Bond Issuance: New vs. Refunding

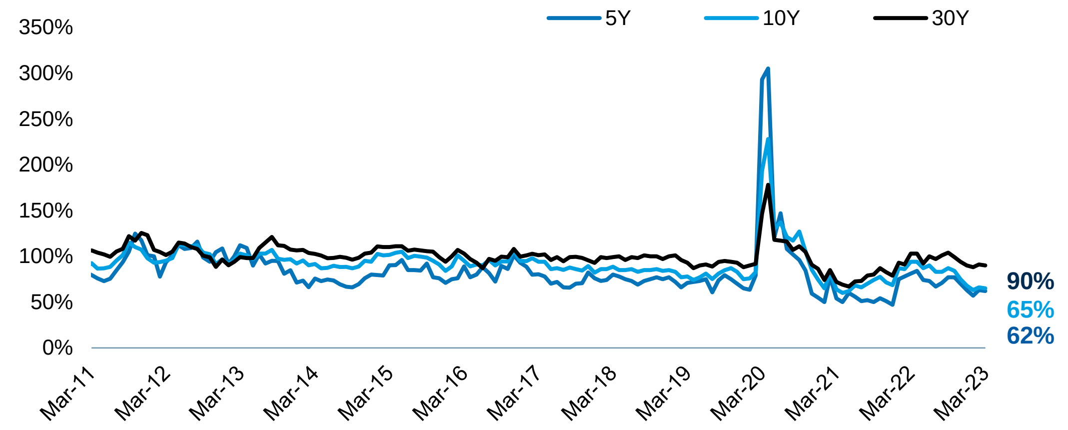


Source: Sifma, BofA Merrill Lynch Global Research, Thomson Reuters Municipal Market Data. Date Range: March 2008–March 2023.
Flow data provided by ICI. Municipal Bond Issuance data from SIFMA, Bloomberg Barclays Research. Private placement issuance counted as new capital.

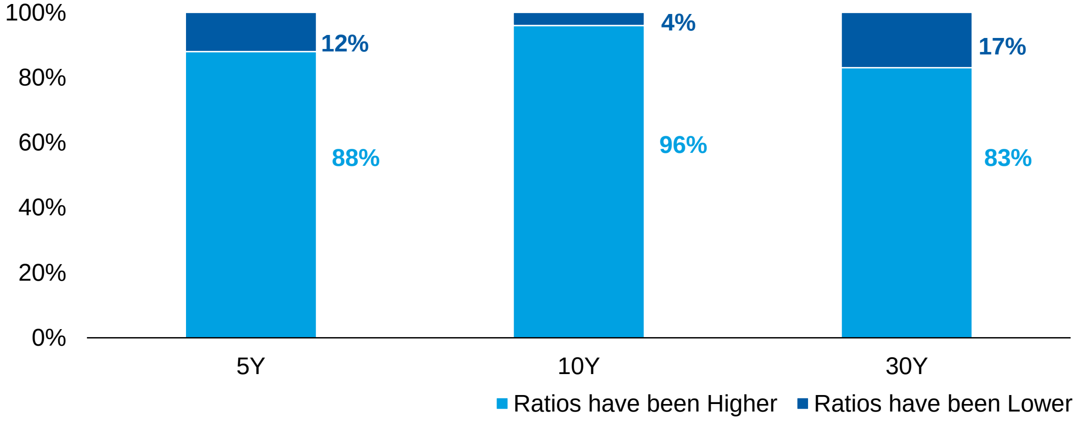
Muni-to-Treasury Yield Ratios

- Performance for munis and treasuries was largely in-line in Q1 and muni/treasury ratios were flat to slightly lower across the curve.
- Specifically, the 5-year muni/treasury ratio richened from 63% to 62%, the 10-year richened from 68% to 65% and the 30-year ratio was unchanged at 90%.
- Over the last 10 years, the 5-year, 10-year and 30-year muni/Treasury ratios have been lower (richer) approximately 12%, 4%, and 17% of the time, respectively.
- This indicates that AAA-rated municipals ended the quarter relatively rich across the curve.

AAA Muni-to-Treasury Yield Ratios (%)



How Attractive Are Muni/Treasury Ratios vs. History

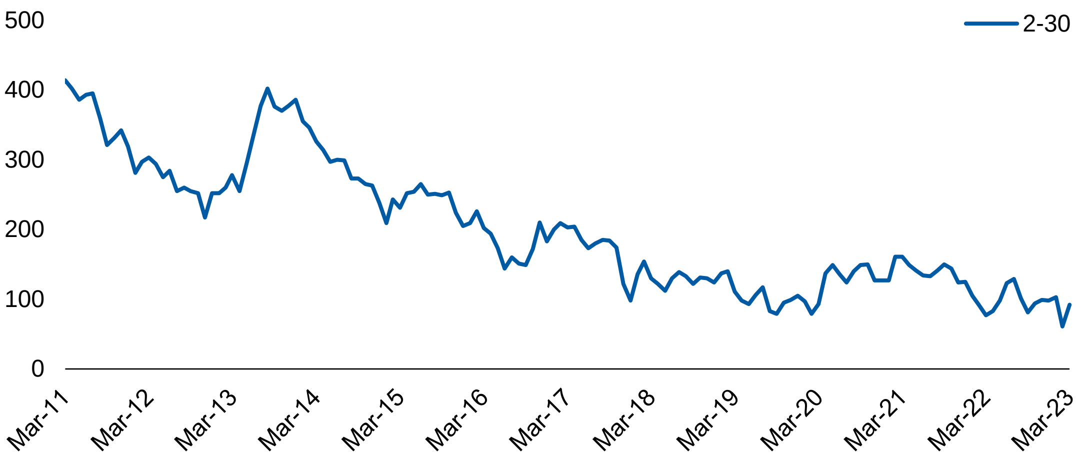


Source: Thomson Reuters as of 3/31/23, Bloomberg as of 3/31/23. Past performance is no guarantee of future results. It is not possible to invest directly in an index. See end of report for important additional information.

Municipal Yield Curve

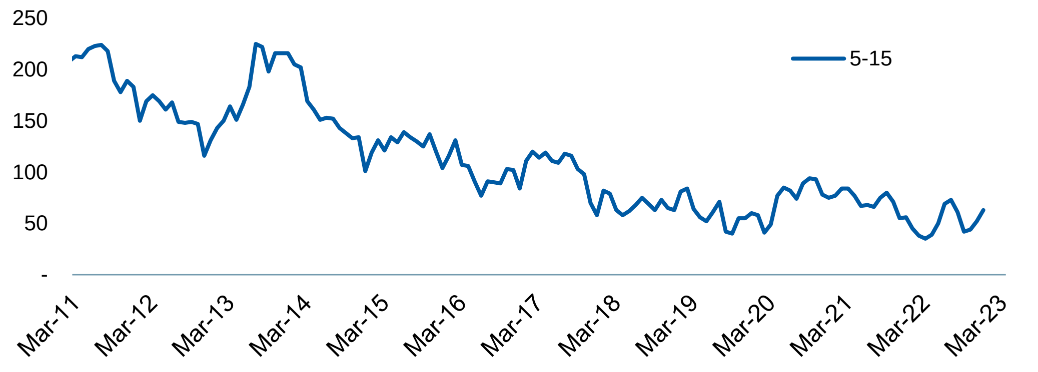
- The municipal curve bull flattened in Q1 and became modestly inverted on the front-end, as 2-year yields declined 22bps while 30yr yields decreased 28bps.
- The treasury curve remained inverted as the 2-year yield ended the quarter at 4.03% while the 30-year yield finished at 3.67%.

2-Year / 30-Year Curve



- At quarter end, the five-to-fifteen year portion of the muni curve was almost unchanged as 5-year yields declined 30bps while 15-year yields decreased 29bps.
- At the end of the quarter, an investor picked up 67% of the yield available by going out 5 years and 87% by going out 15 years.

5-Year / 15-Year Curve



Source: Thomson Reuters as of 3/31/23. Past performance is no guarantee of future results. It is not possible to invest directly in an index. See end of report for important additional information.

Municipal Yield Curve

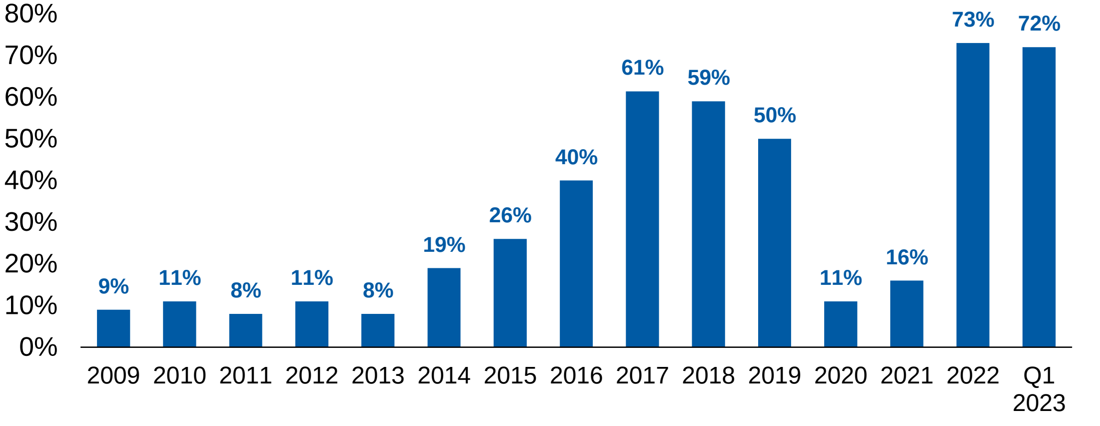
- Following the 50bps hike in December, the Fed raised its policy target 25bps in February and another 25bps in March to end the quarter at 4.75% - 5.00%.

- At quarter end, the market was split 50/50 as to whether the Fed will hike an additional 25bps at the next meeting in May.

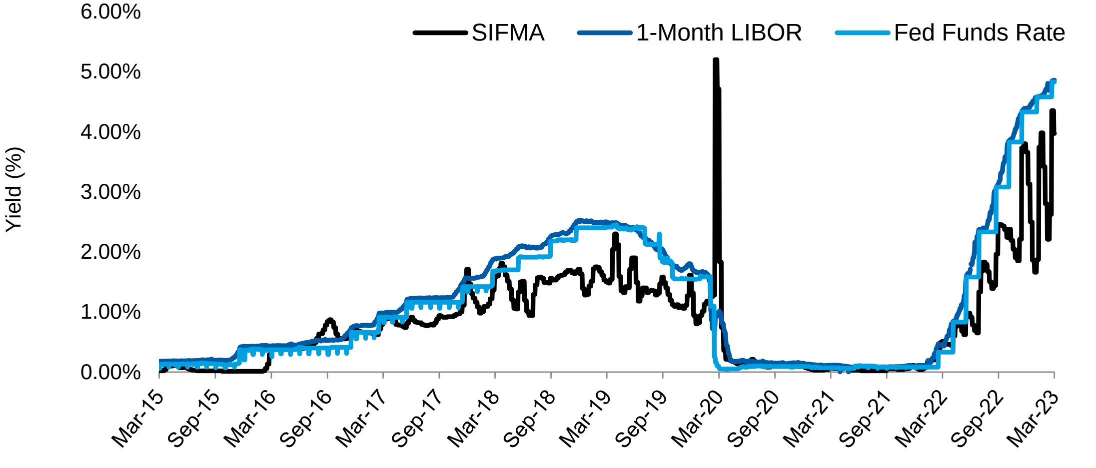
- After jumping 360bps in 2022, the SIFMA* Index increased 31bps and ended Q1 at 3.97%.

- While absolute yields on ultra-short municipals and muni floating rate notes continue to look attractive, we believe investors should consider a balanced approach by thoughtfully adding duration to overall municipal portfolios.

Percentage of Entire Municipal Yield Curve Captured by 2-Year Municipal Bond



SIFMA, LIBOR and Fed Funds Yield (%)

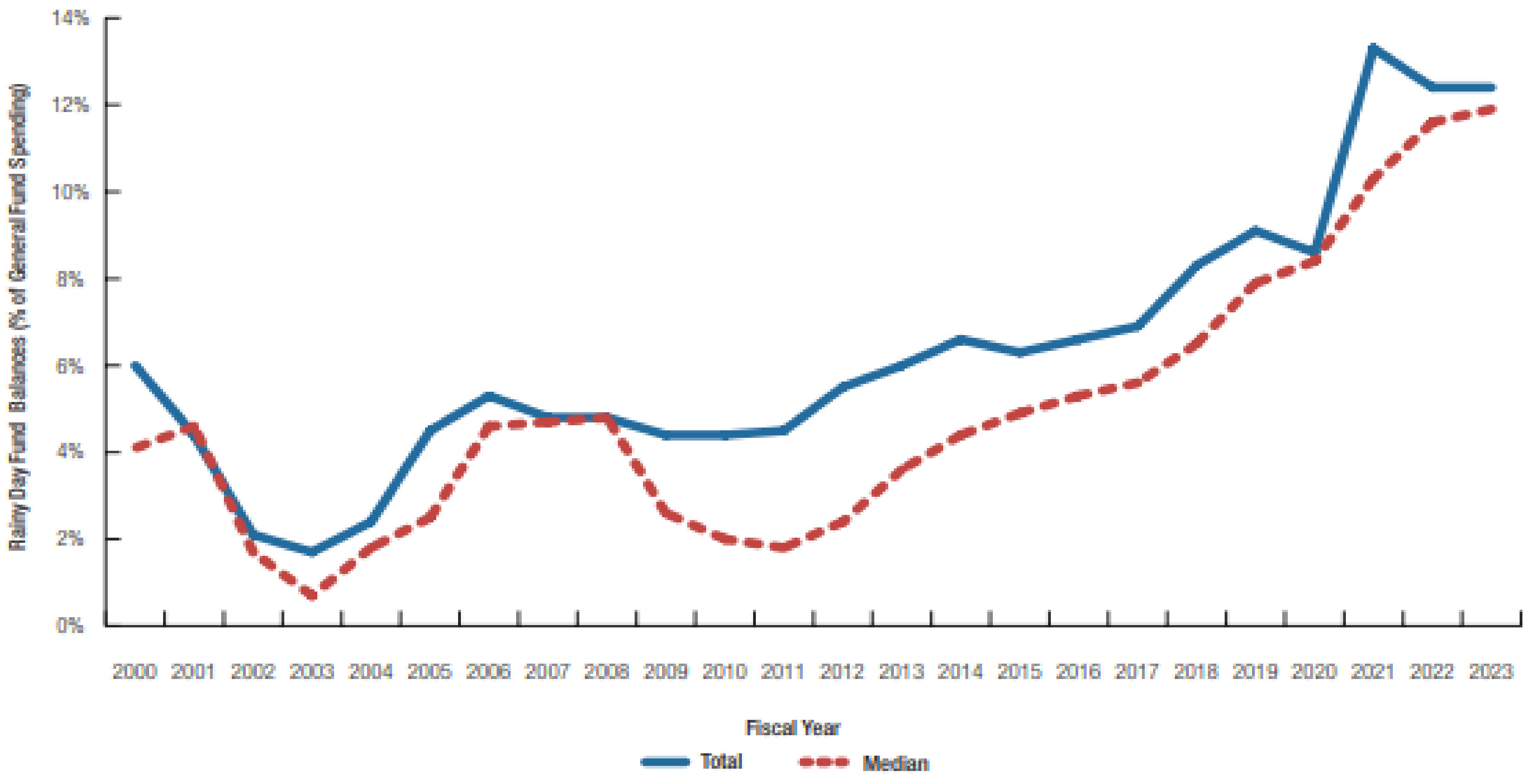


Source: Thomson Reuters, Federal Reserve as of 3/31/23. *SIFMA is a seven-day high grade money market index comprised of tax-exempt variable rate demand obligations. Past performance is no guarantee of future results. It is not possible to invest directly in an index.

States Prudently Building Reserves and Liquidity

Rainy day fund balances reached a record $135B in FY22 equating to 11.6% of general fund expenditures

Rainy Day Fund Balances as a Percentage of Expenditures Fiscal 2000 to Fiscal 2023

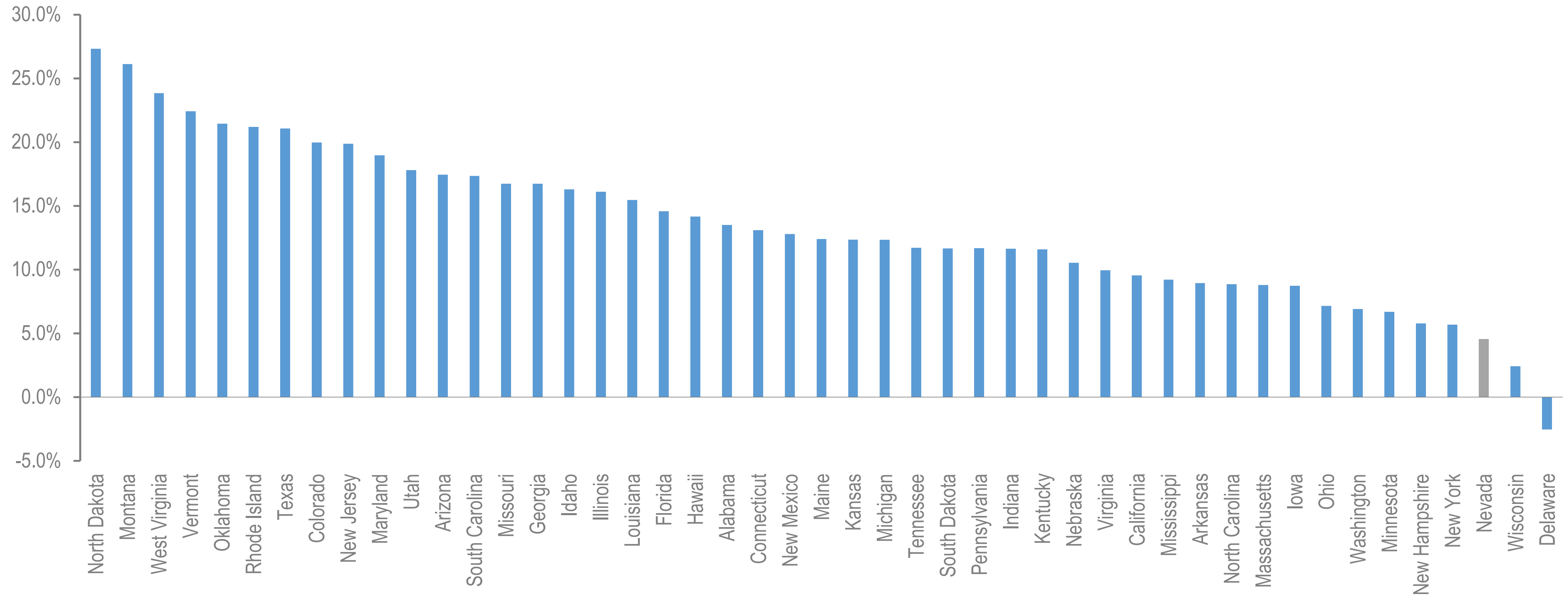


Source: National Association of State Budget Officers.

Robust State Revenues

Calendar year 2022 tax revenue increased 13.4% compared to 2021 illustrating the resilience of collections, lasting impact of robust federal aid, and positive correlation with inflation.

Calendar Year 2022 Total Tax Revenue, % change vs. 2021

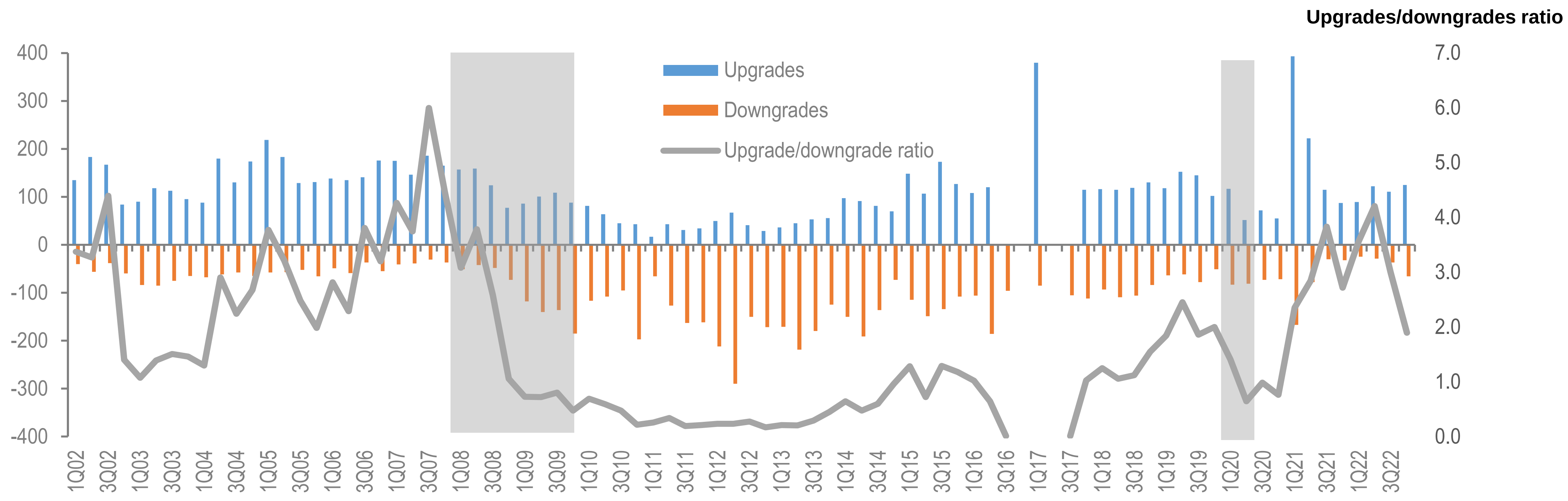


Source: Individual state monthly tax reports, J.P. Morgan. Note: Oregon, Wyoming, and Alaska do not provide monthly tax data. Bars in gray indicate July data is not yet available and YTD period has been adjusted.

Increase in Upgrades Due to Strong Credit Environment

Though upgrades have outpaced downgrades, credit quality may have peaked

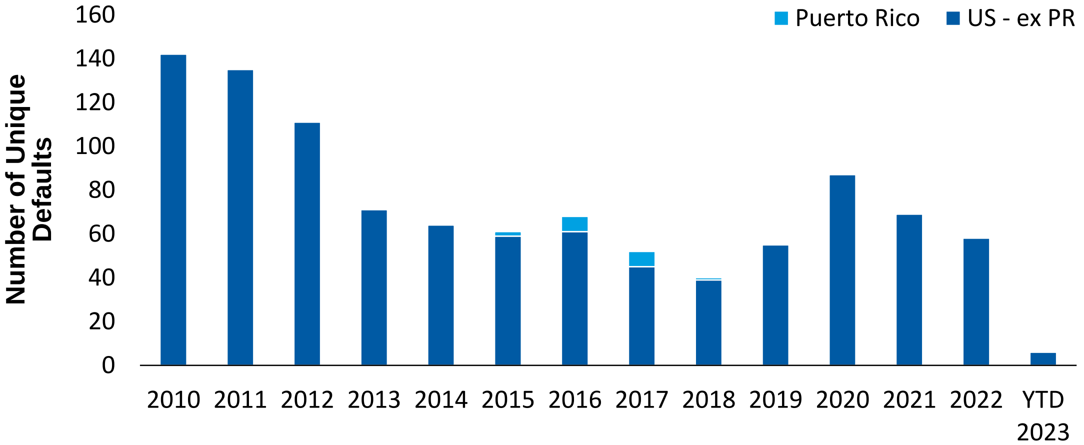
Moody’s Count of Municipal Upgrades and Downgrades,



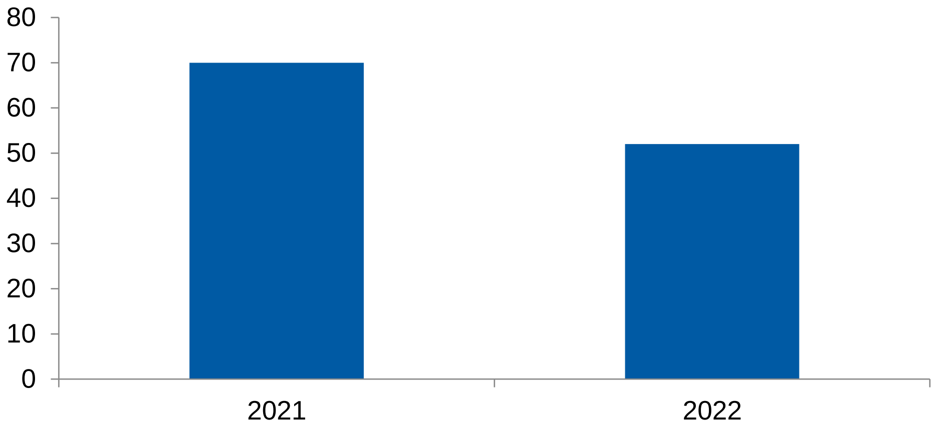
Source: S&P Global Ratings, J.P. Morgan. Gray shaded area indicates recessionary period. Data through 1Q23.

Municipal Default Overview

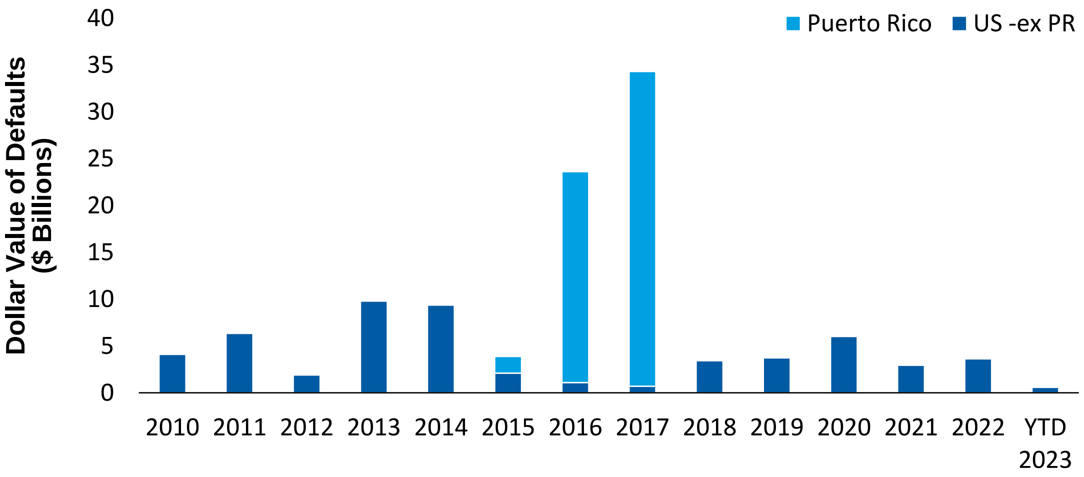
Number of Unique Annual Defaults



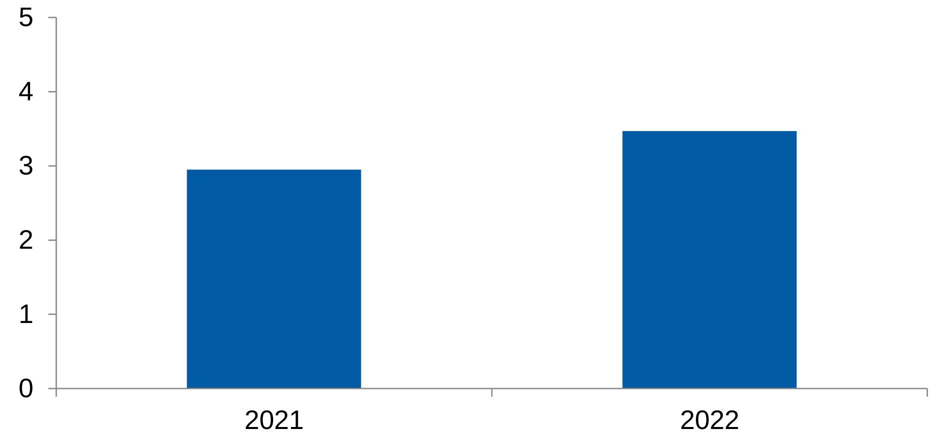
Number of Unique Annual Defaults Decreased by 26% in 2022



Dollar Value of Annual Defaults ($ Billions)



Dollar Value of Annual Defaults ($ Billions) Increased by 17% in 2022

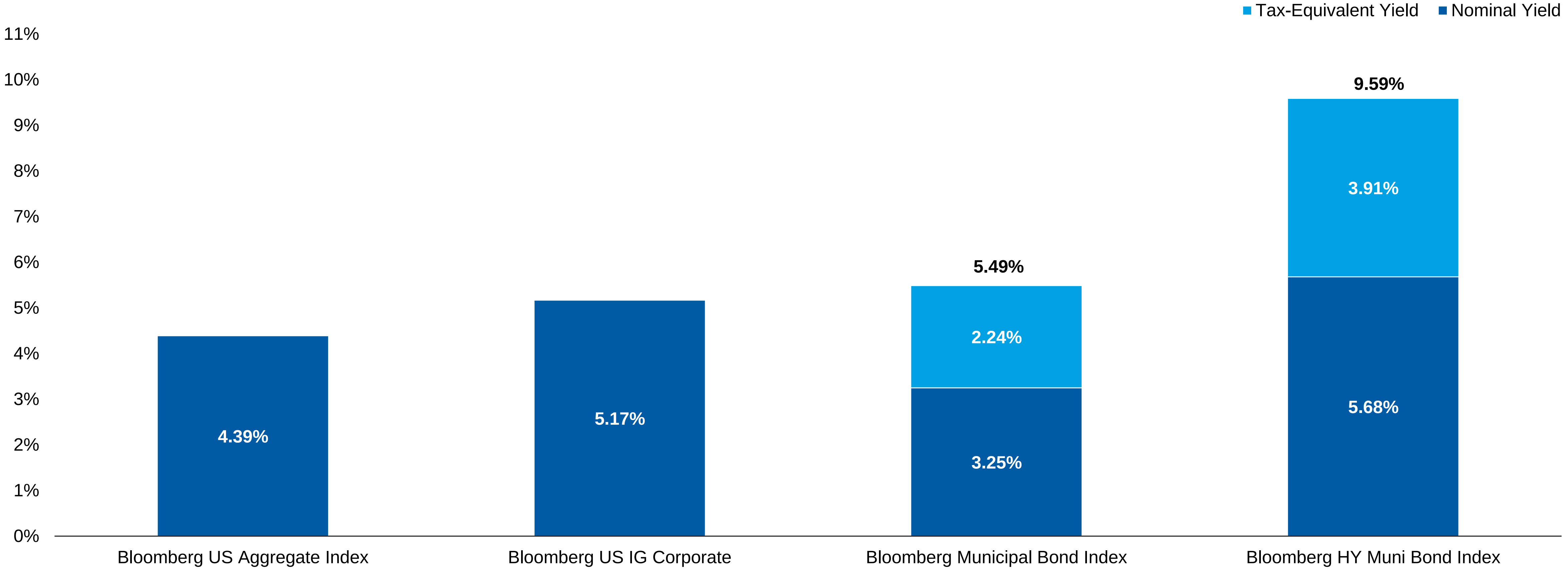


Source: MMA. Default data as of 3/29/2023

Taxable Equivalent Yields

Municipal taxable-equivalent yields appear very attractive relative to other high quality options.

Taxable Equivalent Yields



Sources: Barclays Live as of 3/31/23, Tax Policy Center. This table is for illustrative purposes only and uses the highest current applicable federal tax rates plus 3.8% health care tax. Past performance is no guarantee of future results. It is not possible to invest directly in an index. See end of report for important additional information.

Municipal Market Outlook

- Volatility should persist as the market remains focused on FOMC rate policy, inflation and employment data, and the impact the regional banking crisis has on economic activity.
- Driven by Treasury strength, we continue to believe broad muni indices could be up 5-7% with the long end outperformance.
- We believe strong technicals will drive outperformance in 2023 due to low issuance and a potential shift to positive fund flows.
- We expect high quality muni spreads remain stable as credit fundamentals remain solid and state rainy day balances are elevated.
- In lower-rated municipals, credit selection will be particularly important in a potential recessionary environment.
- We believe certain hospitals and healthcare systems could be opportunities in a sector expected to underperform overall.
- Municipal yields continue to look attractive on a tax-adjusted basis relative to other high quality options.

Appendix: Additional Slides

Overview of Legislation and Municipal-Related Spending in Relief Bills

The below table provides a high-level summary of the fiscal support for municipals through the four most recent pieces of legislation passed by Congress. In aggregate, over $1.7 trillion of capital has been allocated to various parts of the municipal bond market.

	2021 Infrastructure Bill	American Rescue Plan	Dec. Federal Stimulus	CARES Act
Total Muni Market Support	**$550**	**$650**	**$157**	**$347**
States	$136	$408	$30	$169
Locals	--	$182	$30	$164
Community based orgs.	--	–	–	$1
Not for Profits	--	$0.8	$15	–
Healthcare	--	$13	$4	$108
Primary/Sec Education	--	$137	$58	$25
Higher education	--	$40	$26	$17
Airports/Ports	$42	$11	$2	$10
Surface transit	$110	–	$10	–
Mass transit	$39	$30	$14	$25
Other Transportation	$78	$2	$2	–
Housing	--	$39	$25	–
Utilities	$143	–	–	–

Source: US Congress, J.P Morgan. Note: Sum of individual sector amounts may not add up to aggregate total due to double counting, as much of the capital is shared across sectors.

RISK CONSIDERATIONS

An imbalance in supply and demand in the municipal market may result in valuation uncertainties and greater volatility, less liquidity, widening credit spreads and a lack of price transparency in the market. There generally is limited public information about municipal issuers. Investments in income securities may be affected by changes in the credit worthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. As interest rates rise, the value of certain income investments is likely to decline. The London Interbank Offered Rate or LIBOR, is used throughout global banking and financial industries to determine interest rates for a variety of financial instruments (such as debt instruments and derivatives) and borrowing arrangements. The ICE Benchmark Administration Limited, the administrator of LIBOR, ceased publishing certain LIBOR settings on December 31, 2021, and is expected to cease publishing the remaining LIBOR settings on June 30, 2023. The transition process may involve, among other things, increased volatility or illiquidity in markets for instruments that currently rely on LIBOR, such as floating-rate debt obligations. Investments involving higher risk do not necessarily mean higher return potential. Diversification cannot ensure a profit or eliminate the risk of loss. Debt securities are subject to risks that the issuer will not meet its payment obligations. Low rated or equivalent unrated debt securities of the type in which a strategy will invest generally offer a higher return than higher rated debt securities, but also are subject to greater risks that the issuer will default. Unrated bonds are generally regarded as being speculative.

Credit ratings that may be referenced are based on Moody's, S&P or Fitch, as applicable. Credit ratings are based largely on the rating agency's investment analysis at the time of rating and the rating assigned to any particular security is not necessarily a reflection of the issuer's current financial condition. The rating assigned to a security by a rating agency does not necessarily reflect its assessment of the volatility of a security's market value or of the liquidity of an investment in the security. Ratings of BBB or higher by Standard and Poor's or Fitch (Baa or higher by Moody's) are considered to be investment grade quality.

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ADDITIONAL INFORMATION

Important Information and Disclosure

TERMS

Municipal-to-Treasury Yield Ratios are relative value indicators that measure the richness or cheapness of Municipal bond yields to comparable maturity Treasury bond yields.

Yield to Worst is a measure which reflects the lowest potential yield earned on a bond without the issuer defaulting. The yield to worst is calculated by making worst-case scenario assumptions by calculating the returns that would be received if provisions, including prepayment, call or sinking fund, are used by the issuer.

INDEX DEFINITIONS

Bloomberg Municipal Bond Index is an unmanaged index of municipal bonds traded in the U.S.

Bloomberg U.S. Aggregate Index is an unmanaged index of domestic investment-grade bonds, including corporate, government and mortgage-backed securities.

Bloomberg U.S. Corporate High Yield Index measures USD-denominated, non-investment grade corporate securities.

Bloomberg U.S. Corporate Index is an unmanaged index that measures the performance of investment-grade corporate securities within the Barclays Capital U.S. Aggregate Index.

S&P/LSTA Leveraged Loan Index is an unmanaged index of the institutional leveraged loan market.

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MIDDLE EAST

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