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For Debt Stability and Tax Exemption, Consider Muni Bond ETFs.

With the tax deadline around the corner, it's not too late to start thinking about next year by adding tax-free municipal bonds through assets like the Vanguard Tax-Exempt Bond ETF (VTEB).

VTEB tracks the Standard & Poor's National AMT-Free Municipal Bond Index, which measures the performance of the investment-grade segment of the U.S. municipal bond market. MUB seeks to track the investment results of the S&P National AMT-Free Municipal Bond IndexTM, which also measures the performance of the investment-grade segment of the U.S. municipal bond market.

The sampling approach means that both funds hold a subset of bonds within the index in order to replicate the yield, duration, and credit quality of the debt. This method allows the funds to avoid trading expensive bonds that could harm performance and, in addition, minimize tracking errors.

"Under normal circumstances, at least 80% of the fund's assets will be invested in securities whose income will be exempt from federal income taxes and the federal alternative minimum tax," the Vanguard website noted. "Risks of the fund include the fact that changes in interest rates can affect the fund by resulting in lower bond prices (when interest rates go up) or an eventual decrease in income for the fund (when rates decline). Investors who are looking for a fund that may provide federal tax-exempt income and can tolerate moderate price and income fluctuations may wish to consider this fund."

Soaring Demand for Municipal Bonds

Despite economic progress, many fixed income investors may still be hesitant to add more risk with corporate bonds. As such, demand for municipal debt has been high.

Whether investors are searching for more yield, debt that has a lesser likelihood of default, or diversification in their fixed income, they're obviously seeing something they like in municipal bonds.

"Investors in search of higher returns and lower taxes are scooping up debt sold by state and local governments, pushing borrowing costs to near-record lows and boosting coffers from California to Connecticut," a Wall Street Journal report said.

"Investors have poured a net \$39 billion into municipal-bond mutual funds this year through Thursday (May 6), according to data compiled by Municipal Market Analytics, the most over the same period since 2008," the article added. "Returns on the debt, which local governments use to fund public works such as sewers or bridges, have beaten those of corporate bonds and Treasuries."

ETF TRENDS

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