16TH AMENDMENT ADVISORS LLC™

Overview

Looking back on 2021, municipals traded in a relatively tight band. Yields went up in Feb/March, went down slowly in the April to July period, then up again from August to October, then one last rally in November to December. Overall, the 10year municipal yield ("MMD") increased 35bps to 1.07% and the 30year municipal yield rose 13 basis points to 1.53%. The tone of the overall market began to change following the September FOMC meeting and the subsequent November meeting when the Federal Reserve indicated it would slow or "taper" the pace of bond buying by $15bn a month in November and December. In the Fed's December release, policymakers took a more aggressive move towards fighting inflation saying it would cut back its monthly bond buying more rapidly and expect to raise rates at least three times in 2021. Since the more hawkish sentiment from the Fed, bond yields have generally started to rise in anticipation of higher rates in 2022. This is certainly the market we find ourselves in to start 2022.

From a total return standpoint, the Barclays Managed Intermediate Money Index returned +.38% on the year. 16th Amendment's **Long Relative Value** finished 2021 with +.73% return and **Long Performance** reported an estimated 1.40% return on the full year.

Gross municipal issuance for 2021 came in at $481bn. This was 3% below 2020's record pace of $497bn. The difference in supply was driven by lower-than-expected taxable municipal bond issuance. Tax-exempt issuance for 2021 was $345bn, 9% greater than 2020 ($316bn). For 2022 five of the top banks are forecasting an average of $115bn in taxable issuance, roughly 36% below the 2020 taxable issuance. These same 5 banks are predicting that the 2022 gross municipal issuance, on average, will end around $487bn.

Municipal Issuance Forecast 2022 *($ in billions)*

FIRM	TAX EXEMPT MUNI	TAXABLE MUNI	2021 TOTAL
Morgan Stanley	$356	$99	$455
Citigroup	$385	$135	$520
JP Morgan	$358	$112	$470
Barclays	$330	$110	$440
Bank of America	$430	$120	$550
Average Supply Forecasts for 2022	$372	$115	$487
2021 Actual Year End Total	$345	$136	$481

**Morgan Stanley, Citi, JP Morgan, Barclays, Bank of America Securities Research*

HIGHER US TREASURY RATES? – FED RATE HIKING CYCLE?

As we enter 2022, there is a high level of uncertainty in the markets. The Federal Reserve is faced with increased pressure to raise rates to fight inflation and at the same time unwind some of the trades it entered as part of the monetary stimulus and accommodation policies during the beginning of the Covid outbreak. This could turn out to be a very difficult task given the most recent selloff in the equity market and increased geopolitical tensions specifically with Russia over increased military pressure on Ukraine. The Fed will need to manage monetary policy in the face of increased volatility in the market, along with maintaining acceptable levels of growth and employment.

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Most banks are calling for the 10yr treasury to trade in a range this year from a low of 1.62% to a high of 2.25%. That is a wide range of just over 60 basis points. That would imply a real increase in rate volatility this year. Barclay's municipal research analyst Mikhail Foux recently wrote,

> *"There is nothing worse for municipal investors than rate spikes and volatility in general. Responding to this, they frequently choose to stay on the sidelines, even if they have cash to deploy, like they do now. Moreover, historically tax-exempts lag large Treasury moves, while fund flows typically respond to rate volatility."*

10 YR UST Forecast 2022

FIRM	10 YR UST RANGE
Morgan Stanley	1.75%-2.10%
Citigroup	1.62%-2.00%
JP Morgan	1.90%-2.25%
Barclays	1.65%-1.75%
BofA	1.75%-2.00%

**Morgan Stanley, Citi, JP Morgan, Barclays, Bank of America Securities Research*

To the right is a list of top bank 10 year treasury rate forecasts for 2022:

Municipals in 2022

The municipal market started out 2022 with Municipal/Treasury ratios at or near historic low levels suggesting municipal bonds were rich relative to US Treasuries of a comparable maturity. During the first couple of weeks January, municipals lagged the sell-off in US Treasury markets sending ratios to even lower levels. As a general matter, municipal bonds tend to lag moves in treasuries so this short-term change was not unexpected.

DATE	10 YR TREASURY YIELD	10 YR MUNI YIELD	RATIO	DATE	30 YR TREASURY YIELD	30 YR MUNI YIELD	RATIO
December 31st 2021	1.51%	1.03%	68.2%	December 31st 2021	1.90%	1.49%	78.4%
Jan. 18th 2022	1.87%	1.18%	63.1%	Jan. 18th 2022	2.19%	1.64%	74.9%
Change	0.36%	0.15%	-5.1%	Change	0.29%	0.15%	-3.5%

**Refinitiv, Bloomberg*

However, over the past week-to-ten days, municipals have significantly underperformed UST sending ratios to their highest in quite some time. Certainly, part of this recent underperformance was the expected "catch-up" but more importantly is municipal mutual fund flows have turned negative.

DATE	10 YR TREASURY YIELD	10 YR MUNI YIELD	RATIO	DATE	30 YR TREASURY YIELD	30 YR MUNI YIELD	RATIO
Jan. 18th 2022	1.87%	1.18%	63.1%	Jan. 18th 2022	2.19%	1.64%	74.9%
Jan. 28th 2022	1.84%	1.45%	78.8%	Jan. 28th 2022	2.13%	1.85%	86.9%
Change	-0.03%	0.27%	16%	Change	-0.06%	0.21%	12%

**Refinitiv, Bloomberg*

We are paying close attention to the movement in yields and in ratios as they may present a better buying/repositioning opportunity for our strategies. We do believe, however, that we are entering an outflow cycle given the recent move in absolute yields and the likelihood of rate hikes by the Fed. Although the opportunity in the market may be a little further out timewise, we believe the time for a proactively managed municipal portfolio has never been more important given the current choppy environment. We will be very selective in the structure and credit quality of the bonds we choose for our portfolios. This is essential in asset selection as spreads on both investment grade and high yield municipals tend to widen out during outflow cycles, particularly when they last for more than one month. The below charts highlight how much more yield spread volatility there can be in high yield relative to investment grade during common date periods (see March 2020, Sept/Oct 2016, April/May 2015). This is always something to be mindful of when constructing portfolios.

Investment Grade:
Muni Spreads Widen During Outflow Cycles

OUTFLOW START DATE	LENGTH OF OUTFLOW CYCLE (MOS.)	TOTAL IG FUND OUTFLOWS (% OF AUM)	CHANGE IN IG SPREADS (BPS.)
March-20	2	-4	45
September-18	4	-2	18
April-18	2	-1	0
November-16	4	-3	10
June-15	5	-1	5
April-15	1	0	-5
April-14	1	0	0
April-13	11	-13	-5
August-11	1	0	12
November-10	8	-10	14
Median	2	-1	5

Source: Refinitiv, Barclays Research

High Yield:
Muni Spreads Widen During Outflow Cycles

OUTFLOW START DATE	LENGTH OF OUTFLOW CYCLE (MOS.)	TOTAL HY FUND OUTFLOWS (% OF AUM)	CHANGE IN HY SPREADS (BPS.)
January-22	1	0	-4
October-21	1	0	2
March-20	3	-11	211
October-18	2	-3	28
February-18	1	-1	3
October-16	3	-7	39
September-15	1	0	11
May-15	3	-3	37
July-14	1	0	15
March-13	11	-19	26
December-12	1	-1	-11
October-11	2	0	0
Aug-11	1	-1	57
Nov-10	6	-13	43
Median	2	-1	21

Source: Refinitiv, Barclays Research

Should there be any meaningful spread widening, it will present a buying opportunity for our clients. We continue to favor state/local general obligation bonds as well as essential service bonds with rate setting capabilities. We will continue to favor defensive 5% coupons in the intermediate part of the curve. We will extend duration if long rates sell off to a point were the extension risk is mitigated by the pickup in yield.