WESTERN ASSET by Franklin Templeton

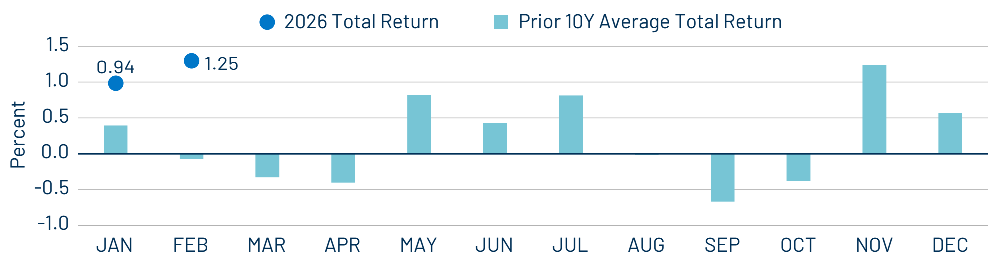
Muni Monthly

Performance Overview

Strong Municipal Performance in February Counters Recent Weakness

In February, market sentiment was shaped by escalating US-Iran geopolitical tensions and sector-specific selloffs driven by concerns about AI's potential disruption to existing business models. Economic data presented a mixed picture, with January nonfarm payrolls increasing by 130,000 jobs, rebounding from December's revised 48,000 gain, while the unemployment rate edged down to 4.3%. Inflation data for January eased from the prior month, with headline Consumer Price Index (CPI) falling to 2.4% year-over-year (YoY) from 2.7% and core CPI easing to 2.5% YoY from 2.6%. All told, Treasuries rallied across the curve, and the municipal yields followed suit but generally underperformed the risk-off sentiment. The Bloomberg Municipal Bond Index gained 1.25% leading year-to-date (YTD) returns higher to 2.20%. February's strong performance counters recent weakness, with the index averaging negative returns in February, largely driven by softening demand ahead of tax season and limited new issuance.

Exhibit 1: 2026 Monthly Performance vs. 10-Year Average



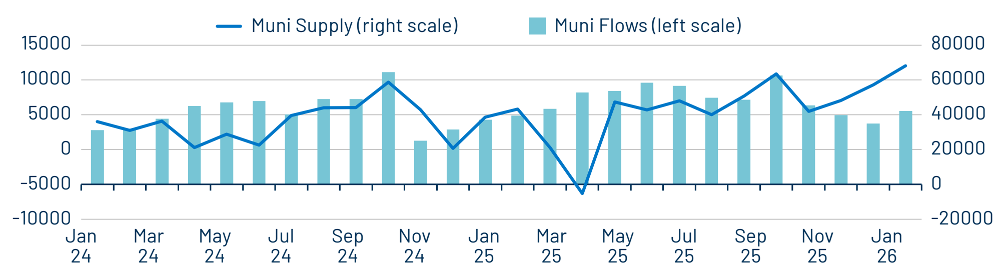
Source: Western Asset, Bloomberg. As of 27 Feb 26.

Technicals

Renewed Investor Demand Bolstered Muni Funds

The strong start of the year has been supported by renewed investor demand, as capital has moved decisively back into municipal mutual funds. Investors appear to show an increasing willingness to capitalize on relatively attractive municipal valuations during periods of elevated market volatility, particularly in longer maturities as the yield curve steepened. According to weekly and monthly Lipper and ICI data, municipal mutual funds and ETFs recorded over $10 billion of net inflows in February. Notably, Lipper estimates that approximately 86% of the $18 billion in YTD inflows has been concentrated in intermediate- and long-duration fund categories. Since January 2024, cumulative net inflows of over $126 billion on top of strong SMA demand have fully offset the $122 billion of net outflows experienced in 2022 and 2023.

Exhibit 2: Muni Demand Accelerated Amid Limited Issuance



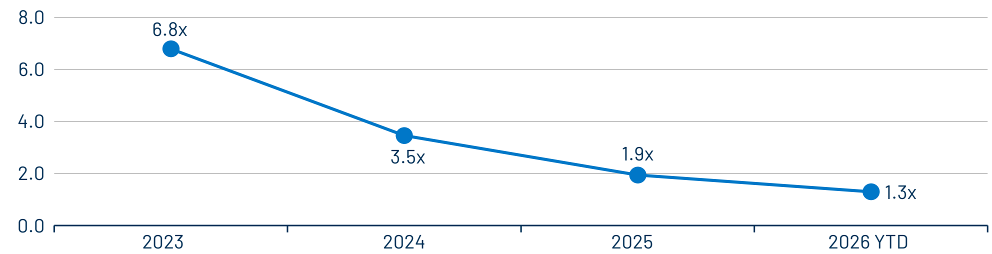
Bloomberg, ICI, Western Asset. As of 27 Feb 26.

Fundamentals

Muni Fundamentals Remained Strong

Municipal fundamentals remained strong, supported by elevated tax collections. However, the pace of upgrades relative to downgrades has continued to moderate. Upgrades have outpaced downgrades YTD by a factor of 1.3x, compared to 3.5x in 2024 and 1.9x in 2025, according to Bloomberg. Notably, Fitch downgraded the city of Chicago during the month from A- to BBB+, while maintaining a negative outlook. Fitch cited consecutive operating deficits and a high reliance on one-time solutions as key drivers of the downgrade.

Exhibit 3: Upgrade/Downgrade Ratio (S&P, Moody's, Fitch Combined by Par Value)



Source: Bloomberg, Western Asset. As of 26 Feb 26; S&P, Moody's, Fitch rating actions combined by par value.

Valuations

Muni Valuation Disparities Create Tax-Efficient Opportunities for Active Managers

The strong YTD performance also represents a meaningful reversal of the underperformance the municipal market experienced in 2025, and muni supply and demand dynamics have shifted valuations in certain segments of the market. For example, AAA rated municipals maturing inside of 10 years now yield less than comparable Treasuries on an after-tax basis, assuming a 37% effective tax rate, largely attributable to high demand for SMA strategies concentrated in shorter maturities. In contrast, using the same tax rate, AAA municipals beyond 20 years offer more than 100 basis points of after-tax yield advantage relative to Treasuries. We believe these valuation disparities create opportunities for active managers to deliver tax-efficient outcomes.

Munis and the Macro[1]

	Prior Month (Revised From)	Consensus	Actual
GDP Annualized QoQ (4Q25)	4.40%	2.80%	1.40%
CPI YoY	2.70%	2.50%	2.40%
PCE	2.80%	2.80%	2.90%
Unemployment Rate	4.40%	4.40%	4.30%
Change in Nonfarm Payrolls	48k (50k)	66k	130k

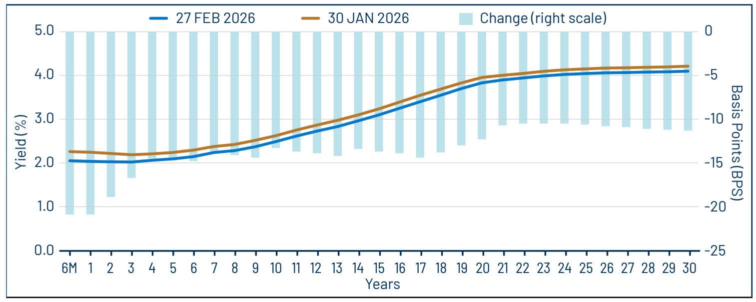
Yield and Curve Changes - AAA Munis vs. Treasuries[3]

	2-Yr	5-Yr	10-Yr	30-Yr
2/28/2026				
AAA Muni	2.16%	2.21%	2.62%	4.29%
Treasury	3.38%	3.50%	3.94%	4.61%
M/T Ratio	64%	63%	66%	93%
Change				
Muni Δ (bps)	▼ -2	▼ -3	▼ -1	–
Treasury Δ (bps)	▼ -15	▼ -29	▼ -30	▼ -26
Ratio Δ (%)	▲ 2	▲ 4	▲ 4	▲ 5
10-Yr Average				
AAA Muni	1.59%	1.72%	2.09%	3%
Treasury	2.36%	2.48%	2.73%	3%
Ratio	67%	69%	77%	93%

After-Tax Yield Pickup[5]

Quality/Maturity Segment	Muni YTW	Taxable Equivalent YTW	Taxable YTW	Taxable Equivalent Muni Yield Pickup	5-Yr Average
10-Yr AAA Munis vs Treasuries	2.47%	4.17%	3.94%	23	63
30Y AAA Muni vs Treasury	4.04%	6.83%	4.61%	222	181
AA Munis vs Corps	3.15%	5.32%	4.53%	79	83
A Munis vs Corps	3.54%	5.98%	4.59%	139	124
BBB Munis vs Corps	4.23%	7.15%	4.92%	223	159
HY Munis vs Corps	5.38%	9.09%	6.71%	238	147

AAA Municipal Yield Curve[2]



Index Returns[4]

	1-Mo Total Return	YTD Total Return
Bloomberg Municipal Bond Index	1.25%	2.20%
Returns by Maturity		
Bloomberg Municipal Bond 1-Year Index	0.41%	0.97%
Bloomberg Municipal Bond 5-Year Index	0.82%	1.81%
Bloomberg Municipal Bond 10-Year Index	1.19%	2.37%
Bloomberg Municipal Bond 20-Year Total Return Index	1.75%	2.78%
Bloomberg Municipal Bond Long Bond Index	1.67%	2.18%
Returns by Credit Quality		
Bloomberg Municipal AAA Index	1.30%	2.21%
Bloomberg Municipal AA Index	1.19%	2.13%
Bloomberg Municipal A Index	1.32%	2.31%
Bloomberg Municipal BBB Index	1.39%	2.35%
Bloomberg Muni High Yield Index	1.67%	2.67%
Returns by Sector		
GO Bond Index	1.13%	2.07%
Revenue Bond Index	1.30%	2.25%
Taxable Muni Returns		
Bloomberg Taxable Municipal Bond Index	2.58%	2.63%
Bloomberg Global Aggregate Index	1.12%	2.06%
Bloomberg U.S. Treasury Index	1.82%	1.72%
Bloomberg U.S. Corporate Index	1.29%	1.47%

Municipal Supply[6]

Year	$B	Month	2025 Issuance	2026 Issuance	YoY	Calls/Maturities	Net
2018	356	January	37.1	35.0	-6%	-23.4	11.6
2019	449	February	39.6	42.2	7%	-35.2	7.0
2020	496	March	43.4				
2021	488	April	52.8				
2022	375	May	53.7				
2023	366	June	58.4				
2024	500	July	56.6				
2025	588	August	49.7				
2026	77	September	48.6				
		October	62.5				
		November	45.4				
		December	39.8				
		Total	**587.8**	**77.2**	**0.9%**	**-58.7**	**18.5**

Demand Technicals - Municipal Mutual Fund and ETF Flows[7]

Year	Flows ($M)	2026	Flows ($M)
2018	8,843	January	9,311
2019	102,554	February	12,034
2020	54,468	March	
2021	105,480	April	
2022	-116,469	May	
2023	-5,695	June	
2024	45,091	July	
2025	61,549	August	
2026 YTD	21,345	September	
		October	
		November	
		December	

[1] *Source: Bloomberg; GDP, CPI, PCE: BEA; Unemployment, NFP: BLS. As of 28 Feb 26.*

[2] *Source: Bloomberg, Western Asset. As of 28 Feb 26. Bloomberg Valuation Service (BVAL) AAA Muni Curve and US On-/Off-the-Run Sovereign Curve.*

[3] *Source: Muni Yields: Thomson Reuters MMD 2-Year, 5-Year, 10-Year and 30-Year AAA Scales; Treasury Yields: 2-Year, 5-Year, 10-Year, and 30-Year Tenors of the US On/Off The Run Sovereign Curve.*

[4] *Source: Bloomberg Municipal Bond Index, Bloomberg Taxable Municipal Bond Index. As of 28 Feb 26. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. Past performance is not an indicator or a guarantee of future results.*

[5] *Source: Bloomberg, Western Asset. As of 28 Feb 26. 10- and 30-Year comparison reflects Bloomberg Valuation Service (BVAL) AAA Muni Curve and US On-/Off-the-Run Sovereign Curve. AA Muni reflects the Bloomberg AA Muni Bond Index. A Muni reflects the Bloomberg A Muni Bond Index. BBB Muni reflects the Bloomberg BBB Muni Bond Index. HY Muni reflects the Bloomberg High Yield Muni Bond Index. AA Corp reflects the Bloomberg AA Corporate Bond Index. A Corp reflects the Bloomberg A Corporate Bond Index. BBB Corp reflects the Bloomberg BBB Corporate Bond Index. Taxable equivalent yield considers top marginal tax rate of 40.8%. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. Past performance is not an indicator or a guarantee of future results.*

[6] *Source: Bloomberg. As of 28 Feb 26.*

[7] *Source: Bloomberg, ICI. As of 28 Feb 26.*

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