

QUARTERLY UPDATE: 3Q 2021 MUNICIPAL FIXED INCOME COMMENTARY



Municipal Fixed Income is a separately managed account investment strategy



written by
Patrick Garboden, Sr. Portfolio Manager

Markets and Performance

Municipal bonds tracked the U.S. Treasury market selloff, driving yields on benchmark 10-year tax-exempt debt to the highest level since late March 2021. This move jolted the calm that had cushioned the \$4 trillion municipal market for most of the third quarter. The breakout in yields after the September Federal Reserve meeting led to speculation that policymakers could begin tapering bond purchases in 2022 and raise short-term Fed Funds rates as soon as late 2023. According to Bloomberg, state and local debt maturing in 10 years yielded 73.20% of Treasuries at quarter-end, compared with 71.54% in the previous session. The municipal-to-Treasury yield ratio was 71.66% at the end of August 2021.

Positive and Negative Contributors to Performance

The Crossmark Municipal Fixed Income model portfolio returned 0.02% for the quarter ending September 30 versus -0.03% for the Bloomberg Quality Intermediate Municipal Index. Investing in high-quality credit with a premium coupon positively contributed to the model portfolio's performance as lower coupon bonds declined more than premium coupon bonds as interest rates moved higher. The shorter duration positioning of the Strategy was a positive contributor to performance in September as concern over potential higher inflation and FOMC bond purchase tapering became more pronounced. Also, investors were increasingly defensive in the news-heavy month. However, the short duration positioning was a negative during August 2021 as low seasonal new issuance gave way to more robust pricing on longer duration bonds. Airport and transportation sectors were positive contributors to performance in the third quarter as spreads narrowed.

Looking Ahead

New municipal bond issuance for October and November 2021 is projected to considerably exceed redemptions from maturities and called bonds for the same period. Should the increase in municipal bond inventory hold, there could be further opportunities to acquire municipal bonds at favorable levels last seen in March 2021. This would make the fourth quarter of 2021 an opportune time to add to existing municipal bond strategies. We continue to find value in the secondary municipal market with bonds rated A or better by Moody's, Standard & Poors, or Fitch at the time of purchase and involved with essential services like water, sewer, power, streets, highways, public education, and general obligations. Our Strategy focuses on maturities in the seven to 20-year range with call features between 2024 and 2030. The Strategy will continue to utilize shorter duration positioning than the benchmark index, focusing on higher-quality municipalities.

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Contact a member of our Advisor Solutions Team

advisorsolutions@crossmarkglobal.com | 888.845.6910

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Crossmark Global Investments, Inc.
15375 Memorial Drive, Suite 200, Houston, TX 77079
888.845.6910 advisorsolutions@crossmarkglobal.com
crossmarkglobal.com

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