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U.S. Municipal Bond Market

The Next, Next Thing in 2020: What the Next COVID-19 Wave Means, Higher-Ed Enrollment Update, Supply & Demand

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Summary

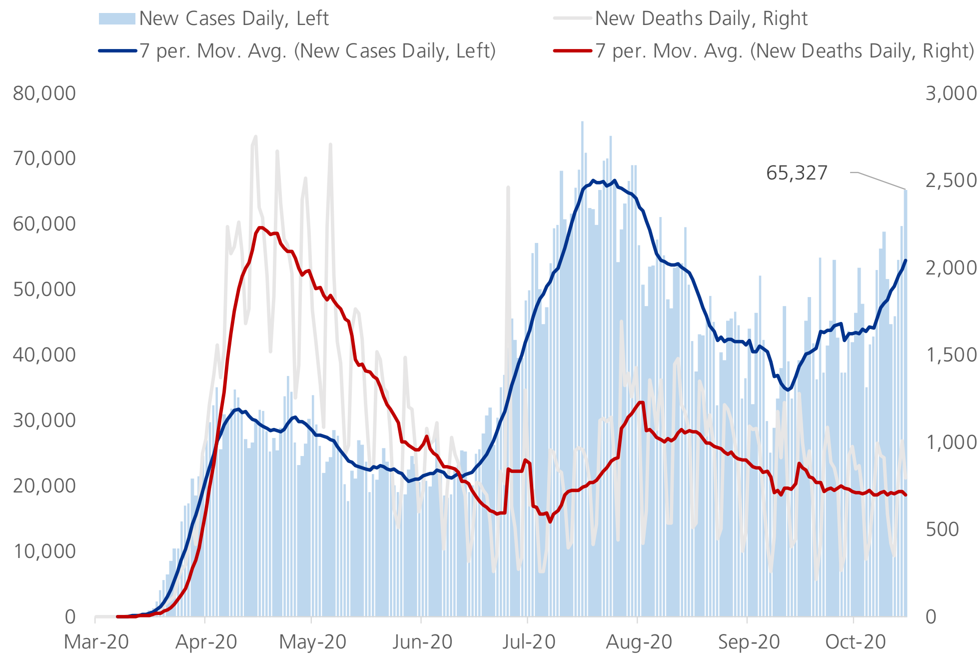
- The number of new U.S. daily COVID-19 cases (65,327 as of Oct. 15, 2020) is the highest since August and the seven-day moving average is growing startling steeper. These results are causing many to forecast that the U.S. may be entering a second (or third) wave of infection.
- Another round or even level of shutdowns, even if not as severe as March or April, could have a suffocating impact on the current budget and credit outlook.
- Enrollment declines for fall 2020 were not quite as bad as what some anticipated, according to data in a new report showing enrollment at public 4 year higher-ed institutions was -1.4% and enrollment at private 4 year higher-ed institutions was -2.0% year-over-year.
- The supply and demand dynamic continues to be in favor of investors as issuer are scheduled to bring $17 billion to market during the week of Oct. 19.

Potential for a Second (or Third) COVID-19 Wave

Remember when Dr. Anthony Fauci said, "You don't make the timeline, the virus makes the timeline" during a CNN interview? That was back at the end of March which now seems ages, or at the very least, years ago. Yet, it still seems the collective "we" may have been pushing back at the wisdom of science. In recent weeks, higher levels of day-to-day activity have returned.

The latest COVID-19 results are causing many to forecast that the U.S. may be entering a second (or third) wave of infection.

New Reported COVID-19 Cases and Death by Day in the United States



Source: The New York Times and HilltopSecurities.

Please see disclosure starting on page 2.

Some students have returned to in-class instruction, and some office workers have returned to office complexes Business and recreational activity have not returned completely to pre-March levels but numbers have leveled off since June.

The leading topic is now the increase in daily new cases of COVID-19 in the United States. Science is pushing back.

Now, the one leading topic of 2020 many were hoping to forget has returned to become the next, next thing of 2020. Just when the volatility from the upcoming 2020 election seemed more manageable and expectations for another round of COVID-19 relief before the election dimmed, the leading topic has shifted back to COVID-19 in the United States. Science is pushing back.

The number of new COVID-19 cases (65,327 as of Oct. 15, 2020) is the highest since August and the seven-day moving average is growing startling steeper. These results are causing many to forecast that the U.S. may be entering a second (or third) wave of infection. This data is receiving national coverage even though the regional increases are varied. On Friday, the cover of the New York Times included an article titled, U.S. Virus Cases Climb Toward a Third Peak. The Dallas Morning News included an article quoting Dallas County Judge Clay Jenkins' written statement:

> "We are on the beginning of a second wave of COVID-19 cases if we do not modify behavior, and with talk of bars opening and increased capacity in other commercial buildings, there is a false sense of security.Given that our numbers are going in the wrong direction, we must turn things around now."

Friday's Dallas Morning News also included an op-ed by the editorial board calling on individuals to do what they can to contain the spread, after noting that closing schools and another commercial lockdown is "politically unachievable."

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Any new interruptions to the economic recovery could have a startling impact on the finances of state and local governments and other municipal entities. We have noted above that activity in many places is still below pre-March levels, but it has leveled off since June resulting in a less than full recovery for government budgets. The Center on Budget and Policy Priorities, for example, forecasts state tax revenue will be down over 20% for a handful of states and down 10% for another handful already. Another round or even level of shutdowns, even if not as severe as March or April, could have a suffocating impact on the current budget and credit outlook.

Higher Education Undergraduate Enrollment Down, Very Close to Last Year's Decline

Concern over enrollment in the higher education sector has been a key consideration for municipal bond investors and rightfully so because of the questions about safety. The data we are seeing so far is that COVID-19 has yet to have a meaningfully negative impact on undergraduate enrollment at public and private 4 year institutions. That being said, it is important for investors to recognize the trajectory of higher-education enrollment was challenged prior to COVID-19 already. We assigned a "Negative" outlook to the higher education sector in August 2019 partially because of enrollment declines.

A recent study Stay Informed with the Latest Enrollment Information from the National Student Clearinghouse Research Center (NSCRC) showed that fall 2020 enrollment of undergraduates at public 4 year institutions was -1.4% compared to fall 2019. For comparison, undergraduate enrollment at public 4 year institutions was -0.8% in fall 2019 compared to fall 2018, so while fall 2020 enrollment was down slightly, it is not by much more than the year prior. Undergraduate enrollment for private nonprofit 4-year institutions was -2.0% in fall 2020, which is a decline that is slightly less than the -2.1% we saw in fall 2019. Overall, undergraduate enrollment was -4.0% in fall 2020 per the report because enrollment at public 2 year institutions was -9.4% this semester.

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Another perhaps more meaningfully negative development that could reverberate into future years is the number of first-year undergraduates fell 16%, according to the data. The executive director of the NSCRC said, "I fear that many of those students will never get back."

Fund flow momentum, while still a net positive, has slowed in the last two months compared to the significant amount of investor dollars that entered the municipal market June through August.

Municipal Bond Supply and Demand Dynamic

The municipal bond supply and demand dynamic will continue to be in favor of investors for the week of Oct. 19. This is because issuers are still rushing to complete financings before the Nov. 3 election. The slate of issuance for the week of the Oct. 19 has grown to $17 billion. The demand side remains somewhat supportive as fund flows were again positive for a second week in a row, as of data reported Thursday. Lipper numbers showed us that another $614 million flowed into municipal funds this week, just a week after $1.7 billion flowed into municipals as of Oct. 7.

Fund flow momentum, while still a net positive, has slowed in the last two months compared to the significant amount of investor dollars that entered the municipal market June through August. An important observation is that it is very likely some of the $20 billion of the funds deposited June through August was just a re-investment of the $31 billion that was pulled from municipal funds in March and April.

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