U.S. Municipal Bond Market

Relative Value Remains Attractive as Economic Outlook Dims and Political Risks Rise

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- Municipal yields declined again last week, reinforcing the view that the window for an attractive entry point is narrowing. ***The ship is leaving the port,*** and investors should stay alert to avoid missing this opportunity.
- ***Relative value remains compelling***, with Municipal-to-Treasury ratios still elevated. Cross-over buyers are still stepping in, and timing is critical as these favorable conditions may not last.
- Weakening GDP and jobs data, rising expectations for rate cuts, and increasing concerns about the independence of key economic institutions are creating a sense of urgency. These developments could put pressure on financial markets and raise doubts about the reliability of the data investors depend on.

Yields Drop—Opportunity Is Still Here, But Fading

Municipal and many broader fixed income yields declined again last week, reinforcing what we've been emphasizing for some time: ***the ship is leaving the port***. This analogy continues to resonate because it captures the growing importance for investors to stay alert and responsive to the opportunity at hand. We remain in one of the most favorable municipal bond buyer's markets in recent memory. The recent recalibration of economic sentiment, elevated issuance, and strong technicals have created a compelling entry point.

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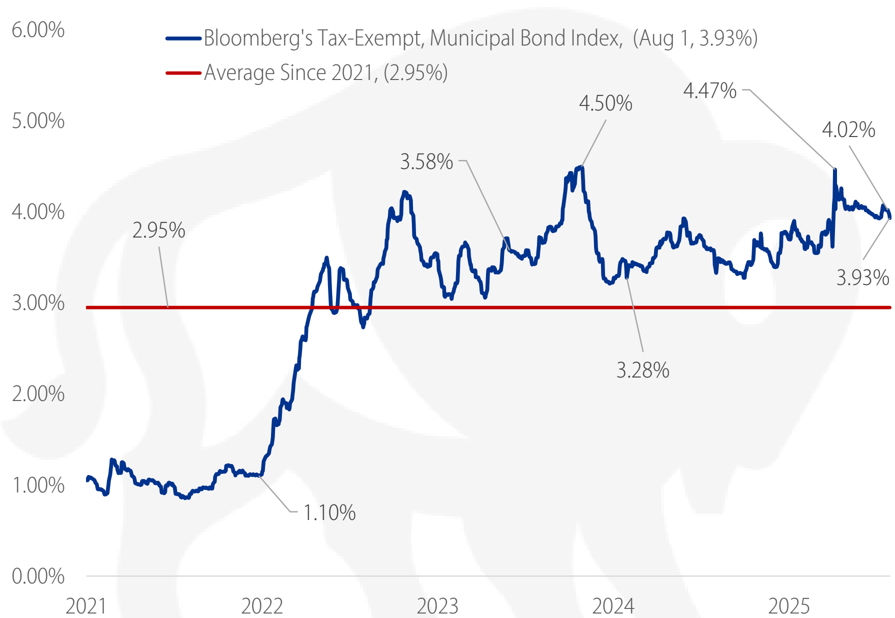
Yields are still historically attractive, relative value remains strong, and municipal credit fundamentals are solid. Municipals continue to stand out as a rare bright spot in today's market. However, the window is narrowing, and recent developments could accelerate that shift. The opportunity is still here, but investors should carefully evaluate the current environment before the ship quietly sails out of reach.

Municipal Yields Dropped Last Week



Source: Bloomberg and HilltopSecurities.

The Bloomberg Municipal Bond Index declined by nine basis points last week, ending at a 3.93% yield. Since just after April's Liberation Day, the index has dropped more than 50 basis points. AAA Municipal Market Data (MMD) yields also moved lower last week, with the 10-year falling nine basis points to 3.25% and the 30-year dropping 11 basis points to 4.60%. These are the types of steady, incremental declines that can quietly sneak up on investors—before you know it, yields are meaningfully lower and far less attractive.

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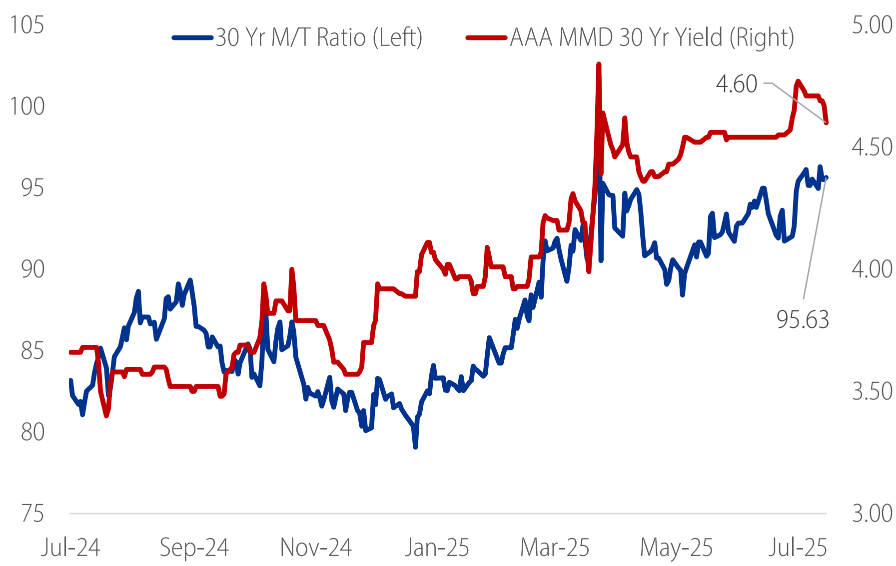
Relative Value in Favor of Municipal Bonds is Still Elevated

Municipal-to-Treasury (M/T) ratios remain elevated, with the long end of the curve continuing to offer compelling relative value despite last week's yield declines. ***This signals that municipals are still undervalued*** relative to Treasuries, and cross-over buyers are continuing to take notice. Their participation reinforces the strength of the opportunity, whether they're entering to hold or to trade. For individual investors and even for cross-over buyers who are waiting for an entry-point, this is a critical moment. M/T ratios are a key measure of relative value, and when they're attractive—as they are now—various non-traditional municipal buyers often step in quickly. These windows of opportunity do not typically stay open long. Timing matters, and the current environment calls for decisive action.

M/T Ratios Remain Attractive Even After Yields Fell Last Week



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Source: LSEG, MMD and HilltopSecurities.

All Signs Still Point to Opportunity Now, Reasons it Could Fade & Yields Could Drop

Just two weeks ago, we published Market Recalibration Sparks the Summer 2025 Municipal Bond Buying Opportunity. Our thesis remains intact: municipals offer generationally attractive tax-exempt yields, strong credit quality, and compelling value across high-grade sectors amid elevated issuance.

Friday's weaker-than-expected jobs report adds a new layer. It's not just alarming, but it is meaningful. It validates concerns about economic softness and makes a stronger case for declining yields in the near term. Revisions to May and June data bring the three-month average to just +35k jobs per month. These types of revisions are symbolic of a weakening economy.

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Even before Friday's jobs data was revealed, on Wednesday of last week, the second quarter GDP report reported the U.S. economy is weakening. Averaging the last two quarters gives a clearer picture of what the economy has in the tank. "The U.S. economy expanded at a modest +1.25% annualized pace in the first half of 2025, less than half the +2.8% pace seen in the second half of 2024," according to Hilltop's Scott McIntyre and Greg Warner.

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The next FOMC meeting is scheduled for September 16–17, and last week's data complicates the decision-making process. The CME FedWatch tool now shows an 80% probability of a rate cut in September, as of Sunday (Aug. 3rd) morning.

Head of Bureau of Labor Statistics Fired on Friday

In a stunning move, President Trump fired Bureau of Labor Statistics (BLS) Commissioner Erika McEntarfer following the July jobs report, accusing her—without evidence—of manipulating the data. This breach of democratic norms threatens the independence of federal statistical agencies and injects uncertainty into the very data that informs financial markets and investors.

There is typically a long-standing bipartisan norm against political interference in federal statistical agencies like the BLS, the Census Bureau, and the Bureau Economic Analysis. These institutions and their employees are guided by principles of objectivity and independence, ensuring that the data they produce is free from political influence. This integrity is essential, as investors and policymakers rely on accurate, impartial data to make informed decisions.

While the BLS Commissioner is a presidential appointee, the data is produced by career civil servants under rigorous, and protected methods—making McEntarfer's firing a serious breach of democratic norms and the most direct threat yet to a core institution that informs financial markets and investors. This act of intimidation, targeting politically inconvenient data, represents the most severe politicization of government bureaucracy the financial sector has witnessed, even considering threats directed at Fed Chair Powell.

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Heidi Shierholz, President of the Economic Policy Institute and former Chief Economist at the U.S. Department of Labor, emphasized the risks of undermining reliable data. She wrote that it is not only undemocratic but also economically dangerous. The economy depends on trustworthy information, and without it, she said, "It's like trying to drive a car blindfolded."

Fed Reserve Leadership in Flux

Adding to the uncertainty, Fed Governor Adriana Kugler announced her early resignation Friday. This opens the door for a new appointment at a time when the Fed's independence is already under pressure. With Chair Powell still facing threats of dismissal, the politicization of monetary policy is becoming an even greater concern for markets.

Recent HilltopSecurities Municipal Commentary

- Risk and Fragile Stability Persist as Public Pension Momentum Slows in 2025, July 28, 2025
- Market Recalibration Ignites a Summer 2025 Municipal Bond Opportunity, July 21, 2025
- Manufacturing Revival Meets Economic Reality, July 17, 2025
- Infrastructure, Muni Investors, and Trump Score Big with the OBBBA, July 3, 2025
- Cyberattacks on U.S. Infrastructure May Be Blowback from U.S. Strike on Iran, June 23, 2025

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Readers may view all of the HilltopSecurities Municipal Commentary here.