Municipal bonds can be issued by states, cities, school districts, counties and towns as well as by special district/agencies for transportation, utility, and healthcare purposes to name a few. (UBS)

Why municipal bonds are a critical component to US infrastructure

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For those investors looking for ways to invest in public infrastructure, look no further than the USD 4.0 trillion US municipal bond market.

As featured in CIO's most recent publication *Made in America*, published 27 June 2023, municipal bonds are a critical component to our nations infrastructure. The US has addressed 75% of its infrastructure needs via this market for over 100 years* providing US governmental entities access to capital in order to fund public infrastructure projects. Municipal bonds can be issued by states, cities, school districts, counties and towns as well as by special district/agencies for transportation, utility, and healthcare purposes to name a few. The proceeds are generally used to build public infrastructure including schools, airports, hospitals, libraries, and a host of other projects for the benefit of residents.

Implications on federal infrastructure investment

The estimated USD 1.2tr in combined new spending from the Infrastructure Investment & Jobs Act (IIJA), the Inflation Reduction Act (IRA) and the CHIPS Act will help municipal governments finance investment in public works, either directly or indirectly. In the absence of these federal monies, municipal issuers would either need to issue debt, substantially increase their rates to directly pay for capital improvements or defer costly infrastructure projects and improvements. The significant boost in federal funding may help change the overall landscape of US infrastructure funding, given state and local governments have historically shouldered an increasing share of these costs.

Which sectors stand to benefit?

The benefits of each infrastructure package will vary by municipal sector, with IIJA largely bolstering transportation-related sectors, and the IRA and CHIPS Act principally advancing the utility sector. Increased investment in public infrastructure often spurs job creation and boosts economic activity. States and local governments will benefit from a positive economic environment, in addition to freeing up monies that otherwise would have been directed toward debt service. There will be a substantial degree of variation among individual credits within each sector with regard to both credit quality and investment performance in an economic slowdown, but the municipal sector has exhibited remarkable resilience during past economic cycles. We expect that to continue.

CIO takeaways

With over USD 225 billion in public infrastructure monies already allocated from recent laws, we expect to see funds disbursed more quickly now that processes and guidance have been established. Leaders will need to leverage all the federal funding during a time of economic uncertainty, but the municipal market certainly stands to benefit from the federal fiscal stimulus, which should help to reduce the USD 2.6tr funding gap identified by the American Society of Civil Engineers in their most recent 2021 Report Card.

For more, reach out to your UBS Financial Advisor for a copy of this month's Municipal Market Guide: Built by bonds, which includes an update on key pieces of legislation.

* McNichol, Elizabeth. August 10, 2017. "It's Time for States to Invest in Infrastructure". Center on Budget and Policy Priorities.