

# Municipal Bond Investor Weekly

High Net Worth Wealth Solutions and Market Strategies // Fixed Income Solutions



**Julian Johnson**

Director  
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## THE WEEK AHEAD

1. FOMC meets Tues/Wed with post-meeting press conf. What will be Chairman Powell's message. We are expecting higher for awhile longer than most expected, but lower longer term.
2. Plenty of economic numbers this week, including the all important April Jobs report on Friday. Underlying data suggests weakening.
3. How confident are consumers in driving the economy? Find out on Tuesday when the Conference Board releases its latest survey.



**DREW O'NEIL**

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## MONDAY'S COMMENTARY

Market Discounts – Nothing to Trifle With  
Illustrative Portfolios

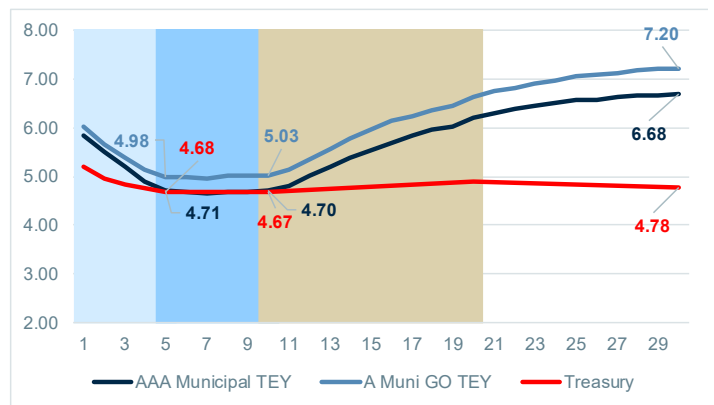
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## THE NUMBERS THIS WEEK

This week munis and Treasuries continued to move higher by 3-6 basis points across the curve. **Opportunity focus is in 20 - 30 years** where AAA muni taxable equivalent yields are more than 100 to almost 200 basis points better than Treasuries on the long end. We can create customized solutions with **Current Yields** greater than 4.00%. See our illustrative portfolios on page 3.

Year		Treasury	Municipal (AAA)	Municipal (A)	Municipal TEY* (AAA)	Municipal TEY* (A)	Muni (AAA)/Tsy Ratio	Muni TEY* (AAA)/Tsy Ratio
1	2025	5.21	3.46	3.56	5.85	6.01	66%	112%
2	2026	4.96	3.25	3.35	5.50	5.66	66%	111%
5	2029	4.68	2.79	2.95	4.71	4.98	60%	101%
10	2034	4.67	2.78	2.98	4.70	5.03	60%	101%
20	2044	4.89	3.68	3.93	6.21	6.65	75%	127%
30	2054	4.78	3.96	4.26	6.68	7.20	83%	140%

\*Taxable equivalent yield @ 40.8% tax rate



## Market Discounts on Munis are Nothing to Trifle With

With interest rates recently moving higher, more municipal bonds are now trading at a discount, particularly longer dated bonds. No time like the present to revisit the tax implications of purchasing **market discount bonds**. Exactly what is market discount? It's when a municipal bond is purchased in the secondary market when its maturity value is greater than its price at acquisition.

As we all know, interest income produced by municipal bonds is generally excluded from gross income for federal income tax purposes. However, many investors are not aware that under certain circumstance, there can be potential tax ramifications from purchasing market discount bonds. Welcome to the land of de minimis.

Determining if a secondary market discount purchase is de minimis will regulate whether that bond's accretion is taxed as a capital gain or ordinary income. The de minimis rule states if a discount is less than a quarter-point (0.25% of face value of the bond) for each full year from the date of purchase to maturity, then the discount is considered de minimis and is treated as a capital gain, not ordinary income. To determine approximate de minimis threshold on a municipal bond, we can use the following formula:

- **Multiply the face value by 0.25% (0.0025)** and **multiply the result by the number of full years between the discounted bond's purchase date and maturity date**. Subtract that amount from the bond's par value.

Municipal bond (100,000 face value) with 10 full years remaining until maturity

$$100 \times .0025 = .25$$

$$.25 \times 10 = 2.50$$

$$100 - 2.5 = 97.50$$

Purchasing a bond using the example at or above 97.50 should result in a capital gain. Alternatively, any purchase below 97.50 would be reported as ordinary income. **In either case, it will affect the "net-yield" on the bond due to additional tax liability.** It is critical investors consult their tax advisor before reporting these types of events. De minimis is relevant anytime discount bonds are trading in the secondary market.

The municipal market continues to provide very attractive relative yields and investors should not fear or completely ignore purchasing market discount bonds. **They simply need to proceed with caution.** An investor in highest federal tax bracket could be significantly impacted on an after-tax basis by not considering de minimis thresholds when purchasing bonds.

**Example:** Aa2/AA/AA New York City GO 3.00% coupon due 03/01/2041 is offered at a yield of a 4.52% YTM (82.212), a significant discount to par. Based on the calculation above the de minimis threshold price would be \$96.00. In this example the bond is being offered at a price well below \$96.00 at 82.212, the total accretion from \$82.212 to \$100.00 would be taxed as ordinary income. As a result, the investor would not realize the quoted 4.52% YTM, because of the income tax they would pay when their bond matures. Assuming an investor is in the highest federal tax bracket, their approximate after-tax yield (ATY) would be around 4.18% YTM --- **still attractive, but not as attractive give the additional tax liability.**

At Raymond James, we follow a best execution policy to ensure our clients receive a fair and reasonable price for their fixed income investments. Our trading platform allows us to assess the de minimis information for each offering. If an offering is not deemed to be fair and reasonable vs current market conditions, our traders will provide an alternative for consideration. **Taxes are nothing to trifle with** --- your financial advisor along with your tax advisor --- and our fixed income professionals --- can help you navigate the opportunities in today's market with discount bonds.

***This commentary was written to provide general information about the de minimis rule. It is not tax advice, and we are not tax advisors. We encourage all investors to consult with their tax advisors to review how this rule could affect your individual investment decision.***

## ILLUSTRATIVE PORTFOLIOS – April 29, 2024

Our illustrative proposals reflect three opportunities along the yield curve with bonds maturing from 1 to 30 years. Municipal and Treasury yields moved higher by 3 – 6 basis points. Long term investors will continue to realize additional yield further out on the curve. Strategically, to lock in long-term, reliable tax-efficient cash flow, our duration focused 10–20-year maturity illustration continues to offer an excellent tax efficient solution. **Looking to maximize yield?** The 20 – 30-year range continues to offer an additional ~70+ basis points (over 10 – 20 years) and may be appropriate for some investors. The yield to worst is ~4.25%, which equates to a **taxable equivalent yield to worst of ~7.20%** for an investor in the top federal tax bracket and subject to the net investment income tax. If the callable bonds are not called, the yield to maturity increases to ~4.40%, which equates to a **taxable equivalent yield to maturity of ~7.40%**. This is a solution with 4-5% coupon bonds with an average coupon of 4.31% and a market price of ~\$98.34. The **current yield is ~4.30%**. An investment with \$1 million par value (~\$0.992 million market value, average price below par) will generate a federally tax-exempt annual coupon cash flow of ~\$43,125.

## National Municipal Bond Illustrative Portfolios

Week of April 29, 2024

### 1 – 10 Years

Totals & Averages @ Market	
Summary Totals	
Original Face	\$1,000,000
Current Face (Par)	\$1,000,000
Market Principal	\$1,051,277
Accrued Interest	\$10,700
Cash & Cash Alternatives	\$0
-	-
-	-
Total Portfolio Value	\$1,061,977
Next 12mo Cpn Cash Flow	\$43,000
Generic Annual Cpn Cash Flow	\$43,000
Weighted Averages	
Coupon*	4.300%
Maturity**	5.74 yrs
Duration	3.94
Yield to Worst	3.203%
Yield to Maturity	3.400%
Market Price*	105.128
Tax Lots Holdings Included	20 of 20

### 10 – 20 Years

Totals & Averages @ Market	
Summary Totals	
Original Face	\$1,000,000
Current Face (Par)	\$1,000,000
Market Principal	\$1,056,546
Accrued Interest	\$12,358
Cash & Cash Alternatives	\$0
-	-
-	-
Total Portfolio Value	\$1,068,904
Next 12mo Cpn Cash Flow	\$45,089
Generic Annual Cpn Cash Flow	\$45,000
Weighted Averages	
Coupon*	4.500%
Maturity**	14.58 yrs
Duration	6.72
Yield to Worst	3.577%
Yield to Maturity	3.922%
Market Price*	105.655
Tax Lots Holdings Included	20 of 20

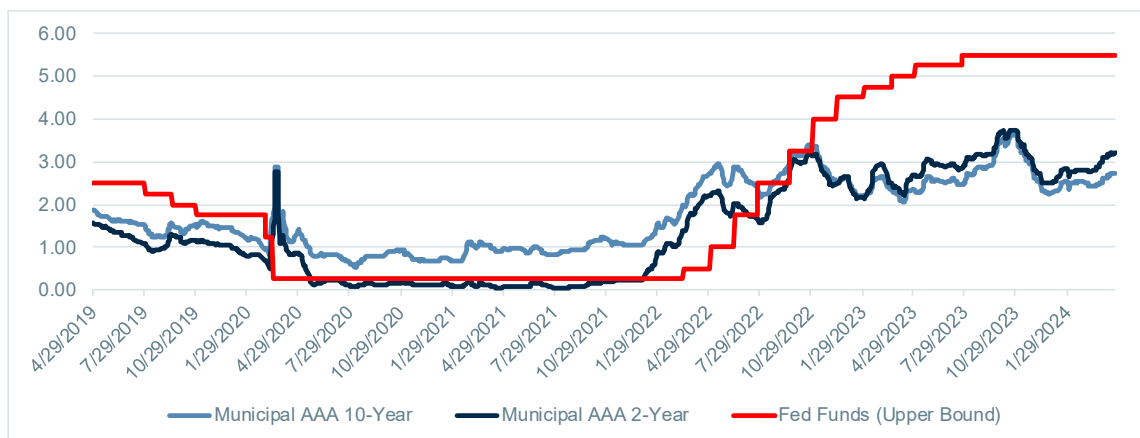
### 20 – 30 Years

Totals & Averages @ Market	
Summary Totals	
Original Face	\$1,000,000
Current Face (Par)	\$1,000,000
Market Principal	\$983,422
Accrued Interest	\$9,526
Cash & Cash Alternatives	\$0
-	-
-	-
Total Portfolio Value	\$992,948
Next 12mo Cpn Cash Flow	\$43,234
Generic Annual Cpn Cash Flow	\$43,125
Weighted Averages	
Coupon*	4.313%
Maturity**	24.68 yrs
Duration	12.23
Yield to Worst	4.259%
Yield to Maturity	4.424%
Market Price*	98.342
Tax Lots Holdings Included	20 of 20

## NAVIGATING TODAY'S MARKET

This week's primary new issue market totals approximately \$7 billion. Multiple states are issuing housing bonds at very attractive levels. See calendar below for additional information.

HISTORICAL YIELDS



Date	Amount	Issuer	ST	Description	Moody's/S&P/Fitch	Maturity
4/29	\$39MM	State of Oregon Housing and	OR	Mortgage Revenue Bonds (Single -Family	Aa2 /NR /NR	
4/29	\$42MM	State of Oregon Housing and	OR	Mortgage Revenue Bonds (Single -Family	Aa2 /NR /NR	
4/29	\$0MM	Michigan State Housing	MI	Rental Housing Revenue Bonds, 2024		
4/29	\$116MM	Illinois Housing Development	IL	Revenue Bonds 2024 Series C (Non-Amt)	Aaa / /	04/01/2025-
4/30	\$136MM	Virginia Resources Authority	VA	(Virginia Pooled Financing Program)	Aaa /AAA /	11/1/24-54
5/2	\$20MM	Mifflin County School District	PA	General Obligation Bonds, Series of 2024		tbd
5/2	\$24MM	Carillo USD	CA	General Obligation Bonds, Election of		

This offering calendar is for information purposes only, and is not intended as an offer for solicitation with respect to the purchase or sale of any securities. For more information on the new issues go to [www.raymondjames.com](http://www.raymondjames.com).

There is no assurance any of the trends mentioned will continue or forecasts will occur. Investing involves risk and investors may incur a profit or a loss. Past performance may not be indicative of future results. Prior to transacting in any security, please discuss the suitability, potential returns, and associated risks of the transaction(s) with your Raymond James Financial Advisor.

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Sourced from Bloomberg: Treasuries: US Fed H15 CMT Curve - The H15 curve is comprised of the constant maturity treasury rates as published daily by the Federal Reserve in the H15 report. Municipal (AAA): BVAL Municipal AAA Yield Curve (Callable) - The curve is populated with high quality US municipal bonds with an average rating of AAA from Moody's and S&P. The yield curve is built using non-parametric fit of market data obtained from the Municipal Securities Rulemaking Board, new issues, and other proprietary contributed prices. The curve represents 5% couponing. The 3 month to 10 year points are bullet yields, and the 11 year to 30 year points are yields to worst for a 10-year call. Municipal (AA): US General Obligation AA Muni BVAL Yield Curve - The BVAL curve is populated with pricing from uninsured AA General Obligation bonds. Municipal (A): US General Obligation A+ A A- Muni BVAL Yield Curve - The BVAL curve is populated with pricing from uninsured A+, A, and A-rated General Obligation bonds. Fed Funds (Upper Bound): The federal funds rate is the short-term interest rate targeted by the Federal Reserve's Federal Open Market Committee as part of its monetary policy. US Treasury securities are guaranteed by the US government and, if held to maturity, generally offer a fixed rate of return and guaranteed principal value. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance.

The illustrative portfolios are intended as a starting point for a conversation on individual bonds. They are not intended as specific recommendations and bonds are shown for illustration purposes only. The bonds listed in the illustrative portfolios are rated A or better, with average ratings from Moody's and Standard and Poor's of Aa2 / AA. The yields shown in the proposals are based on pricing models, not current market offers. Yields shown are indicative of general market levels but are not a guaranteed result. Prices and yields are not inclusive of any fees or commissions.

US Treasury securities are guaranteed by the US government and, if held to maturity, generally offer a fixed rate of return and guaranteed principal value. The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ. The NASDAQ Composite is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance.

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