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Munis Offer Benefits Beyond Tax-Free Income.

Municipal bonds are lauded for the tax-free income they can provide to fixed income investors. A closer look under the hood shows the tangible impact muni sales can provide to the communities that benefit from the funding.

“Municipal bond issuers are responsible for building and supporting the physical infrastructure and the public goods and services that enable citizens to participate more in an inclusive economy,” an Alliance Bernstein report said. The report noted the U.S. muni bond market comprises roughly $4 trillion. That can help fund their respective goals for local communities.

“Challenges like supplying clean water and improving access to quality healthcare can both be tackled through environmentally, socially, and financially productive investments in communities and institutions,” the report added.

Of course, the prime benefit of munis is the tax-free income they can offer that’s beneficial for investors in higher income tax brackets. Rather than opt for a variety of muni bond holdings, an easier way is via one ETF: the well-diversified Vanguard Tax-Exempt Bond ETF (VTEB).

The fund 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. Overall, this index includes municipal bonds from issuers, primarily state or local governments or agencies whose interests are exempt from U.S. federal income taxes, and the federal alternative minimum tax.

Of course, a prime goal for fixed income investors, especially in a year in which rate cuts could happen, is extracting the highest yield in the current macroeconomic environment. To that note, VTEB brings a yield of 3.39% (as of April 2).

A Short-Term Bond ETF Solution
The anticipation of rate cuts puts investors on notice that they may need to lock in rates now before the Federal Reserve loosens monetary policy. To mitigate rate risk, a short-term solution is an option. And if investors want to maintain exposure to municipal debt, Vanguard has a solution.

Investors will want to take a closer look at the Vanguard Short-Term Tax-Exempt Bond ETF (VTES), which can also offer the aforementioned tax benefits. The fund tracks the S&P 0-7 Year National AMT-Free Municipal Bond Index. That index is designed to balance the need for tax efficiency with the need for tax-exempt yield. This balance can translate to potentially higher yields than those afforded by competing strategies, for an appropriate level of duration risk.

As of April 2, the 30-day SEC yield of VTES is 2.95%.

ETF TRENDS

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