

U.S. Municipal Bond Market

No Major Scares for Municipal Investors in October as Momentum Holds

- October could likely turn out to be a strong month for municipal bonds, as we expected, with high issuance, solid demand, and a favorable macro backdrop including an expected Fed rate cut this week.
- Expected rate cuts, softer than expected inflation data, and low market volatility have boosted investor confidence and driven strong inflows into municipal mutual funds.
- As municipal issuance slows in November and December, tightening supply is likely to create a more competitive environment for investors seeking yield, similar to what we saw during parts of September. Our message to investors is clear: **do not wait to invest**.
- The federal government shutdown remains unresolved, adding to general uncertainty, but municipal bonds continue to demonstrate resilience, and we still expect limited to no impact on credit quality or liquidity. However, the longer the shutdown lasts, the more credit stress exposed areas could begin to experience.

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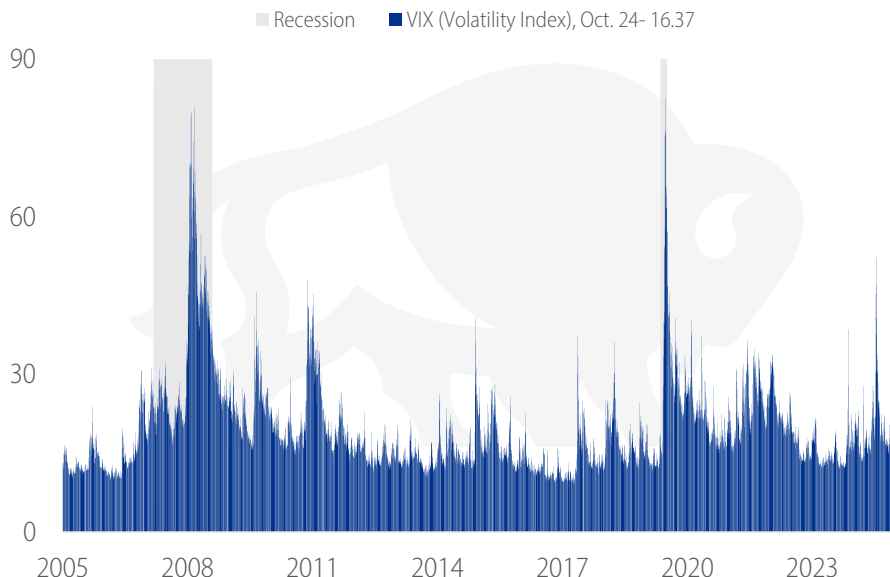
Macro-Economic Drivers: Inflation, Fed Policy, and Confidence

October may not have appeared to be the ideal entry point for municipals, but in hindsight it could prove to be one of the strongest months for municipal investors. While November and December are expected to remain positive, they may not match the momentum and optimism seen in October.

Last week, the September Consumer Price Index result was softer than expected, reinforcing confidence in the Fed's upcoming rate cuts this week on October (28-29) and

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VIX Volatility Index Below 20-Year Average Level



Source: CBOE and HilltopSecurities.

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potentially on December (9-10). This inflation data is a key reason why the FOMC is likely to move lower, supporting continued strength in municipal demand. The VIX volatility index has remained below its 20-year average, signaling unusually low market unpredictability. This is important because it reflects investor confidence and a more stable risk environment, both of which **support continued inflows into municipal bonds**.

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October unfolded **exactly as we projected**: strong issuance, strong demand, and a macro backdrop that favors the municipal market supply and demand dynamic. Looking ahead to the rest of 2025, issuance is expected to cool while demand remains firm as rate cuts likely continue. For investors, the window of opportunity is still open, but it may steadily narrow as supply tightens in the final months of the year.

October Moment Continues

On Oct. 1, we noted that municipal bonds were having a "moment." Investor interest was rising, and we anticipated that more would begin to recognize the value municipals can bring to a portfolio, especially with expectations of falling interest rates. That momentum has continued to build throughout the month.

So far, October has unfolded largely as we expected. The trends we identified have played out with remarkable accuracy, reinforcing our confidence in our near-term outlook for the U.S. municipal bond market. The Bloomberg Municipal Bond Index declined by just over one basis point week over week, closing Friday at 3.55%. We continue to remind investors that although yields have moderated over the last few weeks, they remain historically attractive. This environment still offers a compelling opportunity for those seeking tax-efficient income and portfolio resilience through strong, dependable returns.

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Supply and Demand Dynamic

Municipal issuance has remained strong throughout October. The only reason this week's calendar is relatively lighter is due to the Oct. 28–29 FOMC meeting, an event which typically slows issuance activity. Even so, a calendar exceeding \$7+ billion during a Fed meeting week is notable and reflects issuers' intent to access the market before year-end.

Demand for municipal bonds has been exceptionally robust, just as we forecasted. Since the end of summer, approximately \$9.5 billion has flowed into institutional municipal mutual funds, with another \$1 billion added last week alone, per Lipper. This surge is partially driven by investor expectations of Fed rate cuts, and we believe the trend will continue as the FOMC lowers rates in October and again in December.

Individual investors often react after the fact, and this appears to be another example. Many have been adding money to municipal mutual funds since late summer in anticipation of lower rates. As issuance slows in November and December, supply will tighten and create a slightly different dynamic. In September, investors already found it challenging to source bonds, and that situation is likely to repeat during the final months of the year.

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No Resolution in Sight to the Federal Government Shutdown

The federal government shutdown, now the second-longest in U.S. history, continues to dominate headlines and inject some uncertainty into investors' minds. Negotiations remain stalled, and there is currently no clear path to resolution. The U.S. Department of Agriculture has announced that federal food assistance will cease on Nov. 1, impacting one in eight Americans. Transportation Secretary Sean Duffy warned on Fox News' Sunday Morning Futures that air traffic controllers are "wearing thin," underscoring growing operational strain. The macro-economic impact could begin to turn detrimental to the US economy if the shutdown continues much longer into November or December, and especially if it extends into the new year.

Municipal bonds continue to serve as a cornerstone of stability amid federal uncertainty and potential macroeconomic volatility.

Despite political gridlock and delays in federal data releases, municipal bonds remain resilient. There is no material strain anticipated on municipal credit quality or market liquidity. While the shutdown highlights uncertainty in Washington, it does not diminish the core value proposition of municipals: still generationally attractive yields, tax-advantaged, dependable income with historically low default risk. Municipal bonds continue to serve as a cornerstone of stability amid federal uncertainty and potential macroeconomic volatility. However, the macroeconomic impact to some municipal credits could begin to turn negative if the shutdown continues much longer into November or December, and especially if it extends into 2026. The longer the shutdown lasts, the more credit stress exposed areas could begin to experience, potentially affecting fiscal stability and market confidence.

Recent HilltopSecurities Municipal Commentary

- Preserve Wealth, Capture Yield with Municipal Bonds as Concern Mounts, October 20, 2025
- October's Municipal "Moment" Continues to Unfold Amid Market Uncertainty, October 15, 2025
- The Municipal Bond "Moment" Persists—But Cracks Are Forming, October 6, 2025
- The Secret's Out – Municipal Bonds Are Having a Moment, October 1, 2025
- Intro to the New Era of AI, Infrastructure & Growth, September 18, 2025

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

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