

16Rock Asset Management

Municipal Bonds: Key Insights and Opportunities for 2025

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1 Turning Uncertainty Into Opportunity

The Republican parties new c-suite is poised for action. Policy risks loom over inflation but hinge on lower interest rates. They boiled over once at 5% 10s; Fed lowered odds of a repeat. Uncertainty fuels opportunity—without delay start dollar-cost averaging into generational fixed-income opportunities. Safe assets like municipal bonds are primed for strong performance.

2 Make America Resilient Again

A modern revival of Build America Bonds seems inevitable. Taxable municipals should drive infrastructure financing to draw significant public and private sector investment. With taxpayer limits stretched, realigning federal subsidies are key to tackling income inequality, preserving local autonomy, and modernizing America's economy.

3 Record Issuance and Shifting Trends

Brace for another year of record issuance \$500B. Issuers will fast-track plans and sidestep long maturity lock-ins. Delayed decisions and missed refundings in 2024 signal action ahead, with project costs still driving more need. A shift toward taxable municipals looks possible. Don't expect the advance refunding option or high-yield supply to return anytime soon.

4 The Tax Reform Balancing Act

Eliminating tax-exemption poses a tail risk, not a core threat. Radical reform faces deficit roadblocks and political pushback. Targeted changes may impact Higher Ed, Healthcare, and Private Activity Bonds. With DOGE-driven offsets, tax reform will focus on low-income relief, SALT tweaks, and TCJA extensions. Expect vol-shocks as proposals blur negotiation and reality.

5 Tax Efficiency as a Barrier to Entry

Amid high interest rates and shifting supply-demand dynamics, tax-exempts have passed every test and are poised to tighten toward the top federal tax breakeven rate. Should tail risks unfold, grandfathering could drive valuations tighter. Meanwhile, state and local tax hikes will continue to boost in-state demand, while mutual fund-to-ETF conversions will accelerate liquidity.

6 Geography of Growth

Target states rich in agriculture and manufacturing, where domestic supply chains fuel economic growth. Look beyond local markets as migration patterns shift—focus on credits spanning state lines. Prioritize top-quality credits with essential-purpose proceeds, as slowing tax collections and fading pandemic aid increase fiscal pressure, until rates rally to justify wider spreads.

7 Profit with Purpose

ESG momentum may have peaked, but the drive for purpose-driven philanthropy is stronger than ever. The municipal market offers unique access to credits that uplift underserved communities, affordable housing, and vital public projects. With the right strategy, municipals can deliver both impactful change and solid performance.

8 Navigating High Yield Challenges

The high-yield market leans on fallen angels over fresh opportunities. Puerto Rico highlights risks—costly litigation and governments outlasting creditors. Focused strategies will tighten low-rated IG bonds. Smart security selection is vital, but scaling is tough without concentration risk. Watch out for taxability risk with targeted tax reform, but out-yielding the market will define success.

9 Evolution Driven Demand

An arms race is unfolding, with technology driving rapid advancements and expanding demand across the industry. From market makers to price takers, SMA asset gatherers have created workflow challenges that, in turn, create powerful opportunities. Algorithmic strategies are well-positioned to enhance efficiency, improve liquidity, and unlock performance potential.

10 Redefining Index Eligibility

Issuers and industry professionals must advocate for a revamp of index eligibility to remove bias and better serve taxpayers. Lowering deal size and maturity minimums unlocks huge opportunities. Issuers and taxpayers win from lower interest costs, while eligibility better reflects the market not big firms. Strategies focused on smaller deals offer the highest rewards.

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