**THE DAILY CHECK-IN WITH GOLDMAN SACHS**

**GUEST: SYLVIA YEH, CO-HEAD, GOLDMAN SACHS ASSET MANAGEMENT'S MUNICIPAL FIXED INCOME BUSINESS**
**HOST: LIZ BOWYER, GLOBAL HEAD OF BRAND AND CONTENT STRATEGY**
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**Liz Bowyer:** Hi, Sylvia.

**Sylvia Yeh:** Hi, Liz.

**Liz Bowyer:** So when we spoke around this time last year, the muni market was going through significant volatility based on expectations that the pandemic would put pressures on state and local revenues. How have things played out?

**Sylvia Yeh:** So let's look at 2020, but let's look at it past March. If you close your eyes, it's almost as if that volatility really never happened. What did happen? Well, liquidity returned to our market, and it did so fairly quickly. We had some new buyers come back. The new issue market? It reopened pretty quickly. We had some good structures come to market. They were well received and well distributed.

Issuers took advantage of the rally in treasury rates and actually refunded old tax-exempt debt using taxable munis. The MLF, Municipal Liquidity Facility, that was provided was rarely used. Only a handful of times. And we didn't really see a lot of change in default experience. Flows turned positive, new issue, end of the year at a record high.

What does it mean for all of us? And what did we see? Rates rallied. Credit spreads tightened. The demand for munis continued to remain robust throughout the end of the year. Investment-grade and high-yield munis performed well.

**Liz Bowyer:** And why is that? Why did the muni market fare so much better than expected?

**Sylvia Yeh:** In one word, Liz, resilience. Performance bounced back. And from a credit perspective, the asset class never entered into that crisis that the media spoke about. To the contrary actually happened. And there were a few idiosyncratic issues here and there, but nothing broad. It's interesting, when I speak to David Alter [sp?], who heads up our research effort here at GSAM, what a difference a year makes. We talk about that very often these days. And he actually put together a piece that's worth reading. It's called "Muni Bonds: More Resilient Than You Think." Really frames the market and discusses our view on why we believe it's such a strong asset class.

**Liz Bowyer:** Well, what explains this resiliency?

**Sylvia Yeh:** Three categories, three bullets. The breadth and diversification and stability of the underlying revenue streams. The conservative financial operations and strength of balance sheets. And the conservative debt practices that these municipalities carry. The underlying credit health of the municipal market is improving, and demand for the asset class for that reason remains robust. The bottom line, fundamentals and technicals remain strong for munis.

**Liz Bowyer:** Well, what's the story behind how munis fared during the recent volatility in the rates market?

**Sylvia Yeh:** The weakness was short lived. We welcome higher yields. Many market participants welcome higher yields and were probably looking forward to some volatility. At the beginning of the year, yields were low, ratios were low, munis were expensive. The one takeaway, it's important to note that that backup that we saw was not credit driven; it was rate driven. And for those who follow munis very often, historically, munis tend to follow the path of treasuries. So it really wasn't a surprise.

But typical munis, just like that, the softness disappeared. And muni yields and spreads rallied again. For that brief opportunity where we did see a backup in yields, it really did provide investors with money to put to work a better entry point to the asset class, again, given how depressed yields were at the beginning of the year.

Now, fasten your seatbelts. I mean, we have a lot of data coming out. We have a lot of progress to be made with regard to our path to recovery. And that means -- and you've heard us say this before -- it's important for all of us to remain nimble and flexible because when those pockets of opportunity do show up, we do want to make sure that we're there to enter the asset class when those technicals are more favorable.

**Liz Bowyer:** And what do expect for technicals?

**Sylvia Yeh:** We expect them to remain supportive. And what do I mean by that? If we look at the market, new issue market is happening. Deals are subscribed for. They're well subscribed for. Flows have turned positive again. You know, we are approaching now a period where historically we would have seen some softness in the marketplace because we're approaching tax time. That probably won't happen this year, one, because there's so much cash on the sidelines. And then, secondly, as tax date was moved from April to May, that is actually bringing us closer to another seasonally strong period of time in the muni market where demand is plaintiff.

**Liz Bowyer:** And Sylvia, what will the new fiscal stimulus mean for state and local governments?

**Sylvia Yeh:** The stimulus package is generous, providing direct and indirect support to the sector. It really provides a nice tailwind for the muni market. The Fed help was just that. It was helpful particularly to those few names that significantly needed that help and were impacted by the virus. As an example, the MTA. The majority of high-grade munis, as we mentioned, were well positioned heading into this cycle. And the actual performance through the cycle is far better than a lot of the earlier forecasts.

If we look at the aid and kind of see what it looks like and break it down, state and local governments got a good amount. Transit authorities, education, even states like California and New York received funds and they reported tax revenues well ahead of budget. That's a really good sign.

**Liz Bowyer:** And how will state and local governments be able to use the funds they received from the stimulus?

**Sylvia Yeh:** It's interesting because the use of funds is actually kind of broad and ultimately provides a future budgetary flexibility for a lot of these underlying entities. And they can use these funds for expenses through 2024. So they're looking at pandemic-related expenses, offsetting lost revenue, water and sewer and broadband projects. The things that they cannot be used for, these funds cannot be used for directly or indirectly are going to be tax cuts and pension contributions.

**Liz Bowyer:** So what does all this mean for the muni market?

**Sylvia Yeh:** The market will continue to be dominated by strong fundamentals and technicals. I know I keep repeating myself, but it's worth repeating. If you look at the market today, it's telling. Very strong demand and credit spreads are tighter. If we look at tax-exempt demand kind of going forward, with an improving credit profile and potential tax rate hikes on the horizon, that's going to be supportive for munis. If we look at the taxable muni market, long-duration, high-quality assets are scarce. So they're going to have a natural buyer base gravitating towards those taxable munis.

**Liz Bowyer:** And what about on the supply side? Do you see challenges there?

**Sylvia Yeh:** That's a little unclear. Less deficit financing is a potential. A lot of the monies can be used to replenish reserves, so that's going to be something that we keep an eye on to see how these municipalities are going to use those monies and what types of new programs come back to market.

**Liz Bowyer:** And finally, Sylvia, what sectors of the muni market will you be particularly focused on in the months ahead?

**Sylvia Yeh:** We've been keenly focused on sectors we believe would be mostly impacted and ultimately punished, for lack of a better word, by the market largely because of a perception around the impact of COVID. We're very focused on those fundamentals that we keep talking about. You know, we did not get caught up in the hype of, you know, the fear embedded in the marketplace. We stuck to our guns. We remain committed to security selection discipline. In other words, even across sectors that we like, we stick to the fundamentals of the specific credit and we look for value.

And similarly, for those sectors that we think remain wide, we keep a strong bottoms-up approach.

**Liz Bowyer:** Thanks, Sylvia.

**Sylvia Yeh:** Thanks, Liz. Nice to see you again.