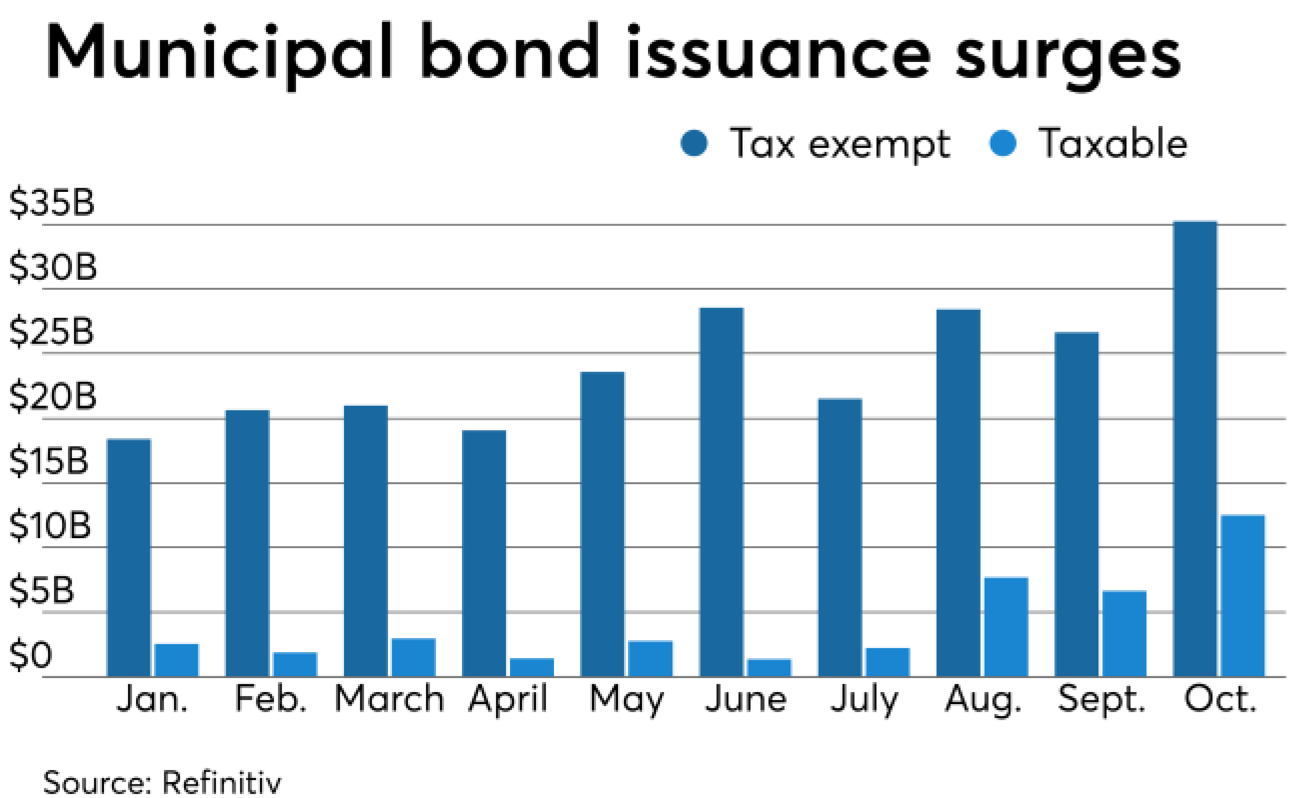
Muni volume hit $52B in October — the most in 22 months — thanks to taxables

By **Aaron Weitzman**
Published October 31 2019, 2:17pm EDT

More in **Bond volume, Primary bond market, Sell side, State of California, State of Texas, State of New York, State of Florida, Commonwealth of Pennsylvania**

Municipal issuance accelerated in October to $52.19 billion, with taxable bonds accounting for about a quarter of the month's supply.



October volume this year is 38.2% higher than last year and is the highest volume for the same month since 2016 when the market produced $53.45 billion, right before the presidential election led to a spike in muni yields and a drop in issuance.

"If you would have told me in May or June of this year that we would have a month $50 billion, I would not have believed you," Tom Kozlik, head of municipal strategy and credit at Hilltop Securities said.

It was the busiest month for municipals since December of 2017, when the market saw $69.83 billion as issuers were rushing to market before the new tax laws came into effect.

For the year so far, volume has risen to $330.33 billion and unless issuance continues with this pace, it is unlikely the market will eclipse the $400 billion mark for the year. Volume will, however, easily surpass last year's total of $338.93 billion.

Taxable bond volume soared almost sixfold from a year earlier to $13.67 billion from $2.36 billion, while tax-exempt issuance increased 13.6% to $37.68 billion.

Peter Block, managing director, Ramirez & Co., said that while the trend of taxable refunding of tax-exempt debt hit the market swiftly, the economics to do such deals already had been in place, albeit facing headwinds.

Peter Block

"There was some hesitancy by most issuers to do taxable advance refundings as exempts. Economics have been there, reducing negative arbitrage from escrow and overall savings from taxable bonds from the exempt bonds, in most cases," he said. "The issuers' options were either waiting by betting that rates stay where they are [or] get better, do a regular refunding, or come with the taxable."

Also last year, the Fed was raising rates and, in 2018 a lot of issuers, still had hope that advance refundings would be restored, Block said.

"As time has rolled on, we are now 22 months into the new tax regime, and realization has set in that advanced refundings are not coming back anytime soon," he said. "Here are we in October, and taxables have accounted for 13.5% of total issuance and are up 100% year-over-year."

Kozlik doubled down on Block's thought, saying he believes that there is "zero chance" of advance refundings getting restored.

"In fact, I think the threat to not only private activity bonds but also the general state and local government tax-exemption grows stronger the worse the U.S. debt to GDP ratio becomes," Kozlik said. "And the U.S. debt to GDP ratio is deteriorating annually."

Not only were advance refundings eliminated, but private activity bonds were put on the chopping block to fund a tax cut, Kozlic said. adding that the tax policy changes were not because of deficit reduction.

"I still see a threat to the tax-exemption," he said.

Tom Kozlik

Kozlik said the taxable refunding strategy works as long as interest rates cooperate. Based on Wednesday's Fed move to lower rates and expectations going forward, the strategy "will likely continue to work in the near term for sure."

Refunding volume for the month more than doubled to $16.55 billion in 407 deals from $6.81 billion in 167 deals a year earlier. New-money volume increased 25.3% to $30.67 billion. Combined new-money and refunding issuance was 23.1% lower from October 2018 to $4.96 billion.

"The reality on new-money, is that governments are still waiting for federal handouts," Block said. "Although we are in the 11th year of expansion, there is still a measure of austerity in state and local governments and it looks like they will be waiting until at least election time."

Issuance of bonds with interest subject to the Alternative Minimum dropped to $838 million from $2.22 billion.

Issuance of revenue bonds gained 18.7% to $31 billion, while general obligation bond sales almost doubled to $21.18 billion.

Negotiated deal volume was up 55.3% to $39.04 billion. Competitive sales increased 24% to $12.91 billion.

Deals wrapped by bond insurance for the month increased 82.6% to $2.99 billion in 188 deals from $1.64 billion in 113 transactions the same month last year.

Seven sectors gained from year-earlier levels, while issuance by the rest of the sectors declined at least 10.4%. Utilities gained to $6.94 billion from $2.82 billion. Education muni deals soared to $14.74 billion from $7.06 billion. Electric power deals grew to $1.93 billion from $795 million and development bonds rose to $3.23 billion from $1.35 billion.

Eight types of issuers increased volume in October, with colleges and universities making the biggest jump, to $3.09 billion from $381 million. District issuance increased to $11.11 billion from $5.31 billion and counties' and parishes' volume rose to $3.67 billion from $2.35 billion.

"Municipal yields dropping over 100 basis points since the end of last year has certainly helped recent issuance momentum," Kozlik said. "If yields fall further that could certainly be a factor in the minds of issuers contemplating whether or not they should access capital."

California continued to lead all states in terms of muni bond issuance. Issuers in the Golden State have sold $50.16 billion of municipal bonds so far this year; Texas stayed in second with $35.59 billion; New York remained in third $34.21 billion; Florida was next with $16.87 billion; and Pennsylvania rounded out the top five with $14.89 billion.

Massachusetts was next with $11.89 billion, followed by Georgia with $9.45 billion, Ohio with $9.19 billion, then Colorado with $8.92 billion and finishing the top 10 is Michigan with $7.74 billion.

The final two months of the year, should see "typical" issuance levels, according to Block.

"There are only six normal weeks left in the year, which should produce roughly $50 billion," he said. "Going into next year, we will not have a typical taxable issuance year (which in the past has meant between $20 and $30 billion) and we see total issuance to be similar to this year, thanks to the increased taxable volume."

Aaron Weitzman