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3 Ways Muni Bonds Could Benefit from Trump Tax Plan

By Amey Stone

Overall, the muni market isn't reacting much — if at all — to President Trump's new tax plan. The **iShares S&P National AMT-Free Municipal Bond Fund** ([MUB](#)) has stayed right around \$9.40 since news of the plan started to trickle out on Tuesday.

Not only is there not a lot of key details in the plan, but investors don't have high hopes for it passing as envisioned.

"One hundred days may not be a fair measure of performance, but given how much this administration has gotten done so far, you'd have to give about a 50-50 shot that nothing gets done on taxes," says **Jim Robinson of Robinson Capital**.

Still, **John R. Mousseau of Cumberland Advisors**, took a stab at pointing out some areas of the muni market that could benefit if the plan goes through in some semblance of its current form.

First, he thinks lower marginal rates are already priced into the muni market and now long-term bond yield ratios will come down, making munis a better bet than taxable bonds. He writes:

Tax cuts have been baked into the muni market, thus the current yield levels — particularly in the long-maturity end — should stay around current levels, and yield ratios will most likely DRIFT DOWN over time. There is no current mention of capping municipal interest in this plan.

Second, bonds that are subject to the alternative minimum tax (AMT), which could go away, are likely to trade better than their non-AMT peers. Mousseau explains:

The plan also calls for the elimination of the Alternative Minimum Tax. The AMT was enacted in 1982 to ensure that individuals paid a certain minimum income tax. The tax limited tax benefits from a variety of deductions (think state and local taxes among other things). One aspect of the bill mandated that income from certain private-activity municipal bonds (municipal bonds issued by corporations, housing bonds over certain cap limits, and other municipal issues that have a private end user) be included in the calculation of the AMT. This provision was one of the most poorly designed parts of the AMT, as individuals who would be subject to the AMT would not buy bonds subject to the AMT. The cumulative amount of tax raised from this aspect of the AMT has been negligible. But the provision has come at a cost to these private issuers... This difference should DISAPPEAR over time if the proposed tax plan is passed.

Finally, he thinks munis in high-tax states will see strong demand if the [deductibility of state and local taxes](#) from federal income tax is eliminated. He writes:

The demand for in-state tax-exempt bonds in high-tax states will climb, pushing yields down relative to yields for other munis.

He notes, however that it could be harder for those states to raise taxes in the future:

There will be a decided pushback on state and local governments to forgo any tax increases and roll back tax rates if possible, since state taxes effectively increase suddenly and significantly from their current levels (which are partly subsidized by the federal deduction).

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