



APA MARKET COMMENTARY: MAY 2026

May was driven by geopolitics and inflation, as early-month oil volatility gave way to a mid-month inflation surprise that pushed rates higher and forced markets to reassess the Federal Reserve's path.

Municipals experienced periods of pressure but remained notably stable overall, finishing the month positive.

Even with consistently elevated issuance, strong demand allowed the market to absorb supply, with a late-month rally emerging as oil prices eased and sentiment stabilized.

In volatile environments like these, we believe active management matters.

MORE MARKET VOLATILITY, YET MUNIS FINISH POSITIVE

- We saw more volatility across muni performance in May, as headlines from the Middle East, oil prices, and inflationary concerns weighed on markets.
- Crude oil moved back above \$100 per barrel at points early in the month, raising concerns about renewed inflation pressure and contributing to higher yields as markets reacted to the risk of persistent energy-driven inflation.
- Despite this market volatility, the Bloomberg Municipal Index posted a positive return of 0.4% for the month.

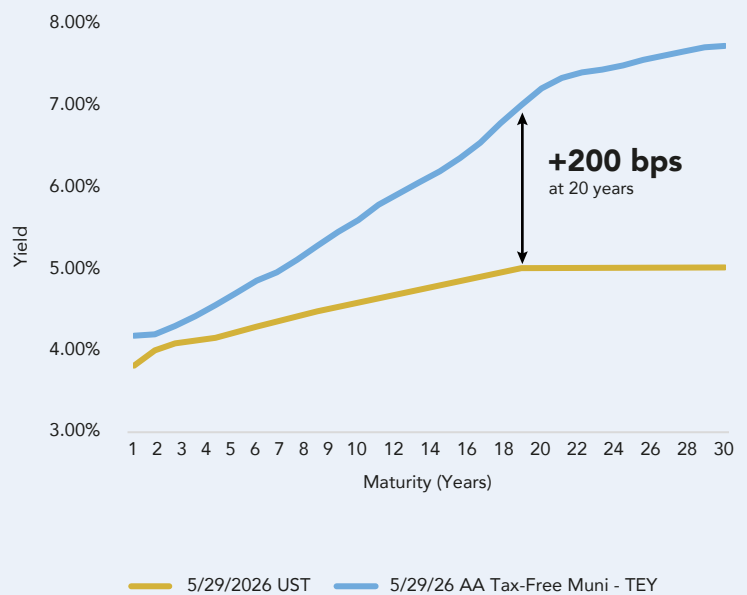
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- Total return performance was positive across the municipal index curve, with the 20-year part of the curve performing the best—an area of the curve we have consistently highlighted as an attractive entry for client portfolios.



Higher yields are helping to offset short-term price fluctuations.

HIGH-QUALITY MUNIS OFFER ATTRACTIVE INCOME TODAY



Source:
The Municipal Market Monitor (TM3)
& U.S. Department of the Treasury
[May 31, 2026]

ACTIVE MANAGEMENT THROUGH VOLATILITY

- Throughout the recent market volatility, APA has been active, utilizing positions with short call protection in client portfolios to defend against potential moves toward higher rates.
- APA continues to look for tax loss harvesting opportunities in client portfolios to take advantage of market volatility, aiming to provide clients with more tax efficiency and higher future income to offset losses. APA looks for these opportunities across the entire year, not just at year-end.

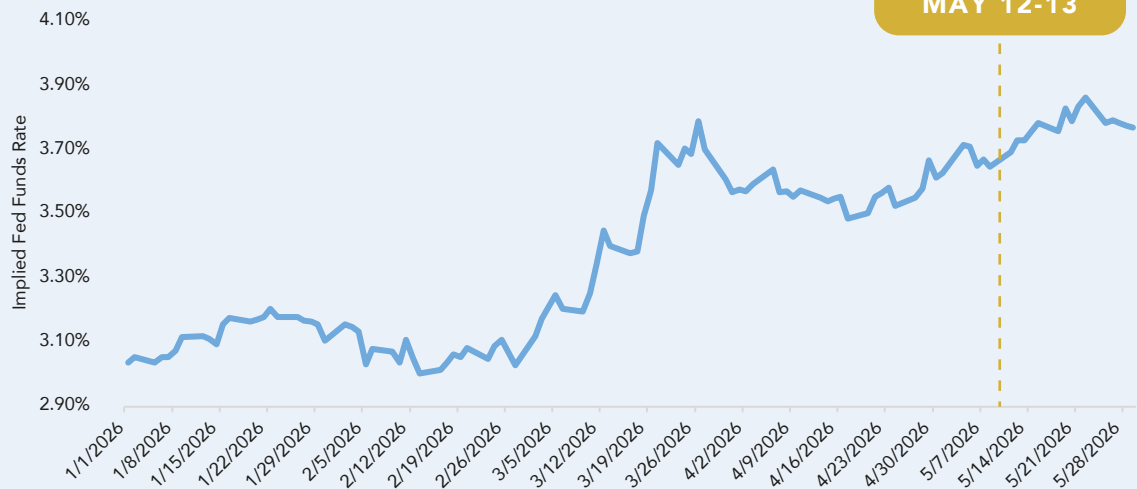


Volatile months like May remind you why your fixed income management should be active.

INFLATION REPRICING SHIFTS THE FED NARRATIVE

- The month’s most meaningful shift came in response to inflation data released on May 12 and 13, when hotter-than-expected readings reinforced the impact of higher energy prices and pushed inflation back to the forefront of the market narrative.
- Bond markets reacted quickly, with Fed rate expectations repricing higher following the inflation data and investors moving away from near-term rate cut expectations. Treasury yields rose sharply as a result, with municipal yields moving higher in tandem, generally by several basis points across the curve and with the most pronounced weakness in shorter maturities.

FED RATE EXPECTATIONS SHIFT HIGHER AFTER INFLATION DATA



Source: Bloomberg [May 31, 2026]

- In the days that followed, markets increasingly considered the possibility of further policy tightening as inflation concerns persisted, while Fed leadership developments added another layer of uncertainty to the policy outlook.
- By late month, those expectations moderated slightly, with markets pulling back from peak tightening expectations while still pricing a higher-for-longer rate environment. This repricing extended to longer-term Treasury rates as well, with the 30-year Treasury yield moving above 5%—a level not seen in years—highlighting persistent inflation concerns and uncertainty around the long-term rate environment.

HEAVY SUPPLY MEETS STEADY DEMAND

- Tax-exempt issuance remained historically strong, continuing the elevated pace of supply seen earlier this year. May supply reached approximately ~\$55 billion, bringing year-to-date issuance to roughly ~\$247B—about 30-40% above the short- and long-term averages.
- Multiple weeks of May saw sizeable new issue calendars, including large benchmark deals from issuers such as Atlanta, San Francisco Airport, and New York City, pushing the month to the 10th highest month of supply on record.



May supply marked the 10th highest month on record.

- Despite this supply, demand remained strong enough to absorb new issuance, with several large deals seeing repricing to lower yields and competitive sales attracting multiple bidders, indicating continued investor appetite.

INFLOWS CONTINUE AMID ELEVATED INCOME LEVELS

- Municipal funds saw strong inflows in May, with weekly flows accelerating late in the month and total inflows likely exceeding \$10B, reflecting continued investor demand for tax-exempt income amidst elevated rate volatility.
- Year-to-date flows are now tracking among the strongest on record, second only to the zero-rate environment of 2021.



Demand remains exceptionally strong, with flows second only to 2021's zero-rate environment.

- As yields moved higher during the month, the income profile available in municipals improved meaningfully, creating more compelling entry points for investors seeking tax-efficient income.
- Municipal yields remained near decade-high taxable-equivalent levels, increasing their relative attractiveness versus other asset classes and supporting continued demand.



40.8% combined federal and ACA tax rate. For informational purposes only.

TAX-FREE YIELD	TAXABLE-EQUIVALENT YIELD
3.00%	5.07%
3.25%	5.49%
3.50%	5.91%
3.75%	6.34%
4.00%	6.76%
4.25%	7.18%
4.50%	7.60%

- Importantly, higher yields did not deter demand; instead, they began to attract incremental capital, reinforcing the idea that elevated income levels can help stabilize flows even in a more volatile rate environment.
- Periods of volatility provided additional, short-lived entry points, allowing patient and selective investors to deploy capital more opportunistically.



In a market defined by higher rates and episodic volatility, active management is key to capturing opportunity.

FUNDAMENTALS STILL DRIVE OUTCOMES

- Credit fundamentals remained broadly stable throughout May, but the month highlighted a growing dispersion between strong performers and credits facing more idiosyncratic pressure.
- On the positive side, several issuers continued to demonstrate meaningful credit improvement, including Detroit, which was upgraded as its multi-year turnaround continues to take hold, supported by strengthened financial performance, improved operations, and a more stable economic base.
- At the same time, areas of stress became more visible, particularly among issuers with structural or operational challenges, as seen in the downgrade of Sacramento City Unified School District, which faces significant deficits and the potential for state or county intervention following sustained financial deterioration.
- Environmental and operating pressures also drove weakness in certain essential service credits, particularly within water and sewer systems, where issuers such as Corpus Christi and Baltimore faced downgrades tied to constrained water supply, governance challenges, and financial strain, reinforcing how weather and infrastructure risks are increasingly translating into credit outcomes.

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Credit remains stable overall—but outcomes are becoming increasingly issuer-specific.

- The broader takeaway from May is that while the municipal market continues to benefit from generally strong fundamentals, credit differentiation is becoming more pronounced, with performance increasingly driven by management execution, balance sheet strength, and exposure to sector-specific risks rather than broad market trends.

THE ROAD AHEAD: SUPPORTIVE TECHNICALS IN AN UNCERTAIN ENVIRONMENT

- Looking ahead, the municipal market enters June supported by a strong technical backdrop, as elevated issuance meets one of the most significant periods of reinvestment demand this year, with nearly \$60B in principal and interest payments expected to return to investors' portfolios. Early June has already seen one of the largest new issue calendars since last August, highlighting the continued pace of supply.
- While geopolitical and inflation-related risks will continue to influence the rate environment, June is typically a constructive period for municipal performance, and current demand dynamics are expected to effectively absorb elevated supply and help anchor valuations in the near term.



Elevated supply and strong demand are creating more opportunities to put cash to work at attractive income levels.

- Net supply is expected to remain positive, contributing to continued growth in the municipal market and expanding the available opportunity set, allowing investors to be more selective and better compensated for taking credit and duration risk.
- In this environment, we continue to favor a modified barbell approach, balancing shorter-duration defensive positioning with longer-duration income opportunities. This positioning allows investors to take advantage of the steepness of the curve while managing interest rate risk, with short-end exposure providing stability and longer maturities offering attractive income as inflation expectations and Federal Reserve policy continue to evolve.



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APA-2606-10