

ASK THE MANAGER

Kara South on Tax-Efficient Income in a Shifting Rate World



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For this edition of *Ask the Manager*, we speak with GW&K Investment Management's Portfolio Manager Kara South, from the team behind the AMG GW&K Muni Income ETF (MUNX), about navigating today's municipal bond landscape. She shares her outlook on the macro backdrop and rate environment, where her team sees the most compelling opportunities — and risks — across municipal bond sectors and states, and how active management in an ETF structure can help deliver tax-efficient income for clients in a shifting rate environment.

Q: What is your outlook for the municipal bond market?

Kara: We have a favorable outlook for the municipal bond market with attractive tax-equivalent yields, a steeper curve, and solid fundamentals. The broader rate direction remains in flux, leaving investors to balance expectations for further policy easing against lingering questions around growth, inflation, and fiscal policy. Despite these uncertainties, demand for tax-exempt municipal bonds remains well supported by historically attractive yields coupled with solid trailing performance, a combination that usually provides a powerful tailwind in this retail-investor-driven asset class. The muni curve remains significantly steeper than where we were at the start of 2025, enhancing expected return going forward. Credit conditions also remain constructive, even as revenue growth normalizes from the unusually strong post-COVID-19 pandemic period. Volatility and uncertainty in the market should provide plenty of opportunity for active managers to add value through security selection and relative-value trading in the year ahead.

Municipal bonds play an important role for investors, especially those in higher tax brackets who want steady, tax-efficient income. MUNX is designed to be a simple, "one ticket" way to get that tax-efficient municipal bond exposure in a diversified, actively managed ETF.

Are there particular sectors or states where you see the most opportunity—or risk—right now?

Kara: States enter 2026 with record-high budget surpluses (also known as rainy day funds), providing ample flexibility to navigate soft economic growth, cost pressures, and federal uncertainty. Many states anticipate decelerating revenue growth and have implemented spending cuts, suggesting that they are bracing for tighter fiscal conditions. However, with the resources at their disposal, we expect most states to effectively manage financial challenges that may arise.

To date, federal policy actions have been largely concentrated in two sectors: higher education and health care. For higher education, the impact has been more headline-driven than financially material. For health care, Medicaid reductions are expected to reach \$1 trillion over the next decade, but the cuts are back-end loaded, providing time for hospitals to adjust. Smaller hospitals with limited resources and high Medicaid exposure are likely to be the most affected.

Regardless of the ultimate impact, negative headlines in a retail-investor-driven asset class like municipal bonds often create opportunities to purchase bonds at attractive levels—opportunities we seek to capitalize on through active management and deep credit expertise.

What are the biggest risks facing municipal bonds in the current environment?

Kara: The biggest risk facing the municipal bond market outlook is broader interest-rate volatility. Expectations for additional Federal Reserve Board (the Fed) rate cuts will need to be balanced against incoming data on inflation and fiscal policy. In addition, headlines related to Federal Reserve independence and the upcoming transition of the Fed Chair introduce another source of potential market volatility. Relative value ratios (muni/Treasury ratios) remain tight on a historical basis, providing less of a cushion against a sell-off in the Treasury market. However, ratios have remained at tight levels since pre-COVID-19 and the market continues to be balanced in terms of supply and demand.

What are the benefits of active management in the municipal bond market?

Kara: The municipal bond market is large, fragmented, and dominated by retail investors, which can leave many bonds mispriced or overlooked. That environment tends to reward active managers who can dig into individual securities rather than simply owning the market in index form. Active management can add value in several ways: selecting stronger credits in challenged sectors, avoiding weaker structures, shifting along the yield curve as rate and valuation relationships change, and taking advantage of attractive pricing in new issues. It also provides a risk management benefit. When fundamentals deteriorate or policy winds shift, an active team can adjust exposure, whereas a purely passive portfolio is required to hold whatever the index includes. We manage our client portfolios for total return with a goal of not only protecting principal, but income as well.

How does MUNX differentiate itself from other municipal bond solutions in the market?

Kara: MUNX offers investors an actively managed, intermediate-duration muni ETF solution leveraging GW&K's long-standing expertise and scale in managing more than \$33 billion in municipal bonds (as of December 31, 2025). The strategy focuses primarily on investment-grade tax-exempt bonds and targets an intermediate duration "core" profile, rather than a narrowly defined high-yield or state-specific mandate. GW&K's philosophy emphasizes intensive, bottom-up credit research, structure analysis, and relative-value opportunities across the yield curve. That includes taking advantage of primary-market concessions and dislocations caused by retail-driven flows. We launched MUNX in collaboration with our long-standing partner, AMG, which helps support and coordinate the ETF's operations and distribution, along with our broader mutual fund offerings.

What role can municipal bonds—and MUNX specifically—play in investor portfolios today?

Kara: Tax-exempt municipal bonds can function as the core fixed income anchor in taxable accounts, delivering attractive after-tax income with historically low defaults, and lower volatility than equities or credit-heavy taxable bonds. In today's environment, intermediate municipal bonds offer the potential to lock in elevated tax-equivalent yields while exhibiting less volatility than long-duration strategies. MUNX is designed to be that core allocation: an actively managed, diversified intermediate muni ETF that can sit alongside Treasuries, taxable core, and credit in a broader fixed income mix. For many clients, MUNX can replace the complexity of a large individual bond account—eliminating the need to build and manage a ladder—while giving advisors an institutionally managed, model friendly vehicle that fits neatly into a unified portfolio construction framework.

How should investors think about muni ETFs versus buying individual municipal bonds?

Kara: For most investors, a fund or an Separately Managed Account (SMA) solution are typically more scalable than building large individual-bond ladders. A diversified ETF like MUNX can hold hundreds of securities across sectors, states, and structures, spreading idiosyncratic risk and benefiting from professional management paired with stringent oversight and risk controls. ETFs also provide daily liquidity and holdings transparency, making them easier to integrate into model portfolios and risk systems. Conceptually, an all-in-one active ETF allows the portfolio management team to manage curve positioning, sector exposure, and trading opportunities, while the investor focuses on asset allocation, tax planning, and client outcomes rather than bond-by-bond decisions.

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