Second Half Tailwinds for Municipal Bonds.

After a strong start to 2021, more tailwinds could keep the momentum going for municipal bonds and the Vanguard Tax-Exempt Bond ETF (VTEB).

The expectation of higher taxes next year could spur a flight to municipal bonds in the second half of 2021. Thus far, the threat of inflation and potentially higher rates hasn't turned investors away from municipal bond products.

"During the first half of the year, municipal bonds (munis) shrugged off the rise in long-term U.S. interest rates and crushed their taxable counterparts," an Advisor Perspectives article noted. "Expectations for higher taxes in 2022 that could be included in a potential stimulus package have kept demand high, while muni net supply was constrained the last few months."

As the stock market continues to flux up and down on Covid news, municipal bonds can provide some level of stability. Municipal bonds are traditionally less volatile than their corporate bond counterparts.

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 Index, 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 to replicate the debt's yield, duration, and credit quality. This method allows the funds to avoid trading expensive bonds that could harm performance. It also minimizes tracking errors.

Continued Strength for Munis

Passage of the trillion-dollar infrastructure could also give municipal bonds a boost. Local government infrastructure projects are typically funded by municipal bonds.

"The driving force for the rest of the year should continue to be technical demand, driven largely by the U.S. government's fiscal plan," the Advisor Perspectives article said further. "Barring a total derailment of the infrastructure and social-stimulus packages, we can expect this demand to stay high and muni yields to remain tight to Treasuries, with returns approximating muni market yields. Any strong selloff in munis is likely to quickly snap back as investors jump in to capture value."

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