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Municipal Bond Outlook: Why Carry Is the Strategy

LPL Research outlines how a Fed on hold, strong reinvestment demand, and elevated yields create compelling opportunities in municipal bonds.

Demand continues to outpace record supply. Municipal bonds remain an attractive income opportunity in a market where the Federal Reserve (Fed) is likely to remain on hold and carry is driving returns. Despite record issuance of roughly $50 billion per month, demand has remained strong, supported by a reinvestment wave that is running approximately 40% above last year and favorable summer technicals.

The yield curve favors intermediate maturities. Within the market, the yield curve presents the clearest opportunity, with nearly 100 basis points of steepness from 1 to 30 years, making the intermediate maturities particularly compelling due to their combination of attractive yield, roll-down potential, and lower long-end volatility.

Credit quality warrants closer attention. At the same time, the exceptionally strong municipal credit environment of recent years is beginning to fade as pandemic-era fiscal support dissipates, downgrades increase, and performance dispersion widens across issuers.

Continue reading.

LPL Research

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