

Executive Summary

- **2025 performance:** Municipal bonds, as represented by the Bloomberg U.S. Municipal Bond Index, delivered a 4.25% return, driven almost entirely by yield as market prices remained flat.¹ After adjusting for tax-exempt status for the top tax bracket, returns rose to 7.36%, comparable to other fixed-income sectors.
- **Supply dynamics:** Issuance reached a record \$579 billion in 2025, up 14% year over year and 30% above the 10-year average. Elevated supply is expected to persist due to deferred maintenance, inflation-driven cost increases, exhausted COVID-related funds, and potential federal policy changes impacting climate, education, and healthcare funding.²
- **2026 outlook:** Issuance is likely to remain high – in the \$510 billion to \$550 billion range – but possibly slightly below 2025 levels. We expect favorable yields and a potentially more accommodative U.S. Federal Reserve (Fed) to support demand and attractive tax-adjusted returns. Credit conditions are becoming more differentiated, requiring rigorous analysis, particularly in healthcare, higher education, transportation, and general obligation (GO) bonds.

2025 Review

Returns – Yields are back

The Bloomberg U.S. Municipal Bond Index delivered a return of 4.25% in 2025. At first glance, the municipal market appears to have materially underperformed other fixed-income asset classes, which posted total returns between 6.00% and 8.00%.

However, a deeper analysis of total return (yield return + market return) reveals that nearly all of this performance is attributable to yields, while market returns remained flat for the year – making 2025 a year for coupon-clipping. Because municipal yields are generally tax-exempt, investors should adjust performance to account for taxation. When adjusting the yield component for the top tax bracket, the municipal market's 2025 return rises to 7.36%,³ aligning more closely with other fixed-income sectors.

In 2025, the municipal market faced heavy supply, creating a performance headwind. Nevertheless, strong demand absorbed the elevated issuance. Investor flows continued into this high-quality asset class, as municipals remained among the highest-yielding fixed-income sectors, offering tax-equivalent yields above 5.00%.

¹ Unless otherwise indicated, all data cited is sourced from Bloomberg as of Dec. 31, 2025.

² Any forecasts, figures, opinions, or investment techniques and strategies set out are for informational purposes only. There is no assurance any estimate,

Supply – The new supply reality is here

The trend of heavy issuance that began in 2024 persisted through 2025 and is expected to remain in place for the foreseeable future. State and local governments surpassed the record of \$507 billion of issuance set in 2024, issuing \$579 billion of new debt in 2025, representing 14% year-over-year growth, and 30% above the 10-year average.

Following the post-COVID period of annual issuance declines from 2021 to 2023, 2024 marked a shift to a new environment of elevated supply. Both near-term and long-term factors are expected to sustain this trend, including deferred maintenance, resumption of pandemic-delayed projects, disaster resilience initiatives, and the withdrawal of federal support for essential state and local programs. If inflation remains elevated, project costs will continue to rise faster than available revenues, further incentivizing borrowing rather than reducing it.

- **Deferred maintenance:** Issuers have postponed capital projects while waiting for interest rates to decline, but a significant drop in long-term rates appears unlikely. Inflation has driven cumulative costs sharply higher for both new projects and the maintenance of existing infrastructure. Research shows that the average project cost in 2025 was 29% higher than in 2019.

forecast or projection will be realized.

³ Tax-equivalent yields equal yield to worst divided by 1 minus the tax rate. The tax rate equals the top federal tax rate of 37% plus the Medicare surcharge of 3.8%.

- **Return to the debt market:** COVID-related funds are exhausted, and a substantial portion of the Biden administration’s infrastructure funding has been clawed back. As a result, municipalities are returning to traditional debt financing for new construction projects and ongoing operations.
- **Federal policy changes:** Potential policy shifts could increase funding needs across various issuers. Areas of impact may include climate-related programs (particularly if the Federal Emergency Management Agency is phased out or curtailed), higher education (due to federal funding restrictions), and healthcare (as hospitals may need to issue more debt to offset cuts to Medicaid).

2026 Outlook

Constructive on returns, diligent on credit

Municipal issuance is expected to remain elevated in 2026. While strong supply will present technical challenges, attractive absolute yields and a potentially more accommodative Fed should likely sustain demand. The Eagle Fixed Income team anticipates attractive tax-adjusted returns for investors, supported by robust flows into municipals. However, the credit landscape is becoming increasingly differentiated, requiring careful analysis as states and local governments navigate structural fiscal pressures and shifting federal support.

The Eagle Fixed Income team expects municipal issuance to remain strong but likely to fall short of another record-breaking year in 2026, with total issuance projected between \$510 billion and \$550 billion. The record activity in 2025 likely included partial pre-funding of 2026 needs, as some issuers accelerated borrowing early in the year amid concerns that the One Big Beautiful Bill Act would curtail the tax exempt status of municipal bonds. (It didn’t.)

We expect elevated supply to continue to pose a technical headwind for municipal performance, while absolute yields remain attractive and help to sustain demand. With the possibility of a new Fed chair adopting a more accommodative stance, money market rates are expected to decline further. As investors seek yield, municipals appear poised to draw flows, supporting attractive returns on a tax-adjusted basis.

Looking ahead to the 2026 credit landscape, the team maintains an overall optimistic view of the municipal market but remains cautious on healthcare, higher education, transportation, state general obligation (GO) bonds, and local GO bonds – particularly

for school districts. Fiscal deficits in Washington, D.C., and slower growth in grants and subsidies are shifting more financial responsibility to states, especially for transportation, Medicaid administration, and climate-resilience projects. This dynamic is prompting states to explore new revenue measures, reprioritize spending, or issue additional debt to maintain essential services. For investors, this creates a more differentiated environment where rigorous credit analysis is critical: while many states and smaller municipalities remain well-positioned with strong reserves, others may face tighter budgets and increased reliance on capital markets to preserve fiscal stability.

Sector outlook – Areas of concern



LOCAL GO (SCHOOL DISTRICTS)

- School districts have historically maintained moderate reserves and adequate margins. During the COVID pandemic, federal funding helped local governments offset rising costs. That funding is now expired, and many local governments feel the impact of higher labor and supply costs accumulated over recent years.
- Enrollment faces continued pressure from increased competition with charter and private schools, a shrinking student pool due to declining birthrates, and shifting federal policies.
- Moody’s reports that K-12 school district revenues fell by 0.5% in 2025 following the expiration of pandemic aid. Operating revenues are projected to grow by 2.1% in 2026, lagging an expected inflation rate of 2.6%. (Moody’s Ratings 2026 Outlook Public K-12 School Districts, Nov. 17, 2025.)
- Districts most at risk include those with declining populations and those that depend heavily on state aid rather than on local property taxes.
- Our team will continue to monitor our school district holdings closely, focusing on reserve levels and any signs of enrollment softening or decline. We also will remain highly selective when evaluating new school districts to add to our portfolios.



HIGHER EDUCATION

- We maintain a cautious credit selection stance in the higher education sector, which faces pressure from a shrinking student population driven by demographic shifts, federal policy changes, reduced federal research funding, and rising costs.
- While enrollment in the sector dropped during the COVID pandemic, it recovered, albeit at a slower rate. Additionally, declining birth rates since 2008 are expected to culminate in a peak of high school graduates in 2025, followed by what many refer to as a “demographic cliff.”
- Moody’s projects an overall enrollment increase of 1.5% in fall 2025, with most gains concentrated at large flagship public universities and private institutions with strong brands. (Moody’s Ratings Sector Comment, Higher Education U.S., Nov. 21, 2025.)
- Federal policy changes continue to create headwinds for the sector, including the cancellation of federal research grants, caps on indirect research cost reimbursements across agencies (subject to legal challenges), the end of Title V grants and other minority student programs, changes to student loans, and efforts to reduce international student enrollment.
- We expect operating margins to contract as revenue growth slows due to declining enrollment and rising expenses.
- Our team continually monitors the impact of federal policy shifts and remains cautious on smaller institutions, those historically reliant on international students, and institutions facing significant enrollment declines or liquidity challenges.



HEALTHCARE

- Hospitals have recovered from the weak margins of 2022 and 2023, but the pace of improvement remains slow. In the medium term, Medicaid cuts enacted by the Trump administration could reduce hospital revenues and weaken financial stability as early as 2027.

- The One Big Beautiful Bill Act will place further pressure on budgets by reducing Medicaid enrollment and lowering reimbursement rates and margins, particularly for hospitals with many Medicaid patients. In anticipation of these changes, several states have started cutting Medicaid reimbursement rates and reducing federal matching dollars.
- Many safety-net hospitals face shrinking drug savings due to uncertainty surrounding eligibility for the federal 340B Drug Pricing Program.
- Some states may expand the Affordable Care Act’s enhanced subsidies to support uninsured individuals, although implementation depends on each state’s political will and fiscal capacity.
- Cuts to National Institutes of Health research funding could also challenge healthcare systems affiliated with academic medical centers.
- Our team continues to monitor the impact of federal policy shifts and remains cautious on rural, independent, and children’s hospitals.



TRANSPORTATION

- Mass transit systems continue to face operational challenges from declining ridership, rising labor costs, and increasing maintenance expenses following the pandemic.
- Recent changes to U.S. mass transportation policy under the current administration have intensified these pressures as the government froze or canceled previously approved funding for numerous transit projects.
- State and local funding also faces economic and political obstacles. Agencies will continue to struggle if they lack sources of dedicated tax revenue growth – such as sales or income taxes – that offset losses in fare revenues.
- Ports and airports maintain strong financial positions and can help mitigate policy risks related to tariffs. Toll road facilities remain stable.
- Given ongoing federal funding uncertainty, our team favors issuers with robust state or local funding sources and sufficient liquidity.

Disclosures

Investing involves risk, including risk of loss. Past performance does not guarantee future results.

Any forecasts, figures, opinions, or investment techniques and strategies set out are for informational purposes only. There is no assurance any estimate, forecast or projection will be realized.

Risk Information

Risks associated with Fixed Income investing: Many investors consider bonds to be “risk free” investment vehicles. Historically, bonds have indeed provided less volatility and less risk of loss of capital than has equity investing. However, there are many factors that may affect the risk and return profile of a fixed-income portfolio. The two most prominent factors are interest-rate movements and the creditworthiness of the bond issuer. Bonds issued by the U.S. government have significantly less risk of default than those issued by corporations and municipalities. However, the overall return on government bonds tends to be less than these other types of fixed-income securities. Investors should pay careful attention to the types of fixed-income securities that comprise their portfolio, and remember that, as with all investments, there is the risk of the loss of capital.

Not every investment opportunity will meet all of the stringent investment criteria mentioned to the same degree. Trade-offs must be made, which is where experience and judgment play a key role.

Income earned from investments in municipal bonds, while exempt from federal taxes, may be subject to state and local income taxes. All capital gains, as well as income earned from other sources, are subject to taxation. Income from municipal securities may also be subject to the Alternative Minimum Tax. Municipal securities typically provide a lower yield than comparably rated taxable investments in consideration of their tax-advantaged status. Investments in municipal securities may not be appropriate for all investors, particularly those who do not stand to benefit from the tax status of the investment. Please consult an income-tax professional to assess the impact of holding such securities on your tax liability.

Be sure to consider your financial needs, goals, and risk tolerance before making any investment decisions. Eagle does not provide legal, tax, or accounting advice. Any statement contained in this communication concerning U.S. tax matters was not intended or written to be used, and cannot be used, for the purpose of avoiding penalties under the Internal Revenue Code. Before making any investment decisions, you should obtain your own independent tax and legal advice based on your particular circumstances.

This material is a general communication being provided for information purposes only. It is educational in nature and not designed to be taken as advice or a recommendation for any specific investment product, strategy, plan feature, or other purpose in any jurisdiction. Nor is it a commitment from Raymond James Investment Management or any of its affiliates to participate in any of the transactions mentioned herein.

Definitions

340B Drug Pricing Program – A U.S. government program in which drug manufacturers participating in Medicaid agree to provide outpatient drugs to covered entities at significantly reduced prices.

Absolute yield, absolute return – The return an asset achieves over a specified period of time.

Fiscal policy – The tax collection and spending a government uses to influence its country’s economy. Fiscal deficit spending consists of government spending over a specific period of time that exceeds the revenues that the government takes in for the same period.

General obligation (GO) bonds – Municipal bonds that primarily rely on the issuer’s credit and taxing authority for repayment, as opposed to bonds in which repayment is pledged from a specific project-related revenue stream, such as tolls or user fees.

Headwind – An event or market force that hinders the prospects for performance in an individual investment or group of investments.

One Big Beautiful Bill Act – An act passed and signed into law in July 2025 that raised the U.S. debt ceiling by \$5 trillion, made permanent tax cuts created by the Tax Cuts and Jobs Act of 2017, and changed a wide range of other aspects of federal tax policy, making changes to health insurance legislation, phasing out or reducing credits for clean energy production or use, and removing tax benefits for illegal immigrants, among other things.

Tax-equivalent yield – The interest rate that a taxable bond must pay to provide the same yield as a comparable tax-exempt municipal bond.

Technicals – Indicators of historic market data, including price and volume statistics, to which analysts apply a wide variety of mathematical formulas in their study of larger market patterns.

Title V – A federal funded grant program to help specified colleges and universities in efforts to improve higher education for Hispanic students.

Total return – When measuring performance, total return is the actual rate of return of an investment or a pool of investments over a given period of time. Total return includes interest, capital gains, dividends, and distributions realized over the specified period. Total return accounts for two categories of return: income including interest paid by fixed-income investments, distributions, or dividends and capital appreciation, representing the change in the market price of an asset.

Yield to worst – A measure of the lowest possible yield that can be received on a bond with an early retirement provision. It is used to evaluate the worst-case scenario for yield at the earliest allowable retirement date. It is always less than yield to maturity as it represents a return for a shortened investment period.

Index

The Bloomberg Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market.

“Bloomberg®” and the Bloomberg Municipal Bond Index are service marks of Bloomberg Finance L.P. and its affiliates, including Bloomberg Index Services Limited (“BISL”), the administrator of the indices (collectively, “Bloomberg”) and have been licensed for use for certain purposes by Raymond James Investment Management and Eagle Asset Management. Bloomberg is not affiliated with Raymond James Investment Management or Eagle Asset Management, and Bloomberg does not approve, endorse, review, or recommend the Eagle Asset Management Fixed Income strategy. Bloomberg does not guarantee the timeliness, accurateness, or completeness of any data or information relating to the Eagle Asset Management Fixed Income strategy.