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- With more individuals sourcing tax exempt municipal bonds for fixed income needs, the municipal bond sector produced the best first quarter return since 2014.
- It would not be unusual to witness a weakening of municipal bond pricing to begin 2Q19 as local and state municipalities bring an increase of new issuance to the market and buying begins to slow due to the high prices.

Tax reporting season is affecting everyone but especially those in high income tax states due to the State and Local Tax deduction that is now capped at $10,000. This new limitation may shock high net worth individuals as their tax liability may be more than anticipated. As more tax payers file their returns, fixed income investors may change their asset allocation to increase holdings in tax-exempt municipal bonds. With tax-exempt municipal bond yields higher than previous years and inflation remaining subdued, real returns with reduced risk will become more appealing. For only the second time in history has tax filings shown an excess of 6 million tax returns with tax exempt income declared proving that more individuals are adding municipal bonds to their asset allocation.

With more individuals sourcing tax exempt municipal bonds for fixed income needs, the municipal bond sector produced the best first quarter return since 2014. Impressive demand of 12 consecutive weeks of inflows that outstripped supply forced prices higher and yield lower which gave local and state municipalities the opportunity to offer new issuance. Favorable yields to state and local municipalities bringing new issues to the market grew by $76.3 billion for the quarter, a 24 percent increase over last year. Granted, some may state the increase was based on a low 1Q18 number as most municipalities pushed new issuance into 4Q17 ahead of the 2018 tax reform act which left a void of issuance in 1Q18. However, notable new issuance in 1Q19 of $1.8 billion for San Francisco International Airport, $2.3 billion in California State general obligations and $1 billion in Connecticut general obligations is an impressive start to the calendar year. It is anticipated that new issuance may top $380 billion for calendar year 2019 which would be a sizable increase over previous years as infrastructure issuance leads the new offerings.

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The rapid increase in prices in 1Q19 brought undesirable comparison with comparable Treasury yields. 10 year municipal bond yields are 78 percent of comparable Treasuries, the lowest percentage since 2001. That decline in the ratio indicates that tax exempt municipal bonds have grown more expensive relative to Treasuries. The historical average is 85 percent municipal yield to Treasury yield. In 4Q18, the yield ratio comparison was 92 percent of municipal bond yield compared to Treasury yields. That is a considerable change in a relative short period of time. It would not be unusual to witness a weakening of municipal bond pricing to begin 2Q19 as local and state municipalities bring an increase of new issuance to the market and buying begins to slow due to the high prices. Crossmark Global Investments Municipal Fixed Income team will be selectively buying bonds as prices normalize.

Crossmark Global Investments continues to find value in the municipal secondary market with bonds rated A or better involved with essential services like water, sewer, power, streets, highways, school education and general obligations. The ideal maturities on the yield curve have moved to the 10 to 20 year range with a call feature between 2021 and 2025. Crossmark Global Investments continues to hold a shorter duration than the Barclay's Quality Intermediate Municipal Index with a focus on higher quality municipalities. Crossmark Global Investments continues to use municipal bond market volatility to opportunistically manage the portfolios entrusted to us.

Our Firm

Crossmark Global Investments is an innovative investment management firm. We provide a full suite of investment management solutions to institutional investors, financial advisors and the clients they serve. We have a multi-decade legacy of specializing in values based investment strategies for clients. Founded in 1987, the firm is headquartered in Houston, Texas and manages approximately $4.9 billion in AUM.

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