

# Municipal Market Weekly Update

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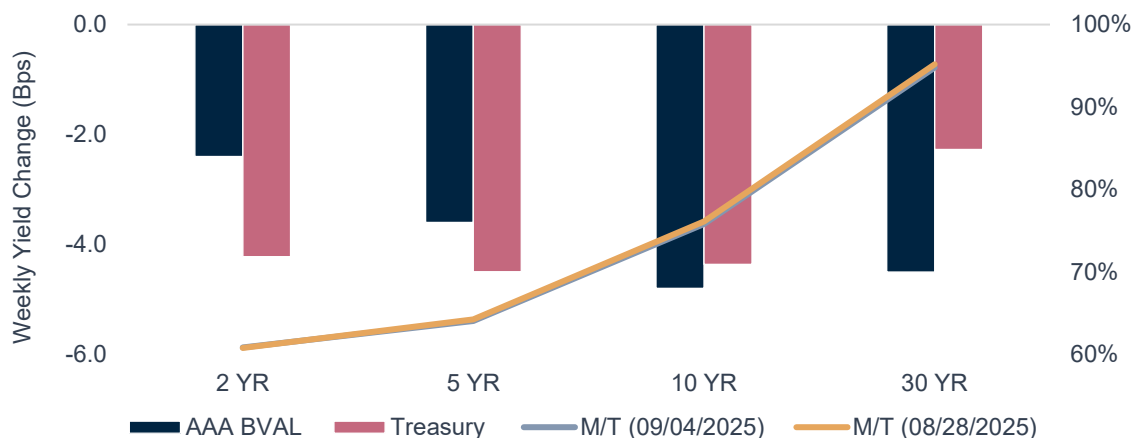
## Munis Credits Emerge as Potential Must Start Defense for Portfolios

- Munis hope to buck September trends
- Lack of correlation puts Munis front and center
- Defensive allocations in portfolios are key

### Relative Performance

September has been historically (and even technically) unsupportive for the muni market, particularly in terms of reinvestment flows. Amid elevated issuance, the market needs all the help it can get from new money fund flows—and robust reinvestment capital plays a key role. Yet, September brings just \$34 billion in principal and interest back to investors, nearly half the volume seen in each of June, July, and August. Historically, returns in September have been weak. The hope is that any Fed action is received positively by the rates market, helping offset softer technicals. The focus of investors should still be capitalizing on value and higher yields, while the market is offering the opportunity to do so.

### MUNIS LAGGED TREASURIES IN THE FRONT AND INTERMEDIATE ENDS, BUT OUTPERFORMED IN THE LONG END<sup>1</sup>



1. Data as of September 4, 2025. 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.

## MUNI MONTHLY INDEX PERFORMANCE<sup>2</sup>

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2025	0.50	0.99	-1.69	-0.81	0.06	0.62	-0.20	0.87	0.32			
2024	-0.51	0.13	0.00	-1.24	-0.29	1.53	0.91	0.79	0.99	-1.46	1.73	-1.46
2023	2.87	-2.26	2.22	-0.23	-0.87	1.00	0.40	-1.44	-2.93	-0.85	6.35	2.32
2022	-2.74	-0.36	-3.24	-2.77	1.49	-1.64	2.64	-2.19	-3.84	-0.83	4.68	0.29
2021	0.64	-1.59	0.62	0.84	0.30	0.27	0.83	-0.37	-0.72	-0.29	0.85	0.16
2020	1.80	1.29	-3.63	-1.26	3.18	0.82	1.68	-0.47	0.02	-0.30	1.51	0.61
2019	0.76	0.54	1.58	0.38	1.38	0.37	0.81	1.58	-0.80	0.18	0.25	0.31
2018	-1.18	-0.30	0.37	-0.36	1.15	0.09	0.24	0.26	-0.65	-0.62	1.11	1.20
2017	0.66	0.69	0.22	0.73	1.59	-0.36	0.81	0.76	-0.51	0.24	-0.54	1.05
2016	1.19	0.16	0.32	0.74	0.27	1.59	0.06	0.13	-0.50	-1.05	-3.73	1.17
2015	1.77	-1.03	0.29	-0.52	-0.28	-0.09	0.72	0.20	0.72	0.40	0.40	0.70

-3.84  6.35

2. Data as of September 4, 2025. Source: Bloomberg. Bloomberg Municipal Bond Total Return Index

While the reader's eye may be drawn to negative trends for October, it is far too early, and there is still much uncertainty surrounding the path from the Fed, to lean into any narrative regarding weaker performance into the fall. Our feeling is that weakness in the economy will lead to a rotation to haven assets like municipals, a theme that carries throughout this report.

Positively, municipals are off to a decent start this month, with the Bloomberg Municipal Index posting a 32bps gain (Bloomberg), reflecting the broader rates rally. Over the past week, AAA muni performance versus Treasuries was mixed across the curve—slight underperformance in the front end, but stronger total returns from 10 years out. This is welcome for a market that's struggled with returns and investor fatigue much of the year. Still, more context is needed. While longer-duration munis have faced losses, they've actually outperformed shorter tenors recently. Since July 29, the Bloomberg Long Muni Index has outpaced the Bloomberg 5-Year Muni Index by nearly 80bps—a trend we've been watching for since tax reform.

## Market Technicals

The Federal Open Market Committee (FOMC) has consistently emphasized its independence and data-driven approach to monetary policy. Yet, with a rate cut this month appearing inevitable, it raises the question: which economic indicators are troubling the Fed, and how severe are those concerns?

While the likelihood of a cut is priced in, the magnitude and pace of future moves remain uncertain. What seems broadly accepted is that Fed action signals meaningful concern about the economy's health—and an intent to counterbalance it.

Recent client conversations have centered on economic risks and their potential impact on fixed income markets. While we don't have a crystal ball, we do see intuitive opportunities in portfolio construction that could add defensiveness.

We're focused on identifying areas in portfolios that may be exposed to frothy or overvalued segments. While muni spreads have been tight this year, they're modest compared to the historically rich valuations in investment-grade and high-yield corporates. If economic conditions deteriorate, we expect these sectors to be the first to show stress—prompting investors to seek alternative safe havens. We believe munis are well-positioned to fill that role.

One key advantage is munis' low correlation with other fixed income sectors like Treasuries, corporates, global aggregates, and securitized credit. When those markets zig, munis tend to zag—introducing a valuable counterweight in core bond allocations.

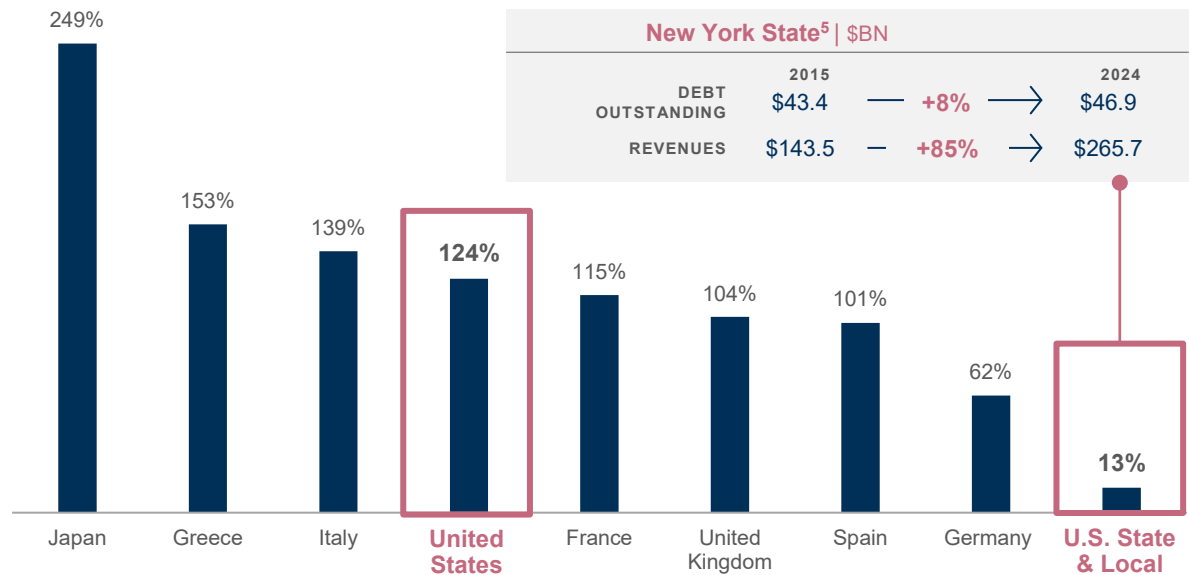
In our view, the case for municipal credit strengthens when you look deeper within the asset class. While overall credit quality is strong, the specifics are compelling: as of August 2025, 14 U.S. states hold AAA ratings from Fitch, compared to AA+ for the federal government. States and local governments also maintain a much lower debt-to-GDP ratio—13% versus 124%—highlighting their fiscal discipline relative to other areas of the fixed income landscape.

### MUNIS LACK CORRELATION<sup>3</sup>

	Bloomberg U.S. Treasury Index	Bloomberg U.S. Corporate Index	Bloomberg Municipal Bond Index	Bloomberg Global Aggregate Index	Bloomberg Securitized Index	Bloomberg Mortgage-Backed Index
Bloomberg U.S. Treasury Index	1.000	0.940	0.381	0.760	0.968	0.965
Bloomberg U.S. Corporate Index	0.040	1.000	0.379	0.730	0.043	0.043
Bloomberg Municipal Bond Index	0.381	0.379	1.000	0.375	0.343	0.338
Bloomberg Global Aggregate Index	0.760	0.730	0.375	1.000	0.747	0.745
Bloomberg Securitized Index	0.968	0.943	0.343	0.747	1.000	1.000
Bloomberg Mortgage-Backed Index	0.965	0.943	0.338	0.745	1.000	1.000

3. Data as of September 4, 2025. Source: Bloomberg.

## MUNIS HIGHLY UNLEVERED<sup>4</sup>



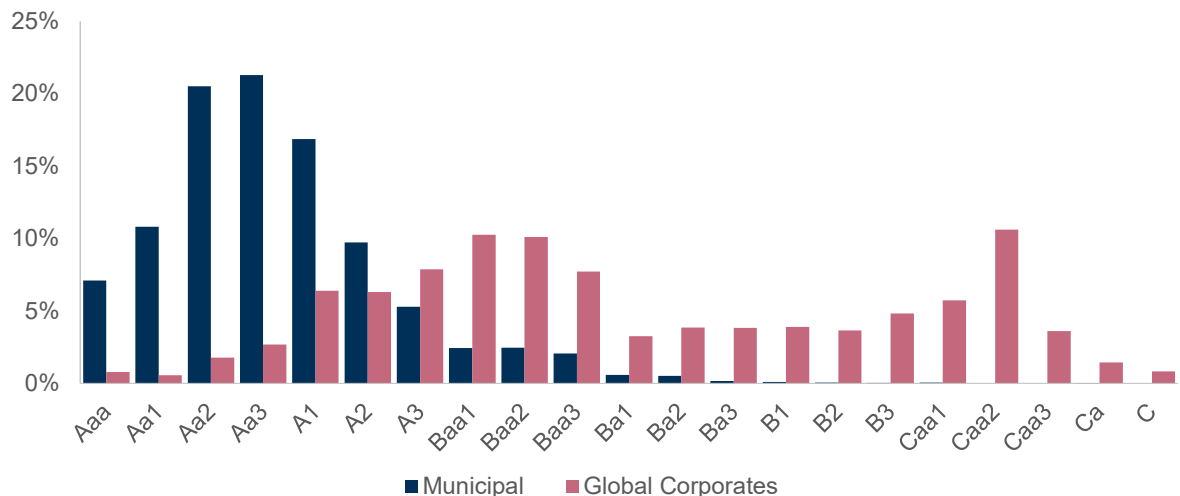
4. Source: Bloomberg. U.S. State & Local: FRED's Economic Data Q4 2024.

5. Does not include SUNY/CUNY revenue bonds or revenues. Sovereign Data: International Monetary Fund, February 2025 ([https://www.imf.org/external/datamapper/GGXWDG\\_NGDP@WEO/ITA?zoom=ITA&highlight=ITA](https://www.imf.org/external/datamapper/GGXWDG_NGDP@WEO/ITA?zoom=ITA&highlight=ITA))

As the economy slows, municipal credit quality—especially compared to corporates—we believe will continue to attract cross-over buyers. This dynamic could possibly position munis as a defensive allocation with upside potential as the Fed embarks on their latest path of monetary policy implementation.

Level debt service, more predictable cash flows vs. corporate credits and revenue streams which are backed by taxes and/or essential service projects translates to the higher credit quality and low ratings volatility for the asset class, all keys for investors looking for a diversified and defensive allocation to their fixed income mix.

## MUNI CREDIT QUALITY STANDS OUT<sup>6</sup>



6. Data as of September 4, 2025. Source: Moody's.

## Questions from the Field

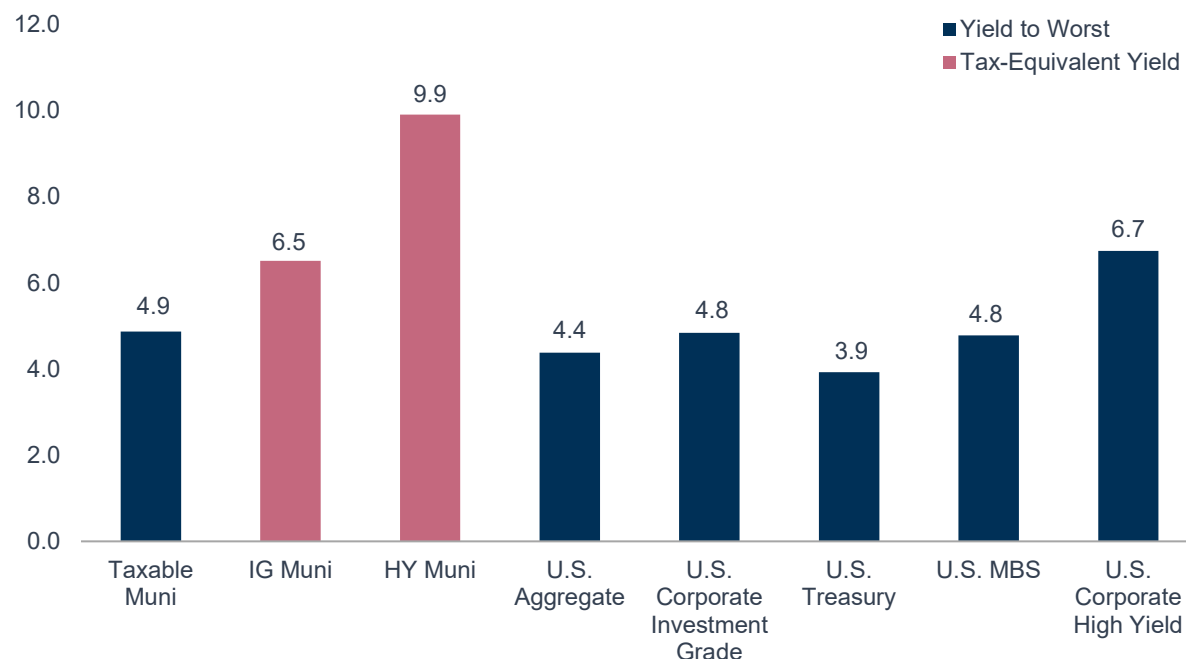
### Q. Should we be rotating into longer-duration paper now, or stay short?

Longer dated Munis have been pressured by tax uncertainty and weaker institutional demand for much of this year, but recent activity from banks and insurers is definitively creating a tailwind. This “on sale” period for tax-exempts has allowed savvy active managers to improve book yield and overall credit quality across portfolios.

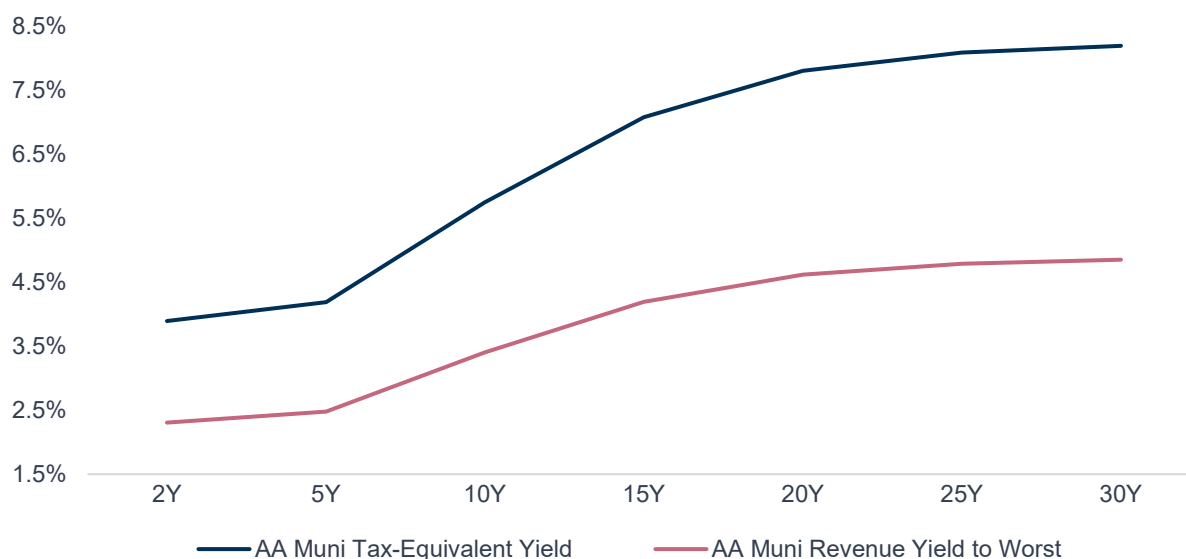
Positively, Longer-duration munis have started to outperform (see above), and if you believe rates have peaked or are near it, extending duration could make sense. This is especially true if you are a long-term investor and are less focused on total return versus increasing yield at increasingly lower dollar prices. That said, creating a barbelled approach—mixing short and long exposures—can certainly help manage any returns volatility, especially with the Fed becoming active in the rates market in short order.

For those still concerned about the volatility in longer duration, we would point to the re-emergence of cross over buyers, now that much of the uncertainty surrounding tax reform extension has subsided. The additional ballast from institutional support on the long end of the municipal curve can and will provide downside support if the curve steepens on the back of upcoming rate cuts.

## INDEX YIELDS (in %)<sup>7</sup>



## AA MUNI TAX-EQUIVALENT YIELD CURVE<sup>8</sup>



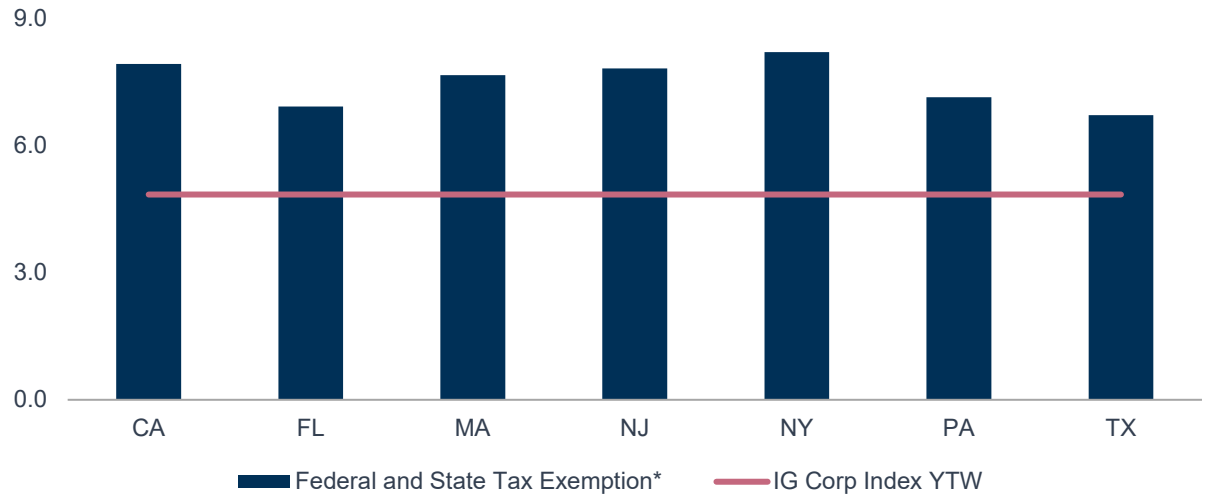
Data as of 09/05/2025.

7. 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.

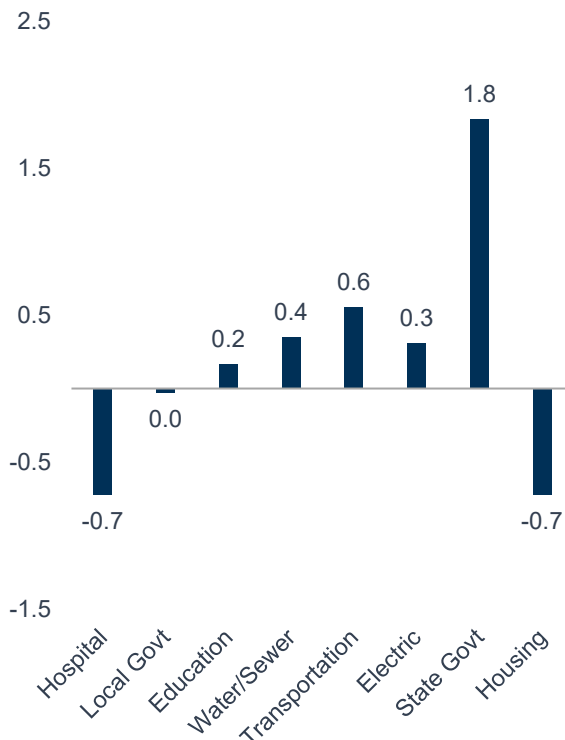
8. Source: Bloomberg. Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax.

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

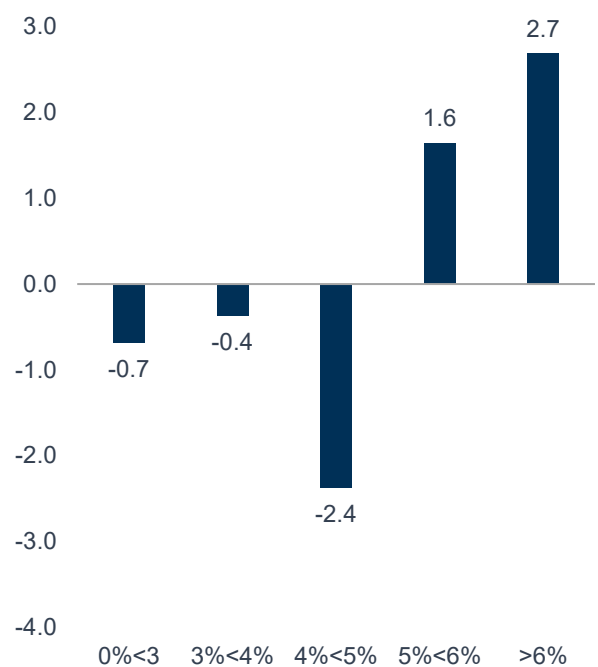
## IN-STATE MUNI TAX-EQUIVALENT YTW (in %)<sup>9</sup>



## YTD TOTAL RETURNS BY SECTOR (in %)<sup>10</sup>



## YTD TOTAL RETURNS BY COUPON (in %)<sup>11</sup>



Data as of 09/05/2025.

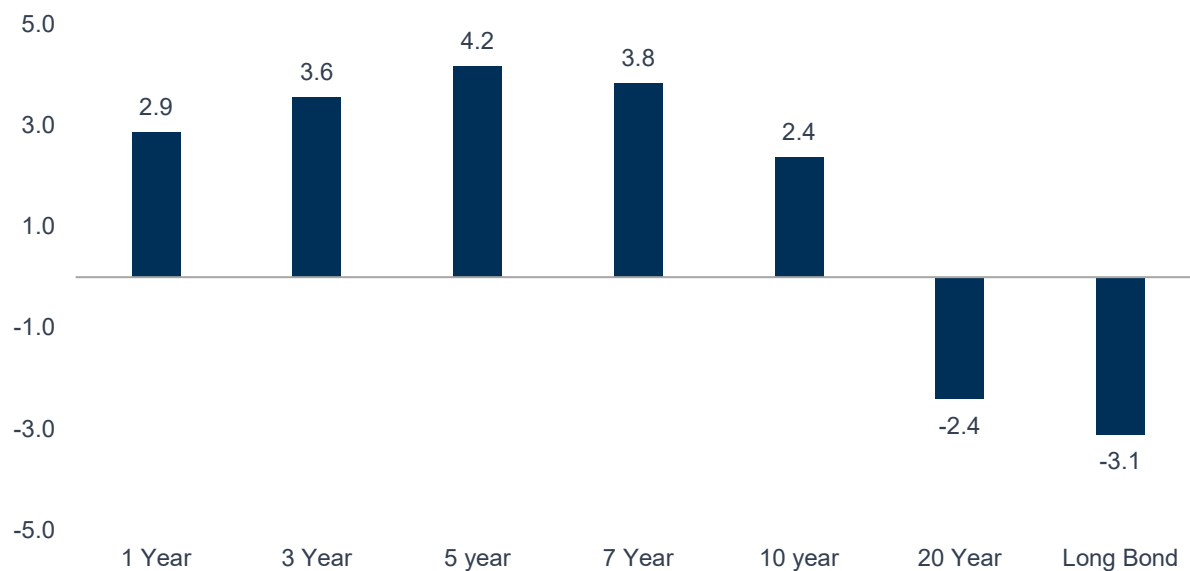
9. Source: Bloomberg. \*Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax. Using respective maximum state income tax rate.

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

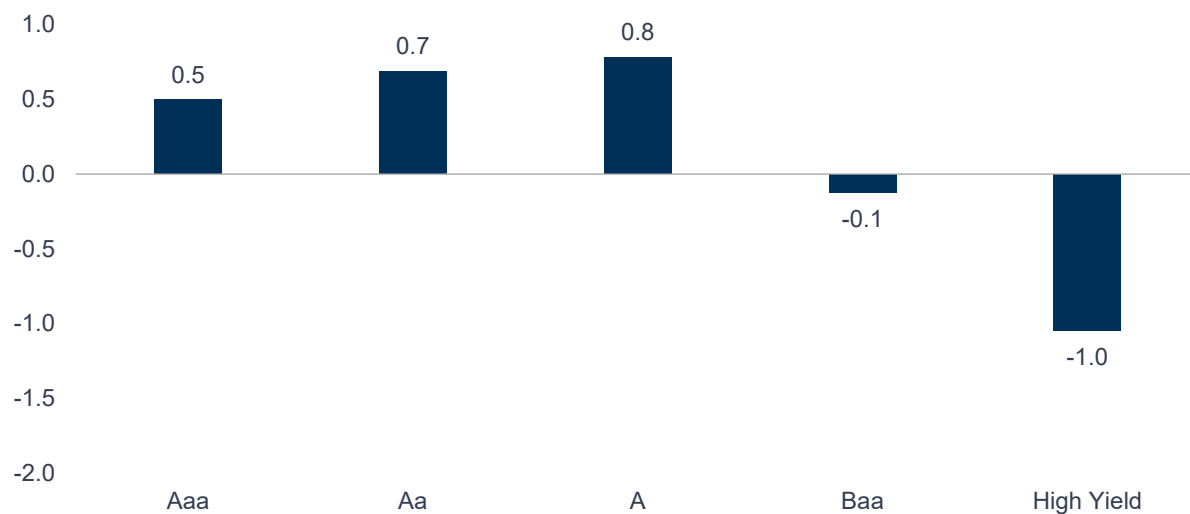
11. Source: Bloomberg. Using 40.8% federal tax rate, including 3.8% Net Investment Income Tax.

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## YTD TOTAL RETURNS BY MATURITY (in %)<sup>12</sup>



## YTD TOTAL RETURNS BY RATING CATEGORY (in %)<sup>13</sup>



Data as of 09/05/2025.

12. Source: Bloomberg.

13. Source: Bloomberg.

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## BLOOMBERG MUNICIPAL YIELD-TO-WORST<sup>14</sup> (YTW)



## MUNI YIELDS

Tenor	08/29/2025	09/05/2025	Change (+/-)
<b>Bloomberg AAA Muni Key Rate Yields<sup>15</sup></b>			
2-year	2.21%	2.15%	-0.06%
5-year	2.37%	2.27%	-0.10%
10-year	3.20%	3.07%	-0.13%
30-year	4.64%	4.49%	-0.15%
<b>U.S. Treasury Key Rate Yields<sup>15</sup></b>			
2-year	3.59%	3.51%	-0.08%
5-year	3.68%	3.59%	-0.09%
10-year	4.23%	4.10%	-0.13%
30-year	4.92%	4.78%	-0.14%
<b>U.S. Treasury &amp; AAA Muni Curve Slopes<sup>16</sup></b>			
	<b>2s10s</b>	<b>10s30s</b>	<b>2s30s</b>
U.S. Treasury Curve Slope	+59 bps	+68 bps	+127 bps
AAA Muni Curve Slope	+92 bps	+142 bps	+234 bps

Data as of 09/05/2025.

14. Source: Bloomberg. "Post GIFC Average" measures the period from 01/01/2010–09/05/2025.

15. Source: Bloomberg.

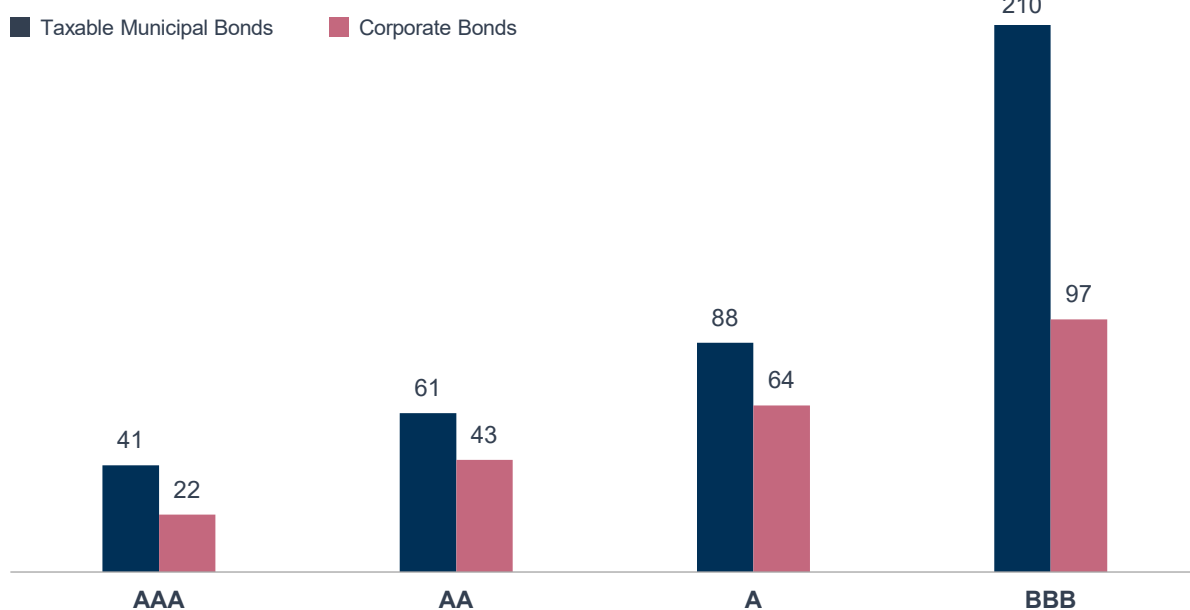
16. Source: Bloomberg. 2s10s—is spread between 10yr and 2yr yield; 10s30s—refers to spread between 30yr and 10yr yield; 2s30s—refers to spread between 30yr and 2yr yield.

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## BLOOMBERG MUNICIPAL HIGH YIELD | AAA YIELD DIFFERENTIAL<sup>17</sup>



## TAXABLE MUNICIPAL AND CORPORATE CREDIT SPREADS<sup>18</sup>



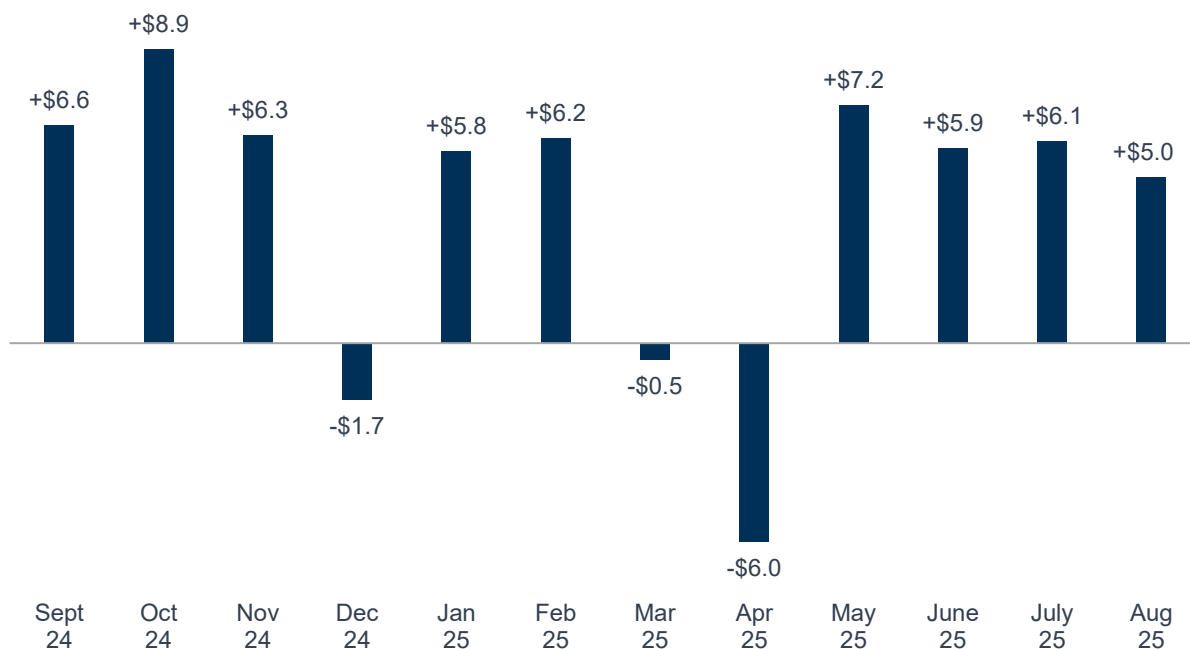
Data as of 09/05/2025.

17. Source: Bloomberg.

18. Source: ICE Data. 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 FLOWS<sup>19</sup> (USD BILLION)



Data as of 09/05/2025.

19. Source: Investment Company Institute (ICI). <http://www.ici.org>.

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## INDEX DESCRIPTIONS

**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 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 Bond Index** 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 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 US and non-US industrial, utility, and financial issuers. The index is a component of the US Credit and US Aggregate Indices, and provided the necessary inclusion rules are met, US 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 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.

## INDEX DESCRIPTIONS (continued)

**Bloomberg Global Aggregate Bond Index** The Bloomberg Global Aggregate 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.

**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.



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