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Trump Tax Effort Could Boost Muni ETFs.

Even against the backdrop of rising interest rates, investors have shown some signs of devotion to municipal bond exchange traded funds and that faith could be rewarded. The iShares National AMT-Free Muni Bond ETF (NYSEArca: MUB) is the largest municipal bond ETF.

Munis also help diversify fixed-income portfolios. Investors who typically follow the Barclays U.S. Aggregate Bond Index will not have municipal bond exposure, so a muni bond ETF can complement core fixed-income positions.

Municipal bonds continue to experienced robust demand from U.S. investors as reliable source of yield, especially among taxable accounts due to the debt securities' favorable tax-exempt status. Recently, Japanese investors have gobbled up U.S. munis as a way of generating income as Japan maintains negative interest rates.

Low and even negative yields on global government bonds have made U.S. assets, including munis, increasingly more appealing relative to other fixed-income assets. For example, foreign investors have increased the amount of municipal debt they hold by 44% to $85 billion from 2009 through 2015, according to the Federal Reserve.

President Donald Trump's tax reform efforts, if realized, could be a significant catalyst for municipal bonds and ETFs like MUB.

"If the plan in President Trump's new tax proposal to eliminate the deductibility of state and local taxes from Federal income tax actually becomes law (still a big "if"), municipal bonds could benefit.

Interest income from municipal bonds are still tax-free, according to the Trump administrations tax reform plans outlined Wednesday," reports Amey Stone for Barron's.

Since muni bond interest is exempt from federal taxes, muni ETFs are a good way for investors seeking tax-exempt income, especially those in higher tax brackets. Due to its tax-exempt status, the asset category is also best utilized in taxable accounts. The tax-exempt status also creates high demand for municipal bonds. Consequently, the perceived bond yields are typically lower than their taxable counterparts.

The VanEck Vectors High Yield Municipal Index ETF (NYSEArca: HYD) and SPDR Nuveen S&P High Yield Municipal Bond ETF (NYSEArca: HYMB) can be used for investors looking for some extra yield in their muni ETF allocations.

"Muni prices could get dampened due to the proposal to drop the top tax rate, which in theory should make munis less attractive to high-net worth investors. But even if the tax-equivalent yield falls a bit, munis are still more attractive than other fixed-income options, analysts from Goldman Sachs wrote earlier this month," according to Barron's.

ETF Trends

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