2022 Municipal Bond Midyear Investment Outlook

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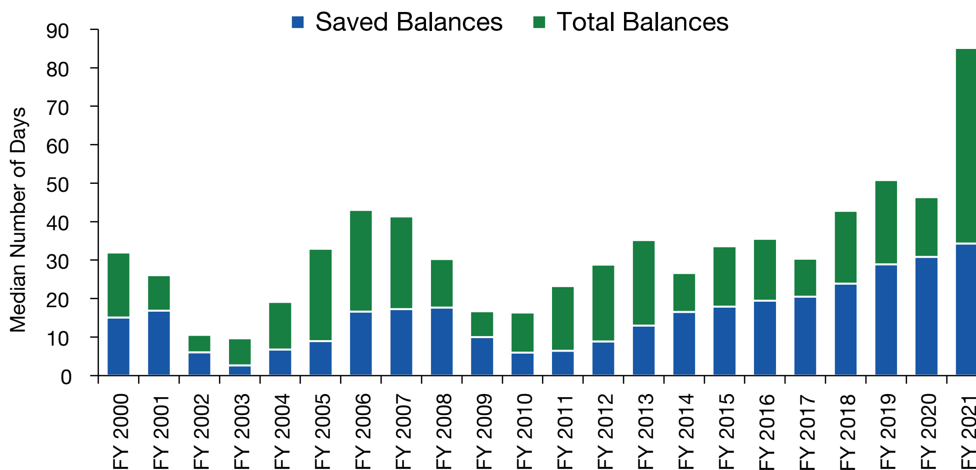
Municipal Bonds are Well Positioned for a Potential Slowdown in U.S. Economic Growth

State governments have been prudently saving tax revenue and federal stimulus to replenish and build rainy-day funds.

In fiscal-year (FY) 2021, rainy-day balances reached a record high of $114.6 billion, according to the National Association of State Budget Officers. This suggests that government finances are in good shape to withstand a potential downshift in the U.S. economy.



Source: Pew Research. "Median number of days" indicates how long states can operate solely from saved funds. Pew's analysis is based on data from "The Fiscal Survey of the States," which the National Association of State Budget Officers (NASBO) publishes each fall and spring. The NASBO is an independent, nonpartisan, nonprofit research and educational organization located in Washington, D.C. It is a professional membership organization for state budget and finance officers. Data as of 12/17/2021, most recent available. For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment.

Defaults among municipal bond issuers have been negligible.

Another positive factor in municipal bonds' favor is their historically low default rates. The municipal bond market has registered a cumulative average 10-year default rate of 0.2% across the full ratings spectrum versus a cumulative average 10-year default rate of 10.6% for corporate bonds.

Credit Quality	10-Year Cumulative Default Rates	
Moody's Rating	Municipals	Corporates
Aaa	0.00%	0.35%
Aa	0.02%	0.77%
A	0.10%	2.04%
Baa	1.09%	3.61%
Investment Grade	0.10%	2.24%
Non-Investment Grade	7.11%	29.66%
All Rated*	0.16%	10.55%

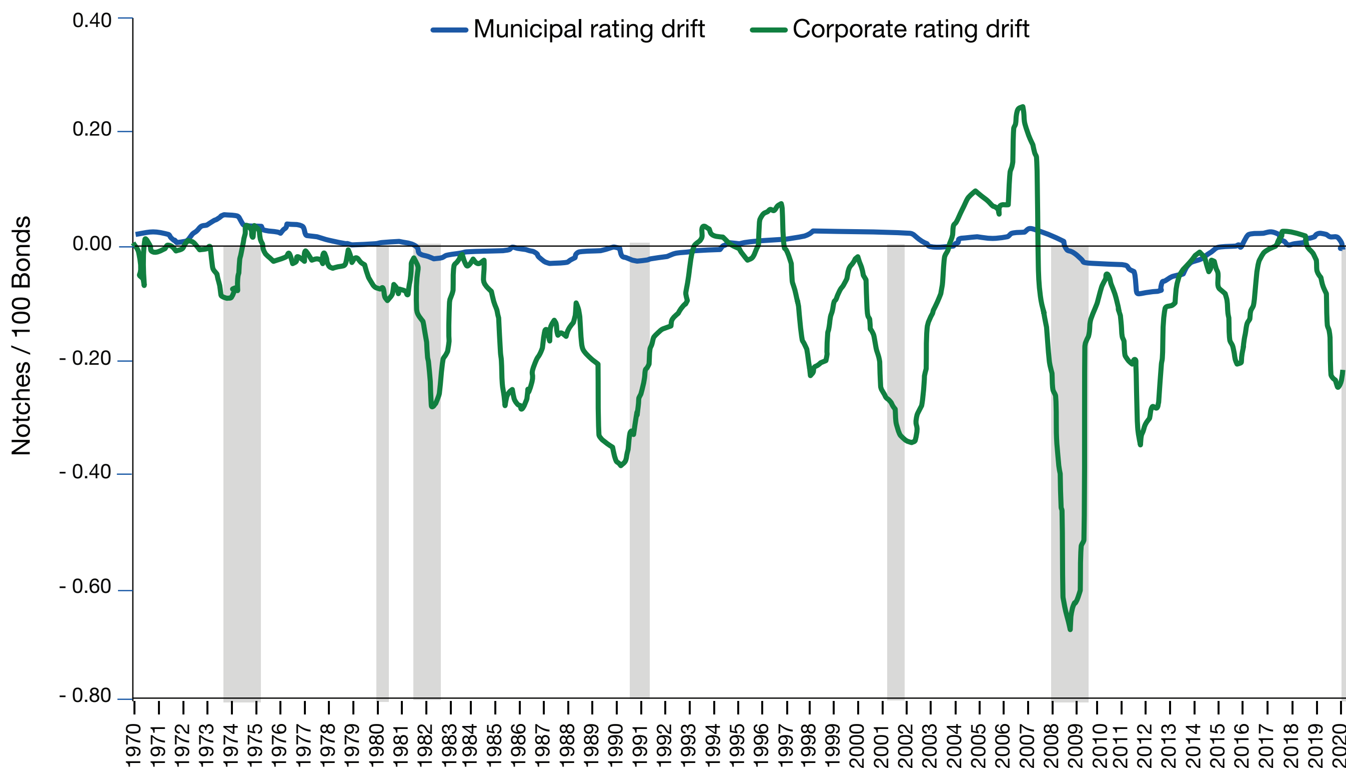
Source: Moody's, "Moody's US Municipal Bond Defaults and Recoveries, 1970–2020," July 2021. Data show the average 10-year cumulative default rates of Moody's rated corporate and municipal bonds for a study covering the period 1970-2019. *Rating outlooks are not assigned to all rated entities. While municipal bonds are backed by municipalities, U.S. government securities, such as U.S. Treasury bills, are considered less risky since they are backed by the U.S. government. High-yielding, non-investment-grade bonds (junk bonds) involve higher risk than investment-grade bonds. Adverse conditions may affect the issuer's ability to pay interest and principal on these securities. For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment.

Investment Implications

Municipal bond funds have experienced outflows in 2022, which has led to higher absolute rates, before reflecting muni's tax-exempt status, and even more attractive relative value versus comparable, taxable fixed-income options.

Municipal Bond Credit-Quality Has Been Resilient

Municipal bond ratings have moved little during recessions compared to corporate bonds.



Source: Moody's Investors Service, JP Morgan, and Lord Abbett. Shaded areas represent U.S. recessions. Rating drift refers to the average movement of credit-rating "notches" (e.g., the incremental difference between 'BBB-', 'BBB', and 'BBB+').[1] For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment.

Potential Investment Opportunities

Investors seeking tax-free income amid current uncertainty around the future path of the U.S. economy may want to consider exposure to municipal bonds. Currently appealing factors supportive of the asset class include:

- Robust rainy-day funds built on strong tax revenues
- Historically very low default rates
- More stable and resilient credit quality profile versus corporate bonds

Potential Investment Risks

The Fed (Federal Reserve) is tightening monetary policy, and overly aggressive tightening, due to persistently higher inflation, may potentially lead to a downturn in economic growth. This may impact municipal bond fundamentals.

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IMPORTANT INFORMATION

[1]Rating notch means the difference between a credit rating assigned by a rating agency (Moody's, S&P, or Fitch) and the rating immediately below it; for example, a rating that has been changed from "BB+" to "BB" would be lower by one notch.

Unless otherwise noted, all discussions are based on U.S. markets and U.S. monetary and fiscal policies.

Asset allocation or diversification does not guarantee a profit or protect against loss in declining markets.

No investing strategy can overcome all market volatility or guarantee future results.

The value of investments and any income from them is not guaranteed and may fall as well as rise, and an investor may not get back the amount originally invested. Investment decisions should always be made based on an investor's specific financial needs, objectives, goals, time horizon, and risk tolerance.

Market forecasts and projections are based on current market conditions and are subject to change without notice.

Projections should not be considered a guarantee.

Equity Investing Risks

The value of investments in equity securities will fluctuate in response to general economic conditions and to changes in the prospects of particular companies and/or sectors in the economy. While growth stocks are subject to the daily ups and downs of the stock market, their long-term potential as well as their volatility can be substantial. Value investing involves the risk that the market may not recognize that securities are undervalued, and they may not appreciate as anticipated. Smaller companies tend to be more volatile and less liquid than larger companies. Small cap companies may also have more limited product lines, markets, or financial resources and typically experience a higher risk of failure than large cap companies.

Fixed-Income Investing Risks

The value of investments in fixed-income securities will change as interest rates fluctuate and in response to market movements. Generally, when interest rates rise, the prices of debt securities fall, and when interest rates fall, prices generally rise. High yield securities, sometimes called junk bonds, carry increased risks of price volatility, illiquidity, and the possibility of default in the timely payment of interest and principal. Bonds may also be subject to other types of risk, such as call, credit, liquidity, and general market risks. Longer-term debt securities are usually more sensitive to interest-rate changes; the longer the maturity of a security, the greater the effect a change in interest rates is likely to have on its price.

The credit quality of fixed-income securities in a portfolio is assigned by a nationally recognized statistical rating organization (NRSRO), such as Standard & Poor's, Moody's, or Fitch, as an indication of an issuer's creditworthiness. Ratings range from 'AAA' (highest) to 'D' (lowest). Bonds rated 'BBB' or above are considered investment grade. Credit ratings 'BB' and below are lower-rated securities (junk bonds). High-yielding, non-investment-grade bonds (junk bonds) involve higher risks than investment-grade bonds. Adverse conditions may affect the issuer's ability to pay interest and principal on these securities.

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Glossary & Index Definitions

Treasuries are debt securities issued by the U.S. government and secured by its full faith and credit. Income from Treasury securities is exempt from state and local taxes.

The **U.S. Federal Reserve (Fed)** is the central bank of the United States.

Yield is the income returned on an investment, such as the interest received from holding a security. The yield is usually expressed as an annual percentage rate based on the investment's cost, current market value, or face value. The tax-equivalent yield is the pretax yield that a taxable bond needs to possess for its yield to be equal to that of the tax-exempt yield on a municipal bond. This calculation can be used to fairly compare the yield of a tax-free bond to that of a taxable bond to see which bond has a higher applicable yield.

Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

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