

Post-Election Recap for the Muni Market

Wellington Management's municipal-bond team offers some insight on how the election outcomes might impact the municipal-bond market.

Insight from sub-adviser Wellington Management



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WITH THE PRESIDENTIAL ELECTION AND LOCAL BALLOT MEASURES DECIDED, SOME UNCERTAINTY HAS BEEN REMOVED FROM THE MARKET. However, Georgia's runoff Senate elections in January will decide whether Congress remains divided or if Democrats gain control of both chambers, which could ultimately impact some wider-reaching measures.

If Congress Remains Divided, We See a Reduced Likelihood of:

- A stimulus bill that includes direct aid to state and local governments
 - **Market Implication:** This would be incrementally negative for states, leading to spending cuts, some deficit borrowing, and the additional use of reserves to balance budgets as the benefit from initial stimulus measures fade. Many temporary state and local job cuts could become permanent.
- Affordable Care Act (ACA) tax-penalty reinstatement
 - Congressional action to reinstate the tax penalty is unlikely with a divided Congress. A Democratic sweep would have been the best scenario for this action. The ACA court case will continue as planned; oral arguments before the Supreme Court started on November 10.
 - **Market Implication:** Base case remains continuation of the ACA, with low likelihood of it being overturned
- Public option for healthcare
 - **Market Implication:** A public option would have meant lower payment rates for providers across that population of insured—versus employer insurance—this would have been a slight credit negative for hospitals
- A large federal infrastructure bill
 - Democratic control of the Senate would likely support a stimulative infrastructure bill given historical Republican opposition
 - With a divided Congress, longer-term renewal of the expiring federal highway bill is the best shot for additional infrastructure spending
 - **Market Implication:** Increased state debt issuance that would have accompanied an infrastructure bill likely won't materialize. Without stimulus, new money debt issuance would likely remain subdued.
- Higher federal tax rates
 - Higher rates would have been bullish for the tax-exempt municipal bond market
 - **Market Implication:** Neutral, takes a positive technical off the table, however, the value of the tax-exemption will go up in some states that increase their state income taxes to manage their fiscal gaps

Key Points

- With the presidential election and many local ballot proposals decided, Wellington's municipal-bond portfolio managers shed some light on what could impact the market going forward.
- Ultimately, the party that controls the Senate will likely determine the likelihood of large stimulus packages.
- A changing landscape outlines the need for careful security selection and the ability to truly understand the value of muni credits.

Individual Credit Highlights:

- **State of Illinois** will likely be downgraded below investment grade. The state will likely need to borrow between \$2–\$4 billion to balance their budget this fiscal year and also consider an increase in their flat tax to solve their longer-term structural gap.
- Reduced likelihood of stimulus will also limit the options for **New York’s Metropolitan Transportation Authority (MTA) and the State of NJ**. A significant drop in ridership is challenging the MTA’s cash flow and they will likely have to rely on a combo of deep service cuts, additional deficit borrowing, and supplemental aid from both the city and the state, which we expect them to provide. New Jersey was also hoping to reduce their reliance of a large deficit financing this year with stimulus funds, an option that now looks more remote.
- **Future of the Municipal Lending Facility:** This program allows the Federal Reserve (Fed) to buy up to \$500 billion in debt from state and local governments
 - Program expires on December 31 unless the Fed and Treasury Department extend it
 - Available to state and local governments and select revenue bond issuers. Illinois and MTA have been the only borrowers thus far.
 - The initial cash flow pressures for states and local governments have been mitigated by better-than-expected tax receipts, available internal liquidity, and spending cuts

State-Level Ballot Measures:

- **State of Illinois Graduated Income Tax Measure** – Proposal to shift flat tax to a graduated income tax, with an increase in the top rate to 6.75%
 - Rejected by voters
 - **Market Implication:** This measure was expected to raise an additional \$3 billion a year for IL and be credit supportive. Between the measure’s failure to pass and a lack of federal stimulus, the state’s credit ratings are likely to fall below investment grade.
- **California Proposition 15** – This measure would have allowed commercial properties in CA to be taxed at market rates rather than purchase price
 - Rejected by voters
 - **Market Implication:** Neutral, passage would have been a positive for local governments but it appears things will remain status-quo
- **Puerto Rico Statehood** – A non-binding referendum asking residents if they would like PR to become a full-fledged state
 - Passed by voters
 - **Market Implication:** Neutral, no change in PR status expected following vote as any change requires congressional approval
- **Arizona Proposition 208** – A 3.5% income-tax surcharge on taxable annual income over \$250,000, top tax rate would increase to 8%
 - Passed by voters
 - **Market Implication:** Marginally positive, will provide additional revenues and indicates voter willingness to support additional revenue sources

Top Ten Holdings

Hartford Municipal Opportunities Fund (as of 10/31/20)

State of Illinois, GO	2.30	Chicago, IL, Transit Auth	1.34
New York State Dormitory Auth Rev	2.14	California State, GO	1.28
State of Texas, GO	1.62	Lower Alabama Gas Dist	1.12
Buckeye, OH, Tobacco Settlement Finance Auth	1.54	Public Finance Auth, WI	1.08
Illinois State Finance Auth Rev	1.50	Michigan Finance Auth Rev	1.07

Hartford Municipal Income Fund (as of 10/31/20)

City of New York, NY, GO	3.12	Metropolitan Transportation Auth, NY, Rev	1.41
New York State Dormitory Auth Rev	3.11	City of Los Angeles Department of Airports	1.39
State of Colorado	1.59	State of Illinois, GO	1.37
Sales Tax Securitization Corp., IL Rev	1.44	Maryland Stadium Auth	1.34
State of California, GO	1.43	Kendall Kane & Will Cntys. Community Unit School Dist. No 308	1.30

Hartford Municipal Short Duration Fund (as of 10/31/20)

State of Texas	3.98	State of Illinois, GO	2.30
New York City Water & Sewer System	3.86	Metropolitan Pier & Exposition Auth, IL	2.22
Metropolitan Transportation Auth, NY, Rev	3.19	New Mexico Mortgage Finance Auth	2.05
Sales Tax Securitization Corp., IL	2.91	Municipal Electric Auth, GA	1.73
Massachusetts Dev Finance Agency, Rev	2.90	Chicago, IL, Board of Education, GO	1.69

Holdings are subject to change. Percentages may be rounded.

Hartford Municipal Opportunities Fund Tickers

I: HHMIX A: HHMAX C: HHMCX Y: HHMYX F: HHMFX

Hartford Municipal Income Fund Tickers

I: HMKIX A: HMKAX C: HMKCX F: HMKFX

Hartford Municipal Short Duration Fund Tickers

I: HMJIX A: HMJAX C: HMJCX F: HMJFX

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Investors should carefully consider a fund’s investment objectives, risks, charges and expenses. This and other important information is contained in the fund’s prospectus and summary prospectus, which can be obtained by visiting hartfordfunds.com. Please read it carefully before investing.

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