



September 30, 2025

Dear Shareholder:

After a flat performance during the first half of the year, the municipal bond market finally jumped into gear in September with municipal bonds staging an impressive rally. September's strong performance was driven primarily by expectations that the Federal Reserve would resume cutting interest rates and by higher-than-normal flows into the municipal bond asset class as investors rebalanced investment portfolios. For the 9-month period ending September 30, the Bloomberg Municipal Bond Index provided a total return of 2.64%.

At its September 17 meeting, the Federal Reserve ("Fed") cut the fed funds target rate by a quarter point to a range of 4% to 4.25%. This represents the first rate cut since December, and it also marks a 125 total basis point reduction in rates since the Fed began its easing cycle in September of 2024. The Fed's long pause was due to inflation concerns arising from tariffs imposed in February and April.

The Fed's statement noted that downside risks to employment have risen and near-term risks to inflation are tilted to the upside. Recent economic data, along with substantial revisions to previous figures, point to a sharp slowdown in job growth. In the Fed's press conference, Chair Powell emphasized that "two-sided risks mean that there is no risk-free path." Two-sided risks is a fancy way of saying the Fed is worried about "stagflation," which is a combination of slow growth, high unemployment, and rising prices. As expected, Chair Powell reiterated that Fed policy decisions would remain data dependent. The Fed's revised dot plot suggests two more quarter point rate cuts this year; an additional quarter point cut in 2026; and, one more quarter point cut in 2027. If these rate cuts happen, the fed funds rate range will end up at 3% to 3.25%.

While tax-exempt yields have already fallen (bond prices up) in response to shifting rate expectations and a softening labor market, the Fed's most recent pivot sets the stage for a more sustained period of declining yields. With this in mind and with tax-exempt yields still at very attractive levels by historical standards, we think the current market offers an attractive entry point for investors. Municipal bonds typically outperform in a declining rate environment while also offering the potential for capital appreciation. Elevated levels of tax-exempt bond issuance that existed during the first half of this year are expected to decline during the year's last quarter. This potentially creates a favorable supply and demand dynamic that should act as a tailwind for municipal bonds for the remainder of this year.

With stock market indices reaching record highs and with additional Fed rate cuts possibly on the way, we think there is a good chance that the recent uptick in asset reallocation will pick up some more steam. It's hard to believe, but there is currently \$7.7 trillion parked in short-term money market accounts! Some of this money will inevitably be reallocated into longer duration, high quality fixed-income assets. While we admit we may be biased, we are convinced that investment grade municipal bonds, with their attractive tax-exempt status, strong credit fundamentals, and inherent diversification benefits, would be a logical landing spot for a portion of these assets.

Thank you for investing with us. We appreciate your business.

Sincerely,

A handwritten signature in blue ink that reads "Allen E. Grimes, III".

Allen E. Grimes, III  
President