[Bond Case Briefs]

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[Municipal Bonds Faring Well Despite Election/Pandemic Uncertainty.]

The municipal and state bond markets are not being hurt as badly as expected prior to the election and before progress was made on a Covid-19 vaccine, according to Adam Stern, senior vice president and director of municipal research at Breckinridge Capital Advisors, a Boston-based financial services firm with $42 billion in assets under management.

Because Democrats did not take control of the Senate (pending run-off elections in Georgia), there is less likelihood of tax increases in the near future, which should lessen the upward pressure on prices and downward pressure on yields that had been predicted before the election, Stern said in an interview today.

At the same time, a vaccine that could begin distribution sooner rather than later will lessen the need for more stimulus money for municipalities and states, he added. Senate Majority Leader Mitch McConnell has indicated he would like to pass a new stimulus package in the lame duck session of Congress that would be less than the $1.5 trillion discussed before the election.

“More fiscal support is likely necessary to maintain the current recovery,” according to a Breckinridge research report. “For munis, additional federal aid would reduce fiscal pressure.” At the same time, “state and local issuers have significantly reduced their payrolls. Service cuts of this sort are beneficial to credit quality in the near-term. However, maintaining these cuts indefinitely will prove challenging.”

Tax-free municipal bonds should still be readily available in the near future, Stern said. “But we find that ratings downgrades are likely regardless of the federal response. Mass transportation issuers would unquestionably benefit from increased federal aid.”

Financial advisors should be on the alert for municipalities and states, such as Chicago and Illinois, that are in dire financial circumstances, he added. Illinois’ credit rating has been downgraded to junk bond status in recent days. Although that is not typical of all states, Illinois presents the type of circumstances advisors should be aware of.

On the plus side, essential service municipal bond issuers have managed through the Covid-19 pandemic better than expected. Loose fiscal and monetary policy, coupled with better management of the virus, has helped limit the worst case outcomes, Stern said in a Breckinridge report. “We anticipate a challenging, but manageable, next several months” for bond investors.”

Breckinridge said a combination of factors has contributed to a less dire outlook than was predicted a few weeks ago. For starters, fiscal stimulus provided under the CARES Act has been effective as transfer payments averaged 8% of U.S. personal income between April and August 2020, and these payments likely produced higher-than-expected sales and income tax collections.

In addition, very low interest rates likely allowed some borrowers to refinance maturing obligations to avoid credit mishaps, as well as enabling a significant amount of debt refinancing.

Finally, people have done a better job of managing and adapting to the coronavirus.

ETF TRENDS

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