
Short-Term Muni Bonds to Ride Out Trump-Induced Volatility: UBS

U.S. municipal debt investors putting fresh capital to work should look to short duration bonds while President-elect Donald Trump's new administration works out new tax and fiscal policies, UBS Wealth Management said on Tuesday.

"To the extent that you're … placing more capital into this market, you probably want to stay shorter on the curve until we have more clarity by the end of 2017 as to exactly what the tax environment is going to be like," said Thomas McLoughlin, head of municipal research at UBS Wealth Management.

Muni bonds, whose yields are exempt from federal income taxes, have long been attractive to wealthy Americans who fall into higher tax brackets.

However, Trump's proposed lowering of tax rates could reduce the appeal of tax-exempt bonds, a major vehicle for states and cities to finance infrastructure, hospitals and schools.

Speaking at the Reuters Global Investment Outlook Summit, McLoughlin said tax reform would be the story for 2017, given how Trump and the Republican party control the White House and held onto majorities in the Senate and House of Representatives.

"The absence of specificity is something that I think the market is struggling with right now," McLoughlin said.

"The municipal market is certainly trying to adjust to determine how real the threat may be to tax exemption and whether or not that threat is overblown; whether or not that threat constitutes complete elimination; or the third option, which is a curtailment in the limitation as to the value of that exemption," he said.

McLoughlin, however, believes the threat to the municipal market's tax exemption status is lower than before as public interest groups have actively lobbied to show the importance of state and local governments in providing infrastructure.

During the election campaign, both Trump and his Democratic opponent Hillary Clinton advocated spending to rebuild U.S. infrastructure.

U.S. voters on Tuesday also approved 562 of 698 state, school and local government bond measures on ballots, clearing the way for the issuance of $60.23 billion of municipal debt, data company Ipreo reported. The amount requested on ballots, $70.1 billion, was the largest par, or face amount, since 2006.

In part, the requested borrowing for big projects was spurred by growing competition for money within municipalities.

"Pay-as-you-go infrastructure is going to be more difficult as pension liabilities rise and occupy a larger share of the budget, and in the case of states, Medicaid funding as well," McLoughlin said.

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