The Week in Muniland

November 3, 2025

Don't Be Spooked by the Fed

Key Takeaways

1. **Volatility in the US Treasury market slowed down the muni market.**
2. **The long end of the muni curve continues to offer significant value.**
3. **The FOMC cut its benchmark rate and announced the end quantitative tightening.**

The muni market posted slightly negative performance this week in large part due to volatility in the US Treasury market. Two, 10- and 30-year AAA muni yields rose two, three and five basis points (bps), respectively. The Bloomberg Municipal Bond Index (the Index) returned –0.07% last week, bringing year-to-date returns to 3.91%.

- **Why it matters:** Although the muni market posted negative returns last week, the month of October posted a strong 1.24% return. More impressive was how long-maturity bonds materially outperformed short-maturity bonds. For example, the Bloomberg 20-year index posted a return of +2.18%, while the Bloomberg 3-year index posted a return of –0.14%. Even more impressive, since August 29, the 20-year index is up 6.15%, while the 3-year index is flat (*Display 1*). From a credit perspective, there hasn't been a notable difference in performance. Month to date, the Bloomberg AAA muni index is up 1.22%, compared to 1.30% for the Bloomberg BBB index. Year to date, the AAA index is up 3.88%, versus 3.65% for the BBB index. High yield, which is very idiosyncratic, nevertheless is up 0.98% for the month and 2.29% for the year to date. We believe muni high yield will perform well going forward, but that will more likely be from a duration perspective than from a material narrowing of credit spreads.

In our opinion, the long end of the municipal yield curve continues to offer the most value and opportunity.

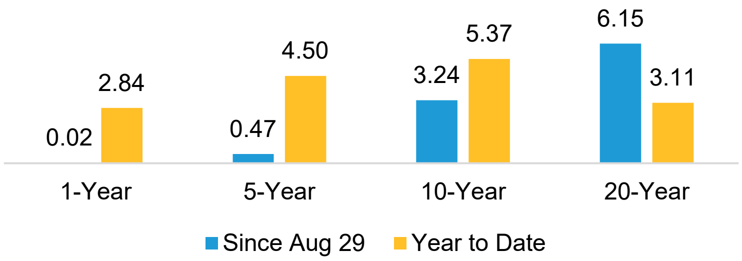
- **Why it matters:** Long-maturity municipals continue to look compelling, even following the rally that began August 29. Given the steepness of the muni yield curve (*Display 2*), we anticipate that the yield curve will continue to flatten and long-maturity bonds will outperform short-maturity bonds. An illustration of potential returns can be seen in *Display 3*. If yields fell by just 50 bps over the next 12 months, the 20-year index would return 8.61%, significantly outpacing the 4.69% return of the 5-year index. For those investors sitting on cash, preferred cash rates are beginning to fall and are paying in the low-to-mid 3% range. On an after-tax basis, that yield declines to 1.75%–2.0%. Cash investors should consider adding duration. Even hopping out to a 2.5-year duration strategy could provide a tax-exempt yield of 3%, which is significantly higher than after-tax cash rates, with not much in the way of interest-rate risk. Sometimes a jump to intermediate-duration bonds is too far for investors. So consider advising a baby step to short duration, and as the client gains comfort, perhaps consider intermediate duration, which is better equipped to take advantage of the steep yield curve.

The Federal Open Market Committee cut its benchmark policy rate by 25 bps to a range of 3.75%-4.0%. The committee also decided to end the reduction of its Treasury holdings (quantitative tightening, or "QT") as of December 1.

- **Why it matters:** In his press conference, Chair Jerome Powell did not give clear guidance about the path forward for rates. Powell also said that "a further reduction in the policy rate at the December meeting is not a foregone conclusion; far from it." Given that the market is pricing for a cut in December, his remarks were clearly intended to be hawkish—to push back on the market's pricing with certainty on what is still an uncertain outcome. That doesn't mean that the Fed won't cut in December, only that it isn't as set on that outcome as the market seems to be. That said, Chair Powell also described this recent cut as "another step toward neutrality," which suggests that there is more easing to come eventually, so the message was not uniformly hawkish. In recent weeks, Fed speakers, including Chair Powell, have begun to hint that balance sheet reduction was nearing its end. Thus, the decision to stop reducing Treasury holdings was not a surprise. The Fed will continue to reduce its holdings of mortgage-backed securities (MBS), but maturing MBS proceeds will be reinvested in T-bills, helping the Fed move back toward its desired Treasuries-only balance sheet.

Displays of the Week: November 3, 2025

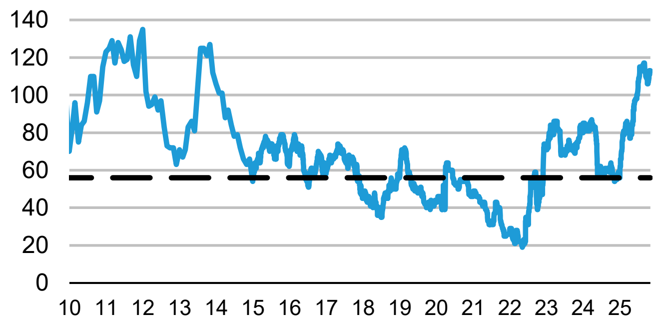
Display 1: Returns by Maturity (Percent)



Long-maturity municipals have returned over 6% since August 29!

As of October 31, 2025. Source: Municipal Market Data and AllianceBernstein (AB)

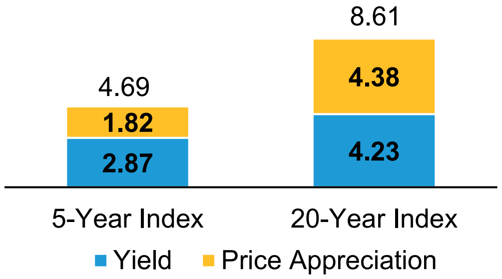
Display 2: 10s/20s Municipal Yield-Curve Slope (Basis Points)



The yield curve is as steeps as it's been since 2014.

As of October 31, 2025. Source: Municipal Market Data and AB

Display 3: 12-Month Hypothetical Return if Yields Fall Just 50 Basis Points

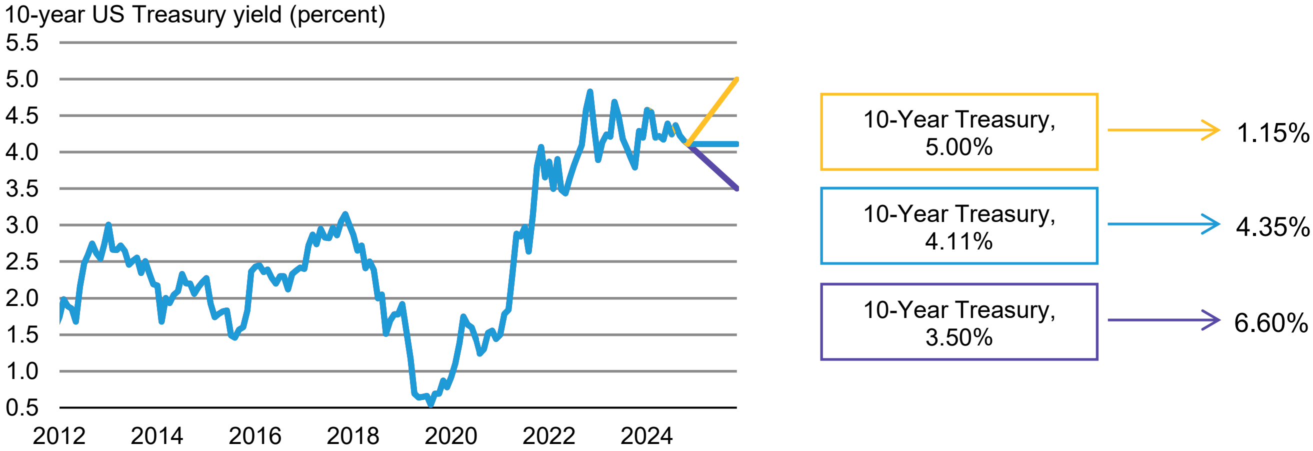


Long-maturity bonds offer more potential for a higher return as yields fall.

Based on respective Bloomberg indices
As of October 31, 2025. Source: Bloomberg and AB

Display 4: Expected 12-Month Municipal Returns Scenario Analysis

10-year US Treasury yield (percent)



Past performance and historical analysis do not guarantee future results.
Display reflects expected returns of the Index under three scenarios:
10-year US Treasury yields rise to 5.00%, remain the same or decline to 3.50% over the next 12 months.
As of October 31, 2025. Source: Bloomberg and AB

The views expressed herein do not constitute research, investment advice or trade recommendations, and do not necessarily represent the views of all AB portfolio-management teams. Views are subject to change over time.

A Word About Risk

Market Risk: The market values of the Portfolio's holdings rise and fall from day to day, so investments may lose value. **Interest-Rate Risk:** Fixed-income securities may lose value if interest rates rise or fall—long-term securities tend to rise and fall more than short-term securities. The values of mortgage-related and asset-backed securities are particularly sensitive to changes in interest rates due to prepayment risk. **Credit Risk:** A bond's credit rating reflects the issuer's ability to make timely payments of interest or principal—the lower the rating, the higher the risk of default. If the issuer's financial strength deteriorates, the issuer's rating may be lowered, and the bond's value may decline. **Inflation Risk:** Prices for goods and services tend to rise over time, which may erode the purchasing power of investments. **Foreign (Non-US) Risk:** Investing in non-US securities may be more volatile because of the political, regulatory, market and economic uncertainties associated with such securities. These risks are magnified in securities of emerging or developing markets. **Currency Risk:** If a non-US security's trading currency weakens versus the US dollar, its value may be negatively affected when translated back into US-dollar terms. **Diversification Risk:** Portfolios that hold a smaller number of securities may be more volatile than more diversified portfolios, since the gains or losses from each security will have a greater impact on the Portfolio's overall value. **Derivatives Risk:** Investments in derivative instruments such as options, futures, forwards or swaps can be riskier than traditional investments and may be more volatile, especially in a down market. **Leverage Risk:** Trying to enhance investment returns by borrowing money or using other leverage tools magnifies both gains and losses, resulting in greater volatility. **Municipal Market Risk:** Debt securities issued by state or local governments may be subject to special political, legal, economic and market factors that can have a significant effect on the Portfolio's yield or value. An investor cannot invest directly in an index. **Investment and Insurance Products:** Not FDIC insured I Not a bank deposit I Not insured by any federal government agency I No bank guarantee I May lose value