Weekly Market Commentary

The Week in Muniland

March 3, 2025

Marching Forward

Key Takeaways

1. **Yields continued to fall in the market last week, capping off a strong February return for municipal bonds.**

2. **The potential impact of the proposals from the Trump administration to reduce federal funding for state and local governments will vary, but we believe most issuers will be largely unaffected.**

3. **Market technicals may soften in March, which could present an attractive entry point for investors.**

The municipal market continued to deliver positive returns last week, with yields falling across the curve. For the week, two-, 10- and 30-year AAA municipal yields fell 10, 10 and 4 basis points (bps), respectively. The Bloomberg Municipal Bond Index (Index) returned 0.61% last week and has returned 1.50% year to date.

- **Why it matters:** Munis have more than clawed their way back from the volatility at the beginning of this year, with the Index returning 2.55% since January 14. The market has benefitted from falling Treasury yields—the 10-year US Treasury yield has fallen nearly 55 bps since it peaked at 4.80% in January, and the market is now pricing in two interest-rate cuts of 25 bps by the Fed this year. Demand for tax-exempt income has remained healthy, and continues to remain healthy, with investors adding $785 million to the market last week, marking the sixth consecutive week of inflows, according to Lipper. Year to date, investors have added nearly $8 billion to the municipal market. That said, supply has been relatively strong. February tax-exempt issuance was $34 billion, which is the second consecutive monthly record for tax-exempt issuance. Through February, year-to-date issuance is now at $69 billion—exceeding the $60 billion that was issued for the same period last year. Issuance will be somewhat heavy this week with $10.9 billion expected to price but should be absorbed relatively well with March 1 coupon payments slated for reinvestment.

Proposals from the Trump administration to reduce federal funding for state and local governments have some investors questioning the potential impact on the municipal bond market.

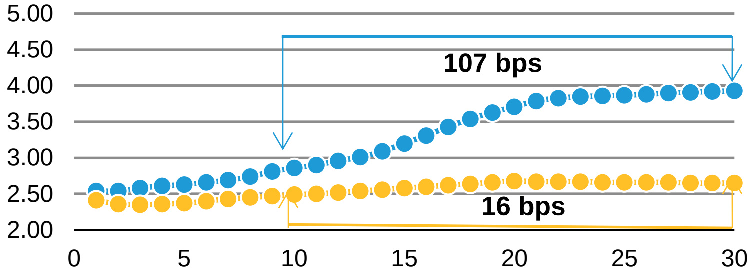
- **Why it matters:** We believe the most recent proposals to reduce federal funding to state and local governments will have a varying impact on municipal bond issuers and sectors of the muni market. While most issuers will be largely unaffected, some may need to tactically adjust to the new reality. More importantly, issuers in the municipal market have a history of successfully adapting to policy change. For example, the Tax Cuts and Jobs Act capped state and local tax deductions at $10,000, which disproportionately impacted high-tax cities (such as New York) and threatened to dampen economic growth and reduce tax revenue. However, the city navigated this shift through prudent fiscal management and adapted to the policy changes without any significant fiscal issues. Overall, the budget flexibility of municipal issuers, the role they play in funding essential services, and the continued demand from investors seeking attractive tax-exempt income are all factors that give us confidence in the continued reliance on the municipal market in the face of potential federal funding cuts.

With February in the rear-view mirror, what should investors expect in March?

- **Why it matters:** With the Index returning 0.99% in February, it was certainly a strong month of absolute performance. Turning to March, net supply is expected to total $7 billion, meaning that issuance is likely to exceed the amount of coupon payments and redemptions, creating a potential headwind for the market. There could also be some selling pressure as investors pull cash for tax season. That said, this seasonality could be mitigated if inflows remain strong. In any case, investors should take advantage of any volatility and use it as an opportunity to add exposure at attractive valuations.

Displays of the Week: March 3, 2025

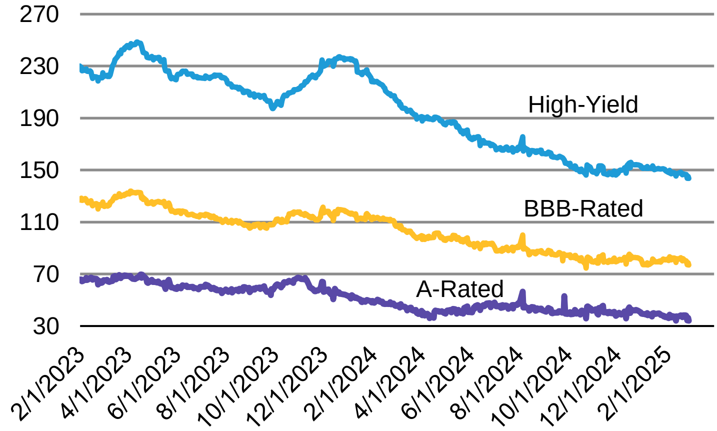
Display 1: Municipal Yield Curve vs. US Treasury Curve After Tax* (Percent)



While the shape of the muni yield curve is normalizing, a barbell maturity structure remains advantageous given the steepness at the long end of the curve.

Tax rate used: 40.8%
As of February 28, 2025. Source: Municipal Market Data and AB

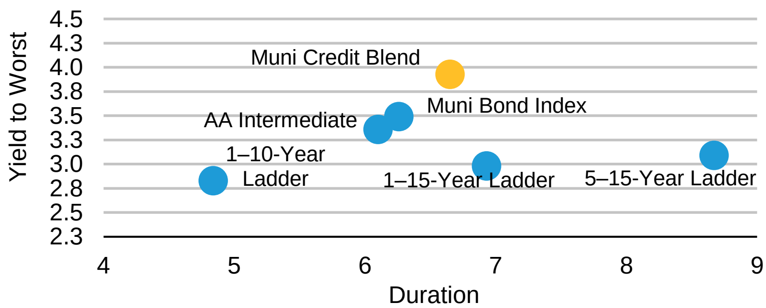
Display 2: Municipal Credit Spreads (Basis Points)



While credit spreads tightened significantly in 2024, credit offers a compelling income pickup versus higher-quality bonds.

As of February 28, 2025
Source: Bloomberg and AB

Display 3: Portfolio Construction for Today (Percent)

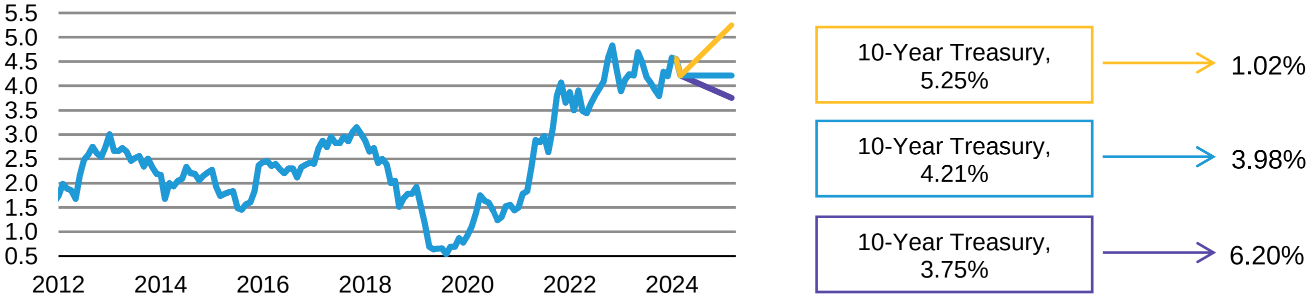


A thoughtful blend of high-grade and credit bonds along with a barbell maturity structure can add nearly 100 bps in yield to a portfolio.

Muni credit blend is a blend of Bloomberg muni indices: 60% high-grade, 30% A/BBB and 10% high-yield.
As of February 28, 2025. Source: Bloomberg and AB

Display 4: Expected 12-Month Municipal Returns Scenario Analysis

10-year US Treasury Yield (Percent)



Past performance and historical analysis do not guarantee future results.
Display reflects expected returns of the Bloomberg Municipal Bond Index under three scenarios:
10-year US Treasury yields rise to 5.25%, remain the same or decline to 3.75% over the next 12 months.
As of February 28, 2025. Source: Bloomberg and AB

The views expressed herein do not constitute research, investment advice or trade recommendations and do not necessarily represent the views of all AB portfolio-management teams. Views are subject to change over time.

A Word About Risk

Market Risk: The market values of the Portfolio's holdings rise and fall from day to day, so investments may lose value. **Interest-Rate Risk:** Fixed-income securities may lose value if interest rates rise or fall—long-term securities tend to rise and fall more than short-term securities. The values of mortgage-related and asset-backed securities are particularly sensitive to changes in interest rates due to prepayment risk. **Credit Risk:** A bond's credit rating reflects the issuer's ability to make timely payments of interest or principal—the lower the rating, the higher the risk of default. If the issuer's financial strength deteriorates, the issuer's rating may be lowered, and the bond's value may decline. **Inflation Risk:** Prices for goods and services tend to rise over time, which may erode the purchasing power of investments. **Foreign (Non-US) Risk:** Investing in non-US securities may be more volatile because of the political, regulatory, market and economic uncertainties associated with such securities. These risks are magnified in securities of emerging or developing markets. **Currency Risk:** If a non-US security's trading currency weakens versus the US dollar, its value may be negatively affected when translated back into US-dollar terms. **Diversification Risk:** Portfolios that hold a smaller number of securities may be more volatile than more diversified portfolios, since the gains or losses from each security will have a greater impact on the Portfolio's overall value. **Derivatives Risk:** Investments in derivative instruments such as options, futures, forwards or swaps can be riskier than traditional investments and may be more volatile, especially in a down market. **Leverage Risk:** Trying to enhance investment returns by borrowing money or using other leverage tools magnifies both gains and losses, resulting in greater volatility. **Municipal Market Risk:** Debt securities issued by state or local governments may be subject to special political, legal, economic and market factors that can have a significant effect on the Portfolio's yield or value. An investor cannot invest directly in an index. **Investment and Insurance Products:** Not FDIC insured I Not a bank deposit I Not insured by any federal government agency I No bank guarantee I May lose value

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