



The Missing Core: Why Taxable Municipals Deserve Strategic Attention Amid Uncertainty

From MacKay Municipal Managers™

Rethinking fixed income in a shifting regime

In today's environment of policy recalibration, macroeconomic divergence, and rising fiscal uncertainty, institutional investors are re-evaluating traditional anchors of portfolio resilience. Amid this complexity, the role of public fixed income is being redefined—not just as ballast, but as a forward-looking source of return and optionality. Within this reassessment, we believe taxable municipal bonds represent a timely and underutilized opportunity to enhance strategic fixed income allocations. Their combination of high-quality income, favorable risk-adjusted returns, and structural resilience position them as a compelling solution for allocators navigating an uncertain investment landscape.

A Conviction-Based Allocation for a Complex Cycle

The current environment has shifted from one of synchronized monetary easing to a fragmented,

unpredictable macro regime. Against this backdrop, fixed income strategy must be intentionally designed to buffer against drawdowns while still capturing risk-premium where it exists.

Taxable municipals present a differentiated solution in this environment:

- **Attractive yield efficiency:** More compelling yield than Treasuries, comparable to corporates but with significantly lower credit risk.
- **Strong credit quality:** ~78% of taxable munis are rated AA or higher—far exceeding the 9% of Global Investment Grade Corporates. Certain taxable municipal issuers (i.e. the 13 U.S. states rated AAA) hold a higher credit rating than the U.S. federal government's AA rating.¹
- **Budgetary discipline:** Municipal issuers are legally required to balance budgets, creating structural fiscal prudence and therefore greater ratings stability over time.
- **Proven downside mitigation:** With a 10-year cumulative default rate of just 0.05%, far below the 1.06% observed in global investment grade corporates², taxable municipals have demonstrated consistent stability—even through stress cycles. While Treasuries have no credit default risk, their mark-to-market drawdown potential is significant.

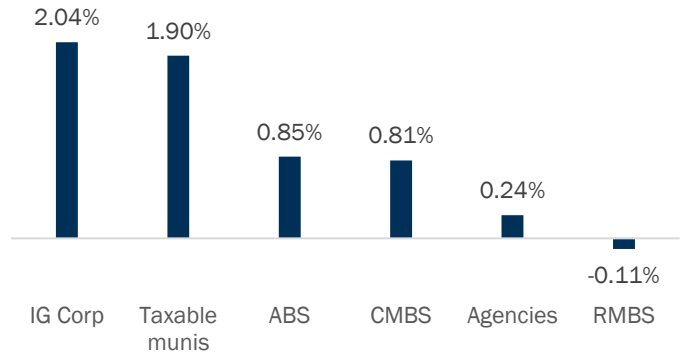
1. Source: ICE Data and Bloomberg
2. Moody's Investor Service

For allocators focused on navigating volatility, this asset class delivers an appealing balance between quality and income—two elements that matter more than ever in today’s environment. In sum, this asset class combines attractive yields and a 10-year average excess return of 1.90% providing a powerful rationale for taxable municipals to warrant strategic consideration, not just as a yield enhancer, but as a long-term, structural component of core fixed income models. (See Figure 1).

Allocators are increasingly concerned about concentration in traditional fixed income exposures—especially Treasuries and Investment Grade Corporates—both of which have exhibited growing sensitivity to policy and market shocks. In short, taxable municipals help institutional portfolios hedge the uncertainty embedded in sovereign risk and macro policy shifts, while maintaining liquidity and scalability. With a ~\$800B market and increasingly active institutional participation, taxable municipal bonds compare well in size to other satellite fixed income sectors including CLOs, ABS, non-agency CMBS and RMBS markets.

Efficient frontier analyses demonstrate that the 5–10 year taxable municipal segment offers compelling returns at lower volatility than many comparable sectors (Figure 2 below).

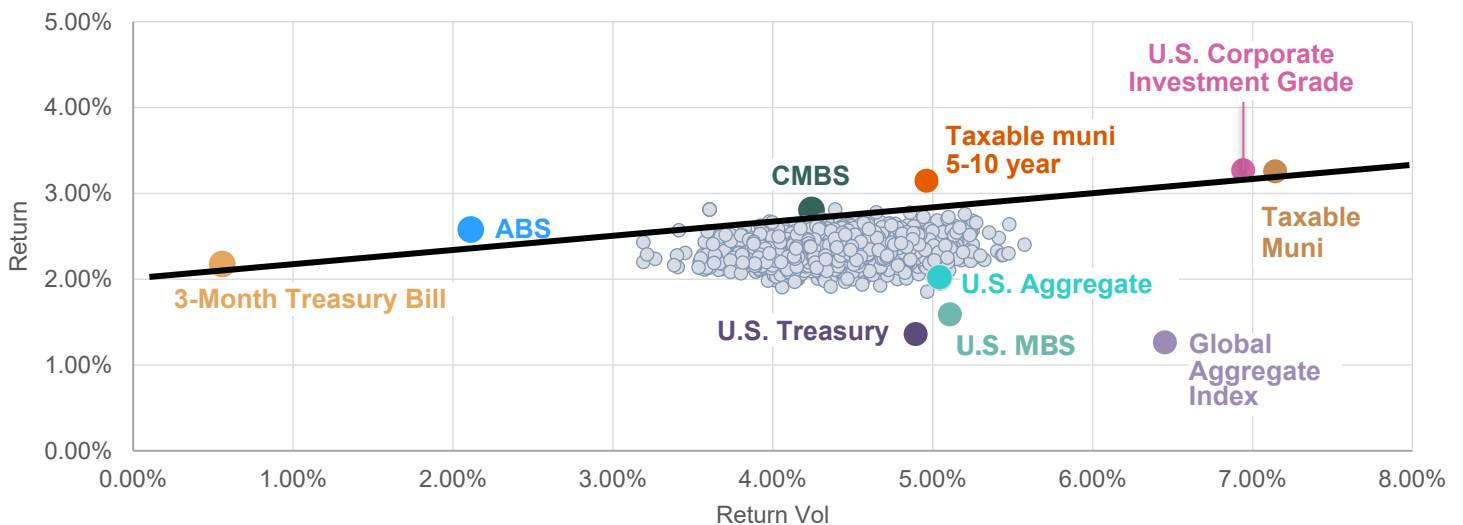
FIGURE 1
10-Year average excess return vs. US Gov



Data as of December 31, 2025. Agencies: ICE BofA U.S. Agency Index; RMBS: ICE BofA U.S. Mortgage Backed Securities Index; CMBS: ICE BofA U.S. Treasury Index; BofA U.S. Fixed Rate CMBS Index; ABS: ICE BofA U.S. Fixed Rate Asset Backed Securities Index; IG Corps: U.S. Corp Master Index; Taxable Munis: ICE BofA Broad US Taxable Municipal Securities Index. Please see disclosures and index descriptions at the end. **Past performance is not indicative of future results.**
Source: ICE Data.

For consultants and model allocators, this makes them ideal candidates for intentional reallocation within core frameworks, especially for institutions revisiting assumptions around liquidity premiums and mark-to-market transparency.

FIGURE 2
Taxable efficient frontier 10-year



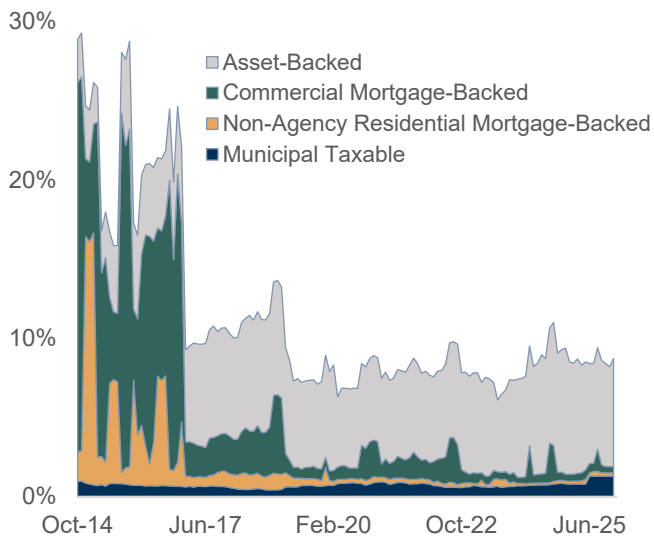
Data from January 01, 2016 to December 31, 2025

US Treasury: Bloomberg Barclays US Treasury Index; US Agg: Bloomberg Barclays US Aggregate Bond Index; IG Corps: U.S. Corp Master Index; MBS: Bloomberg U.S. Mortgage Backed Securities Index; Taxable Munis: ICE BofA Broad US Taxable Municipal Securities Index; ABS: ICE BofA U.S. Fixed Rate Asset Backed Securities Index; CMBS: ICE BofA U.S. Fixed Rate CMBS Index.

Efficient frontier analysis is a portfolio optimization technique to illustrate a portfolio’s or asset’s maximum return for a given level of risk. The efficient frontier analysis above is index-based; MacKay Shields’ portfolios are actively managed and would vary from any applicable or benchmarked index. Actual portfolios would be subject to fees and expenses. No fees or expenses were included in the results above. No representation is made as to the accuracy and completeness of information contained in this presentation that has been obtained from third parties. Please see disclosures and index descriptions at the end of this document. It is not possible to invest directly in an index. Past performance is not indicative of future results.

Source: Bloomberg

FIGURE 3
Percent of total core portfolio AUM



Source: Morningstar, MacKay Shields. Based upon Morningstar US Intermediate Core Universe from 10/31/2014 through 12/31/2025.

A tool for risk-budgeted stability

While core fixed income managers on average allocate less than 1% of AUM to taxable municipals (see Figure 3 above), we observe a behavioral shift among institutional allocators—they are now carving out dedicated taxable municipal sleeves, driven by peer benchmarking,

competitive performance, and deeper education on the benefits of including taxable municipals. Data shows that this asset class introduces sector differentiation that is often missing from core models. Additionally, taxable municipals unique risk-return characteristics help reduce reliance on credit-sensitive sectors, while enhancing total return potential in diversified bond sleeves. Risk diversification and yield enhancement show why the time is right to boost core fixed income allocations to taxable municipals.

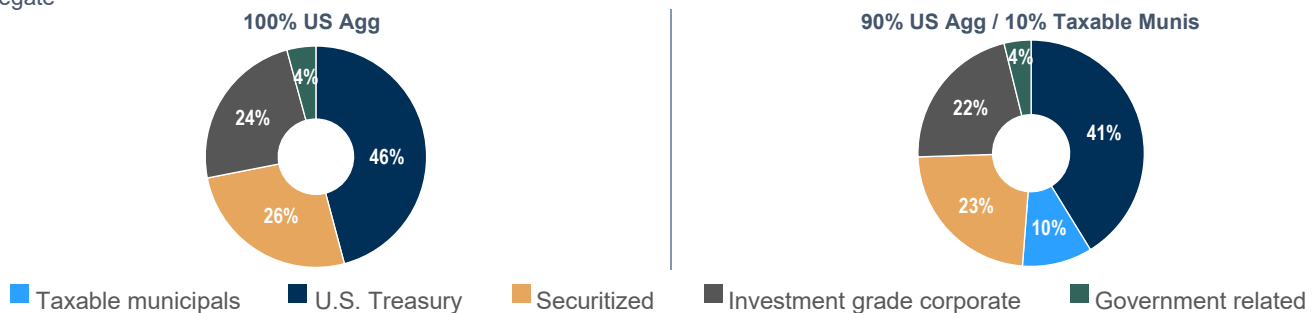
Taxable municipals as strategic diversifiers

Scenario testing shows that integrating even modest allocations (e.g., 10%) of taxable municipals into traditional core bond exposures, such as replacing 10% of the US Aggregate Index (Figure 4), enhances both yield and total return without materially increasing risk. In an environment of elevated volatility and uncertain policy pathways, this acts as an anchor without sacrificing return potential.

As institutional portfolios grapple with the cost of uncertainty—whether from fiscal drag, or credit dispersion—taxable municipals emerge as a forward-looking allocation decision grounded in quality, transparency, and resilience. Taxable municipals are not just a yield enhancer. They are a scalable, resilient, and under-allocated strategic solution—purpose-built for navigating the new fixed income regime.

FIGURE 4
Enhance your core fixed income portfolio

Replacing just 10% with taxable municipals could potentially enhance yield and returns, while keeping the risk profile in line with the us aggregate



	Yield	10-Yr total return	10-Yr std dev	10-Yr Sharpe Ratio	10-Yr correlation to S&P 500
Bloomberg US Agg Bond TR USD	4.32	1.49	5.03	-0.08	0.39
Bloomberg Taxable Municipal TR USD	4.81	2.73	7.13	0.13	0.35
90% U.S. Agg - 10% Taxable Muni	4.37	1.62	5.19	-0.06	0.39

As of December 31, 2025

For illustrative purposes only. Based on Morningstar data and asset allocation percentages determined by MacKay Shields and/or New York Life Investment Management. The returns shown above do not represent the returns of any client portfolio or strategy actually managed by MacKay Shields and should not be construed as such. The returns shown are index-based and mathematically calculated based on the percentages shown; MacKay Shields' portfolios are actively managed and would vary from any applicable or benchmarked index. Therefore, the returns shown are not indicative of investment skill. Actual portfolios would be subject to fees and expenses. No fees or expenses were included in the results above. No representation is made as to the accuracy and completeness of information contained in this presentation that has been obtained from third parties.

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