

The People Elect a New (Prior) President as the Fed Cuts Rates

The events of this past week were inarguably momentous. It was not only marked by a historic presidential election, but also saw the Dow Jones, the Nasdaq, and the S&P 500 all reach new record highs, and included the second Federal Reserve rate cut in as many Federal Open Markets Committee (FOMC) meetings. Despite the positive comments by Fed Chair Jerome Powell that the labor market has cooled and inflation continues to make significant progress toward the Fed's goal, US Treasury rates jumped on the election news and the 20-Year US Treasury closed on Wednesday at 4.71% up 0.16% from the day before and its highest level since early July of this year. US Treasury rates rallied on Thursday with the 20-Year US Treasury closing nine basis points (bps) lower at 4.62%, and as of 9:00 am CST this morning, the same term is down another 6 bps.

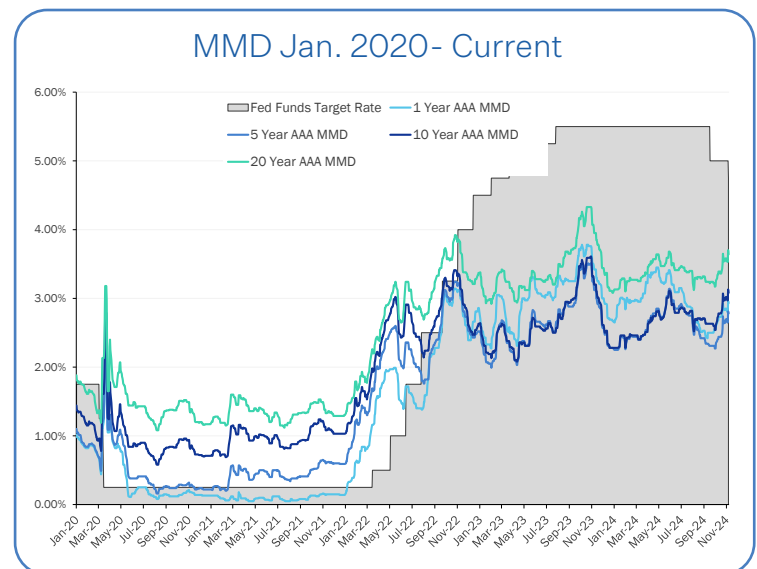
As the White House prepares its transition to a Republican administration, the GOP also won the Senate and might still retain the House. Republican control of both Congressional chambers could give President-elect Trump the power to govern with few constraints, including looser reins on Federal spending. According to Jeffrey Gundlach, CEO of DoubleLine Capital, higher government spending would lead to greater issuance of US Treasuries and push interest rates even higher. While it is still too early to know how Federal policy might be implemented under the new president, the makeup of Washington DC will certainly impact financial markets in general, and, in particular, borrowing rates for our local government clients.

The magnitude of this week's Fed rate cut was 25 bps, or 0.25%, half the size of its previous rate cut, but it signaled that the Fed is committed to the rate-cutting path that it started in September. It was also accompanied by comments from Chair Powell that struck a positive tone regarding the overall state of the economy. He cited third quarter GDP growth of 2.8% on an annualized basis and characterized consumer spending as "resilient," while noting solid conditions in the labor market. His comments regarding inflation made a distinction between headline inflation, which is moving closer to the Fed's long-term goal, and core inflation, which remains elevated.

Even with moderating headline numbers, inflation is still a concern for many Americans especially as some economists determine that President Trump's proposed policies, including large tariffs on imported goods and mass deportations of undocumented immigrants, could serve as an impetus for higher inflation.

For now, the immediate reaction of the municipal bond market to the election result has been higher interest rates, taking its lead

from the US Treasury market. On Wednesday, the day after the election, the 10-Year MMD closed at 3.13%, 16 bps higher than the previous day before rallying to a close of 3.08% on Thursday. The 20-Year MMD experienced similar movements closing at 3.70% on Wednesday, 17 bps higher than Tuesday, and rallying by 6 bps yesterday to 3.64%. Like the 20-Year US Treasury rate, the 20-Year MMD has rallied today as well, coming down as much as 12-14 bps. The graph below shows MMD rates since January 2020.



According to the Bond Buyer, municipal bond fund flows were positive for the week ending Wednesday. Municipal bond mutual funds added \$1.263 billion for the week, which was the 19th straight week of positive fund flows and nearly double last week's \$658.5 million of inflows. High-yield funds also saw positive fund flows for the week at \$333.7 million. These consistent inflows are positive developments for the municipal bond market and will apply downward pressure on borrowing rates for local governments.

Just after the Fed's September rate cut, the markets were anticipating up to nine quarter point rate cuts throughout 2025 with some finally claiming victory over the persistent inflation that had characterized the economy for the better part of the past three to four years. With a hotter-than-expected September inflation report and now President-elect Trump poised to take office, it appears that market participants may have reignited their concerns for sustained inflationary pressures. PMA will continue to monitor the market and new economic data to see how relevant events impact municipal bond interest rates.

If you have any questions regarding the bond market or your specific bond issue, please do not hesitate to contact a PMA advisor on the second page.

PMA is dedicated to staying up to date on market trends and will be ready to guide you through a dynamic and evolving market. If you have any questions about the municipal bond market in general or your specific bond issue, please feel free to contact a PMA advisor below.



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