

U.S. Municipal Bond Market

## Investors are Choosing Stability, Tax-Exempt Income, and the Bonds that Finance America’s Infrastructure

- Investors are shifting capital into municipal bonds, with nearly \$25 billion flowing into municipal mutual funds in 2026 so far per Lipper, including 19 positive weeks out of 21 and more than \$1.5 billion last week alone.
- This demand trend did not start this year. It began building in May 2025 and accelerated in 2026 as investors prioritized stability, tax-exempt income, and yields that have become more compelling.
- Key drivers of demand are likely to remain durable through the end of the year. Money market balances are leveling off and some of that cash appears to be extending into longer duration assets, the tax-exemption remains a powerful incentive for high income buyers, and the narrowing gap between expected stock returns and bond yields could be nudging more capital toward fixed-income, including municipals.

*Tom Kozlik*  
Head of Public Policy and  
Municipal Strategy  
214.859.9439  
tom.kozlik@hilltopsecurities.com

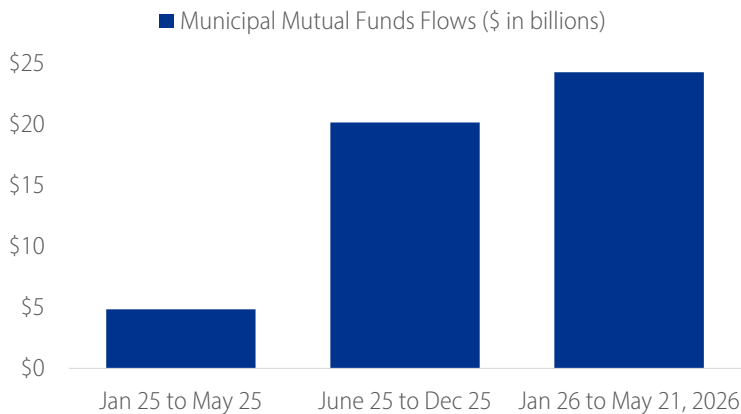
### Demand Has Been the Defining Municipal Bond Market Story of 2026

The story of 2026 so far is a clear shift of capital into U.S. municipal bonds. Nearly \$25 billion has flowed into municipal mutual funds, according to Lipper data. It is an important signal of investor preference.

Demand began to build back in the beginning of May 2025. By 2026, weekly municipal fund flows had nearly doubled, on average, as investors sought stability, tax-free income, and attractive yields. This increase in demand has surprised some investors and market observers. The first five months of 2026 have been volatile. The result has not been broad losses, but a shift in what investors are now choosing to value.

*Nearly \$25 billion has flowed into municipal mutual funds, according to Lipper data.*

### Growing Municipal Bond Demand



Source: Lipper and HilltopSecurities.

The macro-outlook has shifted. In January most were expecting interest rates to move lower, tax policy to support growth, and technology spending would continue to drive the economy.

*In January most were expecting interest rates to move lower, tax policy to support growth, and technology spending would continue to drive the economy.*

Early in the year, markets focused on the economic impact of technology. In January and February, investors were seriously considering the consequences of AI as a general purpose technology. We watched closely as flows were loud to begin the year and then capital chose stability & U.S. Infrastructure, even in mid-February. Interest rates were slowly declining, until Washington escalated the conflict with Iran, and yields started their climb higher.

Memorial Day weekend marks the beginning of summer and often serves as a natural checkpoint. It is a time for investors to account for what has changed and what could come next. An important change is that Kevin Warsh was sworn in as Federal Reserve Chair last week. He faces unique challenges. A Middle East peace agreement is possible but a peace plan remains both uncertain and elusive. U.S. federal debt as a percentage of GDP is now over 100%. Oil prices have eased slightly in recent days, as have yields. However, both remain elevated compared to the beginning of the year.

### What Investors are Actually Doing

One of the most important and underappreciated stories of 2026 is that investors are choosing stability and tax-exempt income, alongside increasingly attractive yields, in the market that finances American infrastructure. This bears repeating. The details, and the reasons behind this shift, matter.

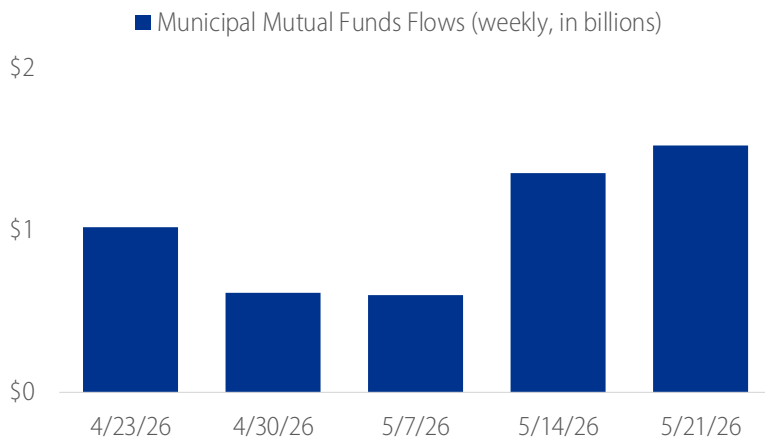
*We watched closely as flows were loud to begin the year and then capital chose stability & U.S. Infrastructure, even in mid-February.*

Investors have deposited almost \$25 billion into municipal mutual funds so far in 2026 per Lipper data. In 2025 the net total inflow was only \$4 billion through a comparable period. From June through December 2025, investors added nearly \$20 billion more.

In total, roughly \$49 billion has moved into municipal funds since the beginning of May 2025.

Last week, more than \$1.5 billion flowed into municipal mutual funds alone, marking the 19th positive week out of 21 so far in 2026.

### Investment Dollars are Flowing into Municipal Mutual Funds



*One of the most important and underappreciated stories of 2026 is that investors are choosing stability and tax-exempt income, alongside increasingly attractive yields, in the market that finances American infrastructure.*

## This is Not Just a Trade

This is not just a short-term trade for most municipal investors. The \$25 billion of fund inflows in 2026 is more than a technical signal.

It is a message delivered in parts.

- Stability matters.
- Tax-exempt income matters.
- Public entities still need capital, potentially in another record amount this year or close to it, and those entities can still attract it.

As a reminder, municipal bonds remain one of the primary ways America finances schools, transportation, housing, utilities, and hospitals. The stability of the market and the tax-exemption are important features.

## Why Demand Has Grown

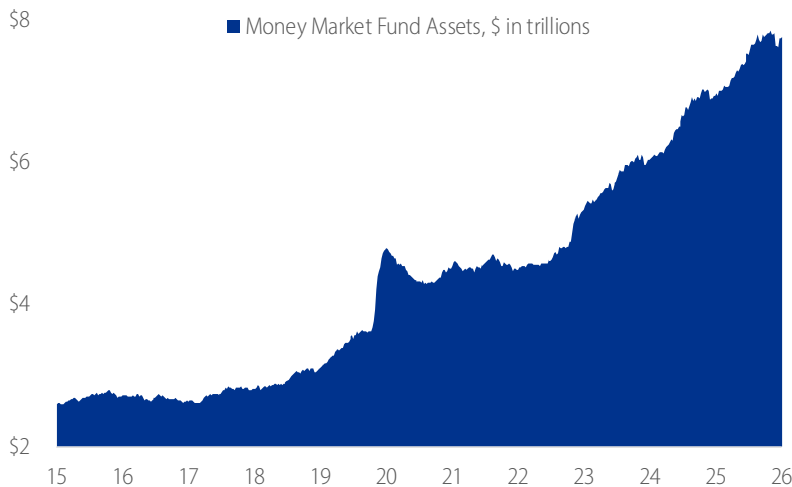
Several forces are driving what is shaping up to be the defining municipal bond story of 2026. Others will likely be uncovered as well. This is what we are seeing now.

A key reason is that investment dollars in money market funds that has grown in recent years is finally starting to level off. We think investors are seeking duration with some of these investment dollars through municipal bond investments. This could continue, especially if yields remain attractive or become even more attractive in coming weeks.

*The \$25 billion of fund inflows in 2026 is more than a technical signal.*

*Several forces are driving what is shaping up to be the defining municipal bond story of 2026.*

## Money Market Balances Have Levelled Off



Source: ICI and HilltopSecurities.

Tax-exempt income in the form of the municipal bond tax-exemption remains a central draw, especially for higher income investors focused on income they prefer to keep from a tax perspective. This is likely to remain a durable source of demand. The threat to the tax-exemption was severe in 2025, it remains elevated now, but we do not see an immediate, or imminent threat to the municipal bond tax-exemption in the near term.

It is also possible that investors have rebalanced out of other asset classes and into municipal bonds since the start of the year. This driver could also continue to play out throughout the rest of 2026.

*The threat to the tax-exemption was severe in 2025, it remains elevated now, but we do not see an immediate, or imminent threat to the municipal bond tax-exemption in the near term.*

Finally, a [Wall Street Journal front-page article](#), just above the fold, this week captured the growing dynamic between equities and fixed-income well. The article argues, “A rough gauge of stocks’ expected returns is only slightly higher than what ultrasafe government bonds would produce.” This dynamic is likely playing an important factor in demand for municipals and very well could continue through the remaining months of 2026.

*Since these drivers of demand are likely to persist, we would be surprised if the municipal bond story of 2026 so far does not continue through the rest of the year.*

Since these drivers of demand are likely to persist, we would be surprised if the municipal bond story of 2026 so far does not continue through the rest of the year.

## Recent HilltopSecurities Municipal Commentary

- [Selection Matters More as U.S. Municipal Credit Continues to Turn Lower](#), May 18, 2026
- [The Threat to the Tax-Exemption Keeps Building Amid Quantitative Stress, Qualitative Drift](#), May 11, 2026
- [Drift Toward Stability Confirmed by the First Four Months of 2026 Municipal Issuance](#), May 4, 2026
- [Powell, Warsh, the Fed Transition and Why Long-End Municipals Still Make Sense](#), April 27, 2026
- [Elevated Municipal Yields Persist as Private Credit Draws Scrutiny, Fiscal Concerns Build, and Long-end M/T Ratios Stay Attractive](#), April 20, 2026

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

*The paper/commentary was prepared by HilltopSecurities (HTS). It is intended for informational purposes only and does not constitute legal or investment advice, nor is it an offer or a solicitation of an offer to buy or sell any investment or other specific product. Information provided in this paper was obtained from sources that are believed to be reliable; however, it is not guaranteed to be correct, complete, or current, and is not intended to imply or establish standards of care applicable to any attorney or advisor in any particular circumstances. The statements within constitute the views of HTS Public Finance as of the date of the document and may differ from the views of other divisions/departments of Hilltop Securities Inc. In addition, the views are subject to change without notice. This paper represents historical information only and is not an indication of future performance. This material has not been prepared in accordance with the guidelines or requirements to promote investment research, it is not a research report and is not intended as such. Sources available upon request.*

Hilltop Securities Inc. is a registered broker-dealer, registered investment adviser and municipal advisor firm that does not provide tax or legal advice. HTS is a wholly owned subsidiary of Hilltop Holdings, Inc. (NYSE: HTH) located at 717 N. Harwood St., Suite 3400, Dallas, Texas 75201, (214) 859-1800, 833-4HILLTOP