Invest locally with federally tax-free options

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Municipal bonds deliver benefits that can help you align your income goals with your personal values. With municipal bonds, you may:

- Invest in infrastructure projects that provide essential services to the communities you care about
- Generate federally tax-free income
- Preserve your capital[1]
- Diversify your portfolio's fixed income risk across the $4 trillion market[2]

1 Subject to the credit risk of the issuer.

2 There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not ensure against market risk or protect against loss in a declining market.

What are municipal bonds?

Municipal bonds, often referred to as “munis”, are issued by states, counties and municipalities to fund a wide variety of capital projects that help improve our quality of life. Since the early 1800s, munis have helped build our nation with projects like new highways and bridges, airports, schools, hospitals, libraries, and many other essential elements of our communities.

How do they work?

Muni bonds are widely available, providing investors with pre-determined interest payments called **“coupons”** that can be free of federal, state and local taxes.

They deliver those periodic payments, usually semi-annually, for a pre-determined period of time until the bond reaches its maturity date or is “called”—another word for when an issuer redeems a bond before its maturity date.

Callable muni bonds may provide investors with the call date, which is when the issuer has the right to call the bond or not.

Muni bonds are available in a range of maturities—from short term to very long term—giving investors great flexibility in how they use munis in their overall portfolios.

Return of principal

When a bond reaches its maturity date or is called, the bond issuer returns investor principal at the face value of the bond or “par value”[1], which is the price at which the bonds are originally issued. Munis are frequently issued in denominations of $5,000, but denominations may vary.

Munis can also be bought or sold at par value, or above or below par value. A bond priced above par is called a premium bond, and a bond price below par is called a discount bond. However, it’s important to understand that while periodic interest payments are made throughout the duration of the bond, the principal, or par value, is only returned at maturity.[1]

Par: Purchase $1,000 face value	▶	Receive $1,000 at maturity + periodic interest payments
Premium: Purchase $1,200 for $1,000 face value	▶	Receive $1,000 at maturity + periodic interest payments
Discount: Purchase $900 for $1,000 face value	▶	Receive $1,000 at maturity + periodic interest payments

This chart is for illustrative purposes only.

1 Subject to the credit risk of the issuer.

You have choices

Municipal bonds offer investors a wide variety of choices with many variables to consider. It's important that you read the official statement and talk to your financial advisor to understand the types of muni bonds you're considering and any associated risks.

Diversification[2]

With more than 50,000 largely recognizable issuers making up the almost $4 trillion municipal bond market,[3] there are so many choices, it may be hard to determine where to start. Understanding two types of muni bonds is a good first step:

— **General obligation (GO) bonds** make interest payments backed by revenue, generally from dedicated taxes such as property taxes. Many issuers of GO bonds have the unlimited authority to tax residents.

— **Revenue bonds** create principal and interest payments backed by specific infrastructure projects that generate revenue. Some examples within your community could include water and sewage projects, or toll roads with revenue created by user fees covering payments on the bonds.

Historically low risk

Municipal bonds often carry high credit ratings (i.e. AAA, AA) as determined by independent credit rating agencies. Historically, muni bonds have a lower default rate of approximately 0.1%[3], making them an option to diversify your fixed income portfolio and may offset other, more volatile asset classes.

Capital preservation

Investors who purchase muni bonds at par receive 100% of par at call or maturity, subject to the credit risk of the issuer.

Invest in your community and your values

Chances are, you can invest in muni bonds that provide funding for important projects in your home town or state, giving you the opportunity to support local projects that improve your quality of life and align with your personal interests, ethics, and values.

2 There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not ensure against market risk or protect against loss in a declining market.

3 Source: msrb.org

Taxable vs. tax exempt

Muni bonds are available as either taxable or tax-free investments. Income from muni bonds may be subject to the Alternative Minimum Tax (AMT). It's important to talk with your financial advisor and/or tax professional to determine which bonds may be right for you.

Tax-exempt muni bonds

With tax-exempt municipal bonds, investors can receive federal, state, and local tax-free interest payments. State and local tax exemptions may apply to residents of the same state where the bond is issued. This gives in-state investors the opportunity to support projects in areas and communities they value.

Tax-free municipal bonds are often held in taxable accounts to gain the full benefit of the tax-exempt status. For specific terms consult the official statement or a tax professional.

Power of taxable equivalent yield

Taxable bonds need to generate higher coupon payments to match tax-free muni bond payments as demonstrated in the taxable equivalent yield comparison below.

The following table illustrates tax-exempt and taxable yields. For example, the table shows that a taxpayer in the 33 percent tax bracket investing in a 3 percent tax exempt muni bond would need a taxable bond yielding 4.48 percent (assuming the bond was not purchased in a tax-deferred account).[3]

Tax-exempt yield	Investor tax bracket						
	10%	15%	25%	28%	33%	35%	39.60%
	Taxable-equivalent yield						
1%	1.11%	1.18%	1.33%	1.39%	1.49%	1.54%	1.66%
2%	2.22%	2.35%	2.67%	2.78%	2.99%	3.08%	3.31%
3%	3.33%	3.53%	4.00%	4.17%	4.48%	4.62%	4.97%
4%	4.44%	4.71%	5.33%	5.56%	5.97%	6.15%	6.62%
5%	5.56%	5.88%	6.67%	6.94%	7.46%	7.69%	8.28%

3 Source: msrb.org

Taxable municipal bonds

Taxable municipal bonds are issued by state and local governments to finance projects that do not meet the public purpose or public use tests under the IRS requirements.[3]

Usually, taxable municipal bonds offer a higher coupon than tax-exempt municipal bonds since investors are forgoing the income tax savings from a comparable tax-exempt bond. Some taxable muni bonds offer state and local income tax-exemption, with earnings still subject to federal income tax.

How can you use municipal bonds in your portfolio?

Implementing bond laddering strategies

Given the flexibility that muni bonds offer, many investors consider bond laddering strategies to generate manageable returns while actively replacing muni bonds that are called or mature.

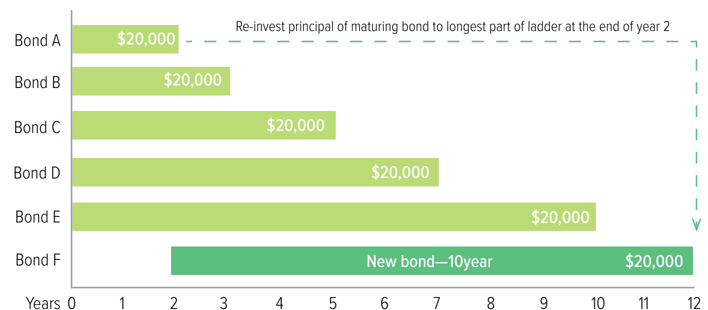
Bond laddering helps investors to minimize exposure to fluctuating interest rates and changing credit risk and be positioned to invest at potentially higher rates. Initial bond purchases are made in multiple issues with different maturity dates, which staggers the purchases like steps on a ladder.

When the first bond matures, the proceeds are reinvested in a bond with a maturity date matching the longest step of the original ladder.

In the illustration to the right, $100,000 is invested across a bond ladder—with five equal investments of $20,000 at different bond maturities from 2 to 10 years. When bond "A" matures or is called, the $20,000 principal is re-invested in a new long-term bond (F) and the ladder shifts down a step. When bond "B" eventually matures or is called, the process repeats, and so on.

Diversified portfolio with bond laddering

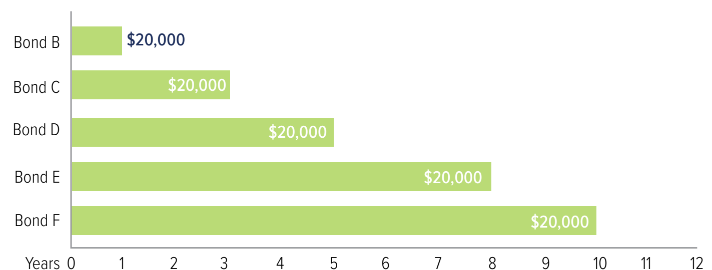
Illustration A



Staggered maturity dates art different intervals allow for reinvestment at longest point of ladder as bonds mature.

New portfolio at the end of year 2

Illustration B



These charts are for illustrative purposes only and are not indicative of any investment

Illustration A shows the initial investment of $100.000 that is split, or laddered, into five bond issues with varying maturities - 2, 3, 5, 7 and 10 years. When the 2-year bond (Bond A) matures, the principal amount is reinvested into a new bond at the longest point of the original ladder. In this example the principal was reinvested in a new 10-year bond (Bond F). **Illustration B** shows how the portfolio would be structured at the end of year 2. The goal is to qive investors the flexibility to either avoid or take advantage of chanqing interest rate and/or credit market environments.

3 Source: msrb.org

What you should know before investing in municipal bonds

Speak with your financial professional and tax advisor about the risks and suitability of municipal bonds in your portfolio.

Call risk
Some munis have call provisions, which means they can be redeemed, or paid off, at the issuer's discretion, or subject to the terms of the muni, prior to maturity. Often, an issuer will call munis when interest rates fall, potentially leaving investors unable to reinvest with similar or better terms.

Credit risk
Munis are subject to the credit risk of the issuer. If the issuer defaults on its obligations, some or all of your payments, including coupons and principal, could be at risk. Additionally, changes to an issuer's credit will generally affect the secondary market value of munis.

Interest rate risk
When interest rates rise, bond prices fall; when interest rates decline, bond prices rise. Changes in interest rates may reduce or increase the market value of munis. The longer the maturity of munis, the greater the impact changing interest rates can have on their price.

Liquidity risk
While many broker-dealers maintain an active secondary market to resell munis at prevailing market rates, there is no assurance that a secondary market will be maintained. If you sell munis prior to maturity, you may receive more or less than your original investment depending on market conditions.

Tax implications
Tax consequences of municipal bonds may depend on the particular terms of the offering. Before purchasing a muni, please consult with your tax advisor. You should also read the applicable tax risk disclosures in the offering document when considering the purchase of a muni. Income from municipal bonds may be subject to the Alternative Minimum Tax (AMT).

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