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Municipal Securities Rulemaking Board

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Third Quarter 2024 Municipal Securities Market Summary

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Municipal Securities Rulemaking Board

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Introduction[1]

In the third quarter of 2024, the municipal securities market was characterized by significantly higher new issue volume, robust yet steady trade count, declining interest rates and a return to strong net inflows to mutual funds. New issue volume for the quarter totaled $136.6 billion, up 39% compared to same period in 2023, with August having the largest issuance for that month since 2020. Trade count remained consistent and strong in the third quarter, likely due to continued strong demand from individual investors. Tax-exempt benchmark yields declined significantly in the third quarter but lagged the move in the Treasury bond market, where yields on the short end declined as much as 111 basis points. Finally, tax-exempt mutual funds and exchange traded funds (ETFs) saw significant positive net inflows.

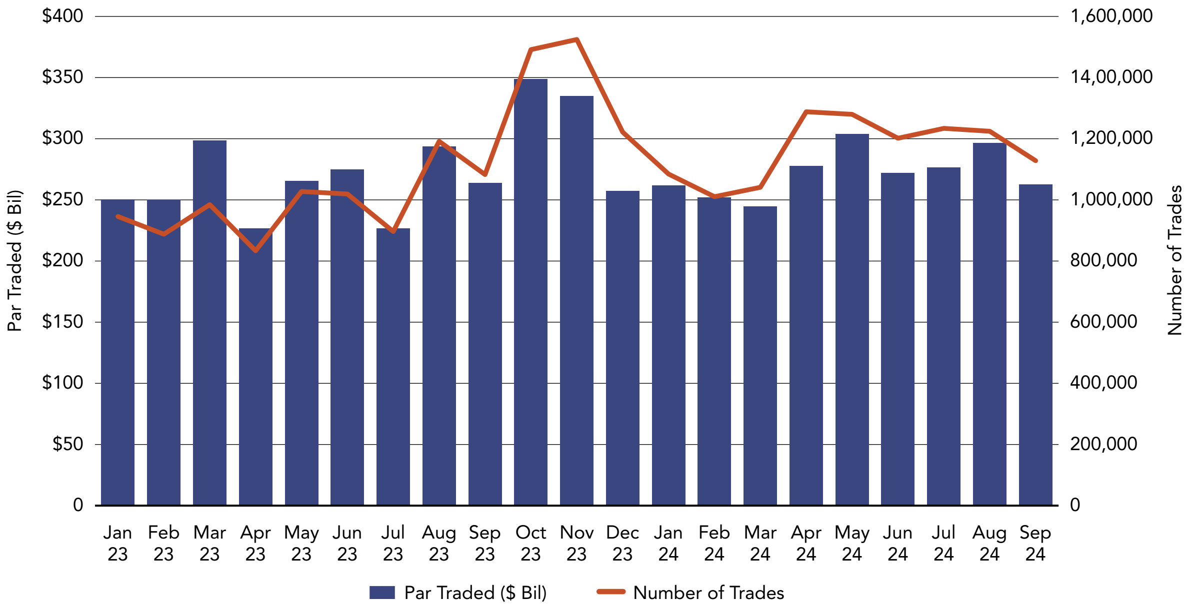
[1] The views expressed in the research papers are those of the author(s) and do not necessarily reflect the views and positions of the MSRB Board and other MSRB staff.

Trading Volume

Municipal securities trading remained robust in the third quarter of 2024. Trade count increased 13% compared to the third quarter of 2023, and year-to-date average daily trade count is up 18% from 2023, which was a record year for trade count. See Figure 1.

Although September snapped a streak of five consecutive months with more than 1.2 million trades, the last 14 consecutive months have seen more than 1 million trades each. Consider that prior to 2022, there had only been eight months with 1 million or more trades. Could this be a fundamental change in the market, investors reacting to higher yields or a combination of both?

Figure 1. Monthly Municipal Market Activity, January 2023–September 2024



Yields

As Figure 2 below shows, benchmark 10-year yields dropped almost 40 basis points from the end of June to early August. Rates then rose slightly in August before declining slightly in September. In September, we saw a 50 basis point cut by the Federal Reserve (Fed), the first cut since March 2020 at the onset of the pandemic.

Figure 2. Bloomberg BVAL 10-Year Callable Yields, January 2021–September 2024

Source: Bloomberg Financial L.P.

Figure 3 shows a strong quarter for benchmark tax-exempt and Treasury yields. This notwithstanding, as the chart shows, the tax-exempt market dramatically underperformed the Treasury market for all maturities but especially on the short end of the curves. Treasury yields for 1- and 2-year maturities were down more than 100 basis points while yields on the rest of the Treasury curve were down 37–94 basis points. Meanwhile, tax-exempt benchmark yields were down 68 basis points for 1-year maturities, 75 basis points for 2 years and 66 basis points for 3 years. Longer maturities were lower by 24-59 basis points for the quarter. Year-to-date, tax-exempt yields are slightly higher for the 3-year and longer maturities. Meanwhile, Treasury yields are down for all but the 30-year maturity and down substantially on the short end of the curve.

Despite the underperformance of tax-exempt securities, the Muni/Treasury ratios at the end of September were comparable to those to the end of June. As Figure 4 shows, the 10-year Muni/Treasury ratio rose from 65% to 69% in the third quarter. As a result, tax-exempt yields for 10-year maturities are now more attractive relative to yields on 10-year Treasury bonds than they were at the start of the second quarter.

Figure 3. Bloomberg BVAL® AAA Callable and U.S. Treasury Yields

Year	BVAL Callable 09/30/2024	TSY 09/30/24	BVAL Q3 Change in BPS	TSY Q3 Change in BPS	Muni/TSY Ratio	Muni/TSY Ratio 06/28/2023
1	2.494	3.98	-68	-111	63%	62%
2	2.369	3.66	-75	-105	65%	66%
3	2.347	3.58	-66	-94	66%	66%
5	2.347	3.58	-59	-75	66%	68%
10	2.612	3.81	-23	-55	69%	65%
20	3.223	4.19	-22	-42	77%	75%
30	3.493	4.14	-24	-37	84%	83%

Sources: Bloomberg Finance L.P., U.S. Department of the Treasury

Figure 4. Bloomberg BVAL AAA Callable to U.S. Treasury 10-Year Ratio, January 2021–September 2024

Sources: Bloomberg Finance L.P., U.S. Department of the Treasury

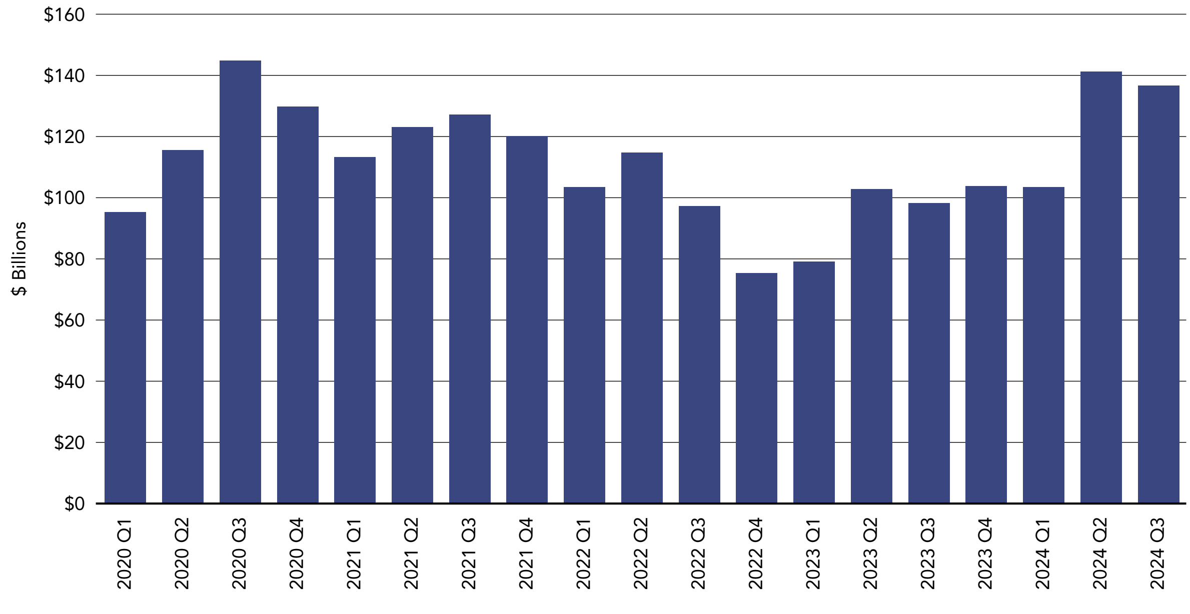
New Issue Volume

New issue volume continues to be robust, exceeding the expectations of most market participants. In the third quarter, new issue volume rose dramatically compared to 2023, with each month in the quarter having over $40 billion in new issues. Total volume for the quarter was $136.6 billion, up 39% compared to 2023. August saw the largest Issuance for that month since 2020. Year-to-date, new issue volume was 381.1 billion, up 35% from the same period in 2023. New issue volume has likely been buoyed by issuers' desire to complete their deals prior to the presidential election in order to minimize uncertainty that the election could cause. Therefore, it is widely expected that new issue volume will remain strong in October but slow significantly in November and December.[2]

In the third quarter, tax-exempt issuance was up 39% and taxable issuance rose 27%. New money issuance increased 16% and refunding volume rose 145%. Year to date, tax-exempt issuance is up 38% after a very slow first quarter and taxable issuance is down 7%. Negotiated volume was up 40% in the quarter compared with a 57% increase for competitive deals.

The increase in new issue volume likely was spurred by an end to COVID relief money for some issuers, a continued high level of tender offers in the market and some large tax-exempt deals that refunded outstanding Build America Bonds. Another contributor to increased new issue volume could be issuers looking to complete deals ahead of the presidential election in November.

Figure 5. Municipal Market Issuance, January 2020–September 2024



Source: LSEG

2 See "Possible Redemption of Build America Bonds", Municipal Securities Rulemaking Board, April 2024. https://www.msrb.org/sites/default/files/2024-04/Possible-Redemption-of-Build-America-Bonds.pdf.

Mutual Fund and Exchange Traded Fund Flows and Other Institutional Investors

In the third quarter, new inflows for tax-exempt mutual funds and ETFs became more consistently positive. According to the Investment Company Institute, in the third quarter through September 25, mutual funds saw net inflows of almost $11 billion, while net inflows into ETFs were almost $6 billion. Stronger net inflows into both mutual funds and ETFs are a positive for the tax-exempt market, especially since we continue to see banks and insurance companies reduce their holdings of tax-exempt debt. Stronger net inflows into mutual funds are also a positive because mutual funds are the primary buyer of the long end of the market, while individual investors, even in separately managed accounts (SMAs), likely prefer bonds in maturities of 20 years or less.

The Fed also released holdings data for municipal securities that showed a continued decline in municipal assets for banks and insurance companies. In fact, the Fed data shows bank holdings down 3% and holdings for property and casualty and life insurance companies down 5% for the first quarter of 2024.[3] Although second quarter data has not been released at the time of publication, conversations with market participants confirm that banks and insurance companies continue to reduce their overall holdings, not by ramping up selling but mostly by allowing maturing securities to run off and be replaced by other assets.

Conclusions

The municipal bond market was quite eventful in the second quarter of 2024, and we saw some fundamental shifts in the market. Highlights include:

- A move to lower yields following the Fed's first rate cut since March 2020, though tax-exempt bonds underperformed Treasurys, especially on the short end of the curve.
- An increase in trade count, up 13% compared to the third quarter of 2023 and 18% year-to-date, indicating continued strong and consistent demand from individual investors directly and through SMAs.
- A significant increase in new issue volume, up 39% compared to the third quarter of 2023, with year-to-date new issue volume reaching $381 billion, up 35% from the same period in 2023, as issuers are likely trying to complete their deals prior to the presidential election.
- Larger net inflows into tax-exempt mutual funds and ETFs, while banks and insurance companies continued to reduce their holdings of municipal securities.

As we enter the fourth quarter, we expect new issue volume to decline significantly in November and December, and it is extremely likely that 2024 will be another record year for trade count.

3 Board of Governors of the Federal Reserve System (US). Financial Accounts of the United States, Z.1 Release. Available at: https://www.federalreserve.gov/releases/z1/.

ABOUT THE MSRB

The Municipal Securities Rulemaking Board (MSRB) protects and strengthens the municipal bond market, enabling access to capital, economic growth, and societal progress in tens of thousands of communities across the country. MSRB fulfills this mission by creating trust in our market through informed regulation of dealers and municipal advisors that protects investors, issuers and the public interest; building technology systems that power our market and provide transparency for issuers, institutions, and the investing public; and serving as the steward of market data that empowers better decisions and fuels innovation for the future. MSRB is a self-regulatory organization governed by a board of directors that has a majority of public members, in addition to representatives of regulated entities. MSRB is overseen by the Securities and Exchange Commission and Congress.

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