

Taxable munis stand out in volatile markets

Taxable municipal bonds proved their resilience in the first quarter of 2026, outperforming other fixed income asset classes despite sharp rate moves and rising geopolitical uncertainty. With yields near historic highs, solid credit fundamentals and limited supply, we believe the case for municipals is strong.

Key takeaways

- Active sector selection in health care and transportation may capture additional yield that we believe more than adequately compensates investors for the underlying credit risk.
- Rebounding demand and limited supply are expected to favor municipal total returns through year end.
- The shape of the taxable muni yield curve, with narrowing yields featured on the long end, may reward investors who favor intermediate dated bonds.

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

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High yields and damped volatility define the outlook

A strong municipal rally early in the first quarter reversed course as geopolitical risks escalated. Surging investor demand drove total returns of 2.63% through February, but rising rates in March pared those gains, leaving the quarter at 0.43% — still meaningful outperformance versus other fixed income asset classes, including U.S. Treasuries.

In our view, investors have not missed the muni rally, and recent weakness in the asset class may offer an opportunity to increase exposure at attractive valuations.

Taxable municipal yields are currently in the top quartile of their 10-year history. The Bloomberg Taxable Municipal Bond Index yielded 4.94% at quarter end versus the Bloomberg U.S. Aggregate Bond Index at 4.57%.

Municipal bonds finance essential services, which can provide insulation from economic downturns. This dynamic showed clearly in the first quarter. Corporate spreads widened 22 basis points (bps) from intra-quarter tightens before partially retracing, finishing the quarter 11 bps wider. Taxable municipal spreads tightened 2 bps for the quarter after widening only 7 bps in early March. That relative stability — combined with similar or better yield — presents a compelling investment opportunity.

Transportation and health care sectors present relative value

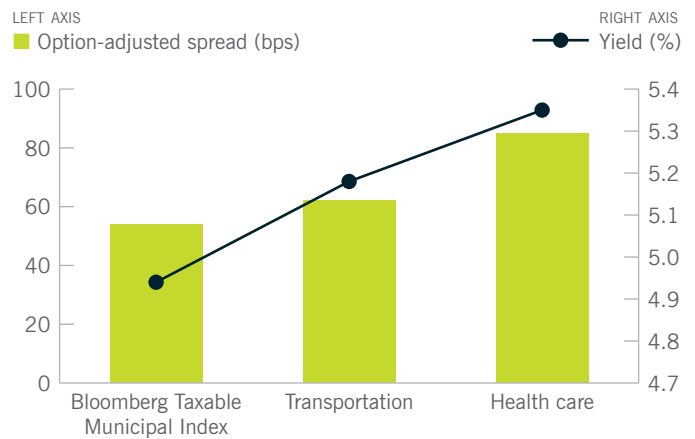
We believe transportation and health care stand out as relative value opportunities, offering wider option-adjusted spreads and higher absolute yields compared to the Bloomberg Taxable Municipal Index average.

Transportation currently offers an option-adjusted spread of approximately 62 bps and an absolute yield of 5.18%, while health care offers a spread of approximately 85 bps and a yield of 5.35%. Both compare favorably to the index average spread of 54 bps and yield of 4.94% (Figure 1).

Limited new issuance creates a technical tailwind

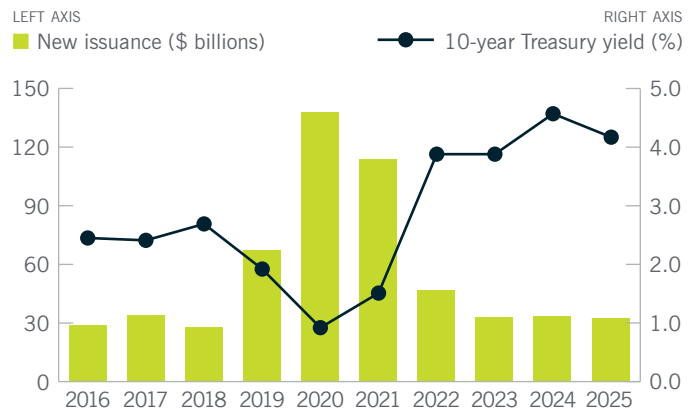
While overall new issue supply is running ahead of 2025's large calendar, the taxable municipal story is different. Issuance of \$5.9 billion is down 14% year-to-date, supporting a favorable technical backdrop. We do not anticipate meaningful supply increases until rates fall sustainably, which would give issuers greater refunding opportunity (Figure 2).

Figure 1: Transportation and health care stand out for yield and spread opportunity



Data source: Bloomberg, L.P., 31 Mar 2026. Performance data shown represents past performance and does not predict or guarantee future results. Option-adjusted spread measures the spread between a fixed-income security and the risk-free rate, adjusted to account for the value of those options. Yield to worst is the lowest potential yield that can be received on a bond without the issuer actually defaulting.

Figure 2: Elevated yields are suppressing taxable municipal supply



Data source: Bloomberg, L.P., 31 Dec 2025. Performance data shown represents past performance and does not predict or guarantee future results.

Taxable municipal issuance totaled \$32 billion in 2025, and we forecast flat issuance versus the prior year in 2026. New issue deals have historically offered a meaningful spread concession over secondary purchases, compounding into additional returns over time.

General purpose, single- and multi-family housing and health care led taxable issuance through the first quarter. Higher education issuance dropped 30% from elevated first-quarter 2025 levels, reflecting federal tax policy uncertainty that preceded passage of the tax bill later in the year.

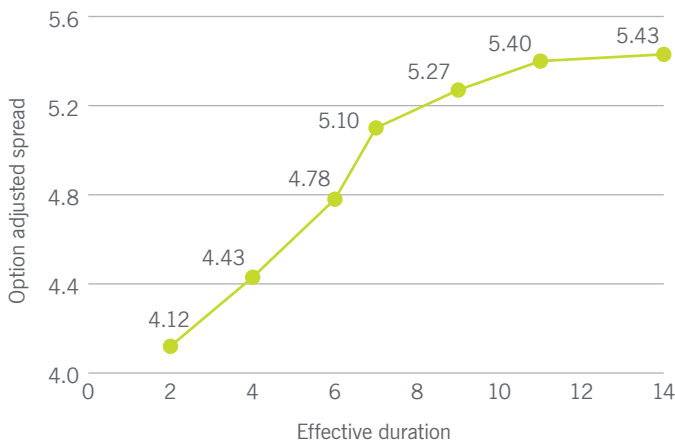
Muted supply should sustain favorable technical conditions through year end. Demand should continue to accelerate, supported by high starting yields, more favorable currency hedging costs and solid credit fundamentals.

The yield curve rewards intermediate-duration positioning

The taxable municipal yield curve is steep from years two through eleven but flattens meaningfully for duration profiles longer than eleven years (Figure 3).

Limited long-end issuance and strong insurance company demand for long-duration paper drive this dynamic. We see attractive yield opportunities in the seven-to-eleven-year duration range, where yields exceed 5%.

Figure 3: The taxable municipal yield curve is nearly flat for durations beyond eleven years



Data source: Bloomberg, L.P., 31 Mar 2026. Performance data shown represents past performance and does not predict or guarantee future results. Representative index: Bloomberg Municipal Index Taxable Bonds Total Return Index Value (Unhedged). Option-adjusted spread measures the spread between a fixed-income security and the risk-free rate, adjusted to account for the value of those options. Effective duration measures a bond's price sensitivity to interest rate changes, specifically accounting for embedded options.

Strong credit fundamentals support the asset class

We favor state and local governments with strong credit profiles, as well as water, sewer and electric utilities, which tend to demonstrate resilience across economic cycles.

State and local governments maintain robust liquidity, with median rainy day fund balances projected to reach 14% by fiscal year end 2026, up from a pre-pandemic average of 8%. Total state and local tax revenue increased 5.4% in 2025, broadly outpacing individual state projections, as most states took a conservative budget approach in anticipation of federal policy and funding uncertainties.

Fiscal year 2027 budget season is well underway. While many proposed state and local budgets reflect deficits, we view these as opening positions rather than final outcomes. Many state and local governments are constitutionally required to pass balanced budgets and have several levers available, including raising tax rates, instituting new taxes, reducing expenditures and drawing down reserves.

New York City's preliminary FY27 budget illustrates this process well. The mayor identified an initial \$5.4 billion gap and proposed two closing scenarios; the city council will offer an alternative, followed by months of hearings and budget negotiations. A compromise is expected by the early July deadline. Strong liquidity, revenue-raising capacity and expenditure flexibility support credit resilience in tax-backed sectors despite headline volatility.

Revenue sectors can be more vulnerable to economic shifts, and we favor those that function as essential service monopolies. Water and sewer, electric utilities, and transportation are prime examples. Water and sewer issuers generally demonstrate strong liquidity and debt service coverage and have rate-setting powers that allow them to adjust user charges over time. We believe sectors that combine operational stability with pricing flexibility are well-positioned to navigate both economic and geopolitical uncertainty.

Outlook: Positioning for opportunity in the second quarter

We believe the taxable municipal market offers compelling opportunities despite near-term volatility. We suggest investors stay invested and use any short-term market dislocations as potential entry points at attractive valuations.

The inverted spread curve makes intermediate duration profiles — particularly in the 7 to 11-year range — an effective way to capture additional yield without extending duration. Selective allocation to health care and transportation bonds may further reward patient investors, as wider relative spreads enhance their near-term attractiveness while elevated income potential supports long-term total return.

Sector fundamentals diverge amid shifting federal policy

The muni sector scorecard shows our views on credit fundamentals, momentum and valuations for major municipal sectors (Figure 4).

Figure 4: Muni sector score card

	+	=	-	
	Positive	Neutral	Negative	
SECTOR	CREDIT FUNDAMENTALS	CREDIT MOMENTUM		KEY TAKEAWAY
State & local governments	=	=		Steady tax revenue growth and strong reserves provide cushion against possible economic slowdown and federal policy uncertainty.
Education	=	-		Pressure due to increased competition for students and affordability coupled with federal policy changes. Large universities will be able to navigate, smaller colleges likely to struggle.
Transportation	+	=		Airport cash balances are healthy and passenger demand remains well above pre-pandemic peak levels, though emerging uncertainty around higher oil prices could impact travel. Capital investment is needed to expand capacity.
Housing	+	=		Need for affordable housing bolsters demand. Labor supply constraints due to immigration policy shifts may delay projects.
Water & sewer utilities	+	=		Essential service, monopolistic providers with robust liquidity will continue to require significant capital investment.
Health care	=	=		Elevated labor and supply costs are normalizing. Most hospitals will adapt to federal Medicaid policy changes coming in 2027. Smaller, rural hospitals may struggle.

Data source: Nuveen, 28 Feb 2026. Certain statements may be deemed forward-looking statements. Please note that any such statements are not guarantees or intended to constitute a prediction of any future performance; actual results or developments may differ materially from those projected.

Five themes are shaping our approach in 2026

	What's happening?	Market implications	Actions to consider
Low money market rates unlock cash rotation	\$7.5T in sidelined cash may move toward higher-yielding assets	Positive flows historically coincided with positive muni returns 79% of the time over the last decade	Position in high-quality munis; lock in yields, particularly with intermediate duration bonds
Opportunities are still available through new issue concessions	2026 issuance is projected at a record ~\$600B overall, while taxable municipal supply should remain limited	Muted supply creates favorable technical tailwind for taxable municipals	Capitalize on potential new issue concessions; apply rigorous credit research to identify value
Flat long-end yield curve rewards intermediate duration positioning	The taxable municipal yield curve flattens significantly beyond eleven years in duration	Investors extending beyond eleven years capture little additional yield, making the risk-return tradeoff unattractive	Concentrate exposure in the 7-11 year duration range to capture the steepest part of the curve without taking on unnecessary duration risk
Federal policy shifts create differentiation opportunities	The One Big Beautiful Bill Act reduces federal support for states, hospitals, universities and utilities	Policy headlines drive volatility; muni tax exemption survived, limiting broad market damage	Selectively add top-tier health care and higher education credits; monitor spread volatility
Record reserve levels anchor credit resilience	Most municipal borrowers enter 2026 with reserves at historic highs and recession-tested revenue sources	Credit deterioration is unlikely broadly, but downgrades may rise in policy-exposed sectors	Focus on transportation and water/sewer utilities which have shown resiliency during market downturns

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For more information, please visit nuveen.com.

Endnotes

Sources

Gross Domestic Product: U.S. Department of Commerce. Treasury Yields and Ratios: Bloomberg (subscription required). Municipal Bond Yields: Municipal Market Data. Open-end fund flows: Investment Company Institute. Municipal Issuance: Siebert Research. Defaults: Municipals Weekly, Bank of America/Merrill Lynch Research. State Revenues: The Nelson A. Rockefeller Institute of Government, State Revenue Report. State Budget Reserves: Pew Charitable Trust. Global Growth: International Monetary Fund (IMF) and the Organisation for Economic Co-operation and Development (OECD). Standard & Poor's and Investortools: <http://www.invttools.com/>. Flow of Funds, The Federal Reserve Board: <https://www.federalreserve.gov/releases/z1/default.htm>. Payroll Data: Bureau of Labor Statistics. Bond Ratings: Standard & Poor's, Moody's, Fitch. New Money Project Financing: The Bond Buyer. State revenues: U.S. Census Bureau.

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Taxable-equivalent yields are based on the highest individual marginal federal tax rate of 37%, plus the 3.8% Medicare tax on investment income. Individual tax rates may vary. Inflation rate used is the PCE Deflator, which is removed from the after tax income of the 3 month T-bill yield, resulting in an after tax and after inflation rate for cash.

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