Allspring

MARKETING COMMUNICATION

Is Your Cash Account Costing You?

It may be time to consider ultra-short municipal bonds

- **Cash yield volatility:** Cash instruments, like money markets and Treasury bills, may offer competitive yields during high-rate environments, but these yields can quickly reset lower as the Federal Reserve (Fed) eases and short-term policy rates decline.
- **Hidden risks:** While perceived as "safe," cash instruments carry income risk, including reinvestment pressure, potential for lower inflation-adjusted returns, and opportunity costs, compared with short-term bonds.
- **Repositioning for tax-free income:** Investors can mitigate cash interest rate risks by reallocating to ultra-short-duration strategies, such as tax-exempt municipal bonds, which can help preserve income on a tax-free basis with limited interest rate sensitivity and incremental credit risk.

For much of the past three years, cash instruments may have felt like a safe haven for many investors. However, as Federal Reserve (Fed) policy became more accommodative and rate cuts followed, yields on money markets and other cash equivalents declined sharply. Because these instruments typically reset in step with policy rates, the income they generated fell in tandem. As yields dropped, several risks became more visible, including reinvestment into lower-yielding instruments, inflation-driven erosion of purchasing power, and declining real income—particularly in the shortest-maturity holdings.

With traditional cash vehicles losing yield and expectations of further rate cuts forthcoming, some investors are seeking alternatives. Ultra-short municipal bonds may offer a way to maintain stability while providing attractive, tax-exempt income.

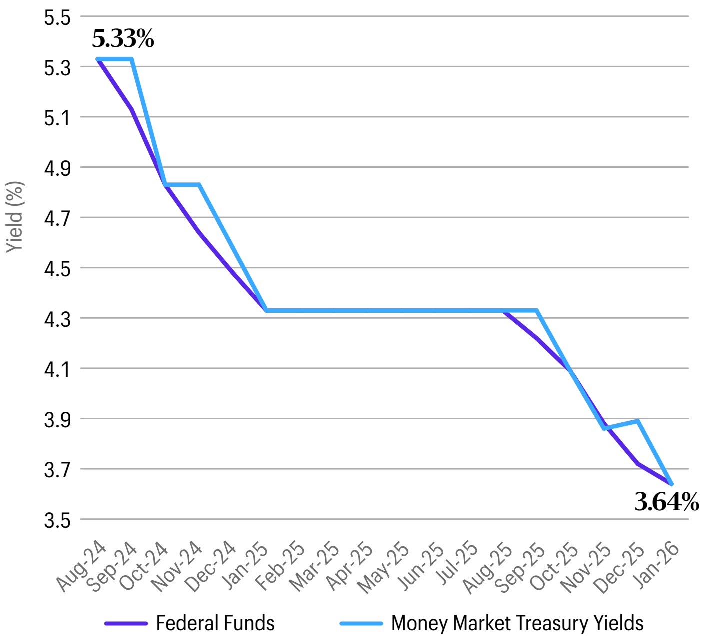
Changing tide of interest rates

In a rising-rate cycle, cash equivalents can look attractive. As money market yields rise alongside the federal funds rate, investors often respond with large inflows into cash-like instruments. But this dynamic is cyclical: when rates fall, yields tend to drop quickly and in lockstep.

Until recently, cash instruments like money markets, Treasury bills, and other cash equivalents offered yields that competed with many conservative fixed income options. However, the yield environment has changed. The market has shifted from a tightening cycle to an easing trajectory, where recent rate cuts by the Fed have become a primary driver of short-term yields.

Since August 2024, the Fed lowered the federal funds rate six times. Over that period, rates fell by a substantial 169 basis points (bps; 100 bps equal 1.00%), from 5.33% to an effective rate of 3.64% as of January 31, 2026.

EXHIBIT 1: FEDERAL FUNDS & MONEY MARKET TREASURY YIELDS



Source: Federal Reserve Economic Data, Federal Reserve Bank of St. Louis. As of January 31, 2026.

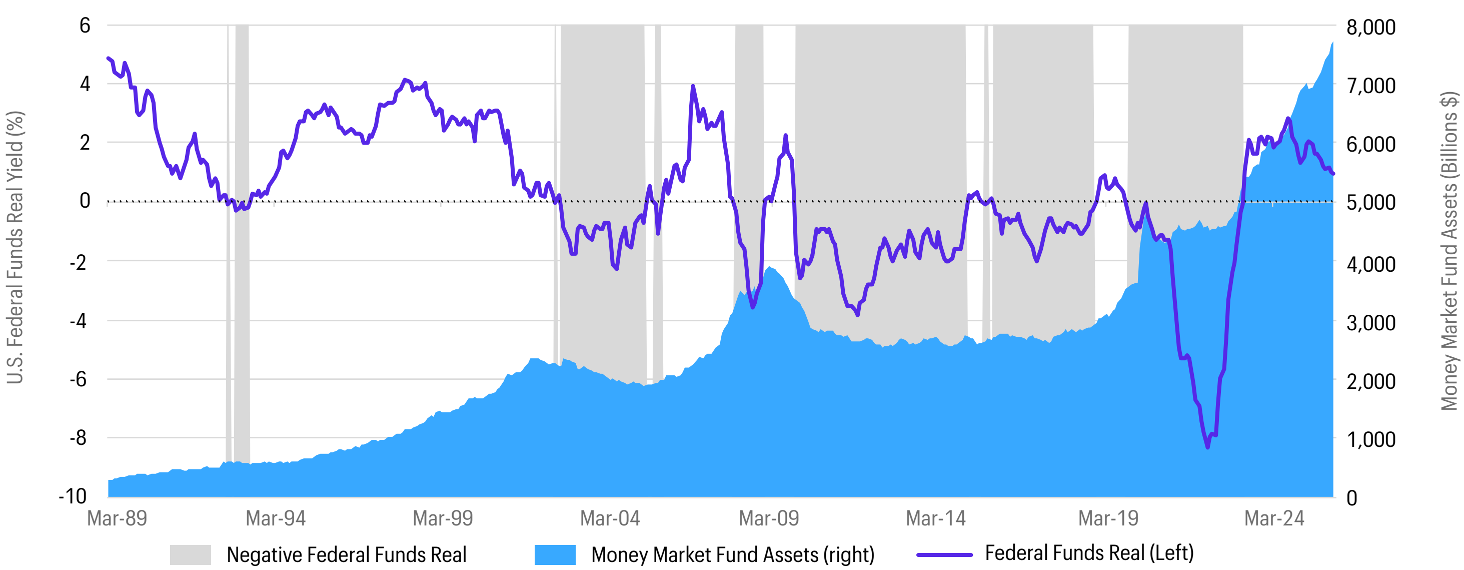
Money market yields are closely linked to the policy rate because the underlying holdings are primarily short-maturity instruments (e.g., Treasury bills, repurchase agreements, commercial paper, and short-dated government securities). As these holdings mature, they are reinvested at prevailing and, more recently, lower yields.

Hidden risks of holding cash

One risk of holding cash instruments is **reinvestment risk**. Money market funds and other cash instruments typically hold securities that mature in days or weeks, which supports liquidity but can create a "reset lower" problem, exposing investors to continuous reinvestment at prevailing market rates. When policy rates are cut, maturing securities are quickly replaced with new holdings at lower yields, causing cash instrument yields to decline in unison with the easing cycle. **This is important because in a falling-rate environment, cash instrument yield deterioration can occur much faster than many investors may expect due to the rapid turnover of these portfolios.**

Another risk is **inflation risk**, where "nominal yields" fail to tell the full story. What ultimately matters is real yield—what an investor earns after accounting for inflation. When the inflation rate exceeds the yield generated by cash instruments, purchasing power can quietly erode. In effect, cash instruments can be nominally stable yet economically risky, particularly in environments where inflation proves sticky or slow to recede.

EXHIBIT 2: U.S. FEDERAL FUNDS REAL YIELD VS. MONEY MARKET FUND ASSETS



Source: Bloomberg Finance L.P. Data as of 31-Jan-26

Finally, there is the risk of **opportunity cost**. Historically, when rates fall, investors often find that short-term fixed income can maintain higher income for longer than cash instruments because it locks in yields over longer maturities. Cash instruments may preserve principal, but it can lag in income generation once a reset begins. Over time, that forgone income can compound into a noticeable gap.

Moving "out the curve"

Moving "out the curve" simply means extending maturities modestly (e.g., shifting from overnight or 1- to 3-month cash instruments into securities with slightly longer maturities of 1+ years). This incremental step can help investors lock in today's yields for a longer period, reducing the risk of the rapid yield resets that may occur when the Fed cuts rates. By modestly extending maturity to capture additional yield, investors can position portfolios to maintain, or possibly enhance income even as short-term rates potentially move lower.

In a falling rate environment, increasing duration can be advantageous. A slight extension allows investors to preserve income longer than cash instruments can, while still keeping overall rate sensitivity relatively low. Because ultra-short and short-term strategies typically maintain limited price fluctuation, they can strike a balance between benefiting from declining rates while avoiding the greater interest rate risk and volatility associated with intermediate or long duration bonds. This targeted approach to duration can help support steadier income with limited rate risk.

For many investors, the real decision comes down to balancing liquidity, yield, and volatility. Cash instruments typically provide maximum liquidity and minimal price movement, but its yields reset rapidly and can fall sharply when policy rates decline. Intermediate and long duration bonds offer higher return potential but can introduce meaningful duration risk. Ultra short and short term bonds tend to strike the "sweet spot" by offering higher yield potential than cash instruments with far less interest rate sensitivity than longer maturity strategies. This makes them particularly well suited for those seeking to maintain or potentially increase yield with only a moderate level of increased risk.

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Why municipal bonds?

Municipal bonds (munis) are debt securities issued by states, cities, and other public entities to fund infrastructure and essential community services. For investors, they offer a way to support public projects while accessing a higher quality segment of the fixed income market.

One of the most powerful features of municipal bonds is their tax-exempt status. Interest income is generally free from federal income tax and, depending on residency and bond structure, may also be exempt from state and local taxes. For investors in higher tax brackets, this can significantly enhance after-tax income and improve the overall value of a muni bond allocation.

Because tax exemption can make a lower nominal yield more competitive than it appears, investors often compare muni yields to taxable alternatives using tax-equivalent yield.

EXHIBIT 3: SAMPLE TAX-EQUIVALENT YIELD

For example, a municipal strategy yielding **3%** tax exempt is comparable to roughly **4.76%** on a taxable basis for an investor in the **37% federal bracket**—meaning the muni bond could **deliver more net income** despite the lower stated nominal yield.

In addition to their tax benefits, high-quality municipal bonds have historically shown relatively **low default rates**, offering an appealing balance of income and stability.

EXHIBIT 3: COMPARATIVE DEFAULT RATES FOR MUNICIPAL AND CORPORATE DEBT[2]

	MUNICIPAL (%)	CORPORATE (%)
AAA	0.00	**1.10**
AA	0.04	1.34
A	0.13	2.39
BBB	**0.96**	5.34
BB	5.07	16.26
B	10.84	27.63
CCC/C[3]	37.80	57.70
Investment-grade	0.22	3.31
Speculative-grade	8.32	25.46

Source: Bloomberg Finance L.P., Allspring, as of 31-Dec-25. Source: S&P Global Ratings. 2. For municipal defaults, S&P's study period was 01-Jan-86 to 31-Dec-24 (dated 06-May-25). For corporate defaults, S&P's study period was 01-Jan-81 to 31-Dec-24 (dated 29-April-25). The calculation represents a 15-year cumulative default rate. 3. S&P's study calculations include all ratings in the C category, from CCC to C.

Strong credit selection remains essential, as the muni market includes a wide range of issuers and structures, but **for investors seeking a conservative alternative to cash instruments, munis can provide both resilience and meaningful income potential, especially on a tax-adjusted basis.**

Getting active with ultra-short municipal bonds

The municipal bond market is vast, diverse, and often highly fragmented, with thousands of issuers and a wide range of structures. In this environment, active management can add meaningful value by conducting detailed issuer-level credit analysis; uncovering relative-value opportunities across sectors; and managing liquidity and downside risks more dynamically than a passive, index-based approach.

Ultrashort municipal strategies are built with a focus on stability and liquidity, typically maintaining duration at one year or less and emphasizing higher-quality issuers. By keeping interest rate sensitivity low and price fluctuations modest, these strategies are often designed to provide a smoother experience—an especially useful profile for investors seeking to shift assets out of cash instruments.

As a result, an actively managed ultra-short muni strategy can serve as an effective bridge between money market funds and longer-term muni portfolios.

This positioning allows investors to seek more stable tax-exempt income, making it a practical option when policy rates are expected to stay consistent or move lower.

Taking action

Are you interested in moving on from lower cash instrument yields? Consider the **Allspring Ultra Short Municipal ETF (AUSM)** or the **Allspring Ultra Short-Term Municipal Income Mutual Fund (SMAIX)**. Each fund offers access to a longstanding, active strategy that we've managed for years.

The strategy invests in municipal securities with an average maturity of one year or less. A relative value approach is conducted by actively managing the four key elements of total return: security selection, sector rotation, duration management, and yield curve positioning.

KEY DIFFERENTIATORS

- Leverages a large, seasoned team of municipal fixed income analysts that's supported by our Investment Analytics team and systems.
- Collaborates across asset classes, such as using taxable fixed income analysts to gain intelligence on corporate bonds.
- May exercise the willingness and ability to move down in credit without compromising the investment process.

Manager description

The **Allspring Municipal Fixed Income team** employs a unique and collaborative approach to investing, where portfolio managers, research analysts, and traders work together while individually covering their own credits. This structure creates independent thinking and supports well-informed decision-making as the team strives to capture maximum alpha and yield potential from market inefficiencies.

Interested in learning more about the ETF, mutual fund, and Allspring's municipal fixed income capabilities? Explore municipal bond investing with Allspring.

For further information

We're committed to thoughtful investing, purposeful planning, and the desire to deliver outcomes that expand above and beyond financial gains.

Click or scan the QR code to check out Allspring's insights:

Duration is a measurement of the sensitivity of a bond's price to changes in Treasury yields. A fund's duration is the weighted average of duration of the bonds in the portfolio. Duration should be interpreted as the approximate change in a bond's (or fund's) price for a 100-basis-point change in Treasury yields. Duration is based on historical performance and does not represent future results.

Alpha measures the excess return of an investment vehicle, such as a mutual fund, relative to the return of its benchmark, given its level of risk (as measured by beta). Alpha is based on historical performance and does not represent future results.

Allspring ETFs are not available for distribution outside of the United States.

Carefully consider a fund's investment objectives, risks, charges, and expenses before investing. For a current prospectus and, if available, a summary prospectus, containing this and other information, visit allspringglobal.com. Read it carefully before investing.

All investing involves risk, including the possible loss of principal. Bond values fluctuate in response to the financial condition of individual issuers, general market and economic conditions, and changes in interest rates. Changes in market conditions and government policies may lead to periods of heightened volatility in the bond market and reduced liquidity for certain bonds held by the fund. In general, when interest rates rise, bond values fall and investors may lose principal value. Interest rate changes and their impact on the fund and its share price can be sudden and unpredictable. Municipal securities risk includes the ability of the issuer to repay the obligation, the possibility of future tax and legislative changes, and other factors that may adversely affect the liquidity and value of the municipal securities in which the fund invests. A portion of the fund's income may be subject to federal, state, and/or local income taxes or the alternative minimum tax. Any capital gains distributions may be taxable. Consult the fund's prospectus for additional information on these and other risks.

It is possible that an active trading market for ETF shares will not develop, which may hurt your ability to buy or sell shares, particularly in times of market stress. Shares may trade at a premium or discount to their net asset value (NAV) in the secondary market. These variations may be greater when markets are volatile or subject to unusual conditions. There can be no assurance that active trading markets for the shares will develop or be maintained by market makers or authorized participants. Shares of the ETFs are not redeemable with the ETF other than in creation unit aggregations. Instead, investors must buy or sell the ETF shares in the secondary market at market price (not NAV) through a broker-dealer. In doing so, the investor may incur brokerage commissions and may pay more than NAV when buying and may receive less than NAV when selling. Investing involves risk, including the possible loss of principal. Bond values fluctuate in response to the financial condition of individual issuers, general market and economic conditions, and changes in interest rates. Changes in market conditions and government policies may lead to periods of heightened volatility in the bond market and reduced liquidity for certain bonds held by the fund. In general, when interest rates rise, bond values fall and investors may lose principal value. Interest rate changes and their impact on the fund and its share price can be sudden and unpredictable. Municipal securities risk includes the ability of the issuer to repay the obligation, the possibility of future tax and legislative changes, and other factors that may adversely affect the liquidity and value of the municipal securities in which the fund invests. A portion of the fund's income may be subject to federal, state, and/or local income taxes or the alternative minimum tax. Any capital gains distributions may be taxable. Consult the fund's prospectus for additional information on these and other risks.

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Credit-quality ratings apply to underlying holdings of the fund and not the fund itself. Standard & Poor's, Fitch Ratings, and Kroll Bond Rating Agency rate the creditworthiness of bonds from AAA (highest) to D (lowest). Ratings from AA to CCC may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the rating categories. Moody's rates the creditworthiness of bonds from Aaa (highest) to C (lowest). Ratings Aa to Caa may be modified by the addition of a number 1 (highest) to 3 (lowest) to show relative standing within the ratings categories. Credit quality and credit-quality ratings are subject to change.

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