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Taxable Munis: The Overlooked Corner of the Market That Deserves a Second Look

When advisors think about municipal bonds, the conversation almost always centers on tax-exempt bonds — and for high-bracket clients, that focus is entirely justified. The tax math favors it, and the yield advantage of the exemption is meaningful at current rates. But taxable municipal bonds represent a growing and often misunderstood segment of the $4.4 trillion muni market, and for specific client situations, they can add value that the tax-exempt segment simply can't match.

The market for taxable munis has grown substantially in recent years. The segment now accounts for roughly $33 billion annually in issuance, up significantly from prior cycles. Much of the growth reflects a practical reality for issuers: certain projects that once qualified for tax-exempt financing — advance refundings, some private activity bonds — lost that status under the 2017 Tax Cuts and Jobs Act. Issuers who still needed to access capital had to do so on a taxable basis. The result is a rich and growing universe of investment-grade taxable muni bonds from high-quality state and local government issuers.

The credit profile of this segment is where things get interesting. A study comparing A-rated taxable municipal bonds to A-rated corporate bonds from 2009 through 2023 found a result that deserves more attention than it typically gets: there were zero defaults among A-rated taxable munis over the 14-year period studied. Among comparably rated corporate bonds in the same sample, there were 11 defaults. The study's author — who is also the chief investment officer for a $4.5 billion insurance company with approximately $1 billion in muni exposure — put it plainly: "I would much rather invest in the muni, both in terms of default rates and in terms of the yield that you're getting off of those."

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