HilltopSecurities

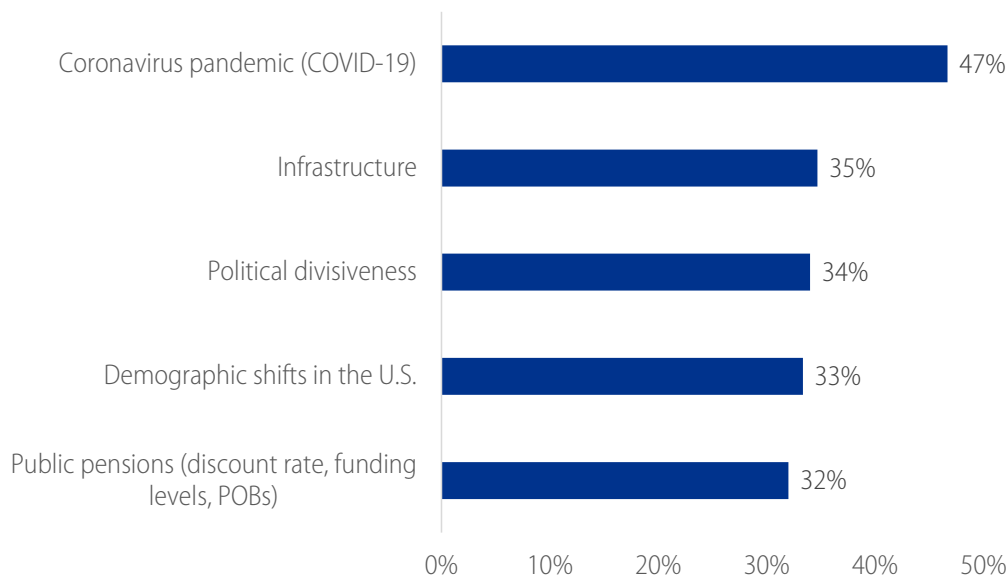U.S. Municipal Bond Market

2021 Municipal Bond Analyst Survey

- A key takeaway from our 2021 survey results is that there is not a clear-cut, or leading issue influencing the municipal bond market right now.
- The coronavirus (COVID-19) pandemic was named by only 47% of those surveyed as one of the most important issues/ trends influencing the municipal bond market in our December 2021 survey of 150 municipal bond credit analysts. Last year, in April 2020, 92% of analysts indicated COVID-19 as a top-five issue or trend.
- There is also a much wider range of issues or trends that analysts believe are influencing the municipal market.
- Public pensions (32%) was a key trend for analysts before COVID-19, this year it dropped to the fifth most important.
- Municipal analysts are closely divided about the appropriateness of the amount of fiscal policy that was focused on public finance in 2020 and 2021.
- Opinions about both state and local government credit quality mostly strengthened in 2021 compared to results from our 2020 survey.
- A little over half of analysts are satisfied in some way with municipal bond market disclosure.
- Most analysts do not think state and local governments are prepared for climate change or cyber attacks.
- Analyst opinions' about how the rating agencies handled COVID-19 is mostly favorable.
- We also saw that analyst opinions' overall about the rating agencies have improved across the board in the results of our 2021 analyst survey.

Tom Kozlik
Head of Municipal Research & Analytics
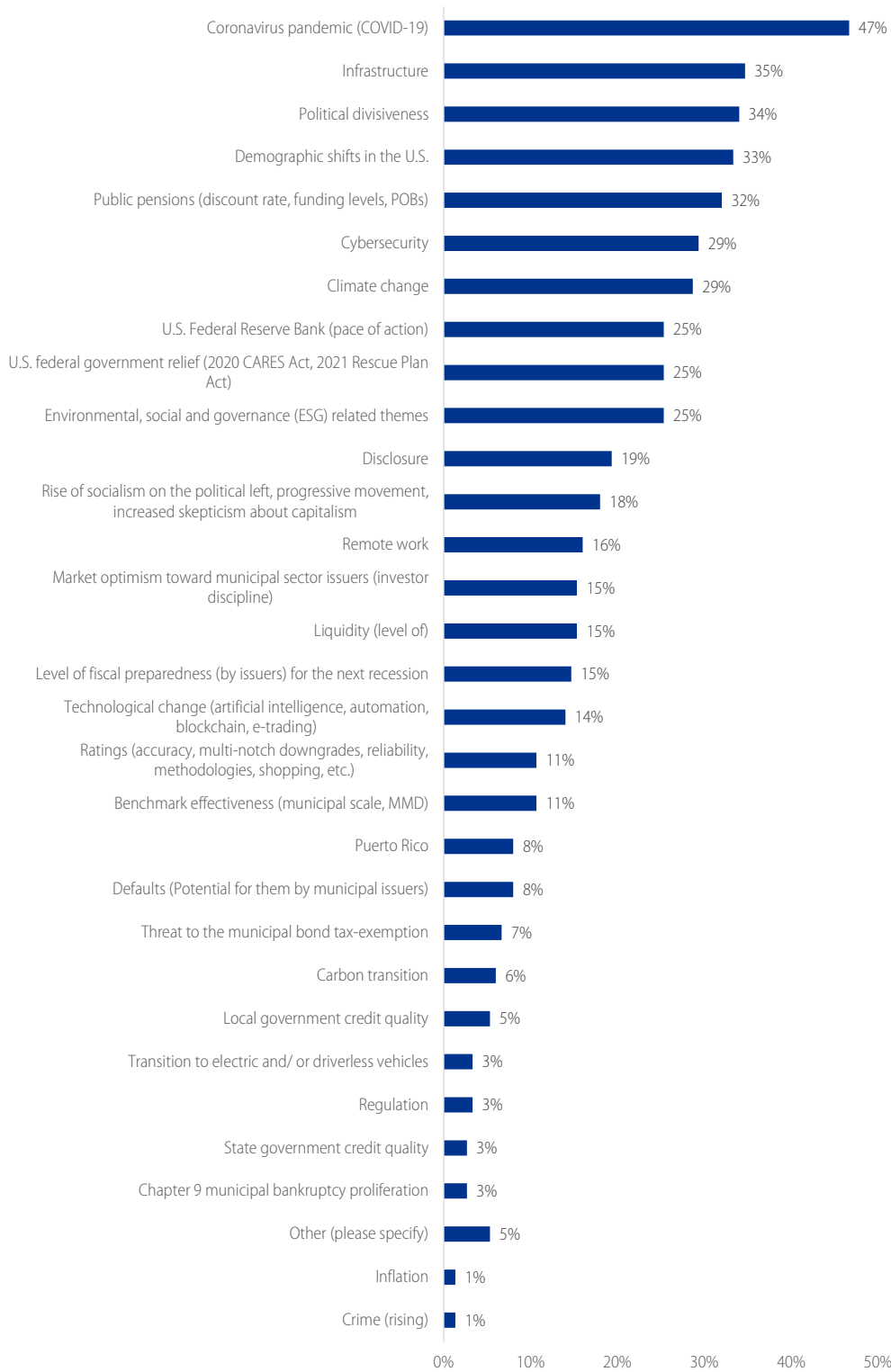*214.859.9439*
tom.kozlik@hilltopsecurities.com

The coronavirus (COVID-19) pandemic was named by only 47% of those surveyed as one of the most important issues/ trends influencing the municipal bond market in our December 2021 survey of 150 municipal bond credit analysts. Last year, in April 2020, 92% of analysts indicated COVID-19 as a top five issue or trend.

Top Five Most Important Issues/Trends Facing the 2021 Municipal Bond Market

Source: HilltopSecurities.

1. What do you think are the 5 most important issues/trends influencing the municipal bond market today? (Nov.-Dec. 2021)

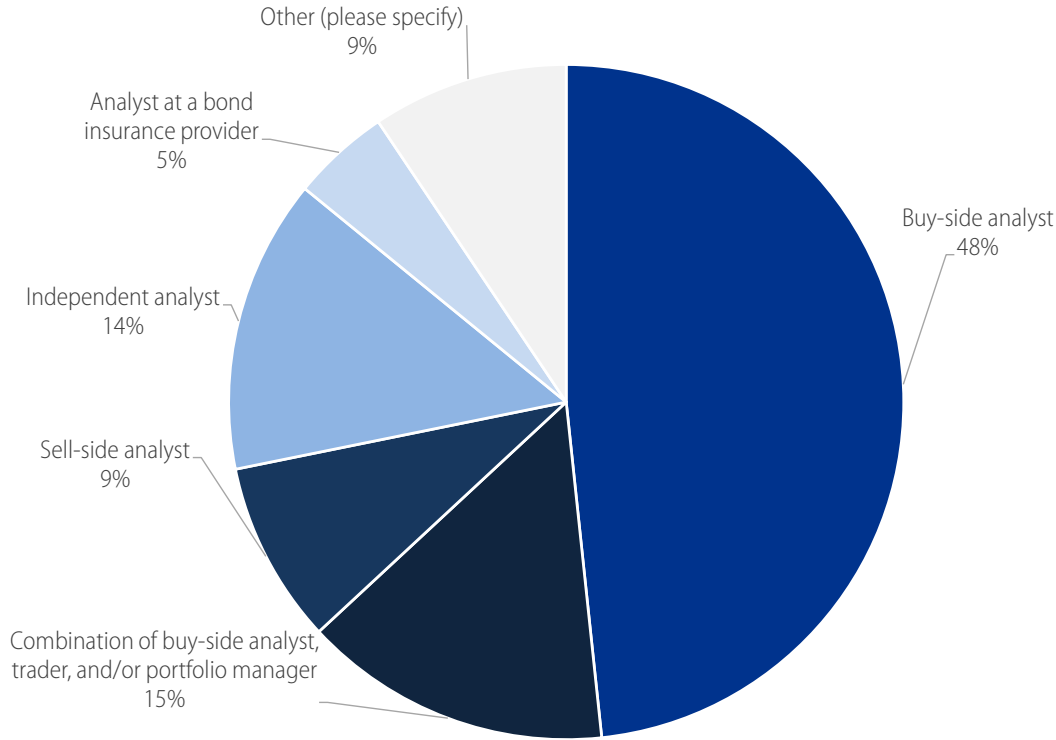| Issue/Trend	Percentage
Coronavirus pandemic (COVID-19)	47%
Infrastructure	35%
Political divisiveness	34%
Demographic shifts in the U.S.	33%
Public pensions (discount rate, funding levels, POBs)	32%
Cybersecurity	29%
Climate change	29%
U.S. Federal Reserve Bank (pace of action)	25%
U.S. federal government relief (2020 CARES Act, 2021 Rescue Plan Act)	25%
Environmental, social and governance (ESG) related themes	25%
Disclosure	19%
Rise of socialism on the political left, progressive movement, increased skepticism about capitalism	18%
Remote work	16%
Market optimism toward municipal sector issuers (investor discipline)	15%
Liquidity (level of)	15%
Level of fiscal preparedness (by issuers) for the next recession	15%
Technological change (artificial intelligence, automation, blockchain, e-trading)	14%
Ratings (accuracy, multi-notch downgrades, reliability, methodologies, shopping, etc.)	11%
Benchmark effectiveness (municipal scale, MMD)	11%
Puerto Rico	8%
Defaults (Potential for them by municipal issuers)	8%
Threat to the municipal bond tax-exemption	7%
Carbon transition	6%
Local government credit quality	5%
Transition to electric and/ or driverless vehicles	3%
Regulation	3%
State government credit quality	3%
Chapter 9 municipal bankruptcy proliferation	3%
Other (please specify)	5%
Inflation	1%
Crime (rising)	1%

A key takeaway from our 2021 survey results is that there is not a clear-cut, or leading issue influencing the municipal bond market right now, according to analysts.

The coronavirus (COVID-19) pandemic was named by only 47% of those surveyed as one of the most important issues/ trends influencing the municipal bond market in our December 2021 survey of 150 municipal bond credit analysts. Last year, in April 2020, 92% of analysts indicated COVID-19 as a top-five issue or trend.

There is also a much wider range of issues or trends that analysts believe are influencing the municipal market.
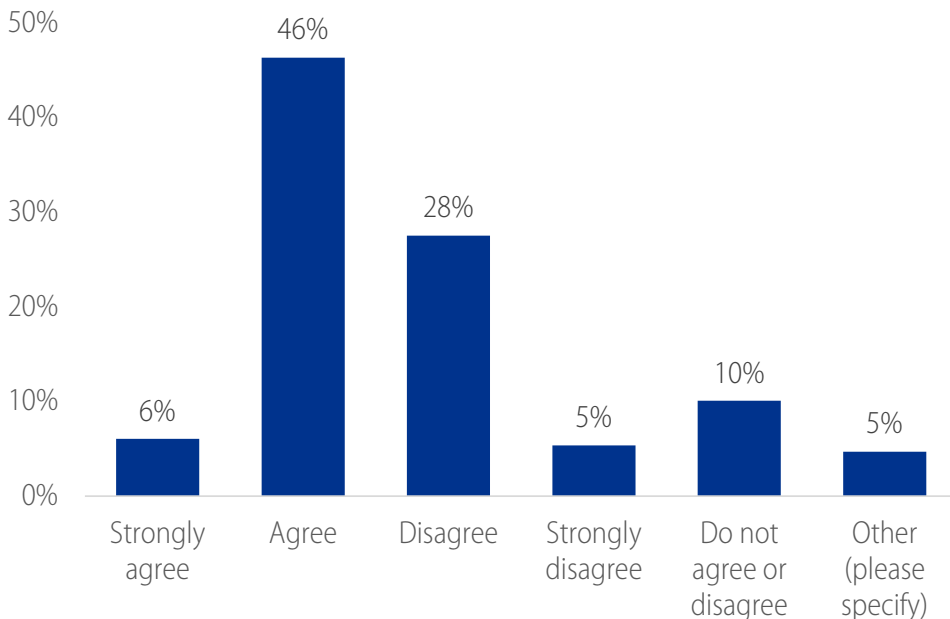
Source: HilltopSecurities.

2. How would your role as a municipal bond market analyst be best described?

Other (please specify)
9%

Analyst at a bond insurance provider
5%

Independent analyst
14%

Sell-side analyst
9%

Combination of buy-side analyst, trader, and/or portfolio manager
15%

Buy-side analyst
48%

63% of those who responded to the survey are Buy-side analysts or a Combination buy-side analyst, trader and/or portfolio manager.

Source: HilltopSecurities.

3. The U.S. government allocated at least $150 billion from the CARES Act (2020) and about $650 billion from the Rescue Plan Act (2021) to state and local governments, and other public finance entities. Do you agree or disagree that this level of federal support for public finance entities was appropriate?

Municipal analysts are closely divided about the appropriateness of the amount of fiscal policy that was focused on public finance in 2020 and 2021.

Strongly agree	Agree	Disagree	Strongly disagree	Do not agree or disagree	Other (please specify)
6%	46%	28%	5%	10%	5%

Source: HilltopSecurities.

A little over half (52%) indicated that they strongly agree or agree that the CARES Act and Rescue Plan Act relief was appropriate.

4. What municipal sectors are most likely to IMPROVE in credit quality (choose three) in 2022?
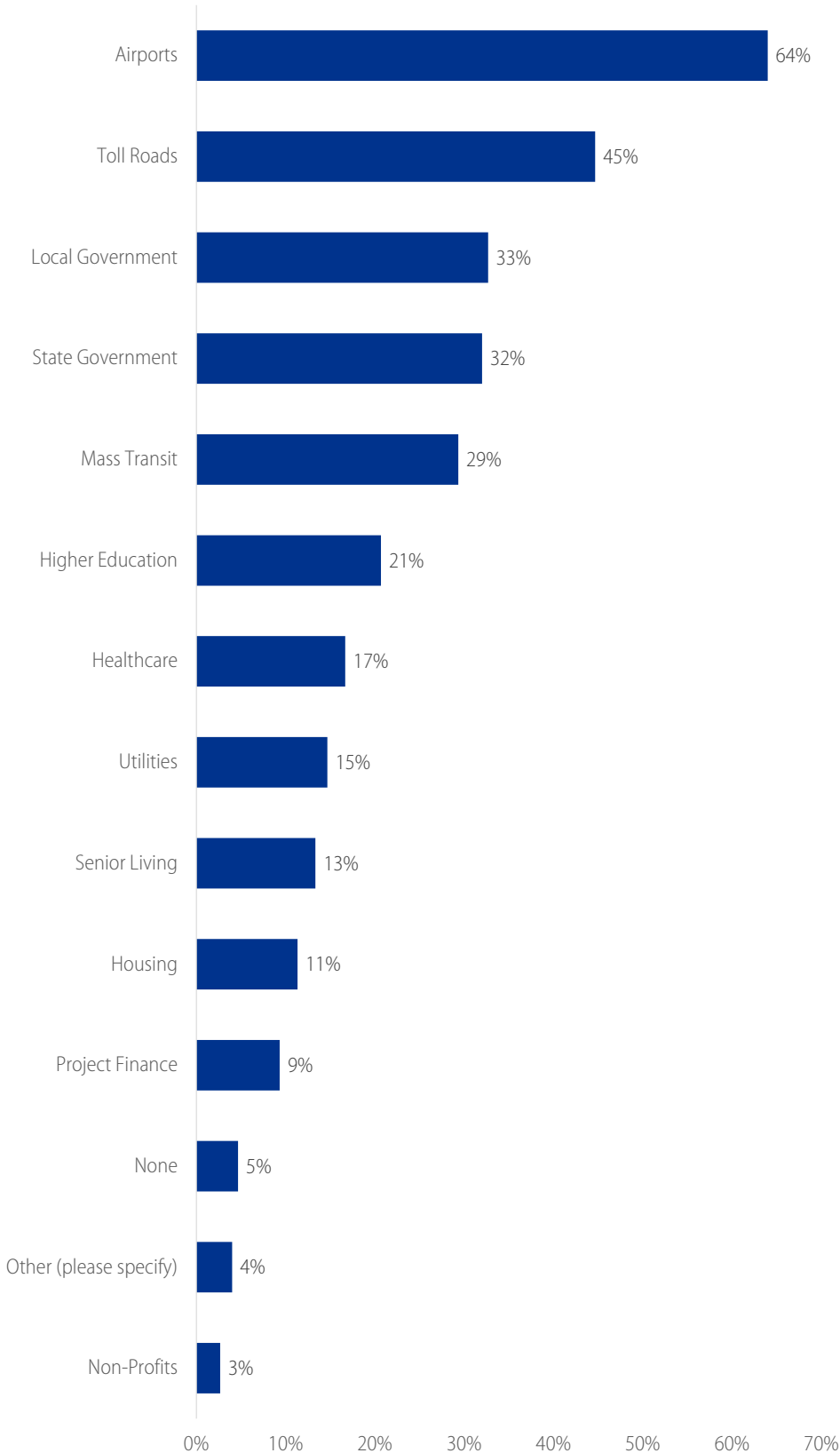
Sector	Percentage
Airports	64%
Toll Roads	45%
Local Government	33%
State Government	32%
Mass Transit	29%
Higher Education	21%
Healthcare	17%
Utilities	15%
Senior Living	13%
Housing	11%
Project Finance	9%
None	5%
Other (please specify)	4%
Non-Profits	3%

Source: HilltopSecurities.

Analysts believe that the airport (64%) and toll road (45%) sectors are among those best positioned to improve in credit quality in 2022.

The local government (33%) and state government (32%) sectors are also likely to improve in credit quality next year according to the municipal analysts who participated in our survey.

5. What municipal sectors are most likely to DECLINE in credit quality (choose three) in 2022?

Sector	Percentage
Senior Living	57%
Higher Education	50%
Healthcare	45%
Mass Transit	32%
Project Finance	24%
Non-Profits	21%
Utilities	15%
Housing	13%
None	11%
Local Government	8%
State Government	7%
Airports	7%
Other (please specify)	6%
Toll Roads	5%
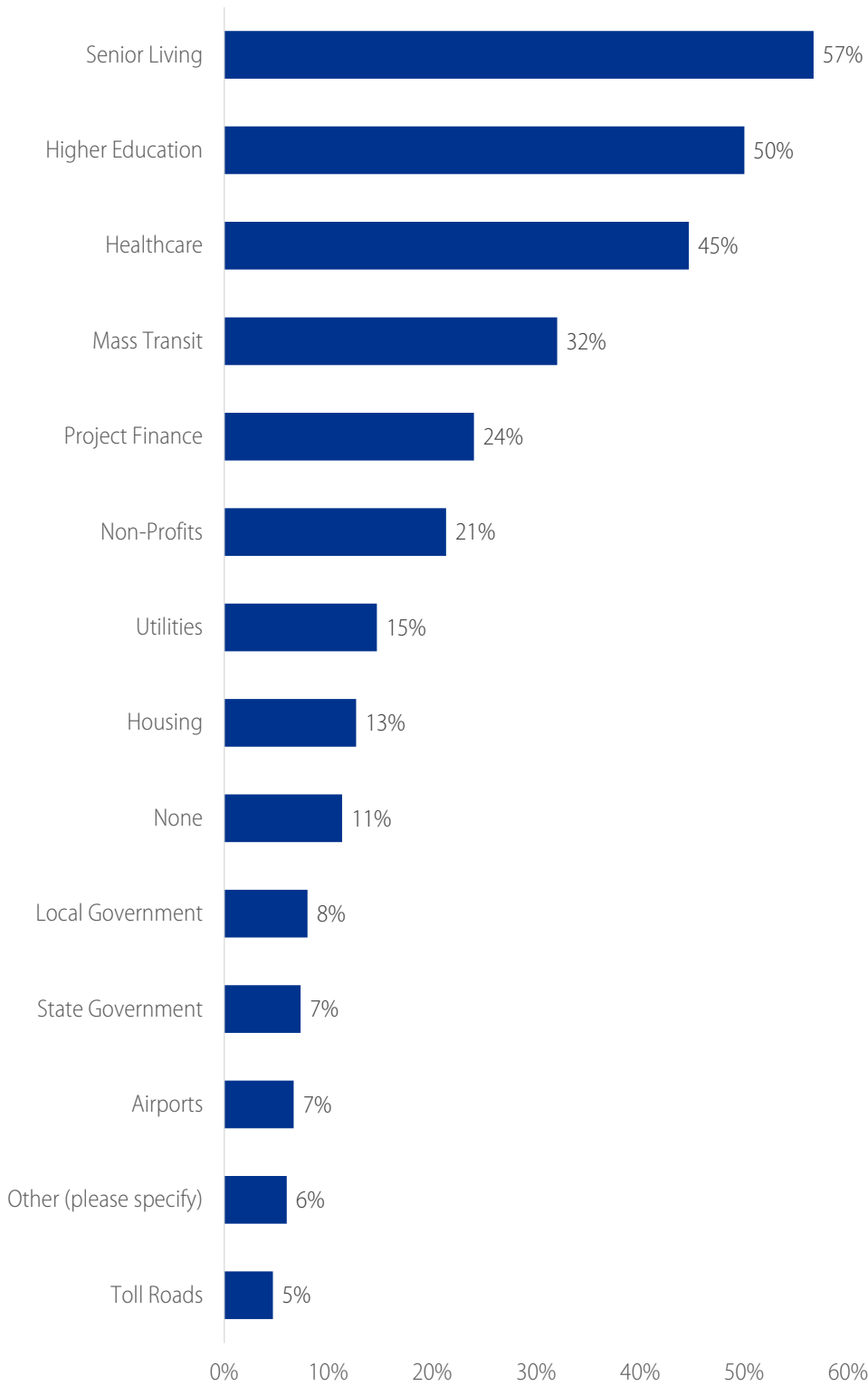
Source: HilltopSecurities.

Various revenue sectors are less optimally positioned for what is likely to transpire in 2022, according to our analyst survey.

Over half of analysts surveyed believe that the senior living sector (57%) and higher education sector (50%) are likely to decline in credit quality in 2022.

Almost half of analysts believe the healthcare sector (45%) will decline in credit quality in 2022.

6. How would you describe U.S. STATE government credit quality currently?

Source: HilltopSecurities.
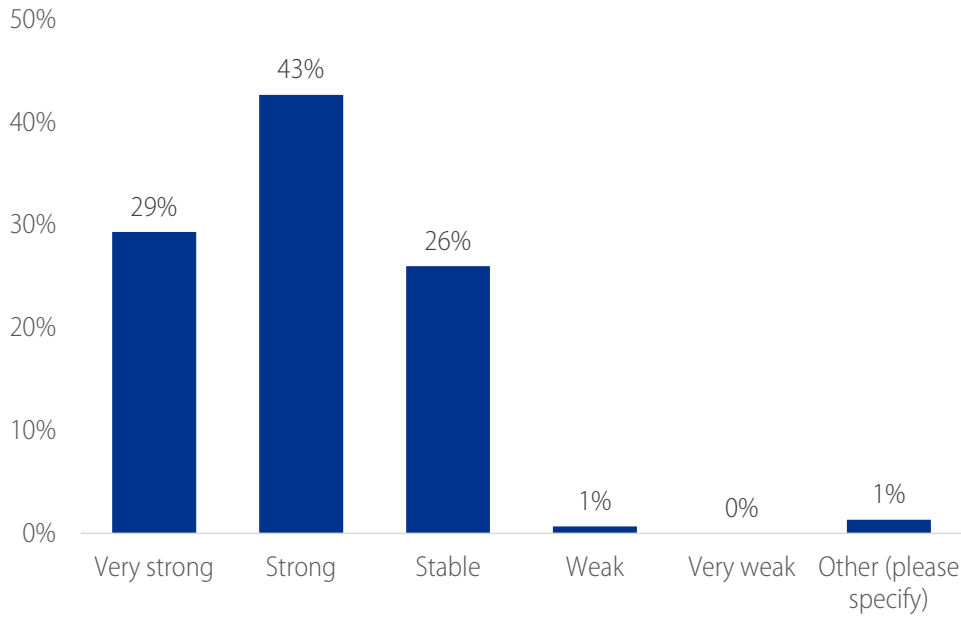
Opinions about both state and local government credit quality strengthened in 2021 compared to results from our 2020 survey.

7. How would you describe U.S. LOCAL government credit quality currently?

Source: HilltopSecurities.
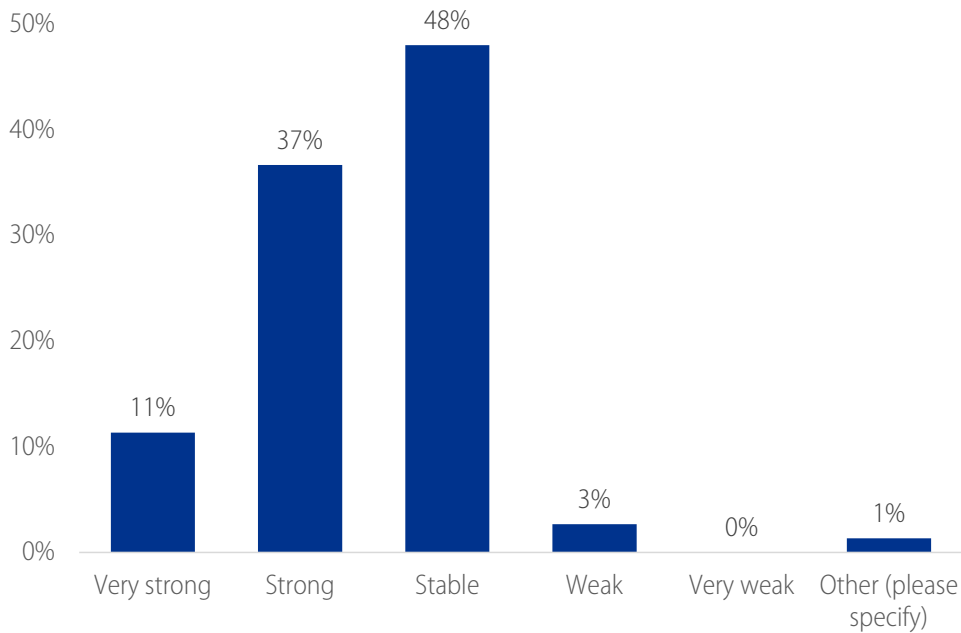
Almost all (98%) of analysts believe state government credit quality is very strong (29%), strong (43%), or stable (26%).

Opinions about local government credit is almost as enthusiastic as 96% of analysts surveyed believe local government credit quality is very strong (11%), strong (37%), or stable (48%).

8. How would you describe your level of satisfaction about aspects such as timing, amount of disclosure in the municipal bond market right now?

Very satisfied	1%
Satisfied	17%
Somewhat satisfied	36%
Somewhat dissatisfied	24%
Dissatisfied	19%
Very dissatisfied	3%
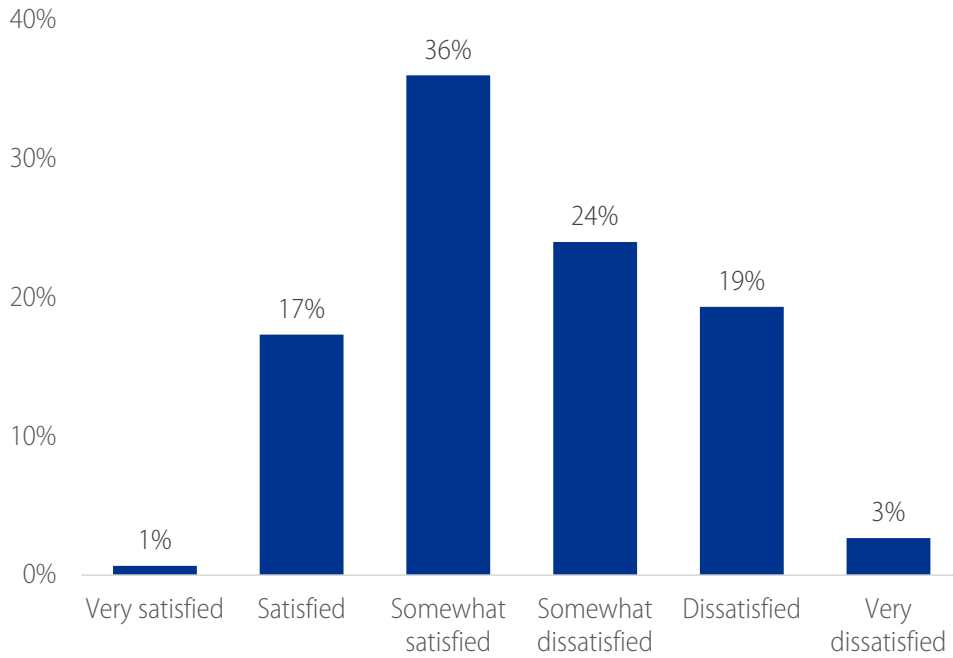
Source: HilltopSecurities.

9. What is the likelihood that recent events related to the COVID-19 pandemic will cause you to ask for or require municipal issuers to disclose additional information on a more regular basis?

The survey results shows that only 54% are very satisfied (1%), satisfied (17%), or somewhat satisfied (36%) with municipal bond market disclosure right now.

Very likely	14%
Likely	36%
Somewhat likely	31%
Somewhat unlikely	9%
Unlikely	7%
Very unlikely	3%
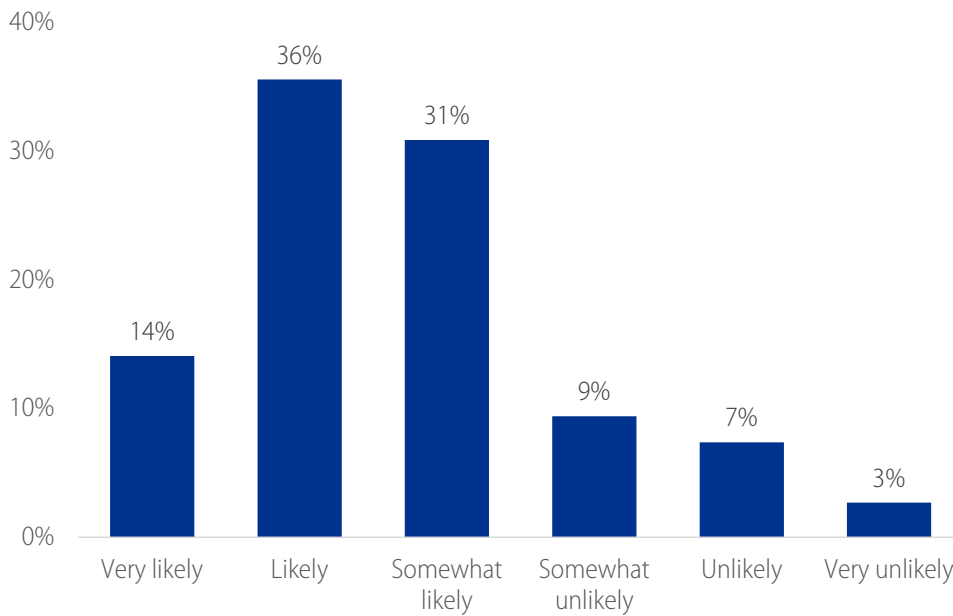
Source: HilltopSecurities.

Most analysts (81%) are likely to ask municipal issuers to increase disclosure going forward.

10. How impactful will results from the 2022 mid-term elections be toward the public finance sector in the near- to medium-term?

Source: HilltopSecurities.

Most analysts (83%) expect the 2022 mid-term elections will impact public finance in the medium term.
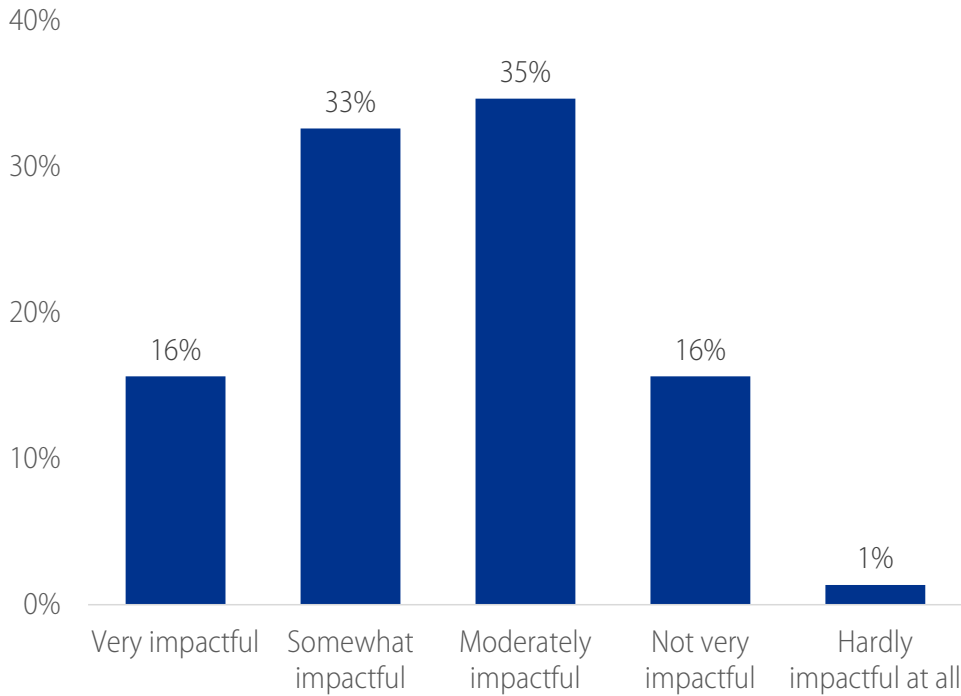
Questions remain about how impactful themes related to remote work will be in public finance going forward.

## 11. How impactful will remote work-related trends be on the public finance sector in the medium- to long-term?
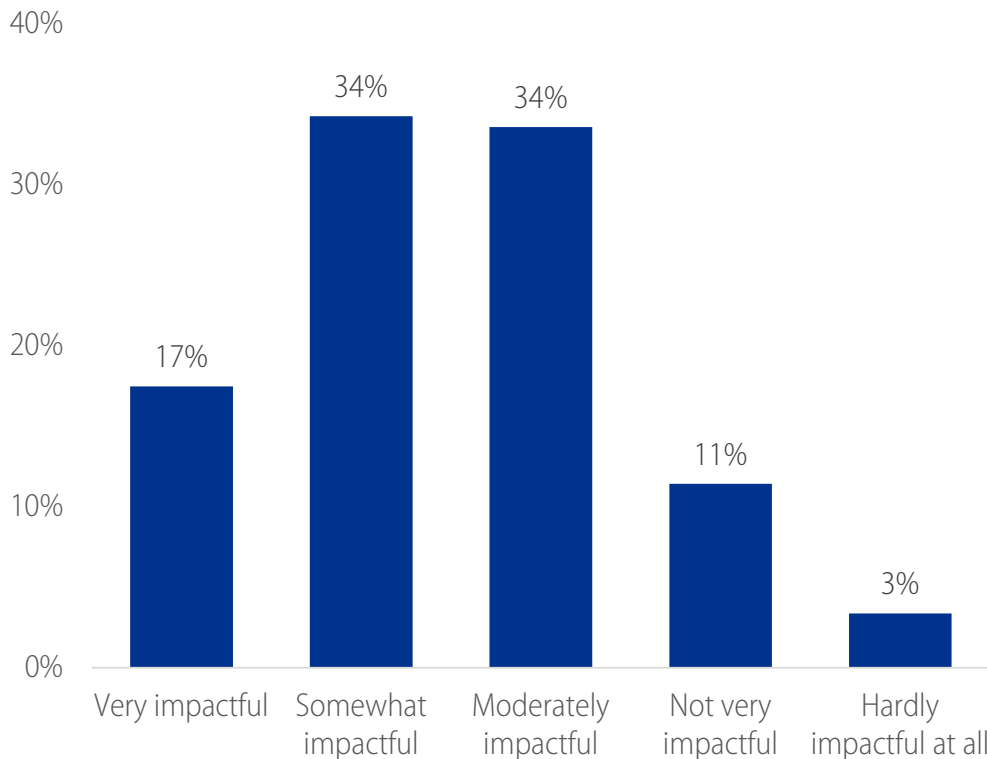
Source: HilltopSecurities.

Not very many analysts (14%) think remote-work related trends will NOT impact public finance in the medium to long-term.

12. What is your opinion of how prepared state and local governments and other municipal market participants are currently for CLIMATE CHANGE?
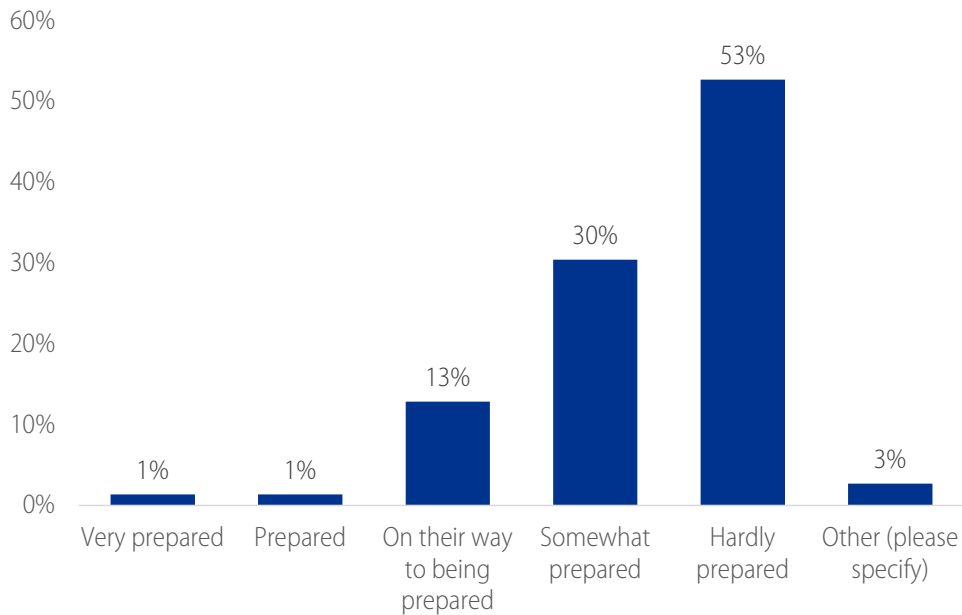
Source: HilltopSecurities.

Most analysts do not think state and local governments are prepared for climate change or cyber-attacks.

13. What is your opinion of how prepared state and local governments and other municipal market participants are currently for CYBER ATTACKS?

Source: HilltopSecurities.
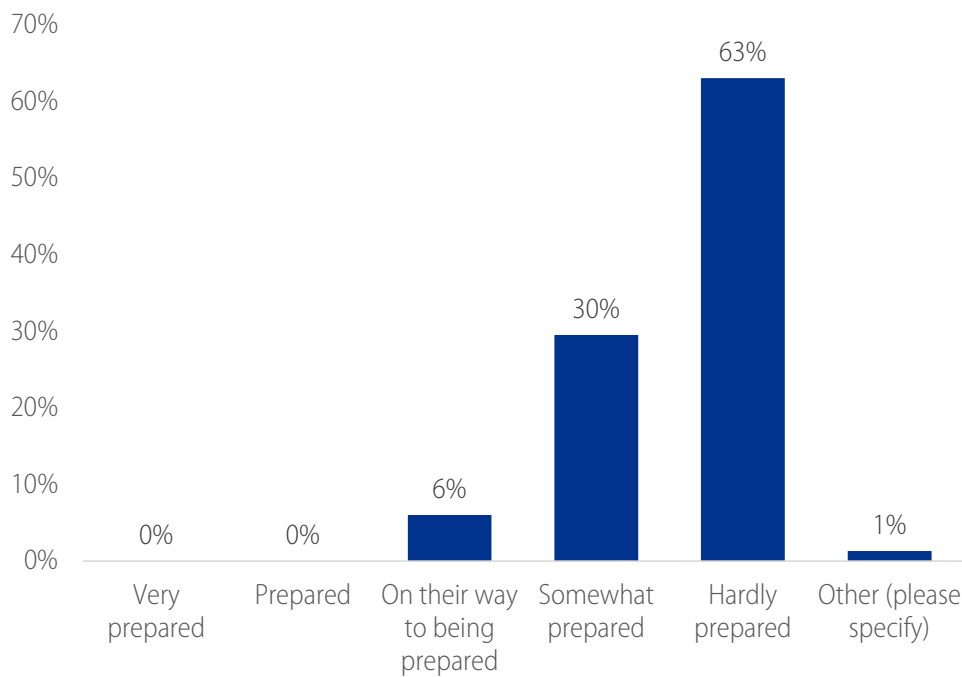
Only 15% of analysts surveyed believe state and local govts. are very prepared (1%), prepared (1%), or on their way to being prepared (13%) for climate change.

While only 6% of analysts surveyed believe state and local govts. are very prepared (0%), prepared (0%), or on their way to being prepared (6%) for cyber-attacks.

14. What is your opinion of how the municipal bond credit rating agencies have covered recent COVID-19 related events and handled sector-wide and individual issuer rating actions?

Rating Agency	Very Favorable	Somewhat Favorable	Neutral	Somewhat Unfavorable	Very Unfavorable	Undecided
Moody's	20.41%	36.05%	21.09%	9.52%	3.40%	9.52%
SP Global	15.75%	36.30%	23.29%	11.64%	4.11%	8.90%
Fitch	13.10%	39.31%	26.90%	5.52%	1.38%	13.79%
Kroll	5.59%	18.88%	32.17%	6.99%	2.80%	33.57%

Source: HilltopSecurities.

Analyst opinions about how the rating agencies handled COVID-19 is mostly favorable: Over 50% of analysts have a "Very favorable" or "Somewhat favorable" opinion of how Moody's, S&P and Fitch covered COVID-19.

15 .What is your OVERALL opinion of municipal bond ratings from the following credit rating agencies?

Rating Agency	Very Favorable	Somewhat Favorable	Neutral	Somewhat Unfavorable	Very Unfavorable	Undecided	Do Not Consider Ratings
Moody's	17.81%	46.58%	21.92%	8.22%	2.74%	0.00%	2.74%
SP Global	10.96%	45.89%	23.97%	11.64%	4.11%	0.00%	3.42%
Fitch	11.03%	48.28%	24.83%	6.90%	1.38%	0.69%	6.90%
Kroll	3.45%	22.76%	29.66%	11.72%	7.59%	4.14%	20.69%

Source: HilltopSecurities.

Analyst opinions overall about the rating agencies have improved across the board. This year Moody's again received the highest amount of support (64%) in the "Very favorable" and "Somewhat favorable" categories as it relates to analysts' OVERALL opinion of their municipal ratings. This is up slightly compared to the 61% we saw for Moody's last year.

Description and Methodology of the 2021 Municipal Bond Analyst Survey

The results are based on a survey conducted by HilltopSecurities in November and December 2021. The above data was collected from 150 municipal bond credit analysts/ specialists. Analysts from the rating agencies were not asked to participate in the survey.

Please email Tom Kozlik at tom.kozlik@hilltopsecurities.com if you are a municipal bond credit analyst/specialist and would like to participate in the 2022 survey.

We would like to thank everyone who participated in this year's Municipal Bond Analyst Survey, 2021.

Over half of analysts (59%) put Fitch in the "Very favorable" and "Somewhat favorable" categories. Over half of analysts (57%) also put their opinion about S&P in the "Very favorable" and "Somewhat favorable" categories.

Recent HilltopSecurities Municipal Commentary

- <u>Our 2022 Municipal Bond Issuance Forecast</u>, Nov. 22, 2021
- <u>Employee Retirement – An Unexpected But Very Real Obstacle for State & Local Governments</u>, Nov. 18, 2021
- <u>House Passed $1.2 Trillion Infrastructure Plan on Friday, Boosting What We Deemed (in March) as the Golden Age of Public Finance</u>, Nov. 8, 2021
- <u>2020 Municipal Bond Analyst Survey</u>, April 28, 2020

Readers may view all of the HilltopSecurities Municipal Commentary <u>here</u>.