Invesco

Investment Insights

# Thoughts From The Municipal Bond Desk

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**Overview**

- Municipal credit conditions appeared resilient, with year-to-date defaults down roughly 70% year over year. Defaults are expected to remain limited in 2026 and concentrated in sectors facing specific challenges.[1]
- The ongoing conflict in the Middle East has increased inflation expectations and interest rate volatility, even as broader liquidity conditions remain stable at present.
- Recent investment outflows are largely tax-driven and may offer potential entry points for investors seeking tax-efficient and short-duration municipal exposure.

**Tim: Defaults are down thus far in 2026. Doesn't that support our view that credit fundamentals continue to be resilient?**

**Mark:** I think so! When you look at the numbers, the story is really encouraging. First-time payment defaults in March totaled just $49.5 million, which shows a sharp 79% year-over-year decline.[1] And those defaults were concentrated in a single borrower.[1] The March number also means that year-to-date defaults are rather low at $257.2 million – a 70% drop year over year.[1] Looking ahead, I expect defaults to remain low and mostly limited to sectors experiencing unique challenges. These are areas such as nursing homes and senior living, hospitals, industrial development, and some education sectors.[1] That said, even within these sectors there are many healthy credits, which is why thorough, bottom-up research is so important. The fact that there have been no Chapter 9 bankruptcy filings so far this year[1] further supports our view that overall credit conditions remain solid, even though there may be occasional problem spots. On balance, I think munis continue to offer a very compelling credit picture heading into the second half of the year.

**Tim: What are the implications for interest rates and inflation if we see a prolonged conflict the Middle East?**

**Mark:** Great question, and it's one we're watching very closely. The conflict has already had a direct impact on financial markets, raising inflation expectations and pushing interest rates higher. Rising energy prices have increased breakeven inflation rates across world economies,[2] which has contributed to increased interest rate volatility. But while global financial conditions have tightened, I do not see evidence of acute liquidity stress. The longer-term impact on economic growth, however, remains unknown. I will say that elevated inflation pressures could force central banks to tighten monetary policy. On the other hand, I believe an extended conflict is likely to weigh on economic growth and labor markets, which could preclude central bank tightening. The bottom line is that central banks are in a difficult position, and investors should be prepared for a wider range of rate outcomes than we've seen in recent quarters.

**Tim: Investment flows turned negative recently. Was this due mainly to seasonal pressures, as investors looked to pay their tax bills?**

**Mark:** Yes, that's exactly right. Consistent with historical patterns, outflows increased as investors made withdrawals to pay tax liabilities. Certain investors may also have been taking advantage of the opportunity to do some tax-loss harvesting given that municipal yields have risen. On April 13 alone, the municipal market experienced $319 million in net outflows, driven largely by $243 million in withdrawals from municipal ETFs. Not surprisingly, significant redemptions also came from ultra-short duration strategies.[3] Tax-exempt money market funds, for example, posted a fifth consecutive day of withdrawals, totaling $3.8 billion, on April 13.[3] That said, I think the tax-driven selling may be creating attractive entry points for investors seeking tax-efficient cash and short-duration exposure. We've seen this pattern before, and historically these seasonal dislocations tend to reverse once tax season passes, so patient investors could be well rewarded here.

## Munis by the numbers

A quick look at some commonly used municipal market datapoints.

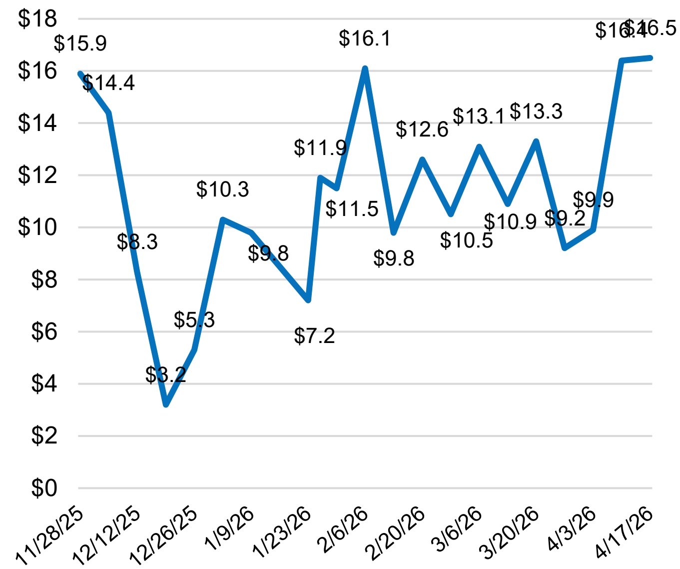
### 2026 Fund Flows - Weekly and Monthly Reporters ($millions)

Week ended April 15, 2026

| | Combined | Open End Mutual Funds | ETFs |
|---|---|---|---|
| All term muni funds | 27,806 | 15,390 | 12,417 |
| Investment Grade | 24,246 | 12,093 | 12,152 |
| High Yield | 3,561 | 3,296 | 264 |
| Long Term (10yr +) | 14,937 | 7,133 | 7,805 |
| Intermediate (5-10yr) | 9,379 | 6,169 | 3,210 |
| Short / Intermediate (3-5yr) | 2,683 | 1,694 | 989 |
| Short (1-3yr) | 807 | 394 | 413 |
| National funds | 23,844 | 12,889 | 10,955 |
| New York | 536 | 223 | 313 |
| California | 2,554 | 1,477 | 1,077 |

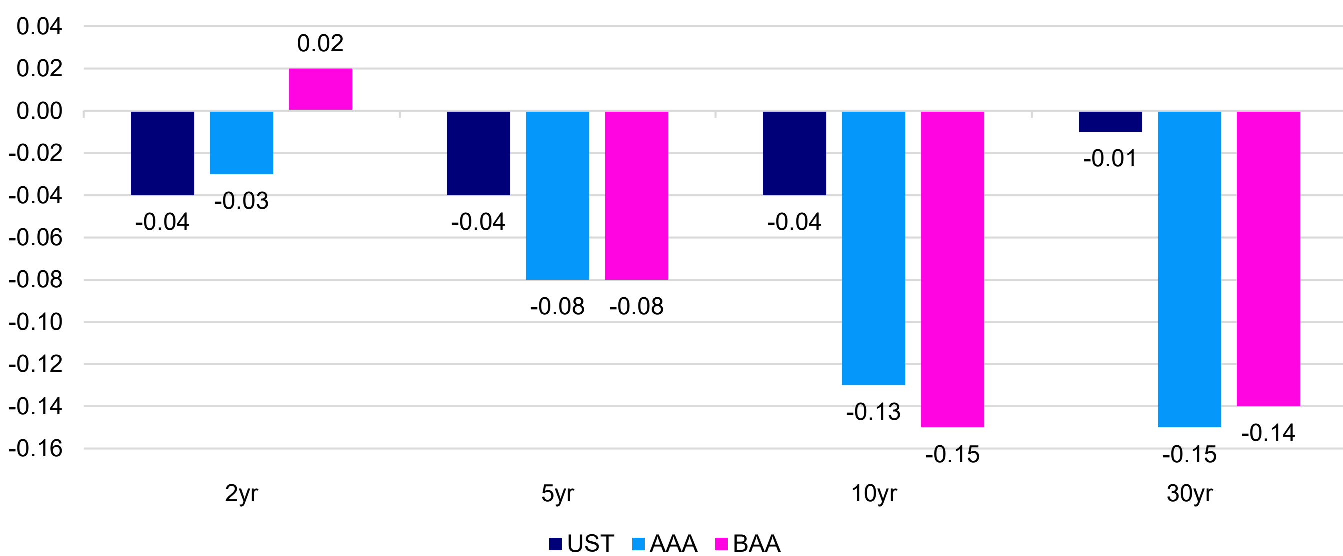
Source: Year to date LSEG Lipper Global Fund Flows, J.P. Morgan. Data refreshed on April 16 2026. Note: Figures shown on this table are combination of weekly and monthly reporters.

### 30-day Visible Supply ($billions)




Source: Bond Buyer Weekly 30-Day Visible Supply - Total dollar volume of bonds to be offered over the next thirty days. It does not include 'Sealed Bids Invited' or 'Proposed Bond Issues'. Only includes Municipal Bonds. From November 28, 2025 – April 17, 2026.

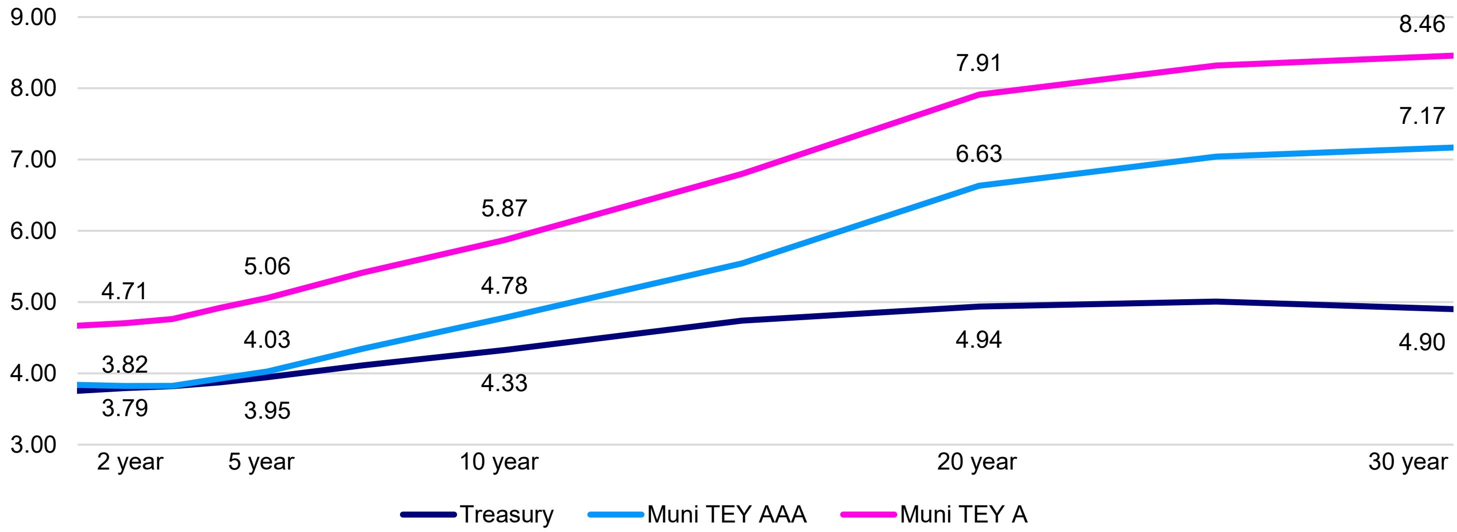
### 1-Month Yield Change 3/23/2026 – 4/22/2026 (% Change)




Source: Refinitiv MMD Curve, US Department of Treasury, from March 23, 2026 – April 22, 2026. UST = United States Treasury. A credit rating is an assessment provided by a nationally recognized statistical rating organization (NRSRO) of the creditworthiness of an issuer with respect to debt obligations, including specific securities, money market instruments or other debts. Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest); ratings are subject to change without notice. NR indicates the debtor was not rated and should not be interpreted as indicating low quality. For more information on rating methodologies, please visit the following NRSRO websites: www.standardandpoors.com and select 'Understanding Credit Ratings' under Rating Resources 'About Ratings' on the homepage.; https://ratings.moodys.io/ratings and select 'Rating Methodologies' on the homepage.; www.fitchratings.com and select 'Ratings Definitions Criteria' under 'Resources' on the homepage. Then select 'Rating Definitions' under 'Resources' on the 'Contents' menu.

## Munis by the numbers

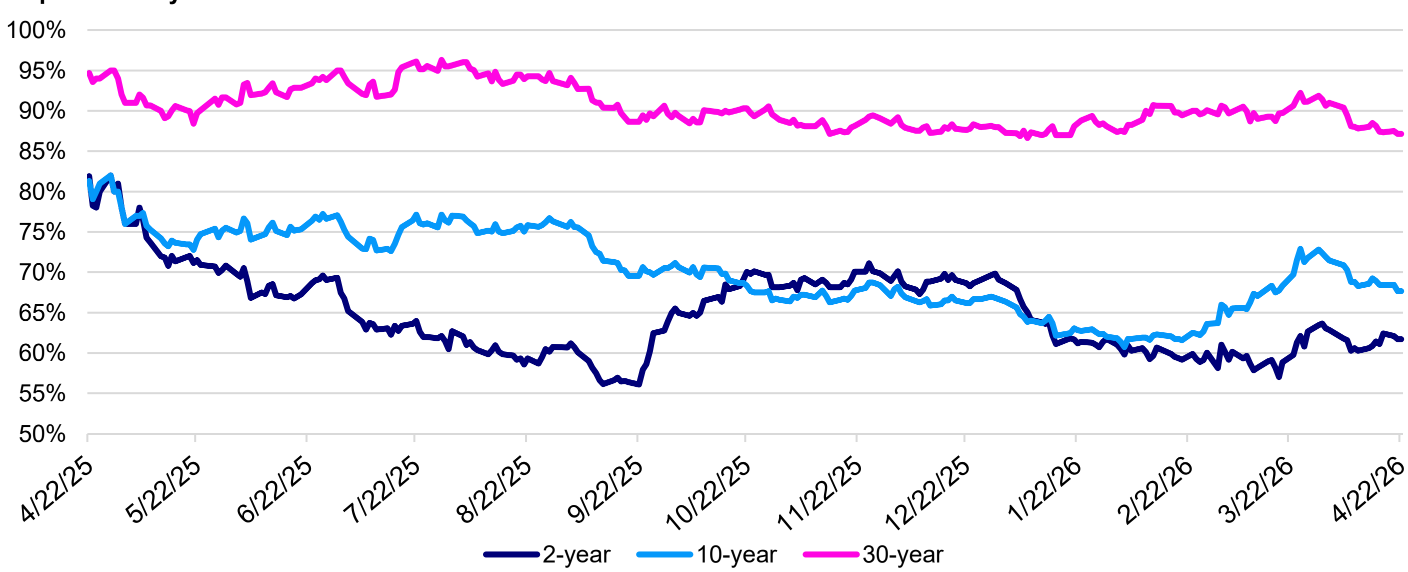
### Current Muni Treasury Ratio and Tax-Equivalent Yields (%)




| Term | US Treasury (UST) | Muni AAA | Muni A | Muni TEY AAA | Muni TEY A | Muni UST Ratio | Muni TEY UST Ratio |
|---|---|---|---|---|---|---|---|
| 2 year | 3.79 | 2.26 | 2.79 | 3.82 | 4.71 | 59.7% | 100.9% |
| 5 year | 3.95 | 2.38 | 2.99 | 4.03 | 5.06 | 60.4% | 102.0% |
| 10 year | 4.33 | 2.83 | 3.48 | 4.78 | 5.87 | 65.4% | 110.5% |
| 20 year | 4.94 | 3.93 | 4.68 | 6.63 | 7.91 | 79.5% | 134.3% |
| 30 year | 4.90 | 4.24 | 5.01 | 7.17 | 8.46 | 86.6% | 146.2% |

Source: Bloomberg as of April 22, 2026. TEY = Tax-Equivalent Yield. UST = United States Treasury. US Treasury is represented by the public obligations of the US Treasury. Treasurys are backed by the full faith and credit of the US government as to the timely payment of principal and interest, while legislative or economic conditions could affect a municipal securities issuer's ability to make payments of principal or interest. Muni AAA is represented by the Municipal AAA GO bond yield, a Municipal Market Data proprietary yield curve of AAA-rated state general obligation bonds, based on the institutional block size of $2million-plus market activity in both the primary and secondary bond market. The Muni TEY AAA is the Tax-Equivalent Yield is assuming a top tax rate of 40.8% of the Muni AAA yield. Muni A is the Bloomberg Municipal Bond A Index is an unmanaged index of the A-rated municipal bond market. The Muni TEY A is the Tax-Equivalent Yield is assuming a top tax rate of 40.8% of the Muni A yield. The Muni UST Ratio is the comparison of the Muni AAA vs. the yield on the US Treasury. The Muni TEY UST Ratio is the Tax-Equivalent Yield is assuming a top tax rate of 40.8% of the Muni UST Ratio. An investment cannot be made directly into an index.
Tax-equivalent yield assuming a top tax rate of 40.8%, 37% federal tax rate and 3.8% net investment income tax (NIIT), effective Jan. 1, 2026. Irs.gov, as of October 9, 2025. Top marginal tax rate for single taxpayers with more than $640,600 in taxable income or couples with more than $768,700. NIIT is the net investment income tax investment income for single taxpayers with more than $200,000 in taxable income or couples with more than $250,000.

### Municipal/Treasury Ratio




Source: Thomson Reuters TM3, as of April 22, 2026. US Treasury is represented by the public obligations of the US Treasury. Treasurys are backed by the full faith and credit of the US government as to the timely payment of principal and interest, while legislative or economic conditions could affect a municipal securities issuer's ability to make payments of principal or interest. The Municipal AAA GO bond yield is represented by the Municipal Market Data proprietary yield curve of AAA-rated state general obligation bonds, based on the institutional block size of $2million-plus market activity in both the primary and secondary bond market. Past performance does not predict future returns. An investment cannot be made directly into an index.

Breakeven inflation rate is a measurement that aims to predict the effects of inflation on certain investments, by analyzing known market inflation rates from recent years.

**Sources:**


1. BofA Global Research, as of April 10, 2026.
2. "War in the Middle East Challenges Global Financial Security," International Monetary Fund Blog, as of April 14, 2026.
3. J.P. Morgan Global Markets Strategy, as of April 14, 2026.


**About risk**

Municipal securities are subject to the risk that legislative or economic conditions could affect an issuer's ability to make payments of principal and/or interest.

Junk bonds involve greater risk of default or price changes due to changes in the issuer's credit quality.

Any reference to a rating, ranking or an award is not a guarantee of investment performance and is not constant over time.

The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested. The values of junk bonds fluctuate more than those of high-quality bonds and can decline significantly over short time periods.

All fixed income securities are subject to two types of risk: credit risk and interest rate risk. Credit risk refers to the possibility that the issuer of a security will be unable to make interest payments and/ or repay the principal on its debt. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa.

Municipal bonds are issued by state and local government agencies to finance public projects and services. They typically pay interest that is tax-free in their state of issuance. Because of their tax benefits, municipal bonds usually offer lower pre-tax yields than similar taxable bonds.

All data as of April 22, 2026, unless otherwise stated.

All data provided by Invesco unless otherwise noted.

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