# 2024 Top 10 Trade Ideas

1. **There's an accident waiting to happen.** Inflation, aggressive Fed policies, geopolitical risk, and now fiscal debt and deficits have reached a boiling point. Surging treasury rates reflect a vicious cycle of lender confidence fading after months of responding to strong economic growth. Rate volatility is at an unacceptable level and U.S. tax risk (income tax rates going lower) has hit rock bottom. That's good for municipal bonds as revenue raising measures become a focus. The Trump tax cuts on individuals are set to sunset in 2025 along with favorable SALT tax deductions. The inability of Congress to move anything along in a Presidential cycle should induce even more confidence. This is the gale force wind for municipal bonds to outperform for years to come; get long the long end.

2. **Election year politics aside, two-thirds of states are single party majority.** The willingness and ability of state governments has rarely been in such harmony. However, the road ahead has challenges and budget projections may be too optimistic. We foresee negative headlines and credit downgrades into June which is fiscal year-end for most states. Underweight cyclical states (California) and governments with poorly funded pension plans (Illinois). Overweight resource rich states (Oklahoma), essential service sectors (Water & Sewer), and transportation systems that benefit from global transmission (Atlanta Airport). Watch other cyclically sensitive states where education issues have taken hold which favor Republicans. It's possible that in New Jersey Republicans run on an education platform that worked well in Virginia. Delocalize the local municipal market, overweight credits that spread risk across multiple geographies (Kaiser Permanente). Systemic risk to the asset class remains low, and its infrastructure characteristics generally outperform other credit markets in challenging economic environments.

3. **Keep rotating sectors and credits, fundamental research drives return.** Market fluctuations will create stronger trading momentum. Portfolio construction must afford flexibility and maximize after-tax performance. Underweight select single-facility for-profit hospitals, small private universities, and the senior living sector. Consolidation and merger & acquisition trends have positive outcomes, but it's a painful trade getting there - switch to an overweight as relative value dips below intrinsic value. Small private universities are struggling relative to public universities with lower debt burdens and state support. Management teams that can adopt artificial intelligence (AI) to drive down legacy costs and broaden online programs are best positioned. Maintain a core overweight to school districts, and local governments with a dense wealth base and triple income tax system (Kansas City). Underweight high yield municipal bonds. Shift focus to the private municipal loan market. For qualified buyers, municipal bridge loans provide a unique path to emerging project finance that's helping to modernize the U.S. economy. They're short duration, at high levels of taxable income, and have conversion benefits back into the tax-exempt municipal market.

4. **New issue supply is set to grow as is the market's seasonal pops and drops.** We anticipate tax revenue to decline alongside inflation, COVID stimulus to wear off, and pent-up voter needs to get loud. The municipal advanced refunding option is dead; however, utilizing the taxable municipal bond option is set to grow as rates rally. Switch your dedicated municipal portfolio to include taxable municipal bonds. There is $1t of high-quality debt outstanding, routine issuance, priced on top of corporate bond yields, with long duration properties. Taxable municipals can help monetize seasonal fluctuations that are most pronounced in the tax-exempt market. Overweight short and long maturities in taxable municipals to monetize yield curve steepening and regulatory capital driven demand. Expect strong uncorrelated performance from both the tax-exempt and taxable municipal market. For those who can, use CDX as a credit hedge which provides good protection in what's expected to be rising corporate default rates.

5. **Get ready for Build America Bonds 2.0 (BAB).** America's aging infrastructure must be prioritized. It's just going to take time and unfortunately another catastrophe for change to occur. It's not that trillions of infrastructure needs can't be financed it's just more than the tax-exempt municipal market will allow. Policy makers need to get more creative. Implementation of BABs 2.0 will require more Federal support, more local autonomy, and a lower subsidy. Broader demand can also be created. For example, public pension plans are like private sector 401k's, a portion of deferred benefits should get invested locally and taxed if you leave. Also, all retirees that meet a minimum age and even young savers can be given IRA-like incentives that can create a stronger foundation for America's economy and lower interest expense for municipalities. Positive developments will drive tax-exempt and taxable municipal bond outperformance. Opportunity to position a dedicated taxable municipal portfolio and/or swap out of corporate bonds is now. Overweight small non-index eligible deals which define the municipal market and offer the best value.

6. **Mission-driven style investing moves into the spotlight.** As ESG fades due to political backlash, municipal bonds have impact and neatly align with many philanthropic and Corporate Social Responsibility (CSR) initiatives. Europe has top-down policy drivers that create a regulatory need for ESG qualifying assets and capital-efficiency. In the U.S. it's a bottom-up grass roots movement with purpose. There is a hidden tax in the U.S. that most affects ethnically diverse communities. These municipalities pay higher borrowing rates and residents are subject to downstream consequences. Position portfolios for a slow and steady credit tightening cycle in sectors and credits with the largest impact (multi-family housing and HBCUs). Overweight bond structure features such as Bond Banks and state intercepts that could see a broader use case and help drive interest savings. Monoline insurance is also a cheap structural feature, expect penetration to rise and insured spreads to compress.

7. **AI is catching fire in the municipal marketplace.** Look no further than the number of trades that have skyrocketed past the amount of par trading. Municipal algo trading is a mega-trend that has a long way to go before it catches up to other markets. The municipal market has a rich history of trade data, issuer credit fundamental data, benchmark barometers, geographical detail, etc. that can be used to create an effective modeling framework. Regulation is pushing for more issuer disclosure and real-time trade reporting to improve transparency. Municipal portfolios, which can appear inefficient, are constructed differently than other asset classes due to the market's fragmentation and complexity. A new front has opened for electronic trading that is delivering institutional liquidity, instant trade execution, and market leadership - once thought of as only achieved by the market's largest investors. Overweight small lot expressions, processes that optimize after-tax trading strategies, and customize a Separately Managed Account (SMA) that is designed to deliver the best individual outcome-oriented solution.

8. **Switch out of municipal mutual funds and active ETFs.** Municipal Separately Managed Accounts (SMA) are growing fast and can now be accessed at more competitive fees. Investors deserve a personalized approach that eliminates collateral damage and yield-seeking peer and index portfolio construction bias in pooled vehicles. Passive ETFs have created lasting access to the markets beta but do not deliver the market's rich alpha opportunities. Active ETFs are breaking ground on the alpha side but do not deliver a customized approach. ETFs enjoy more consistent exchanged based liquidity, but they are price insensitive when it comes to trade execution. They also fail to provide access to one of the municipal market's biggest benefits, priority retail order period for new issues. Overweight a Ladder strategy out to the 7-year maturity point in tax-exempts, non-callable discount coupon structures, out-of-state credits that achieve in-state tax-efficiency, and small-lot high-quality bonds that will trade with a liquidity premium because of the industry's large SMA movement.

9. **Buy the dip in municipal closed-end funds (CEF).** Something is telling when you have the highest interest rates in over a decade, and we've seen little CEF product growth. Performance has been terrible. Consolidation of funds has taken over the industry and share buyback programs have done little to improve performance. Expense ratios need to come down and the stage is set for shareholder activism to get loud. Exchange based liquidity for CEFs has been ineffective, and the yield-seeking behavior within funds has created concentration risk. Leverage ratios are high and many CEFs use Tender-Option-Bonds (TOBs) which adds tax risk. Expect TOB financing costs to improve and cuts to CEF dividends over with. We're at the point where NAV discounts provide an attractive entry point. Risk-reward is compelling from the lens of an investor, but painful for fund providers. Overweight deep discount CEFs with good call protection that will benefit most from rates normalizing. Guard against a TOB-leverage vol-shock by underweighting the 15-year sector of the tax-exempt municipal bond curve.

10. **AAA-rated benchmark yield curve preference switches course.** The tax-exempt municipal market, unlike corporate or taxable municipal bonds, trades on a yield basis not on a spread to treasuries. This creates a ton of friction and many more opportunities. The market has long benchmarked itself to one provider and we're seeing movement to new more technology-driven provider(s). Technology advancements have gone a long way to remove subjectivity and improve real-time transparency. Portfolio construction should optimize multiple curve inputs and now-casting process solutions. Strategies that focus on basis arbitrage and use multiple price and curve inputs add a new source of real return generation.

## 16Rock Asset Management | Municipal Bonds

# Executive Summary

## About

16Rock is a full-service asset management firm specializing in U.S. Municipal Bonds with a global perspective. We cater to the modern needs of institutions and high-net-worth individuals around the world. Our passion is to help clients translate their desires and aspirations into sophisticated outcomes that exude order. Our team leverages decades of experience to construct highly curated portfolios. We offer tailored managed account solutions, transition management services, and through our alternative investment capabilities, products designed to deliver absolute return excellence.

## Alternative Investments

16Rock's municipal opportunity strategy is actively managed, unconstrained, and absolute return driven. The strategy is designed to achieve investment excellence, translating market fragmentation into durable performance. Our approach utilizes interest rate protection and a multi-strategy framework in portfolio construction. The strategy seeks positive risk-adjusted outcomes in all market environments. It has an emphasis on capital preservation and is designed to maximize the benefits of the market's infrastructure characteristics.

## Separately Managed Accounts

16Rock specializes in Municipal Bonds catering to the modern needs of investors with a global perspective. We seek to provide outcome-oriented managed account solutions for institutions and high-net-worth individuals around the world. We aim to translate individual aspirations into customized portfolios. Our expertise spans across many styles and objectives including tax-efficiency, lifestyle and liability matching, regulatory capital complexities such as Solvency II, ladders, ESG, and Impact.

## Transition Management

16Rock seeks to provide clients with a strategic entry and exit into the Municipal Bond market. We help clients execute new investment strategies and change allocations following macro events, market catalysts, or simply a new risk outlook. We preserve confidentiality, manage transition costs, and facilitate minimal disruption to a portfolio. Our services range from short-term opportunistic trading to comprehensive liquidations and advisory of existing portfolios. Our team strives to leverage decades of experience and deep relationships in the market to provide superior execution, creative solutions, and timely outcomes.

## Team


## Contact

James Pruskowski
Chief Investment Officer

(212) 332-1600
james.pruskowski@16rock.com

One Rockefeller Plaza, Suite 1202
New York NY, 10020

www.16rock.com
www.linkedin.com/company/16rock

**IMPORTANT DISCLOSURE INFORMATION**

16Rock Asset Management LLC ("16Rock" or "Company") is an SEC registered investment adviser located in New York, New York. A copy of the Company's current written disclosure Brochure discussing our advisory services and fees continues to remain available upon request by contacting us at info@16Rock.com. Please refer to www.16Rock.com/disclosure for a complete discussion of Important Disclosure Information.

The discussion and comments presented herein are intended for general information purposes only. They represent opinions and views 16Rock, as of the date hereof, and subject to change, and may no longer be accurate as of a future date. Certain data is provided by third parties and is presumed to be accurate. Such data has not been independently verified. No portion of this presentation serves as the receipt of, or as a substitute for, personalized investment advice from 16Rock, or any other investment professional of your choosing. Different types of investments involve varying degrees of risk, and it should not be assumed that future performance of any specific investment or investment strategy, or any non-investment related or planning services, discussion, or content, will be profitable, be suitable for your portfolio or individual situation, or prove successful. 16Rock is neither a law firm nor accounting firm, and no portion of its services should be construed as legal or accounting advice. No portion of the content herein should be construed by a client or prospective client as a guarantee that he/she will experience a certain level of results if 16Rock is engaged, or continues to be engaged, to provide investment advisory services.

The content of this report may not be used or considered as an offer to sell or a solicitation of an offer to buy securities, including any interest in any investment fund or strategy managed or sponsored by 16Rock or any of its affiliates. Such offers will be made only by distribution of a private placement memorandum, or similar agreement, only in compliance with applicable law, only in jurisdictions in which such an offer would be lawful and only to individuals who meet the investor suitability and sophistication requirements set forth in such materials. No information contained or referenced in this report constitutes investment, legal, tax or other advice nor is it to be relied upon in making an investment decision.

Please remember that different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment or investment strategy (including those undertaken or recommended by the Company), will be profitable or equal any historical performance level(s). No amount of prior experience or success should be construed that a certain level of results or satisfaction will be achieved if the Company is engaged, or continues to be engaged, to provide investment advisory services.

16Rock Asset Management LLC
One Rockefeller Plaza, Suite 1202
New York, NY 10020

(212) 332-1600 | info@16Rock.com | www.16Rock.com | www.linkedin.com/company/16rock