Bond Case Briefs

Municipal Finance Law Since 1971

Vanguard Sees Muni Bond Supply Slowing to $400 Billion in 2022.

- **Issuers are flush with revenue and aid, says Vanguard's Malloy**
- **Forecast on lower end of muni estimates compiled by Bloomberg**

Vanguard, one of the largest municipal fund managers, expects states and localities to slow bond sales by at least 11% to about $400 billion next year because of a faster than anticipated revenue rebound and billions of dollars in federal aid.

"A lot of municipals are flush with cash," Paul Malloy, head of municipal investments at Vanguard, said in an interview. "They don't need to borrow as much." The firm has almost $267 billion in muni assets.

Vanguard's forecast, including municipal-backed corporate debt, is lower than 2022 forecasts from 11 other strategists compiled by Bloomberg. The 2022 supply estimates ranged from Morgan Stanley's projection of $420 billion to Bank of America's forecast for $550 billion.

Last year, municipal issuers sold about $454 billion in long-term debt as the pandemic shuttered businesses, drove up unemployment and led tax revenue to drop temporarily. With three weeks left in 2021, long-term municipal issuance has reached about $450 billion, according to data compiled by Bloomberg.

On Credit

Malloy expects lighter sales next year because state and local governments have "a lot of cash" and municipal issuers "are in really great shape" from a fundamental credit perspective, he said. The pandemic's revenue hit has subsided for many.

Texas, among the largest state issuers, is an example of the pull back in debt overall, he said. The state usually borrows to prevent a deficit until more revenue arrives.

The state's total sales tax revenue for the three months ending in November 2021 rose 22% from the same period a year ago and is up almost 16% compared to 2019, according to a statement on the Texas comptroller's website.

In addition to rebounding revenue, state and local governments are getting $350 billion from President Joe Biden's American Rescue Plan Act.

On Rates and Valuation

Another reason to reduce borrowing next year is the cost may increase for municipal governments, Malloy said. The 10-year AAA muni benchmark could move up by mid-2022 from the current 1.05%, driven by yields in the Treasury market, Malloy said.

Muni issuers have benefited from rates hovering around historical lows partly because supply largely has not kept pace with investor demand this year and the imbalance has kept a lid on yields.

“It’s not going to be as cheap to borrow as it has been,” Malloy said. “It’s the macro story.”

One of the biggest questions for 2022 will be valuations, Malloy said. The muni to Treasury ratio is likely to range between 70% and 75% for debt maturing in 10 years, he said. The ratio was about 71.3% at the last close.

The ratio may hover around 80% for 30-year debt and 50% for bonds maturing in two to five years, he said.

On Covid

The pandemic is “an X-factor,” Malloy said. “Always out there for the foreseeable future.”

The virus and its variants will contribute to volatility in the market but medical advances and improvements in responses globally mean Covid “doesn’t have the same potential for scarring” as it did at the outset, he said.

Bloomberg Markets

By Shruti Singh

December 10, 2021, 11:26 AM PST