# Opportunities in the Municipal Bond Market

March 27, 2024

**Elizah McLaughlin, CFA®**
*Portfolio Manager*

**All information as of 12/31/23 unless otherwise noted.**
© 2024 FMR LLC. All rights reserved.

# Topics for Discussion

# Why Municipal Bonds

# Why Invest in Municipal Bonds?

| 1 | 2 | 3 | 4 | 5 | 6 |
|---|---|---|---|---|---|
| Potential to earn attractive amounts of after-tax income | Potential to earn attractive rates of total return | Investing in an asset class whose credit quality is generally high | Investing in an asset class whose default rates have historically been low | Potential to diversify holdings | Psychological payoff of knowing that your investment is helping to finance projects that serve the public good |



Fidelity INVESTMENTS

# Municipal Bond Overview

# Types of Municipal Bonds

| General Obligation Bonds (GOs) | |
|---|---|
| **Repayment Source** | Backed by state or local government's authority to levy taxes |
| **Common Issuers** | States, Counties, Cities, Town, School Districts |

| Revenue Bonds | |
|---|---|
| **Repayment Source** | Secured by revenue stream of a project or issuer |
| **Common Issuers** | Hospitals, Toll Roads, Airports, Public Utilities, Colleges, and Universities |

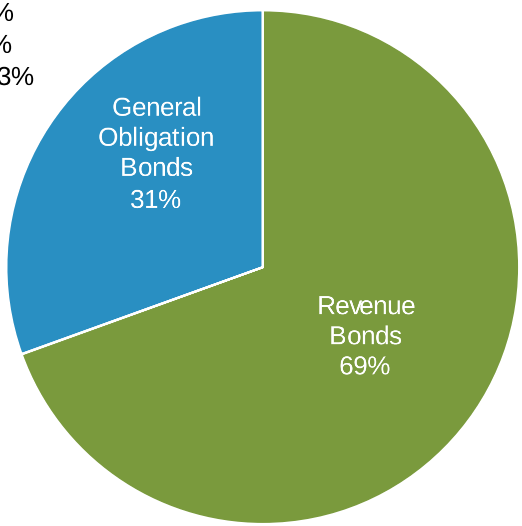
While municipal bonds are secured by either a governmental entity's taxing authority or the revenue stream of a specific project or issuer, they are not default-free, and thus are subject to credit risk.

As a result, municipal bonds and corporate bonds are often compared to one another.

# Municipal Bond Issuers and Owners

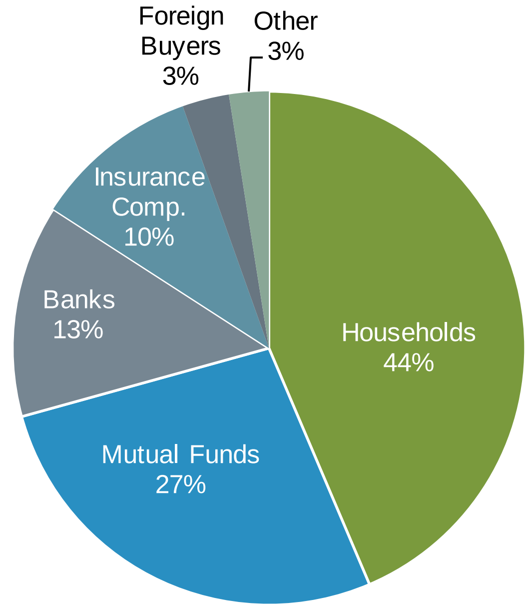
## Municipal Bond Issuers*

Local GO: 15%
State GO: 13%
Prerefunded: 3%



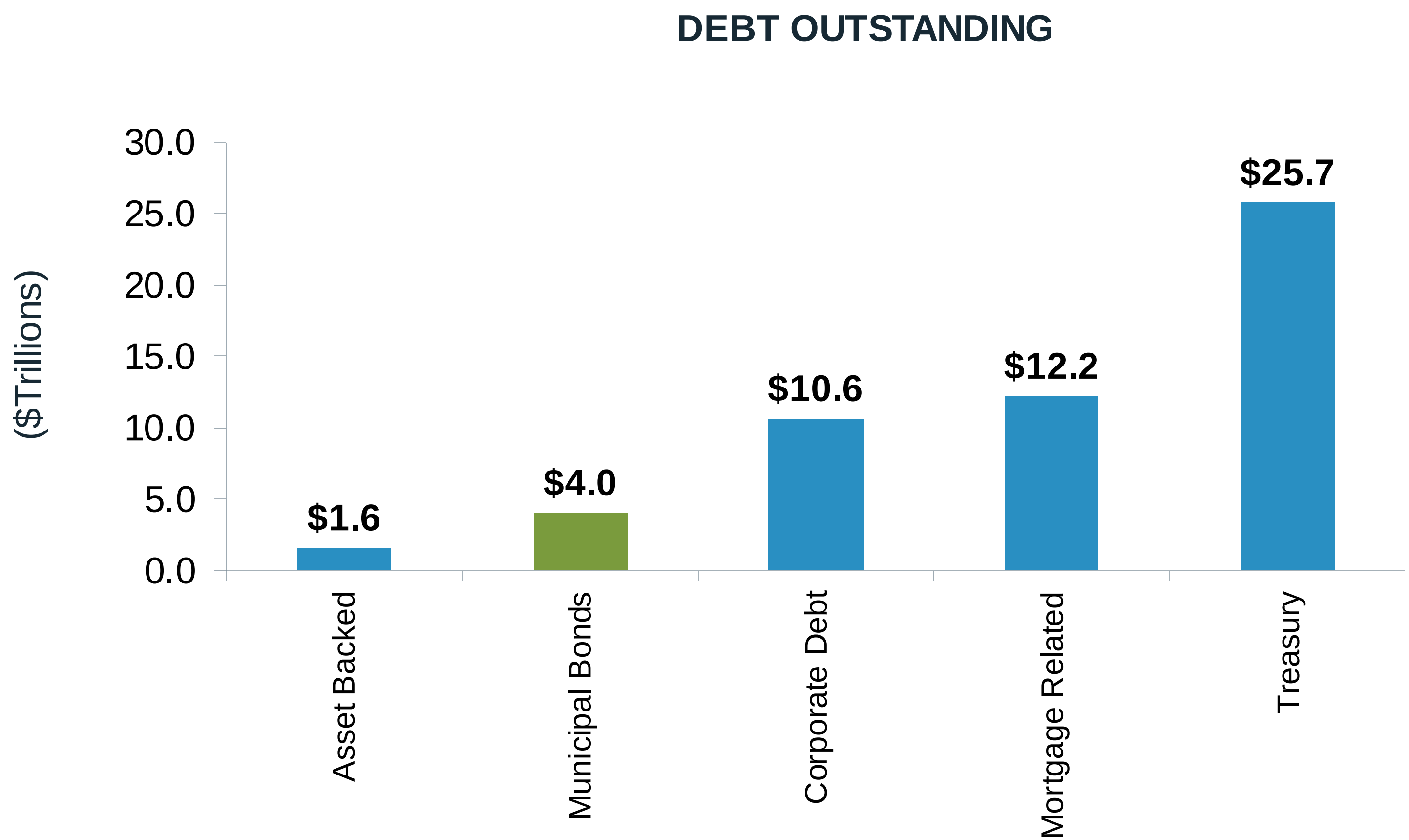

| | |
|---|---|
| Transportation: | 15% |
| Special Tax: | 10% |
| Hospital: | 9% |
| Water & Sewer: | 9% |
| Leasing: | 7% |
| Education: | 7% |
| Industrial/Corporate: | 5% |
| Electric: | 5% |
| Housing: | 3% |

## Municipal Bond Owners




* Based on the market capitalization of the Bloomberg Municipal Bond Index as of January 31, 2024.
Source: Left: Bloomberg; Right: The Federal Reserve as of Q4 2023

# Municipal Bond Market Size




Source: SIFMA Fixed Income Outstanding as of Q3 2023.

All figures are shown in USD.

# Municipal Bond & Corporate Bond Comparisons

- The municipal bond market is highly fragmented, with a large number of issuers and securities outstanding compared to other markets
- There are over 20 times as many municipal issues as there are corporate issues
- This large number of issuers and bond issues outstanding creates opportunities for active municipal bond managers

**Corporate Versus Municipal Bond Comparisons**

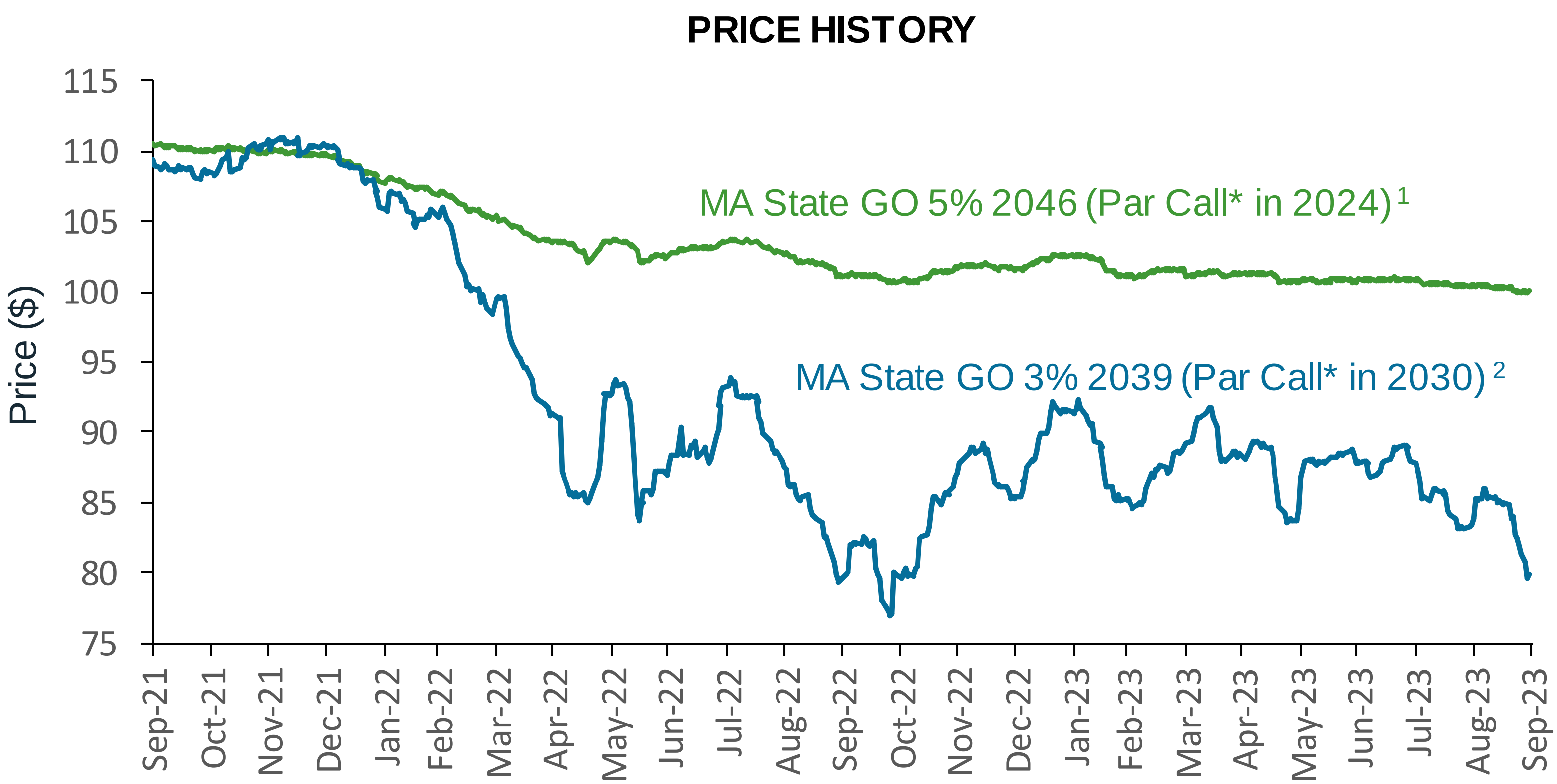
| | Corporate Bonds | Municipal Bonds |
|---|---|---|
| Market Size | $10.6 trillion* | $4.0 trillion* |
| Number of Securities | ~43,000 | ~1,000,000 |
| Daily Trading Volume | ~$53.6 billion | ~$12.5 billion |
| New Issuance Volume | $1,444 billion | $381 billion |
| Market Type | Over-The-Counter | Over-The-Counter |
| Default Rates[1] | 1.44% | 0.04% |

[1] 30-Year average of annual default rates from S&P 2022 Annual U.S. Public Finance Default Study and Rating Transitions and S&P 2022 Annual Global Corporate Default Study and Rating Transitions.

Sources: MSRB, Federal Reserve, FINRA, SIFMA, Moody's and Bloomberg Note: Calendar year 2022 data unless otherwise noted.

*Amount outstanding as of 9/30/2023

# Municipal Bonds Are Not All Created Equal




*Par Call: a provision that allows the Municipal Bond issuer to call or redeem the bond at par ($100) in the specified year, which is prior to the actual maturity date.

**Past performance is no guarantee of future results.**

For illustrative purposes only.

Notes: [1] Price reflected for CUSIP 57582RGV2 which is a Massachusetts State GO 5% coupon with a maturity of 3/1/2046 and a par call on 3/1/2024.

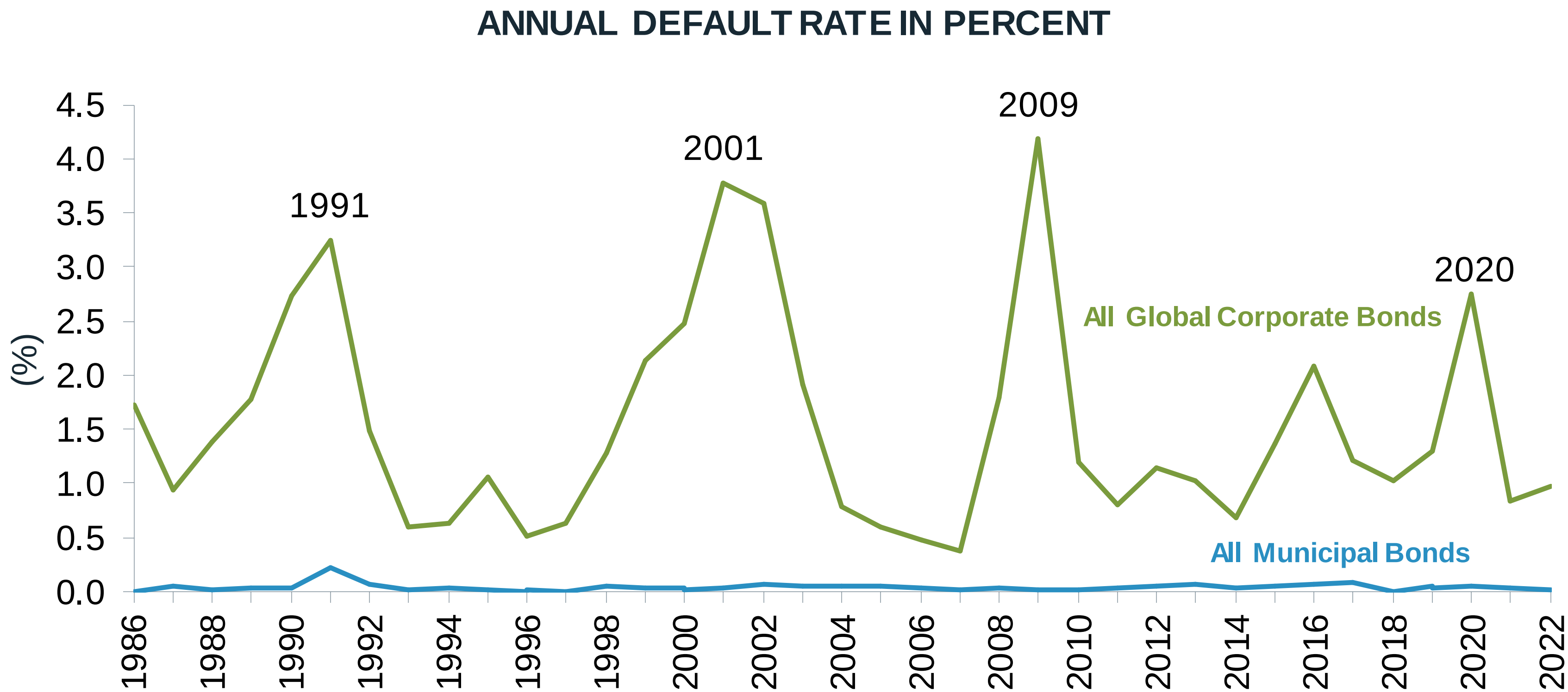
[2] Price reflected for CUSIP 57582RD29 which is a Massachusetts State GO 3% coupon with a maturity of 7/1/2039 and a par call on 7/1/2030.

Sources: Bloomberg and Fidelity as of 9/30/2023

# Municipal Bond Market Overview

## Global corporate bonds versus municipal bond default rates

- Municipal bonds have historically defaulted at a significantly lower rate than Global Corporate bonds.
- Over the past 30 years, Global Corporate bonds have experienced an average 1.5% default rate versus a 0.04% default rate for municipal bonds.



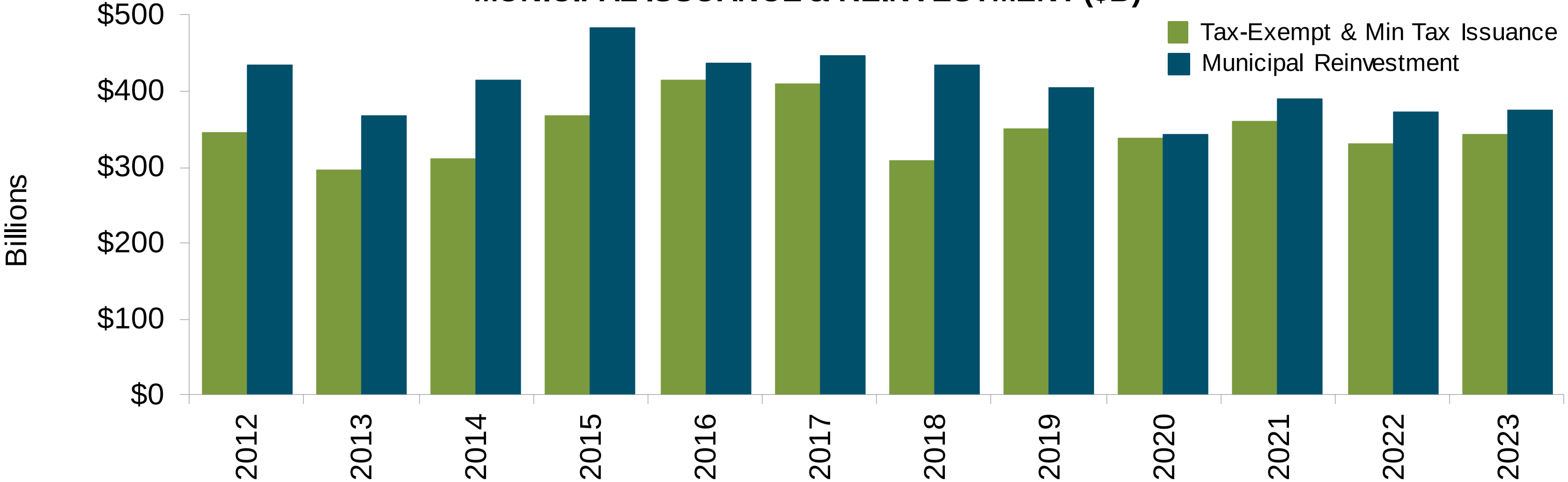

Past performance is no guarantee of future results.

Sources: S&P 2022 Annual U.S. Public Finance Default Study and Rating Transitions and S&P 2022 Annual Global Corporate Defaut Study and Rating Transitions.

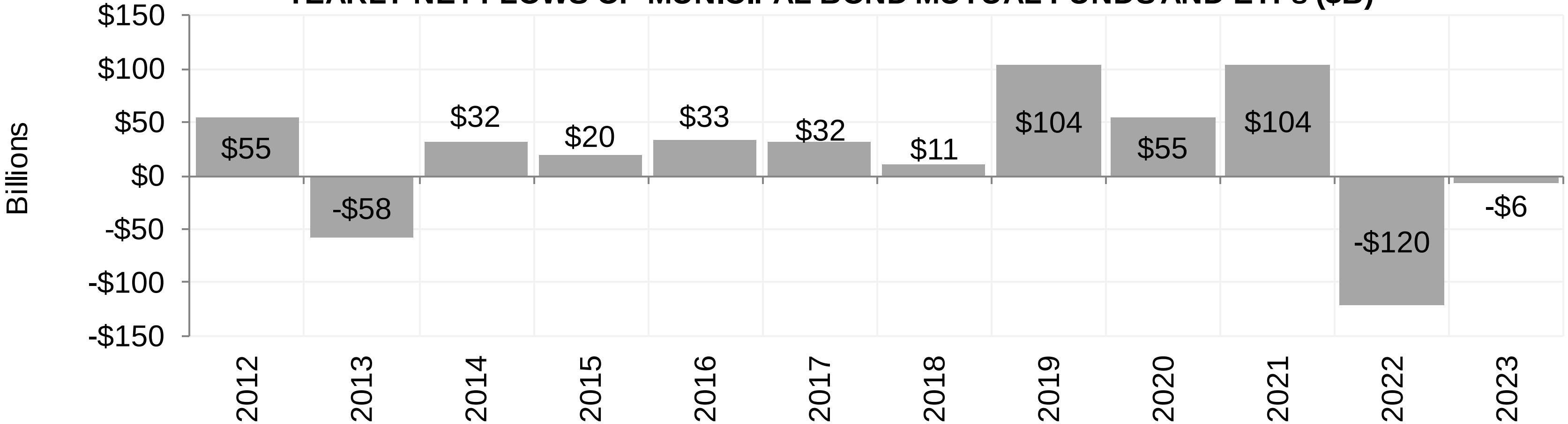
# Market Environment

# Municipal Supply & Demand

**MUNICIPAL ISSUANCE & REINVESTMENT ($B)**

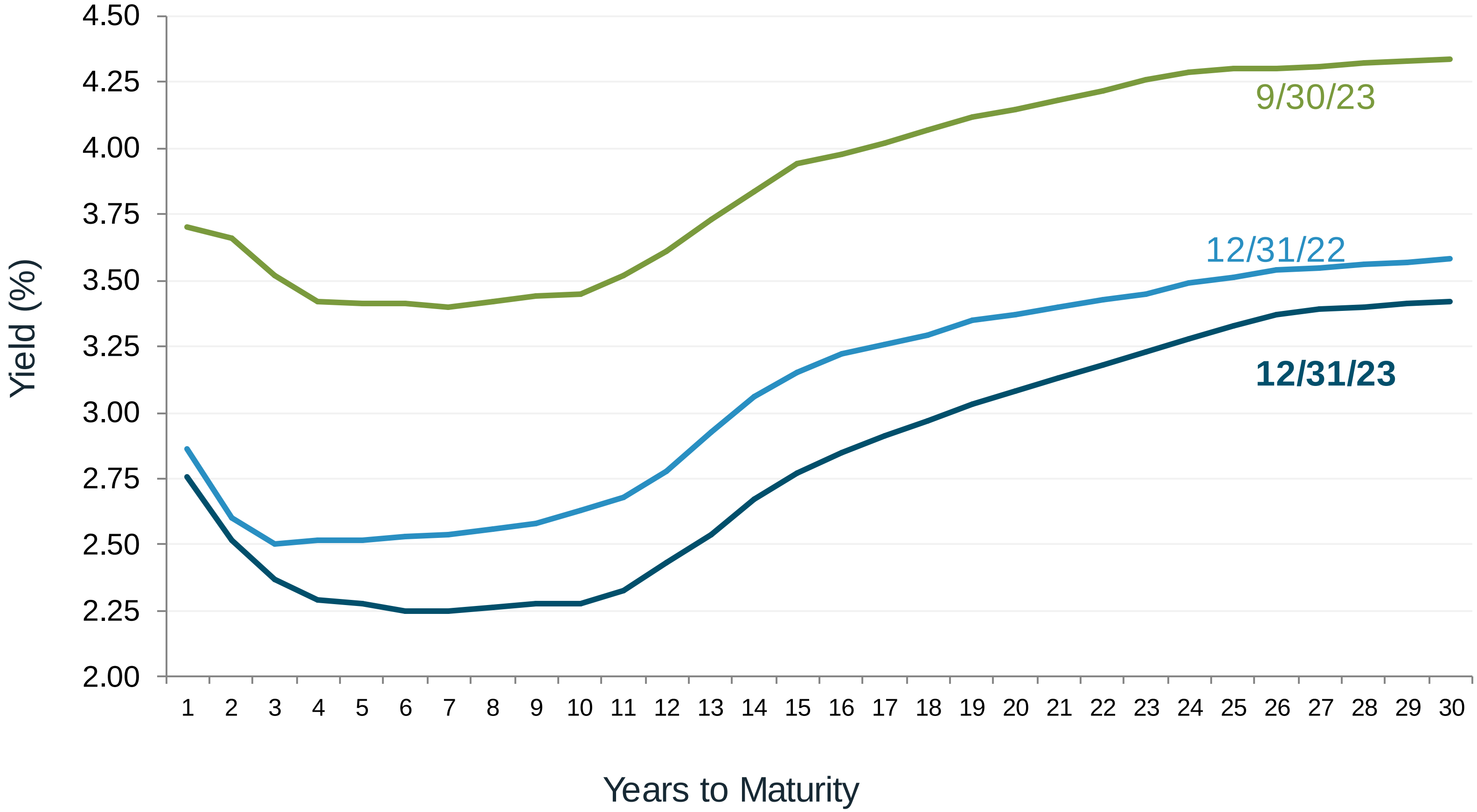



**YEARLY NET FLOWS OF MUNICIPAL BOND MUTUAL FUNDS AND ETFs ($B)**




Source: Fidelity Investments, JPMorgan, and Thomson Reuters as of 12/31/23. Morningstar Direct as of 12/31/23. Yearly Net Flows represent the aggregate total of all mutual funds and ETFs within the Morningstar Municipal Bond US Category Group

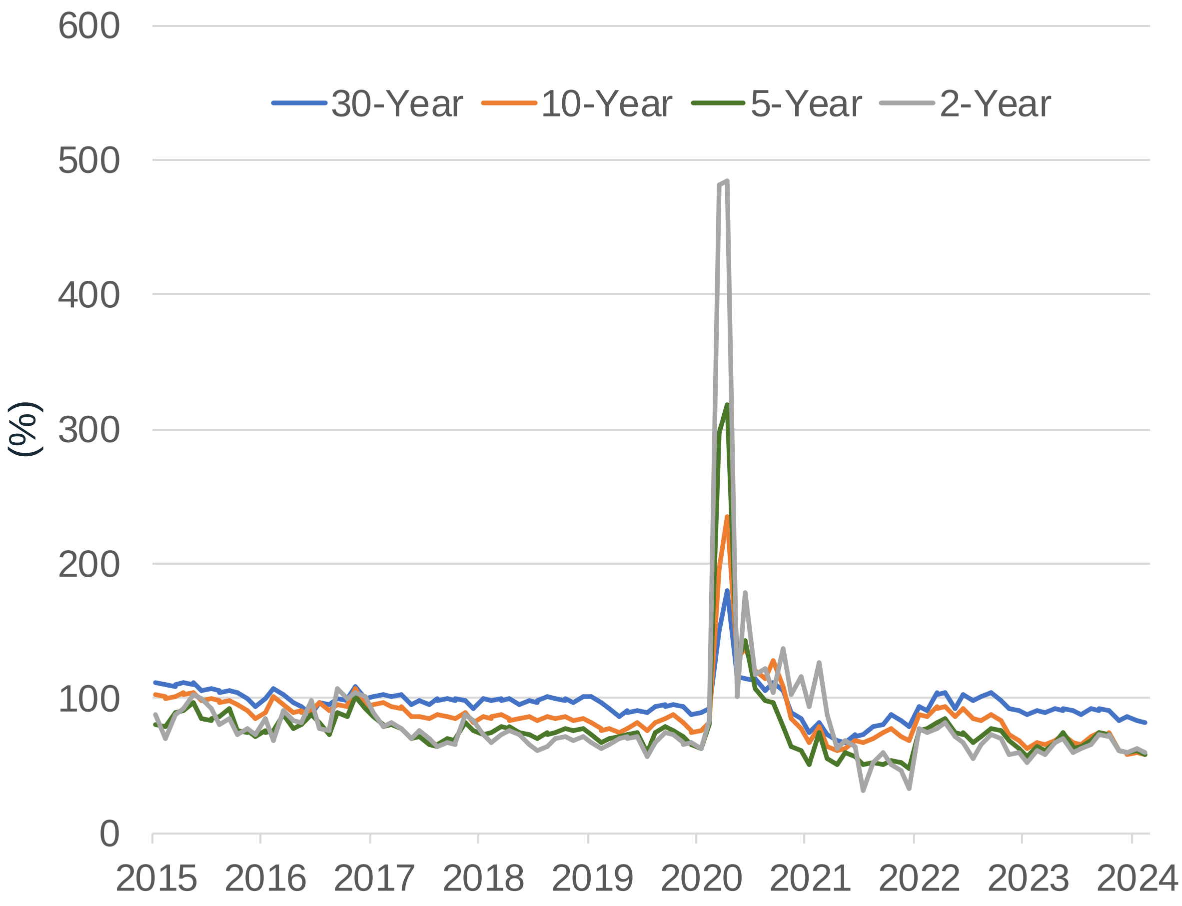
# Municipal Yields




**Past performance is no guarantee of future results.**

Source: Refinitiv (TM3) as of 12/31/23. Municipal Market Data (MMD) AAA Muni Curve.

# Municipal/U.S. Treasury Ratios*




## CURRENT AND HISTORICAL RATIOS (%)

| | 2/29/24 | 5 -Year Avg | 10 -Year Avg |
|---|---|---|---|
| 2YR | 59 | 88 | 82 |
| 5YR | 57 | 78 | 78 |
| 10YR | 58 | 84 | 88 |
| 30YR | 82 | 93 | 97 |

**Past performance is no guarantee of future results.**

*The Municipal/Treasury Ratio is a comparison of the current yield of municipal bonds to U.S. Treasuries. It aims to ascertain whether or not municipal bonds are an attractive buy in comparison.

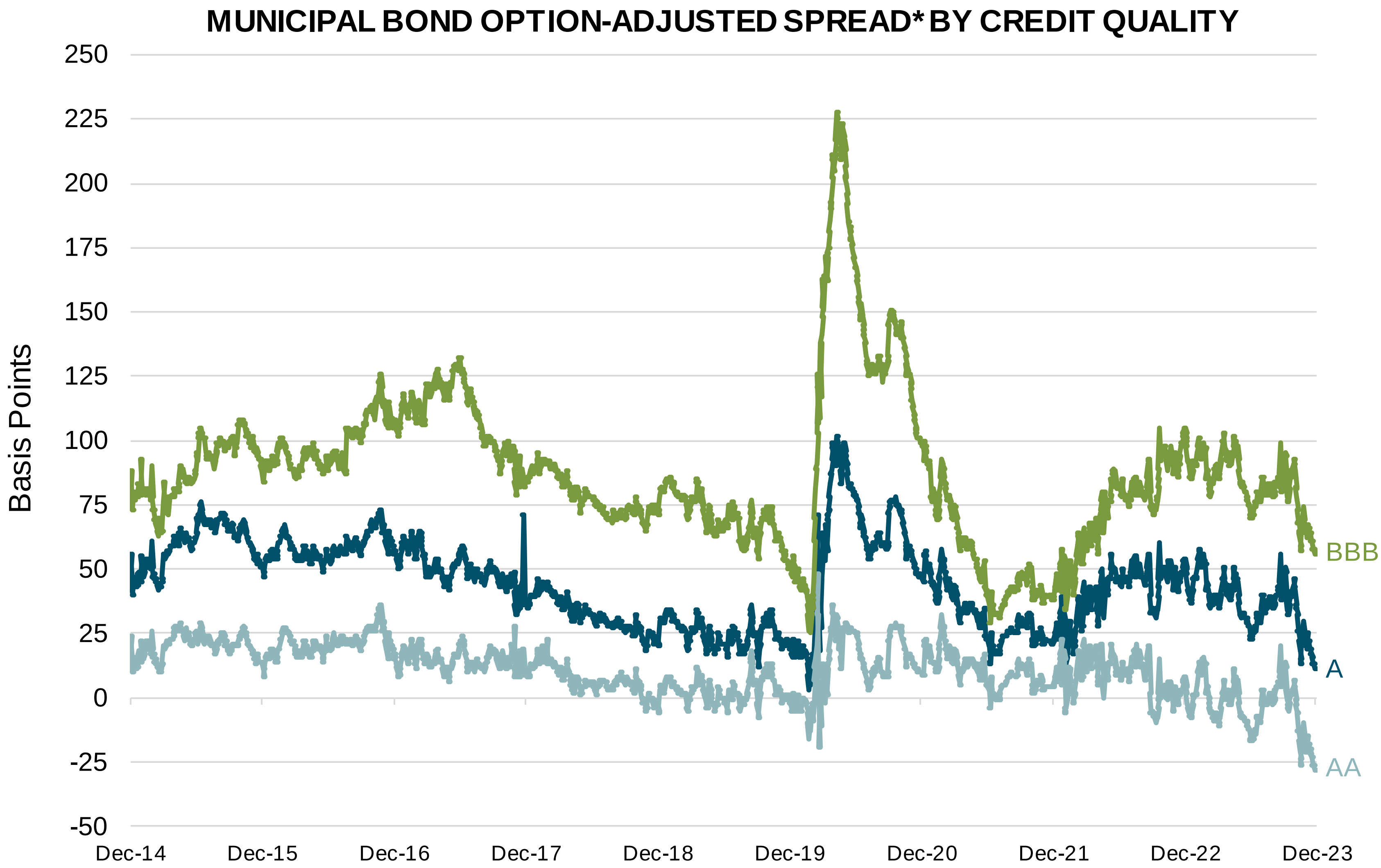
Note; Municipal is represented by AAA rated municipal securities.

Source: Refinitiv (TM3) as of 2/29/24. Historical ratio averages as of 2/29/24.



Fidelity INVESTMENTS®

# Municipal Credit Spreads




*Option-Adjusted Spread: An option-adjusted spread converts the difference between the fair price and the market price of a fixed income security into yield and calculates a spread that makes the tw o prices equal.

The AA, A and BBB rated series are reflective of the sub-components of the Bloomberg Municipal Bond Index.

**Past performance is no guarantee of future results.**

Source: Fidelity and Bloomberg as of 12/31/23.

# Fidelity Municipal Bond Team

## Dedicated and experienced team offering diverse strategies

| | | SHORT NATIONAL | INTERMEDIATE NATIONAL | LONG NATIONAL | STATE-SPECIFIC |
|---|---|---|---|---|---|
| | **Strategies** | • Conservative Inc Muni Bond*<br>• Limited Term Municipal Inc | • Intermediate Municipal Income<br>• Municipal Core Plus*<br>• Sustainable Int Muni Income*<br>• Municipal Bond Index* | • Municipal Income,<br>• Tax-Free Bond* | AZ, CA**, CT, MA, MD, MI, MN, NJ, NY, OH, PA |
| | **Benchmark** | Bloomberg 1-6 Year Municipal Bond Index | Bloomberg 1-17 Year Municipal Bond Index | Bloomberg 3+ Year Municipal Bond Index | Various State-Specific Indices |
| | **Mutual Fund Assets** | $5.3B | $11.6B | $8.0B | $8.3B |
| | **Separate Account & Other Assets** | $1.5B | $6.6B | $6.5B | - |
| MUNICIPAL BOND PLATFORM | $47.8B Total AUM | $6.8B | $18.2B | $14.5B | $8.3B |

| | | NUMBER OF ASSOCIATES | AVERAGE INDUSTRY EXPERIENCE |
|---|---|---|---|
| INVESTMENT TEAM | **Portfolio Managers** | 3 | 24 years |
| | **Managing Director of Research** | 1 | 12 years |
| | **Research Analysts** | 11 | 15 years |
| | **Research Associates** | 6 | 2 years |
| | **Traders[1]** | 3 | 17 years |
| | **Quantitative Analyst** | 1 | 3 years |

*Fidelity Conservative Income Municipal Bond Fund uses the 50% Bloomberg 1-Year Muni Bond Index/50% iMoney Net Tax-Free National Retail Blended Index; Fidelity Municipal Core Plus Bond Fund uses the Fidelity Municipal Core Plus Bond Composite Index; Fidelity Sustainable Intermediate Municipal Income Fund uses the Bloomberg 3-15 Year Blend (2-17) Muni Bond Index; Fidelity Municipal Bond Index Fund uses the Bloomberg Municipal Bond Index; Fidelity Tax-Free Bond Fund uses the Bloomberg 3+ Year Non-AMT Municipal Bond Index.

**We offer a limited term and long duration California mutual fund

1 – One Trader TBH

Source: Fidelity Investments, Assets as of 12-31-23. Headcount and experience as of 2/29/24. Assets include cash holdings. Separate Account & Other Assets include the assets of open-end mutual funds designed exclusively for Fidelity's managed account offerings. Data is unaudited. Totals may vary due to rounding.



Fidelity INVESTMENTS

# Important Information

In general, the bond market is volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa. This effect is usually more pronounced for longer-term securities.) Fixed income securities also carry inflation risk, liquidity risk, call risk, and credit and default risks for both issuers and counterparties. Unlike individual bonds, most bond funds do not have a maturity date, so holding them until maturity to avoid losses caused by price volatility is not possible. Any fixed income security sold or redeemed prior to maturity may be subject to loss.

The municipal market can be affected by adverse tax, legislative, or political changes, and by the financial condition of the issuers of municipal securities. Interest income generated by municipal bonds is generally expected to be exempt from federal income taxes and, if the bonds are held by an investor resident in the state of issuance, from state and local income taxes. Such interest income may be subject to federal and/or state alternative minimum taxes. Investing in municipal bonds for the purpose of generating tax-exempt income may not be appropriate for investors in all tax brackets. Generally, tax-exempt municipal securities are not appropriate holdings for tax-advantaged accounts such as IRAs and 401(k)s.

**Interest rate risk** - Like all fixed income securities, the market prices of municipal bonds are susceptible to fluctuations in interest rates. If interest rates rise, market prices of existing bonds will decline, despite the lack of change in both the coupon rate and maturity. Bonds with longer maturities are generally more susceptible to changes in interest rates than bonds with shorter maturities.

**Call risk** - Many municipal bonds carry provisions that allow the issuer to call or redeem the bond prior to the actual maturity date. An issuer will typically call bonds when prevailing interest rates drop, making reinvestment less desirable for the holder. Some municipal bonds, including housing bonds and certificates of participation (COPs), may be callable at any time regardless of the stated call features. In some cases, bond issuers will call bonds to modify an indenture through a new offering. Investors should also be aware of special or extraordinary redemption provisions. These are provisions that give a bond issuer the right to call the bonds due to a one-time occurrence, such as a natural disaster, interruption to a revenue source, unexpended bond proceed, or cancelled projects.

**Liquidity risk** - The vast majority of municipal bonds are not traded on a regular basis; therefore, the market for a specific municipal bond may not be particularly liquid. This can be attributed to the large number of municipal issuers and variety of securities. With limited exceptions for some large more actively traded issues, the chances of finding a specific municipal bond in the secondary market at any given time are relatively small. According to the Municipal Securities Rulemaking Board (MSRB), it is much more common to identify basic characteristics of a municipal bond in which an investor is interested in investing (e.g., state, creditworthiness, maturity range, interest rate, or yield, market sector, etc.) and then to make a choice from a set of municipal securities that meet those criteria. Selling prior to maturity can present a challenge for municipal bond investors due to the fragmented and thinly traded nature of the market.

**Revenue sources risk** - With revenue bonds, the interest and principal are dependent on the revenues paid by users of a facility or service, or other dedicated revenues including those from special taxes. In general, the consumer spending that provides the funding or income stream for revenue bond issuers may be more vulnerable to changes in consumer tastes or a general economic downturn than the income stream for general obligation bond issuers. "Essentiality" is a key investor consideration for a project financed with revenue bonds. For example, a facility that delivers fundamental or essential services, such as water and sewer, may be more likely to have dependable revenues through multiple economic cycles. When evaluating revenue bonds, it is important to consider:

The overall economic health of the region or customer base and the impact it might have on the entity's ability to sustain its revenues.
- The exact source of the revenues that will service and repay the debt. Is the bond solely dependent upon one source of revenue or is a larger entity standing behind the issue?
- The entity's track record of operational effectiveness through multiple economic cycles. Is there a track-record of solid growth attracting more customers or taxpayers from more diverse sources?
- The legal provisions that may be in place to protect the bondholder, such as rate covenants and debt service reserve funds.
- The competence of financial management of the entity. Has its credit rating been maintained or strengthened over a period oftime?
- How has it weathered previous economic downturns? How much debt does it have? How much of its cash flow is committed to paying down debt vs. investing in new projects or supporting services of value for the community?

**Credit and default risk** - Credit risk is the risk that the issuer will default or be unable to make required principal or interest payments. Despite the fact that many municipal bonds have high credit ratings, there is a risk of default in any bond investment.

**Tax risks** - Because tax-exempt interest generated by municipal bonds is usually more beneficial for investors in higher tax brackets, municipal bonds may not be appropriate for all investors, particularly those in lower tax brackets. In addition, if you are subject to the federal alternative minimum tax (AMT), the interest income generated by certain municipal bonds (mainly private activity bonds) may be taxable.

**Inflation risks** - As with all bonds, investors run the risk that inflation will diminish the purchasing power of a municipal bond's principal and interest income.

Fidelity INVESTMENTS

# Important Information

**Repudiation risk** - There can be no assurance that bonds validly issued will not be partially or totally repudiated by the issuing state or municipality, should that be deemed reasonable and necessary to serve other important public purposes.

**Other risks** - Not all risks can be quantified in a bond's prospectus or offering circular. A type of risk called "special event risk," law suits or significant legal changes, another community's public works project, unusual weather, an economic downturn, or other events could impact the issuer's ability to meet their financial commitments.

**Past performance is no guarantee of future results.**

Diversification does not ensure a profit or guarantee against loss.

The Chartered Financial Analyst (CFA®) designation is offered by the CFA Institute. To obtain the CFA charter, candidates must pass three exams demonstrating their competence, integrity, and extensive knowledge in accounting, ethical and professional standards, economics, portfolio management, and security analysis, and must also have at least 4,000 hours of qualifying work experience completed in a minimum of 36 months, among other requirements. CFA is a trademark owned by CFA Institute.

Fidelity does not provide legal or tax advice. The information herein is general and educational in nature and should not be considered legal or tax advice. Tax laws and regulations are complex and subject to change, which can materially impact investment results. Fidelity cannot guarantee that the information herein is accurate, complete, or timely. Fidelity makes no warranties with regard to such information or results obtained by its use, and disclaims any liability arising out of your use of, or any tax position taken in reliance on, such information. Consult an attorney or tax professional regarding your specific situation.

Views expressed are as of the date indicated, based on the information available at that time, and may change based on market or other conditions. Unless otherwise noted, the opinions provided are those of the speaker and not necessarily those of Fidelity Investments or its affiliates. Fidelity does not assume any duty to update any of the information.

References to individual securities are for illustrative purposes only, and should not be construed as investment advice.

Indexes are unmanaged. It is not possible to invest directly in an index.

**Bloomberg Municipal Bond Index**: market value-weighted index of investment-grade municipal bonds with maturities of one year or more.

**Bloomberg 1-6 Year Municipal Bond Index:** market value-weighted index of investment-grade fixed-rate municipal bonds with maturities between one and six years.

**Bloomberg 1-17 Year Municipal Bond Index:** market value-weighted index of investment-grade fixed-rate municipal bonds with maturities between one and 17 years.

**Bloomberg 3+ Year Municipal Bond Index:** market value-weighted index of investment-grade fixed-rate municipal bonds with maturities of three years or more.

**Before investing in any mutual fund, consider the investment objectives, risks, charges, and expenses. Contact Fidelity for a prospectus or, if available, a summary prospectus containing this information. Read it carefully.**

© 2024 FMR LLC. All rights reserved.

Fidelity Brokerage Services LLC, Member NYSE, SIPC, 900 Salem Street, Smithfield, RI 02917

1079585.2.0