

Municipal Market Weekly Update

MACKAY MUNICIPAL MANAGERS.™ THE MINDS BEHIND MUNIS.



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And We Are Back!

- Munis outperform to ring in the new year
- Recapping 2025 to set table for 2026
- Active momentum quite apparent in product creation

Relative Performance

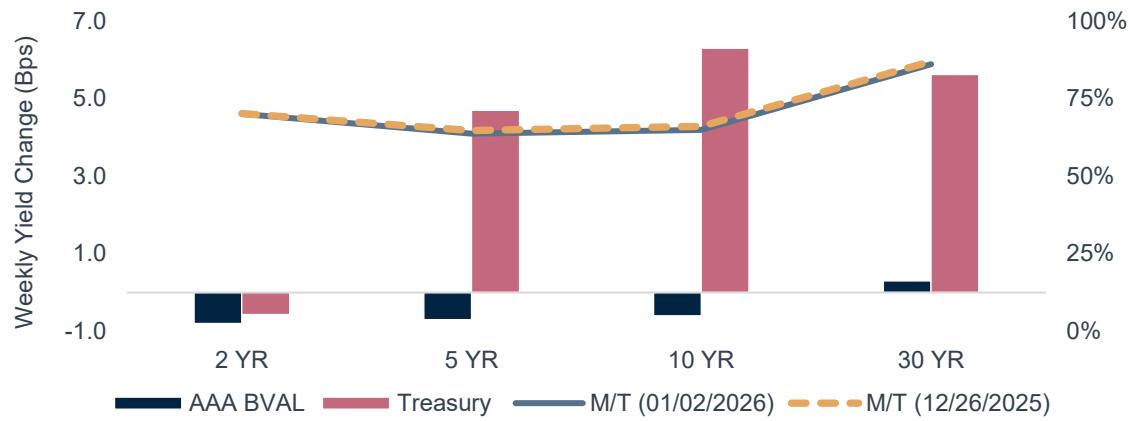
Welcome back to the new year and the anticipation is that municipals are well poised to capitalize on the positive momentum that was present down the final stretch of 2025.

Municipals outperformed Treasuries over the week, as AAA muni yields were largely unchanged while U.S. Treasury yields moved higher. AAA muni rates declined by less than 1 basis point across the front and intermediate portions of the curve, while the 30-year rose modestly by approximately 0.3 basis points.

Treasuries, by contrast, sold off more meaningfully across the curve, driving improved muni-to-Treasury ratios and supporting relative performance for tax-exempts.

From a total return perspective, municipals benefited from rate stability in an environment of rising Treasury yields, underscoring the defensive characteristics of the asset class and the continued support from technicals despite elevated supply.

FIGURE 1: MUNIS OUTPERFORM¹



1. Data as of January 02, 2026. Source: Bloomberg. Spot Muni, Spot AA rates.

Past performance is no guarantee of future results, which will vary. It is not possible to invest directly in an index.



Investment
Management

Technicals

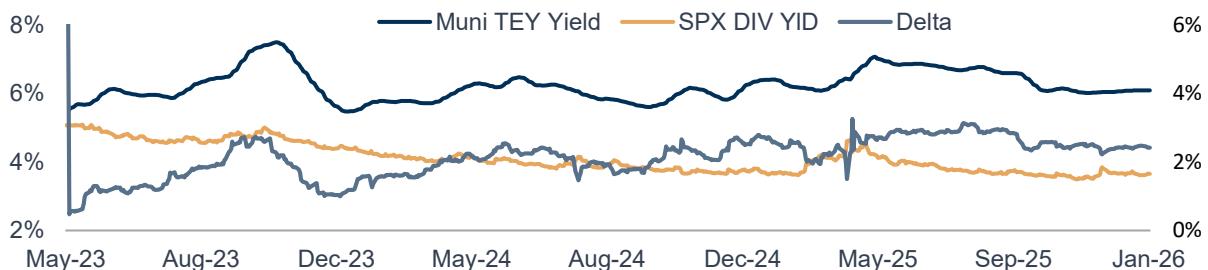
While we are a mere week away from highlighting our top 5 insights for 2026, we thought that this most recent weekly would provide a solid opportunity to recap 2025 and set the table for the year ahead.

Big Picture

The municipal market spent much of 2025 working through a long-overdue normalization—and investors are finally being paid again for taking thoughtful risk. After starting the year in the red, tax-exempts staged a meaningful comeback and will finish 2025 with returns around 4.1%, or north of 6.0% on a tax adjusted basis.² That's a very strong outcome for high-quality fixed income.

Importantly, municipals remain a relatively cheap asset class. Long muni tax-equivalent yields are offering nearly 160 basis points of additional spread versus same-duration corporates, and over 240 basis points of incremental income relative to the S&P 500 dividend yield.

FIGURE 2: TAX EQUIVALENT YIELD OF MUNIS V/S S&P 500 DIVIDEND YIELD³



Why 2025 Returns Were So Asymmetrical

The uneven performance—weak in the first half and very strong in the second—was largely driven by a return to normalcy along the muni yield curve. We entered the year with an inverted, extremely flat curve that offered little compensation for duration or credit risk. The subsequent steepening was uncomfortable in real time, but ultimately necessary.

Curve Normalization is Now Working for Investors

With a more traditionally sloped curve, investors are once again being compensated through roll-down,⁴ and credit spreads are being priced more appropriately rather than artificially compressed. That dynamic was a key contributor to the strong second-half recovery, and we believe sets up a healthier market backdrop heading into 2026.

Supply: Record Issuance, Strong Absorption

New-issue supply finished 2025 right near \$600 billion—a new high-water mark.³ Just as important, the market has absorbed this supply without meaningful dislocation, underscoring strong underlying demand. We expect issuance to remain elevated in 2026, supported by improving fund flows.

Data as of 01/02/2026.

- Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax. This illustration does not constitute tax advice. The information contained herein should not be used as a substitute for advice from your tax advisor. Neither MacKay Municipal Managers nor MacKay Shields LLC advise clients on tax matters. Consult your tax advisor for further information.
- Source: Bloomberg.
- Roll-down refers to the capital gain an investor earns as a bond's yield decreases and its price increases simply by the passage of time, assuming the yield curve stays the same, because investors demand less yield (and pay more) for shorter-term bonds.

Looking Ahead To 2026

We believe the municipal market is well positioned for positive returns in 2026. The absence of major tax-policy uncertainty removes a key overhang from 2025. If economic growth slows further, municipals may potentially serve as a relative safe(r) haven given their lower default history, relative to corporates, and diversification benefits.

As the Fed continues to cut rates, we expect yields on money markets and T-bills to decline, creating a natural reallocation tailwind into municipals. This is where active management matters most—particularly at the front end, where ratios are richer. Notably, tax equivalent yields of munis in the front of the curve can still offer a yield benefit over treasuries.⁵

Bottom Line

After a year of adjustment, the muni market enters 2026 on far more stable footing—with healthier curves, better income, and renewed opportunities for active investors.

Questions from the Field

Q. Was 2025 A Strong Year for Muni Product Creation?

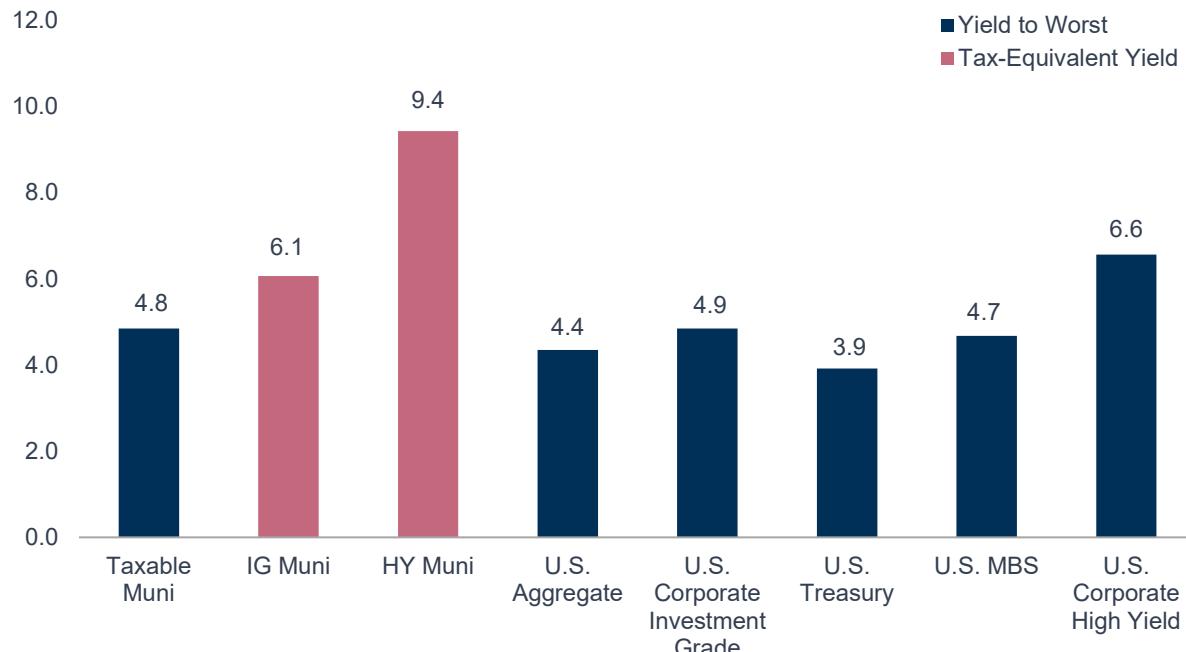
A good way to look at the pace and depth of new product creation for municipals is using the ETF (Exchange traded Funds) market as a litmus test. Currently, there are 157 municipal bond/tax-free focused ETFs. However, of that 157, 35 were created/have an inception date in 2025. That means that almost 23% of all muni ETFs were created in just the past year, alone. Digging deeper into the data, the real story is whether the momentum in product creation is focused around active or passive. Out of the 157 ETFs, 106 are actively managed, according to data from Bloomberg. In 2025, 24 out of the 35 ETFs that were created are actively managed, meaning that almost 70% of all new ETF products are active vs passively managed. This is a large tone shift compared to prior years new ETF launch paces.⁵

5. Source: Bloomberg

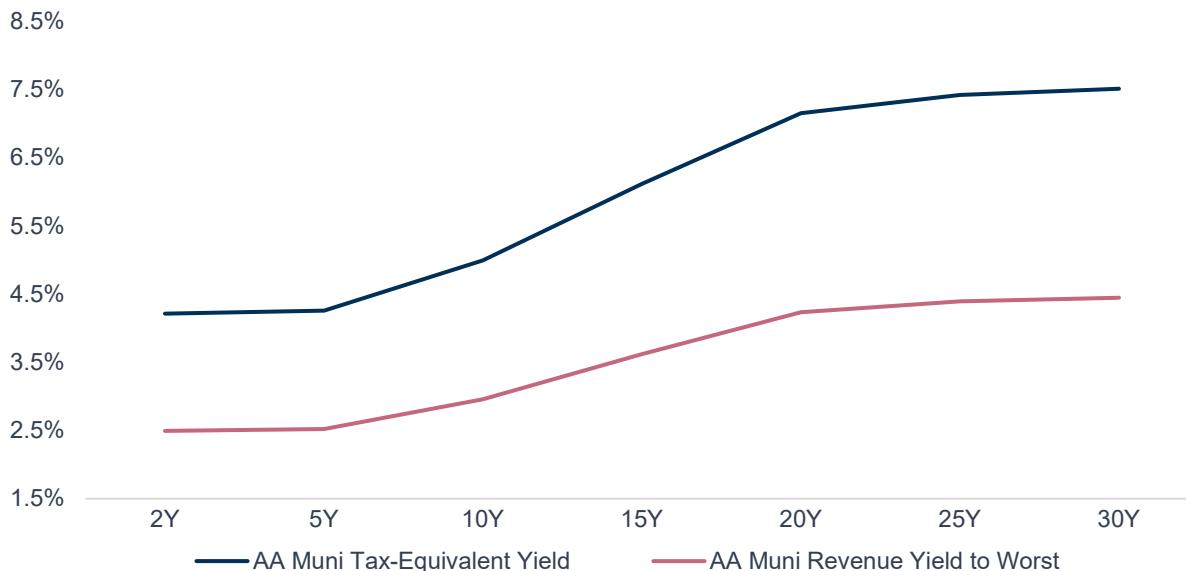
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INDEX YIELDS (in %)⁶



AA MUNI TAX-EQUIVALENT YIELD CURVE⁷



Data as of 01/02/2026.

6. Source: Bloomberg. Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax. Taxable Muni: Bloomberg Taxable Municipal Bond Index; IG Muni: Bloomberg Taxable Municipal Bond Index; HY Muni: Bloomberg High Yield Municipal Bond Index; U.S. Aggregate: Bloomberg U.S. Aggregate Bond Index; U.S. Corporate Investment Grade: Bloomberg U.S. Corporate Investment Grade Index; U.S. Treasury: Bloomberg U.S. Treasury Index; U.S. MBS: Bloomberg U.S. Mortgage-Backed Securities Index; U.S. Corporate High Yield: Bloomberg U.S. Corporate High Yield Index.

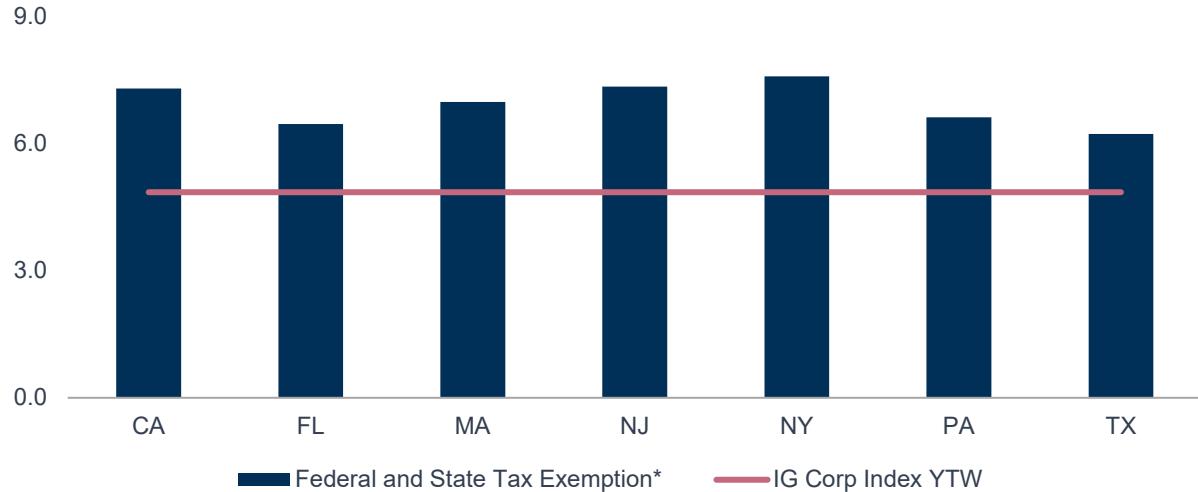
7. Source: Bloomberg. Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax.

Past performance is no guarantee of future results, which will vary. It is not possible to invest directly in an index.

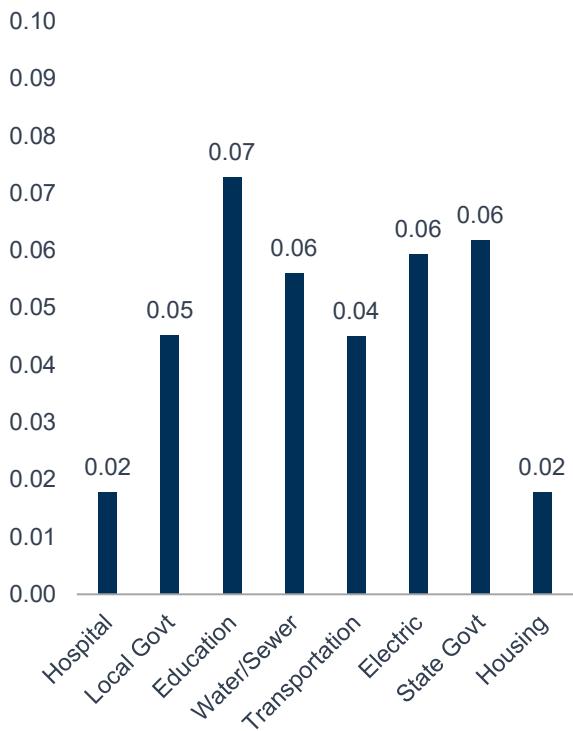
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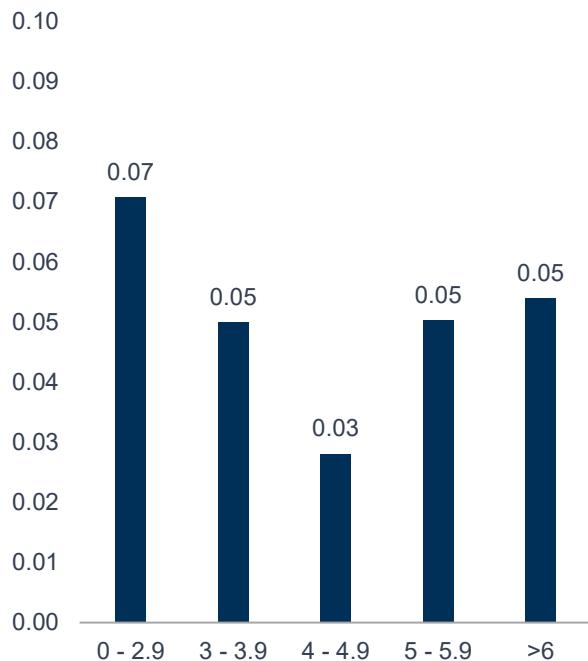
IN-STATE MUNI TAX-EQUIVALENT YTW (in %)⁸



YTD TOTAL RETURNS BY SECTOR (in %)⁹



YTD TOTAL RETURNS BY COUPON (in %)¹⁰



Data as of 01/02/2026.

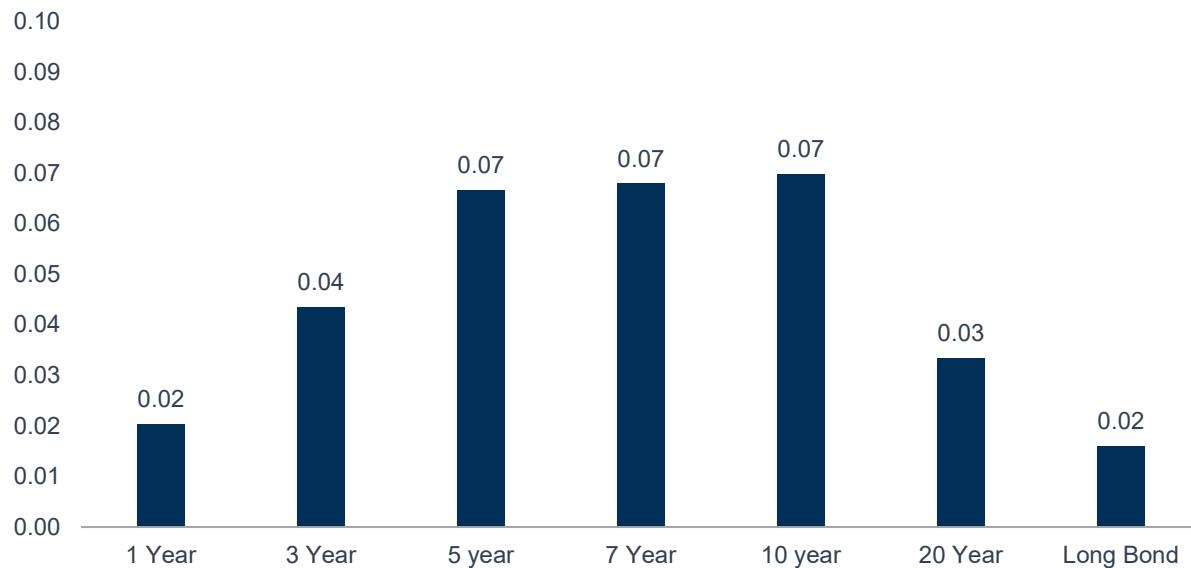
8. Source: Bloomberg. *Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax. Using respective maximum state income tax rate.

9. Source: Bloomberg.

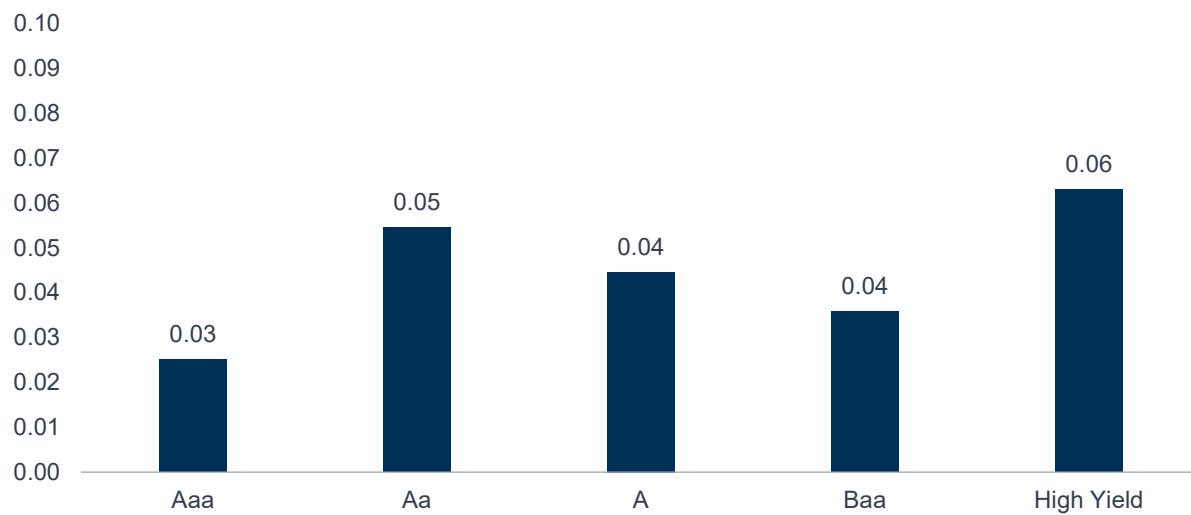
10. Source: Bloomberg.

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YTD TOTAL RETURNS BY MATURITY (in %)¹¹



YTD TOTAL RETURNS BY RATING CATEGORY (in %)¹²



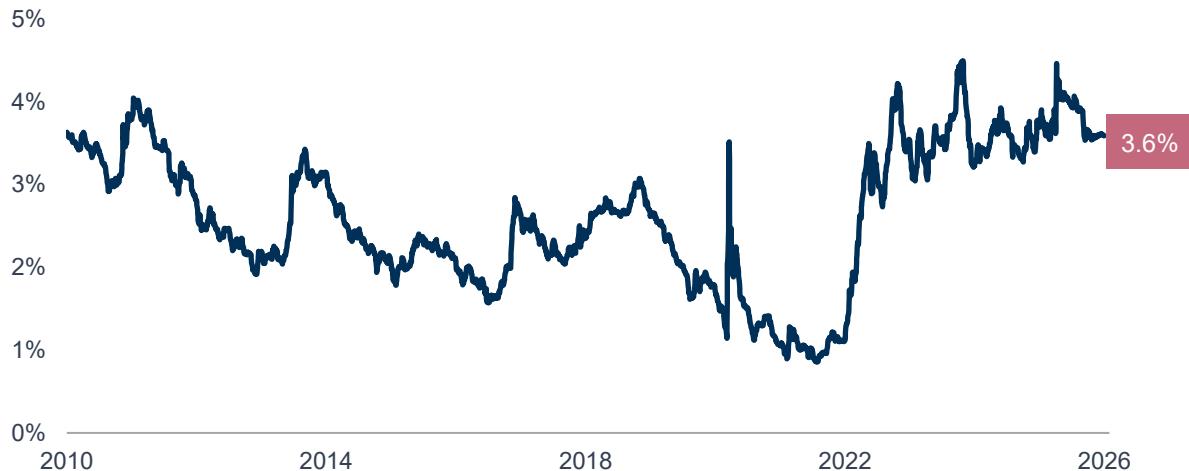
Data as of 01/02/2026.

11. Source: Bloomberg.

12. Source: Bloomberg.

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BLOOMBERG MUNICIPAL YIELD-TO-WORST¹³ (YTW)



MUNI YIELDS

Tenor	01/02/2026	12/26/2025	Change (+/-)
Bloomberg AAA Muni Key Rate Yields¹⁴			
2-year	2.43%	2.44%	-0.01%
5-year	2.38%	2.39%	-0.01%
10-year	2.72%	2.73%	-0.01%
30-year	4.19%	4.19%	0.00%
U.S. Treasury Key Rate Yields¹⁴			
2-year	3.47%	3.46%	0.01%
5-year	3.74%	3.68%	+0.06%
10-year	4.19%	4.14%	+0.05%
30-year	4.86%	4.81%	+0.05%
U.S. Treasury & AAA Muni Curve Slopes¹⁵			
	2s10s	10s30s	2s30s
U.S. Treasury Curve Slope	+72 bps	+67 bps	+139 bps
AAA Muni Curve Slope	+29 bps	+147 bps	+176 bps

Data as of 01/02/2026.

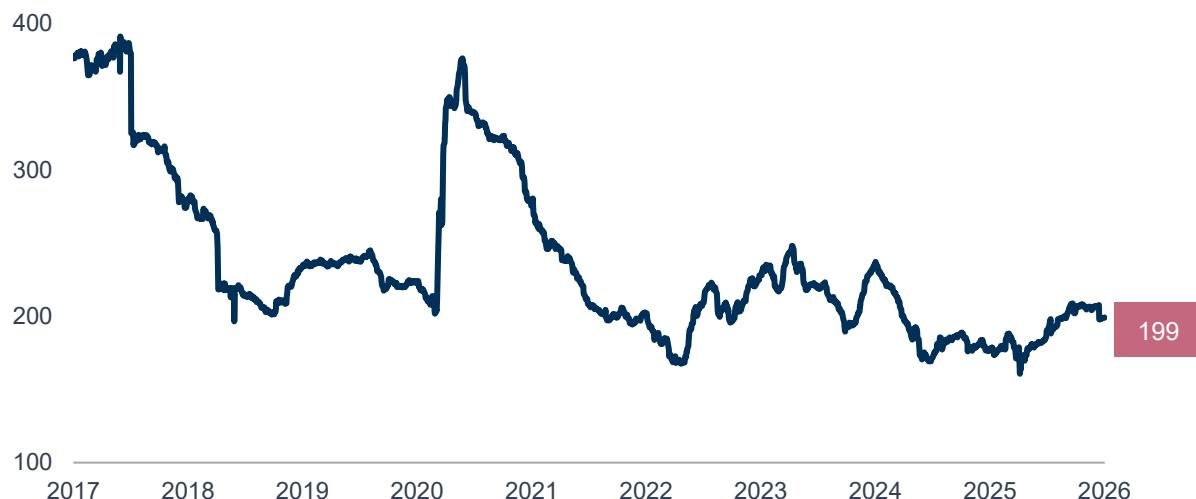
13. Source: Bloomberg. "Post GIFC Average" measures the period from 01/01/2010–01/02/2026.

14. Source: Bloomberg.

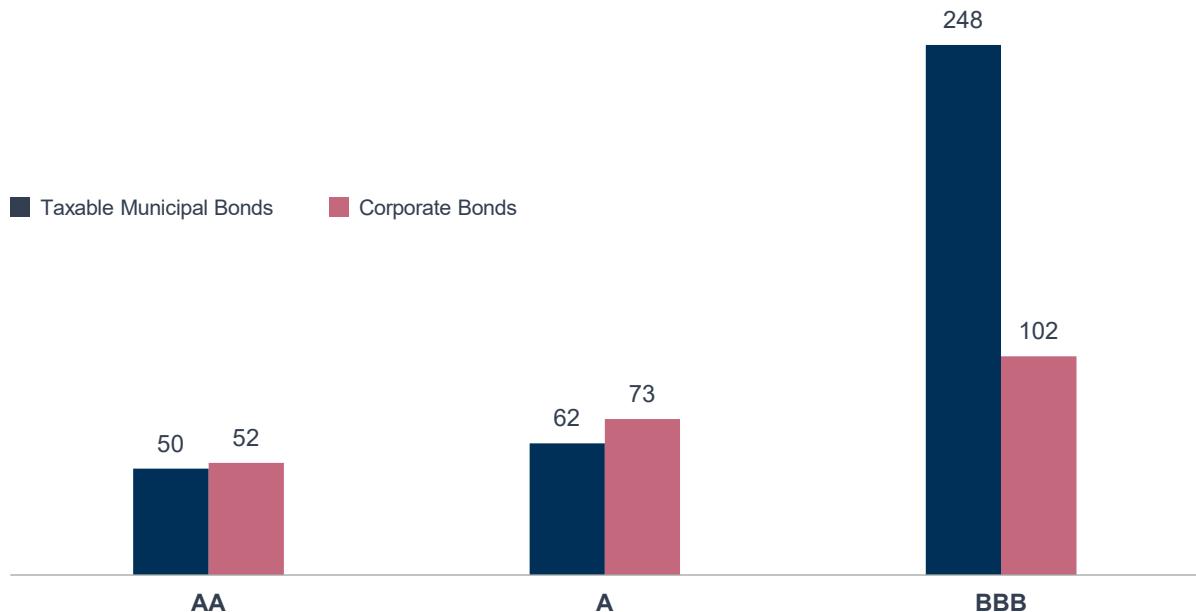
15. Source: Bloomberg. 2s10s—is spread between 10yr and 2yr yield; 10s30s—refers to spread between 30yr and 10yr yield; 2s30s—refers to spread between 30yr and 2yr yield.

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BLOOMBERG MUNICIPAL HIGH YIELD | AAA YIELD DIFFERENTIAL¹⁶



TAXABLE MUNICIPAL AND CORPORATE CREDIT SPREADS¹⁷



16. Data as of 01/02/2026. Source: Bloomberg.

17. Data as of 01/02/2026. Source: Bloomberg. The spread, better known as the option-adjusted spread (OAS) is the measurement of the yield of a fixed income security over that of a risk-free rate of return, which is adjusted to take into account an embedded option.

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LONG TERM FUND FLOWS¹⁸ (USD BILLION)



Data as of 01/02/2026.

18. Source: Bloomberg.

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DEFINITION OF TERMS

Option-Adjusted Spread

The option-adjusted spread (OAS) measures the spread between a bond’s rate and the risk-free rate, while adjusting for any embedded options like callables or mortgage-backed securities.

Standard Deviation

Standard deviation is a statistical measurement that looks at how far discrete points in a dataset are dispersed from the mean of that set. It is calculated as the square root of the variance.

Tax Equivalent Yield

The tax-equivalent yield is the return a taxable bond needs to equal the yield on a comparable tax-exempt municipal bond. Investors use this calculation to compare the returns between a tax-free investment and a taxable alternative.

Volatility

Volatility is a measurement of how varied the returns of a given security or market index are over time. It is often measured from either the standard deviation or variance between those returns. In most cases, the higher the volatility, the riskier the security.

Yield to Worst

Yield to worst is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract. It is a type of yield that is referenced when a bond has provisions that would allow the issuer to close it out before it matures. YTW helps investors manage risks and ensure that specific income requirements will still be met even in the worst scenarios.

INDEX DESCRIPTIONS

Bloomberg U.S. Taxable Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term taxable bond market. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies if all three rate the bond: Moody’s, S&P, Fitch. If only two of the three agencies rate the security, the lower rating is used to determine index eligibility. If only one of the three agencies rates a security, the rating must be investment grade. They must have an outstanding par value of at least \$7 million and be issued as part of a transaction of at least \$75 million. The bonds must be fixed rate and must be at least one year from their maturity date. Remarketed issues (unless converted to fixed rate), bonds with floating rates, and derivatives, are excluded from the benchmark.

Bloomberg Municipal AMT index refers to a specific Bloomberg municipal bond index that includes bonds subject to the Alternative Minimum Tax (AMT). Unlike most municipal bond indices, which exclude AMT-subject securities, these indices contain bonds that typically offer higher yields to individuals who are subject to the AMT.

Muni IG ex. AMT and ex Territories Index is the Bloomberg Municipal Bond Index excluding AMT and U.S. Territory exposure.

Bloomberg Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following agencies: Moody’s, S&P, Fitch. If only two of the three agencies rate the security, the lower rating is used to determine index eligibility. If only one of the three agencies rates a security, the rating must be investment-grade. They must have an outstanding par value of at least \$7 million and be issued as part of a transaction of at least \$75 million. The bonds must be fixed rate, have a date-date after December 31, 1990, and must be at least one year from their maturity date. Remarketed issues, taxable municipal bonds, bonds with floating rates, and derivatives, are excluded from the benchmark. The index has four main sectors: general obligation bonds, revenue bonds, insured bonds (including all insured bonds with a Aaa/AAA rating), and pre-refunded bonds. Most of the index has historical data to January 1980. In addition, sub-indices have been created based on maturity, state, sector, quality, and revenue source, with inception dates later than January 1980.

Bloomberg 5-Year Muni Index is a capitalization weighted bond index created by Bloomberg intended to be representative of major municipal bonds of all quality ratings with an average maturity of approximately five years.

Bloomberg Municipal 1-10 Year Blend 1-12 Year Index measures the performance of short and intermediate components of the Municipal Bond Index — an unmanaged, market value-weighted index which covers the U.S. investment grade, tax-exempt bond market.

Bloomberg Municipal Long Bond 22+ Index (often referred to as the Bloomberg Long-Term Municipal Bond Index) tracks the performance of long-term, tax-exempt U.S. municipal bonds with maturities of 22 years or longer. This index serves as a benchmark for high-quality municipal debt and covers various sectors, including general obligation, revenue, insured, and pre-refunded bonds.

INDEX DESCRIPTIONS (continued)

Bloomberg High Yield Municipal Bond Index is a flagship measure of the U.S. municipal tax-exempt non-investment grade bond market. Included in the index are securities from all 50 U.S. States and four other qualifying regions (Washington DC, Puerto Rico, Guam, and the Virgin Islands). The index includes state and local general obligation bonds and revenue bonds. All bonds in the Municipal High Yield Bond Index are tax exempt and hence are not eligible for other indices that include taxable high yield bonds, such as the U.S. High Yield Index and EM USD Aggregate Index.

Bloomberg U.S. Aggregate Bond Index measures the performance of investment grade, U.S. dollar-denominated, fixed rate taxable bond market, including Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS, and CMBS. It rolls up into other flagship indices, such as the multi-currency Global Aggregate Index and the U.S. Universal Index, which includes high yield and emerging markets debt.

Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by U.S. and non-US industrial, utility, and financial issuers. The index is a component of the U.S. Credit and U.S. Aggregate Indices, and provided the necessary inclusion rules are met, U.S. Corporate Index securities also contribute to the multi-currency Global Aggregate Index. The index includes securities with remaining maturity of at least one year.

Bloomberg U.S. Treasury Index measures the performance of public obligations of the U.S. Treasury, including securities that roll up to the U.S. Aggregate, U.S. Universal, and Global Aggregate Indices

Bloomberg Securitized Bond Index The Bloomberg U.S. Securitized: MBS, ABS, and CMBS Index tracks all USD-denominated, investment grade, securitized issues within the "Parent Index". MBS must have a weighted average maturity of at least one year. CMBS and ABS must have a remaining average life of at least one year.

Bloomberg U.S. Municipal Bond Index Total Return Index Value
Unhedged Index covers the USD-denominated long-term tax-exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and pre-refunded bonds

Bloomberg U.S. Aggregate Total Return Value Unhedged Index
(LBUSTRUU:IND) is a benchmark that measures the performance of the U.S. investment-grade, fixed-rate, taxable bond market, excluding any currency hedging. It tracks a broad universe of U.S. dollar-denominated securities, including U.S. Treasuries, government-related debt, corporate bonds, mortgage-backed securities (MBS), and asset-backed securities (ABS).

Bloomberg U.S. Treasury Total Return Unhedged Index measures U.S. dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury.

Bloomberg U.S. Mortgage-Backed Securities Index is formed by grouping the universe of individual TBA-deliverable MBS pools into pool cohorts and then applying the index inclusion rules at the cohort level. Each cohort is a representation of its mapped individual pools and contributes their total amount outstanding to the U.S. MBS Index.

Bloomberg U.S. Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.

Bloomberg Global Aggregate Bond Index is a flagship measure of global investment grade debt from twenty-seven local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers.

