Bond Case Briefs

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Investor Jitters or Legitimate Concerns? Decoding the State Revenue Decline and Its Impact on Municipal Bonds.

Municipal bonds are typically seen as a boring fixed income sector. Volatility and defaults are both low. So, when any type of risk begins to grow, it tends to make investors nervous. And right now, a major risk is starting to brew.

The cash that helps pay for muni bond coupons—state and local revenues/taxes—is starting to slip.

But should investors actually be concerned or is this just a case of the boy who cried wolf? Is the recent dip in state revenues the start of a worrisome trend? The data suggests that it may not be a real concern.

Trending Lower

Taxes. They are the lifeblood of state and local governments. States rely on income taxes for about 40% of revenues and sales taxes for more than 35% of total revenues. Without this cash flowing in, they can't pay for essential services and expansion plans. They also can't pay their debts. Normally, this isn't a worry and muni bonds feature some of the lowest default rates of any bond type. But when something upends the apple cart of taxes, investors start to take notice. And that's just what is happening today.

State and local governments' revenues are starting to slide.

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