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Why Municipal Bonds Are Worthy Core Holdings for Investors.

Tax-exempt bonds have acquitted themselves well through the ups and downs of recent years.

I received a piece of reader feedback after publishing *For Investors Who Can Get Beyond Headline Risk, Opportunity Beckons in Bonds* that was as actionable as it was succinct. “What about municipals?” wrote in a longtime Morningstar.com reader. Fair question. In an article focused on calendar-year returns for Morningstar’s fixed-income indexes, I had neglected the “tax-exempt” market.

The truth is, we at Morningstar are in the mode of thinking of municipals differently. We separate out “Municipal Bond” from “Taxable Bond” in our monthly analysis of asset flows and in research like the Morningstar Diversification Landscape Report. Muni-bond yields are lower because of their tax exemption, so they are something of a different animal.

That said, municipal bonds play a foundational role in many investor portfolios, including mine. In the previous article’s quilt chart depicting calendar-year returns for Morningstar’s fixed-income indexes, we compared wildly different investment types, from the fixed-rate Morningstar US Core Bond Index to the floating-rate Morningstar LSTA US Leveraged Loan Index. So why not examine the tax-exempt market through the lens of the Morningstar US Municipal Bond Index?

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