

Municipal Bonds

Light Supply Meets Steady Demand

Strong summer technicals should provide support.

Both tax-exempt and taxable municipal bonds continue to experience supportive market conditions. Reinvestment demand from large principal and coupon payments provides a tailwind to tax exempt valuations. Taxable spreads have inched tighter on the back of lackluster supply. Credit quality is plateauing as tax receipts flatten while certain states continue to enact tax cuts.

Sector Commentary

- Tax exempts continue to perform well despite the headwinds of heavy issuance and volatile Treasury rates. Tax exempt/Treasury yield ratios are essentially unchanged over the last 12 months, with 5/10/30-year AAA ratios hovering around 67 percent, 68 percent, and 86 percent, respectively.
- We are in the midst of the two biggest months of the year for principal and interest (P&I) payments, averaging \$64 billion per month during July and August. Heavy reinvestment demand from P&I flows should provide a strong technical tailwind for the summer months.
- Taxable issuance remains light, down 16 percent year over year to just \$21 billion, while demand from institutions remains steady.

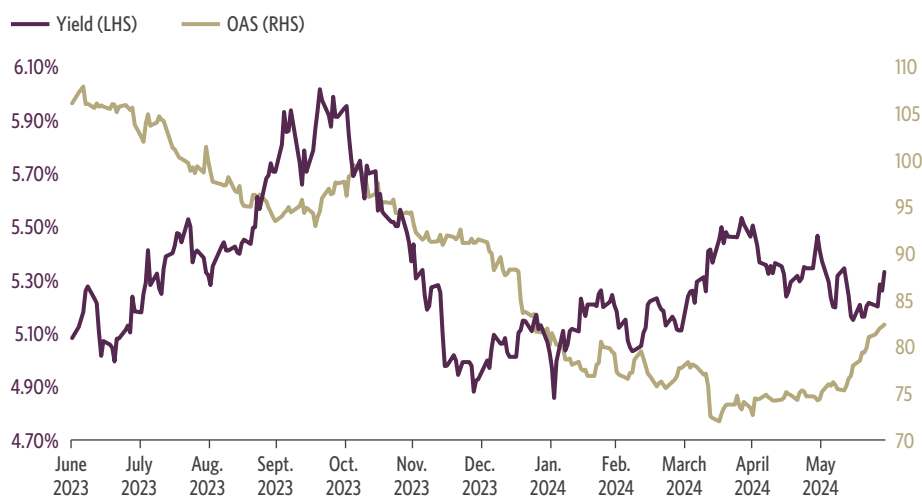
Investment Themes

- At current ratios and spreads, we prefer taxables over tax exempts for institutional investors due to their low tax rates.
- For retail investors, the taxable equivalent yields on tax exempts remain attractive, and the strong summer technicals should provide support at current valuation levels into late third quarter.
- Despite flat to declining tax receipts for most states, some are still enacting cuts to tax rates. Since 2021, 26 states have reduced income tax rates, so we think tax receipts will have a difficult time outperforming overall economic growth. Given the concurrent drawdown of stimulus funds, we are keeping an eye on how states budget for the upcoming fiscal year 2025 and whether they are using realistic assumptions for revenue and expenditure growth.

By Allen Li and Michael Park

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Taxable Muni Spreads Have Inched Tighter, But Remain Attractive



Source: Guggenheim Investments, Bloomberg. Data as of 6.30.2024.

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