Municipal Comment March 2020

Shelter from the Storm

In the midst of incredibly volatile recent market conditions driven by coronavirus fears, it's been an optimal time to have an allocation to municipal bonds. Given that our client investment objectives include capital preservation, predictability, stability and balance of risk, Riverbend Capital muni portfolios have delivered during the recent upheaval.

Our typical portfolios are comprised of:

- Essential service revenue bonds (water/sewer/electric utility)
- General Obligation bonds from states, cities, and counties with strong balance sheets, rainy day reserve funds, and often multiple layers of backing
- Higher education bonds from nationally recognized institutions with positive enrollment trends and significant endowments
- Healthcare facilities that are part of larger profitable networks with dominant market share.
- Transportation issues with consistent revenue streams and solid credit profiles

The portfolios we manage are conservative, defensive, and well-positioned for potential economic strain.

Good News - Relative Value Restored!

The municipal bond market does not move in lockstep with UST's. In the last few days munis haven't kept pace with the rally in UST's. Municipal bond yields have certainly moved lower, but not at the daily double-digit pace of the Treasury market. This has resulted in a considerable widening of muni ratios, restoring relative value vs. Treasuries across the curve. The ten-year ratio of muni to UST yields spiked 24% in three days last week. In a dramatic reversal from just a few weeks ago when munis were very expensive vs. UST's, munis now look favorable as ratios to Treasury yields are at the highest levels since 2016.

AAA tax-free muni yields are higher than UST across almost the entire curve (3/6/20)

	MATURITY	RATIO
1	2021	141%
2	2022	113%
3	2023	105%
5	2025	95%
10	2030	111%
15	2035	113%
20	2040	109%
30	2050	112%

Muni Appeal

The year began in much the same way that 2019 ended. The consistent flow of new money into municipal bond mutual funds driven by investors seeking tax-exempt income, and light new issue supply, resulted in strong market performance and sustained rich ratios to UST's. Demand for munis has been nearly insatiable in the aftermath of the Tax Cuts and Jobs Act of 2017 as investors with fewer tax deductions have sought the muni tax-advantage. Years of positive performance have also made munis an attractive option to investors. Indeed, munis haven't had a down year since 2013, as measured by the ICE Bank of America US Municipal Securities Index.

Muni credit continued to improve in 2019, with rating agency upgrades outpacing downgrades in recognition of states and municipalities reserves reaching post-2008 highs levels. These rainy-day funds exist to mitigate the effects of diminished revenue from income and sales taxes in periods of decreased economic activity. Some states and municipalities are better prepared than others, but most are well-positioned for a potential downturn. This readiness can be partly attributed to the experience of managing through the 2008 financial crisis and fiscal conservatism in its aftermath.

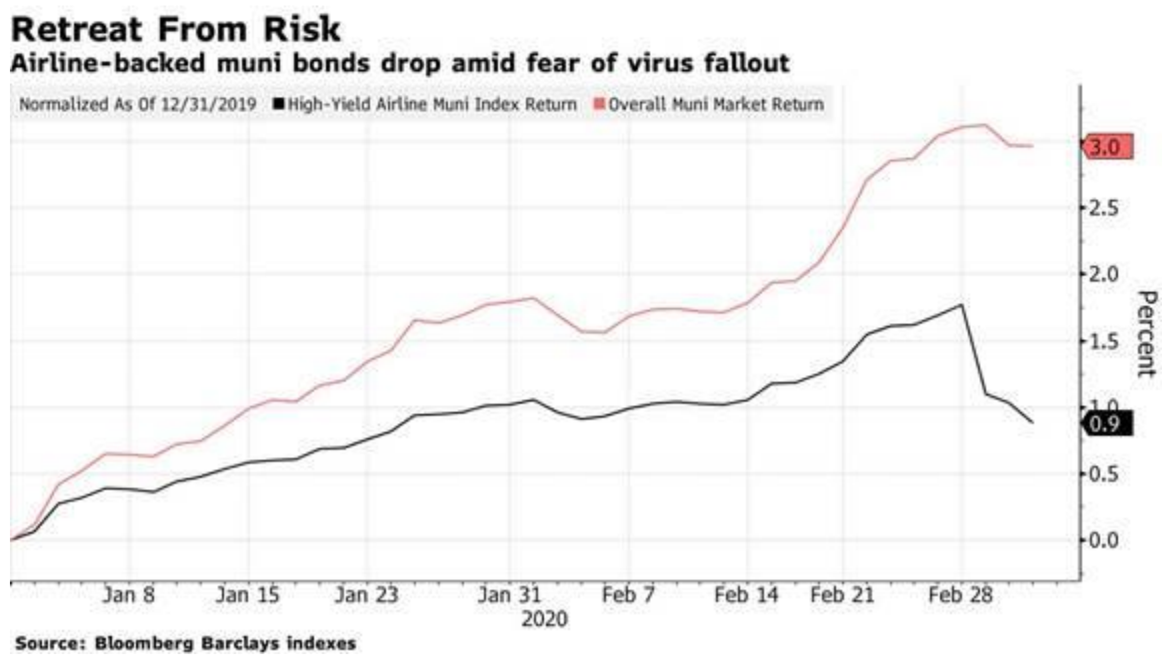
Wear a Mask on the Flight to Quality

While this is a year unlike any that the municipal market has previously experienced, we are entering a seasonal period of increased new issuance and fund-redemptions related to April tax payments. This phenomenon frequently results in lackluster market performance in March and April as anticipated supply exceeds proceeds from maturities, coupons and call, and it often presents a potential opportunity to invest available cash.

At this time, it is prudent to prepare for a greater aversion to risk in the market and a subsequent widening of credit spreads. Riverbend muni portfolios include a broad range of muni issuers with a diverse variety of revenue sources. Our emphasis on bond selection and our ongoing commitment to high quality credits has portfolios prepared for this scenario.

In the event of a virus-related slowing of the U.S. economy, project-specific issuers such as convention centers, stadiums, and TIF districts for retail development may be among the first to feel the effects. We have virtually no exposure to these sectors in client portfolios.

There are also transportation sub-sectors that could be impacted by effects of the virus uncertainty. For example, some airport bonds are essentially corporate-backed obligations of commercial airlines issued though a municipal conduit. The Bloomberg Barclays High-Yield Airline Muni Index which includes these issuers has already experienced a slight downturn. We have no exposure to these credits in our client portfolios.



Transportation

Mass transit authorities are supported by a combination of passenger revenue and appropriations, and most have adequately funded debt service reserve funds. Ports, particularly those in California with significant China volume, are already experiencing a drop off in shipments. However, most ports have contractually guaranteed minimum annual levels of revenue, low debt and ample liquidity. Distress in these areas is unlikely in the near- or medium-term.

General airport revenue bonds are backed by gate leases, landing and terminal fees, ground operations, vendor amenities, parking revenues, etc, At this point trading in these credits is unaffected and spreads have not widened. Should passenger volume remain low for an extended period, these issuers could be impacted.

Healthcare

While hospitals continue to engage in preparation for an outbreak of the coronavirus, weaker credits may face service capacity challenges if inundated with patients seeking testing and treatment. A surge in ER visits could negatively affect operations in specific cases, although providers can generally rely on reimbursement from Medicaid or the private insurance coverage of patients. In an extreme scenario some hospitals may experience limited pressure, but overall credit quality is unlikely to be impaired.

Riverbend and You

While virus-related market upheaval may continue, we will adhere to a disciplined strategy involving high quality credits and lower duration. We do not consider this to be the appropriate time to reach for yield by lowering credit standards or extending duration.

Riverbend muni portfolios have been providing ballast in a challenging time, by balancing risk and offering stability in the midst of uncertainty.

Please feel free to contact us anytime if you'd like to discuss the topics cited in this update, or any others related to the municipal bond market.

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