

## U.S. Municipal Bond Market

# Municipal Yields Remain Generationally Enticing Amongst the Latest Flight to Quality, Future Attractive Investment Opportunities May Occur But Will Be Less Frequent

- Investor conviction remains elusive. We reiterate that municipal bonds have and should continue to be included in the flight-to-quality activity during future instances of investor uncertainty.
- The investment backdrop changed again over this past weekend when attacks in the Middle East increased geopolitical tensions.
- We believe, especially now, that municipal yields are at generationally enticing levels.

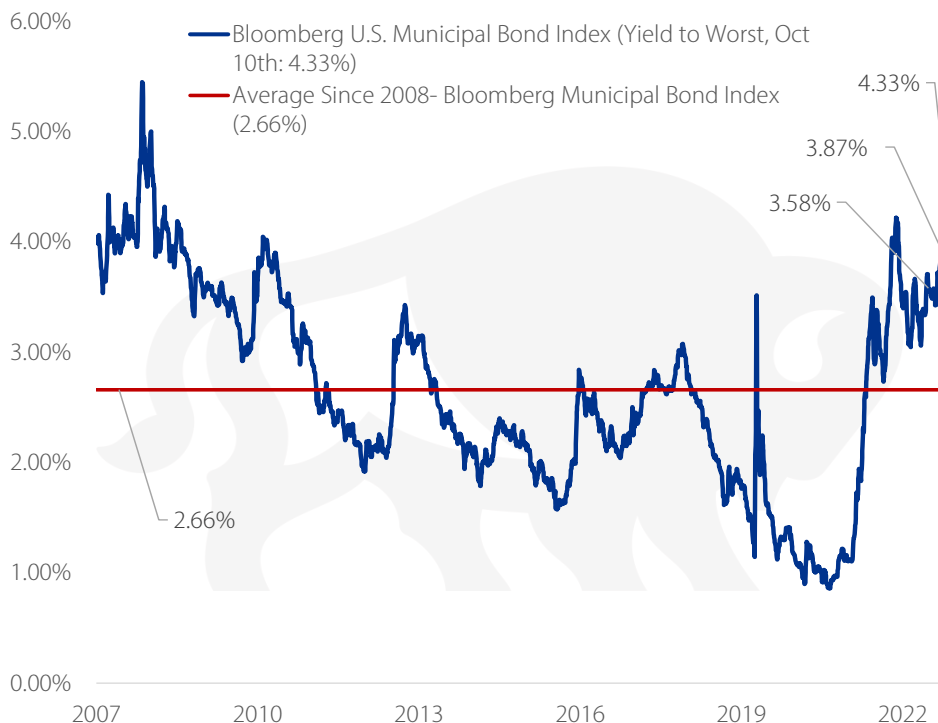
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## Municipals Participating in the Flight-to-Quality has been Customary to the Investment Backdrop Over the Last Two Years

Investor conviction remains elusive. Conviction for municipal bond investing should be stronger considering the market dynamic and very strong credit quality (and Golden Age of Public Finance). What we are seeing instead is that some investment dollars have flowed toward short term options containing variable rates in response to uncertainty and volatility. We have seen investment dollars flow out of municipal mutual funds in eight of the last ten weeks. We understand massively impactful developments have occurred in the last 24 or so months and have been challenging for investors to navigate.

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## Municipal Yields are Even More Enticing Now, Compared to This Summer



Source: Bloomberg and HilltopSecurities.

Please see disclosure starting on page 3.

- The U.S. Federal Reserve has crusaded against inflation by raising its overnight funds target rate to 5.25% and 5.50%.
- Russian invaded Ukraine in February 2022.
- Regional banking sector stress in March 2023.

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The investment backdrop changed again over this past weekend when attacks in the Middle East increased geopolitical tensions. The potential for additional military activity in the region hangs over the data dependent Federal Reserve now, and it is possible the Fed continues its pause during its November and possibly even during its December 2023 meeting(s).

Municipal bond investments, especially those of the highest credit quality, participated in the flight-to-quality trading activity in the wake of the events (noted above) that caused the highest level of market uncertainty over the last almost two years. After the military attacks and the banking sector stress especially we saw and agree investors should be viewing municipals as a primary fixed-income option.

## Generationally Enticing Municipal Bond Yields

To begin the summer we indicated in our report Municipal Yields are Historically Attractive - Our View on How to Finish Out the Second Quarter of 2023 that investors should be taking notice of the U.S. municipal bond market opening. The Bloomberg U.S. Municipal Bond Index yield was at a 3.58% at the time. More recently, just before the Federal Reserve's September 2023 meeting we noted that municipal yields were peaking to end the 3rd quarter of 2023 in our market update titled Appealing Municipal Market Indicators and Strong Economic Data is Fueling the Golden Age of Municipals Despite Near-Term Uncertainty. The Bloomberg U.S. Municipal Bond Index yield was at a 3.87% then.

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Municipal yields quickly increased by about 40 basis points after the Fed announced it was pausing to reassess the economic situation. Municipal yields fell slightly to begin this week, however the fact that market forces were able to increase yields without the Fed acting in September is being heavily considered by some market observers as a signal that future Federal Reserve action could be limited. The Bloomberg U.S. Municipal Bond Index yield was at a 4.33% as of October 10th.

Fed watching remains the primary focus of most investment markets, including the municipal market. We continue to believe that municipal investors should not try to time the market. We agree with those who have been saying and writing that fixed income generally is at or near generationally attractive levels. We believe, especially now, that municipal yields are at generationally enticing levels. The Federal Reserve is now less likely to continue its crusade higher now compared to last week. Future investment opportunities as attractive as this for municipal investors may occur, but the opportunities will be less frequent.

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## Recent HilltopSecurities Municipal Commentary

- Appealing Municipal Market Indicators and Strong Economic Data is Fueling the Golden Age of Municipals Despite Near-Term Uncertainty, Sept. 19, 2023
- Transformative Technology and its Economic Impact, Sept. 6, 2023
- Save the Tax-Exemption, A Call to Action for U.S. Public Finance, August 17, 2023
- First Half Public Finance Primary Issuance Down 20%, Foreshadows Potential Scarcity of Municipal Investment Options, July 5, 2023
- Municipal Yields are Historically Attractive – Our View on How to Finish Out the Second Quarter of 2023, June 8, 2023

Readers may view all of the HilltopSecurities Municipal Commentary [here](#).

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