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Municipal Bonds: Exempt From Taxes, Not Risks

History suggests recent muni tailwinds can quickly turn into headwinds.

Against a backdrop of broader market uncertainty, municipal-bond funds have once again demonstrated their resilience. The Morningstar US Municipal Bond Index's 5.5% one-year return through July 2026 beat most major Morningstar fixed-income indexes, and investors have taken notice. They've poured into the asset class at a near-record pace over the one-year period through June 2026, with approximately $105 billion of inflows into exchange-traded funds and mutual funds, lifting muni-bond prices and fund returns higher. And muni investors who took more credit and interest rate risk fared even better.

The temptation to chase the performance of that riskier muni cohort is understandable. After all, muni-bond funds' resiliency is rooted in several advantages—tax-exempt income, high credit quality, and historically low default rates—which make these funds a fixture in long-term portfolios. But investors looking to enter the market at this time should be vigilant, as the same forces that drove the past year's gains can quickly reverse.

Here are two funds that have thrived in the current environment by taking outsize risks relative to their muni Morningstar Category peers. Their impressive results reflect strong tailwinds, though, not necessarily enduring long-term investment edges.

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