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Municipal Market Shrinks $7.84 Billion in February; Returns Fall.

(Bloomberg) — The U.S. municipal bond market shrank in February by $7.84 billion, contracting for at least the 14th month in a row as redemptions and maturities overwhelmed sales of new securities.

States and localities issued $31.5 billion of new bonds last month, compared with $23.2 billion that came due and $16.2 billion of debt called early, according to data compiled by Bloomberg. Since the start of 2014, the amount of outstanding securities has decreased by $167.6 billion, reducing the $3.5 trillion market by 4.54 percent.

The shrinkage helps explain why munis outperformed Treasuries even as the U.S. debt market declined last month. The Bank of America Merrill Lynch US Municipal Securities Index lost 0.99 percent in February, the first drop since the end of 2013, while the Bank of America Merrill Lynch US Treasury & Agency Index fell 1.69 percent, the most since May 2013.

Municipal bond sales are set to be little changed in the next month while the amount of redemptions and maturing debt falls.

States and localities plan to issue $11.4 billion of bonds over the next 30 days, according to data compiled by Bloomberg. A week ago, the calendar showed $11.6 billion planned for the coming month. Supply figures exclude derivatives and variable-rate debt. Some municipalities set their deals less than a month before borrowing.

California Bonds

California plans to sell $1.9 billion of bonds, Maryland has scheduled $922 million, Los Angeles Department of Water and Power will offer $495 million and Cypress and Fairbanks Texas Independent School District will bring $297 million to market.

Municipalities have announced $13.1 billion of redemptions and an additional $10 billion of debt matures in the next 30 days, compared with the $26.3 billion total scheduled a week ago. Last year, the market shrank by 4 percent. This year, maturities are poised to drop 38 percent to $176 billion from the 2014 levels.

Issuers from New York have the most debt coming due in the next month, with $2.52 billion, followed by California at $1.17 billion and Wisconsin with $488 million. California has the biggest amount of securities maturing, with $803 million.

Investors added $274 million to mutual funds that target municipal securities in the week ended Feb. 18, compared with $693 million in the previous period, according to Investment Company Institute data compiled by Bloomberg.

Muni Yields

Exchange-trade funds that buy municipal debt increased in value by $206 million last month, or 1.29 percent, to $16.1 billion.

State and local debt maturing in 10 years now yields 106.2 percent of Treasuries, Bloomberg data show. Since 2000, the gap has averaged 93.8 percent.

Bonds of Michigan and California had the best performance over the past year compared with the average yield of AAA rated 10-year securities, the data show. Yields on Michigan's securities narrowed 11 basis points to 2.38 percent while California's declined 10 basis points to 2.30 percent.

Puerto Rico and New Jersey handed investors the worst results. The yield gap on Puerto Rico bonds widened 66 basis points to 9.61 percent and New Jersey's rose 13 basis points to 2.70 percent.

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