



Nuveen's Miller: Legislation, Economic Reopening Give Munis A Boost

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Chuck Jaffe, in this episode of The NAVigator podcast interviewed John Miller, head of municipals at Nuveen. Read the Q & A below as John says that the combination of the American Recovery Act, and the progress towards recovery and the growing vaccination numbers, have made it so that state and local governments that had been crying poverty are now seeing a boom.



He notes that municipal tax revenues have held up better than expected through the pandemic, and now are poised to increase; coupled with stimulus monies, he believes conditions are right for improved credit quality which should help muni bonds thrive for at least the next few years.

John Miller

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CHUCK JAFFE: John Miller, head of municipals at Nuveen is here, and we're talking interest rates, infrastructure, and credit trends now on The NAVigator. Welcome to The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry from users and investors to fund sponsors and creators. If you're looking for excellence beyond indexing, The NAVigator's going to point you in the right direction. And if you're looking for more direction on closed-end funds and business-development companies

check out the Alliance website, AICAlliance.org. Today on The NAVigator I'm joined by John Miller, head of municipals at Nuveen, which is online at Nuveen.com. It's one of the big players in the closed-end fund space, both as an investor and as a fund sponsor. John, thanks for joining me on The NAVigator.

JOHN MILLER: Thank you so much for having me.

CHUCK JAFFE: I'm curious what you consider the headline that anybody who uses municipal closed-end funds should be thinking about. Is it more the American Recovery Act that we just saw and the implications that it has on taxes and infrastructure? Is it the infrastructure spending bills that we're seeing that are going there? Or is it interest rates? What's the priority for you that investors in the muni space should be saying, "This is my watchlist"?

JOHN MILLER: Everything that you just mentioned is very critical for thinking about municipals, and I would also add to that the outlook for taxes and tax policy changes. The big change in the last 12 months really has been the combination of the American Recovery Act with the reopening and the progress on the vaccine. Just within a 12-month period of time, the state and local governments have gone from crying poverty to the position where they're in a boom. And it's very interesting to see because tax receipts actually have hung in there a lot better than expected, now they're starting to really go up. So the overall 12-month budget for the state has been very close to flat for the last year. Nobody a year ago would have predicted that their budgetary condition would be roughly flat year-over-year. But now on top of that, the states are receiving a huge stimulus money from the American Recovery Act. The numbers are pretty astounding, about \$360 billion in direct fiscal support to state and local governments, that's over 16% of their total budgets. So it kind of wipes out those deficits that some states had been projecting and puts them into a surplus mode probably for the next two years at least for most states. And again, that's after revenues having held up relatively well. But in addition, states pay for things like K-12 education funding, they typically help support funding of things like charter schools, and colleges, and health care. And those sectors are also getting funding, like \$129 billion for K-12 in addition to the \$360 billion that I mentioned that are going to the states themselves. Another \$10 billion for capital projects, another \$40 billion for higher education, another \$8 billion for airports, so these are significant improvements in credit quality. So what you're seeing is the ratings agencies that rate municipal credits, they have sector outlooks and most of the sector

outlooks have been moved to negative over the course of the last year. And with the passage of this new stimulus act, the ratings agencies are now moving these outlooks from negative to stable. So there's been a big shift in credit quality of municipals and that is right in advance of what we all hope is going to be more and more significant reopenings as a higher and higher percentage of the population are vaccinated.

CHUCK JAFFE: The expectation was that municipalities were really going to suffer, especially any that relied at all on tourism and other municipal taxes they might get as part of their revenues.

JOHN MILLER: Correct.

CHUCK JAFFE: If they're doing better than expected now, is there a bit of a boom coming? Everyone keeps talking about how we're going to see all the pent up demand and people are going to go places. So are there municipalities that have managed to sort of tide it along and keep going that are now going to see some major boom in terms of how things are going? Or when you were talking about revenues and how things were, you were more on the state level than the local level, meaning that they still have some catching up to do in places like Chicago or what have you?

JOHN MILLER: You're bringing up a good point, because some revenue streams have held up extremely well, and those being personal income taxes. Personal income taxes have not been nearly as impacted as one would have expected. Things like capital gains which are collected by many states, they were relatively strong in 2020 because of the strength of the stock market. More of the upper income echelons pay higher components of state taxes, so those groups have held up well economically and therefore those tax collections are extremely stable. Property tax collections which are really the lynchpin of support for local governments, those have been growing at a 5% or 6% or 7% rate year-over-year depending on the location because the single family housing market in particular has been quite strong. That's not to suggest that there isn't any pressure at all, because as you point out, areas like Las Vegas, convention center credits, hotel oriented credits, stadiums, certainly those have been impacted negatively but that has not been really at the crux of the municipal market as a whole. They might grab some headlines, that stadiums and airports have a softening of revenues over the past year. That's much more of a significant decline than what I mentioned which are personal income taxes, property taxes, and sales taxes have all been very stable.

But the stable revenues which are now increasing are overall more important to the sector, they're overall more important to the asset class. And now all of the components that we just mentioned are getting a boost from what's happening, so a rising tide is lifting all those now.

CHUCK JAFFE: We talked a little bit about infrastructure and of course some of the other things we've discussed, well, their future may depend on what's happening legislatively. How worried are you about the political scene throwing a wrench into the positive scenario you see?

JOHN MILLER: When it comes to munis, the politics are actually in the favor of munis. Because to be honest, munis started to react more positively as certain of the major election results started to come in. So for example, munis had a leg up particularly in the credit sensitive areas, in the higher yielding areas, they had a leg up when president Biden was elected in November. Then they had another leg up when the Georgia runoffs when Democrat, creating the 50/50 Senate, and because that made the American Recovery Act to get past the 50/50 Senate. Then what are we looking for now going forward, what's next on the agenda? Well, two of the important priorities on the agenda going forward are an infrastructure financing bill which could have some components which help the municipalities, in part because infrastructure is capital projects that typically would be paid for by the states. If the federal government comes in and helps support these capital projects with different tools like build back better bonds and things like this, that could further boost some of the trends that we're talking about here. But also what we're about to come upon as well is the pay-for side of the equation, and the pay-for side of the equation is so far the federal government has been deficit financing these programs and they want to raise revenues, and they want to raise revenues on the highest tax bracket both individuals and corporations. So there are trial balloons being floated as we speak to say, how about taking that top tax bracket from 37% to 39.6%? And the corporate tax, which had been cut under Trump, maybe going up to perhaps in the neighborhood to maybe 28% under Biden. As well as making capital gains and dividends taxed at the same rate as your ordinary income, which would then be 39.6%. So that would be a major change, and for a tax-exempt municipal bond, the taxable equivalent yield would be higher for individuals in those tax brackets. In other words, the tax exemption itself would become more valuable.

CHUCK JAFFE: Interesting. I pointed out Nuveen, very active in the municipal space, very active in the closed-end fund space. I know that you guys are developing some new products. You may not actually be able to talk about them, but is the optimism you have for this space fueling these? When you have as diverse a product lineup as you've got, do you guys need another product? Is there something out there that you need to fill out the lineup? Is it a different way of looking at things? What's going to make it that you're adding something? Is it your product line? Is it the market that's driving it?

JOHN MILLER: Yeah, I would give you a couple different prongs around which we are really focusing. Given the market dynamics I just described, we haven't discussed interest rates, but the Federal Reserve met and they are still intending to stand pat on zero interest rate policy, the majority of the Federal Reserve board through the end of 2023 at least. And that creates a steepening yield curve environment that we've been in, and steepening yield curve meaning lower rates on the short end which are more directly controlled by the Fed, potentially some higher rates on the long end of the curve. Closed-end funds tend to take advantage of the steepness of that yield curve, so we always want to be thinking about ways of taking advantage of that for our shareholders. Then in addition, what we just talked about on things like the recovery, inherently in municipal fundaments themselves in terms of the credit fundamentals, that favors credit risk over interest rate risk generally. So we want to utilize our research team and our access to bonds to maximize credit spread. Credit spreads widened because of the pandemic themselves and now they're starting to narrow. When you can buy a bond at wider credit spreads, that's another way of saying higher yields. For taking on some of this credit risk, we think these credit risks are coming down with the reopening of the economy as well as the stimulus, and that should benefit higher yielding municipal bonds, non-rated, below investment grade rated, or lower rated. And so we want to have flexible products that can take advantage of these things.

CHUCK JAFFE: John, really interesting. Thanks so much for joining me to talk about it.

JOHN MILLER: Thank you, Chuck.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. I'm Chuck Jaffe and you can check out my show on your favorite podcast app or by going to MoneyLifeShow.com. To learn more about closed-end funds, interval funds, and business-development companies go to AICAlliance.org, the

website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. Thanks to my guest, John Miller, head of municipals at Nuveen. Learn more about the firm at Nuveen.com and on Twitter @NuveenINV. John's on Twitter as well, he is @JohnMNuveen. The NAVigator podcast is new every Friday, subscribe on your favorite podcast app and join us again next week to learn more about investing with closed-end funds. Until then, stay safe everybody.

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