

Investment Insights

Impact of Rate Cuts on Munis



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We believe the municipal bond market is well positioned to provide positive returns based on potential Federal Reserve (Fed) rate cuts. The market anticipates that there will be two rate cuts in 2025. The Fed cited indicators that economic activity has continued to expand at a solid pace and unemployment has stabilized at a low level. Future decisions will be based on incoming data, the evolving outlook and the balance of risks, with a continued commitment to a 2% inflation target and maximum unemployment.¹

Municipal bond returns have been positive at the end of the last five Fed hiking cycles

Bloomberg Municipal Bond Index returns have been positive over the one-, two-, and three-year periods at the end of all Fed hiking cycles since 1995.

End of Fed Hiking Cycle	Fed Funds Rate	1 Year Post Cycle	2 Years Post Cycle	3 Years Post Cycle
February 1995	6.00%	12.84%	8.06%	8.76%
May 2000	6.50%	12.14%	9.29%	9.65%
July 2006	5.25%	4.27%	3.54%	4.06%
December 2018	2.50%	7.54%	6.36%	4.72%
July 2023	5.50%	3.73%	1.85%	N/A

Source: Bloomberg, as of October 31, 2025. The Bloomberg Municipal Bond Index is an unmanaged index considered representative of the tax-exempt bond market. An investment cannot be made in an index. **Past performance is no guarantee of future results.**



Tim Spitz
Head of Municipal Business
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As the Fed cuts rates, we believe municipal bonds will perform well

If spreads are unchanged, a parallel downward shift in rates may provide positive total returns.

Index	Duration	Parallel Shift (basis points)			Yield to Worst	Parallel Shift (basis points)		
		-100	-75	-50		50	75	100
Bloomberg Municipal 1–3-year Index	1.59 years	4.40%	4.00%	3.61%	2.81%	2.02%	1.62%	1.22%
Bloomberg Municipal 5-year Index	3.64 years	6.51%	5.60%	4.69%	2.87%	1.05%	0.14%	-0.77%
Bloomberg Municipal 10-year Index	5.82 years	9.04%	7.59%	6.13%	3.22%	0.31%	-1.15%	-2.60%
Bloomberg Municipal Bond Index	6.65 years	10.22%	8.56%	6.90%	3.57%	0.25%	-1.42%	-3.08%
Bloomberg US Treasury Index	5.91 years	9.82%	8.34%	6.87%	3.91%	0.96%	-0.52%	-2.00%

Source: Bloomberg, as of October 31, 2025. The Bloomberg Municipal 1–3-Year Index is an unmanaged index of municipal bonds with a remaining maturity of one to three years. The Bloomberg Municipal 5-Year Index is an unmanaged index of fixed-rate, investment-grade municipal securities with maturities of four to six years. The Bloomberg Municipal 10-Year Index is the eight to 12-year maturity component of the Bloomberg Municipal Bond Index. The Bloomberg Municipal Bond Index is an unmanaged index considered representative of the tax-exempt bond market. The Bloomberg US Treasury Index is represented by the public obligations of the US Treasury. Treasuries 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. An investment cannot be made in an index. **Past performance is no guarantee of future results.**

Add in the Tax-Equivalent Yield Benefit of Municipal Bonds

With the tax-equivalent yield of municipal bonds, positive returns can be found across the duration spectrum.

Index	Duration	Parallel Shift (basis points)			Tax- Equivalent Yield	Parallel Shift (basis points)		
		-100	-75	-50		50	75	100
Bloomberg Municipal 1–3-year Index	1.59 years	6.34%	5.94%	5.54%	4.75%	3.95%	3.55%	3.16%
Bloomberg Municipal 5-year Index	3.64 years	8.49%	7.58%	6.67%	4.85%	3.03%	2.12%	1.21%
Bloomberg Municipal 10-year Index	5.82 years	11.26%	9.80%	8.35%	5.44%	2.53%	1.07%	-0.38%
Bloomberg Municipal Bond Index	6.65 years	12.68%	11.02%	9.36%	6.03%	2.71%	1.04%	-0.62%
Bloomberg US Treasury Index	5.91 years	9.82%	8.34%	6.87%	3.91%	0.96%	-0.52%	-2.00%

Source: Bloomberg, as of October 31, 2025. The Bloomberg Municipal 1–3-Year Index is an unmanaged index of municipal bonds with a remaining maturity of one to three years. The Bloomberg Municipal 5-Year Index is an unmanaged index of fixed-rate, investment-grade municipal securities with maturities of four to six years. The Bloomberg Municipal 10-Year Index is the eight to 12-year maturity component of the Bloomberg Municipal Bond Index. The Bloomberg Municipal Bond Index is an unmanaged index considered representative of the tax-exempt bond market. The Bloomberg US Treasury Index is represented by the public obligations of the US Treasury. Treasuries 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. An investment cannot be made in an index. **Past performance is no guarantee of future results.**

Tax-equivalent yield assumes a top tax rate of 40.8%: 37% federal tax rate and 3.8% net investment income tax (NIIT), effective Jan. 1, 2025. Irs.gov, as of October 22, 2024. Top marginal tax rate for single taxpayers with more than \$626,350 in taxable income or couples with \$751,600 or more. NIIT is the net investment income tax investment income for single taxpayers with more than \$200,000 in taxable income or couples with \$250,000 or more.

Spread is the difference between yields on differing debt instruments, calculated by deducting the yield of one instrument from another.

Duration is a measure of a bond fund's price sensitivity to changes in interest rates. It takes into account mortgage prepayments, puts, adjustable coupons and potential call dates.

Yield to Worst is calculation that considers coupon, price, and any callability features the bond might have, including a worst-case yield scenario if a bond will be called before maturity.

A basis point is a unit that is equal to one one-hundredth of a percent.

Sources:

1. Federal Reserve, as of January 29, 2025.

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.

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 October 31, 2025, unless otherwise stated.

All data provided by Invesco unless otherwise noted.

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