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Munis Defying History of March Losses With Best Rally Since 2008.

(Bloomberg) — The $3.5 trillion municipal market is on pace for its best March performance since 2008, defying a history of weakness in the month as higher tax rates stoke demand.

Munis have gained about 0.3 percent in March, after posting losses in the month in eight of the past 10 years, partly as investors sold to pay tax bills, Bank of America Merrill Lynch data show.

With the top federal tax rate climbing to 39.6 percent as of last year, the highest since 2000, investors have less incentive to sell before the April 15 tax-filing deadline. Underscoring the heightened demand, muni mutual funds have lured $1.3 billion in March, the most for the month since 2012, Lipper US Fund Flows data show.

“Given the higher federal marginal tax rate, there’s more of a compelling argument to hold muni positions,” said Jeffrey Lipton, head of muni research at Oppenheimer & Co. in New York.

City and state debt has earned about 1.1 percent this year, after a 9.8 percent gain in 2014, the best annual performance since 2011.

Munis still aren’t keeping up with Treasuries, which have returned 1.3 percent this year.

Surging supply is contributing to the underperformance, said Dan Heckman, a fixed-income strategist who helps oversee $126 billion at U.S. Bank Wealth Management in Kansas City.

Issuers are taking advantage of interest rates close to generational lows to refinance, pushing 2015 sales to about $92 billion, compared with $54.1 billion in the same period last year, data compiled by Bloomberg show.

If history is any guide, April may bring more gains. Local-government bonds rose in April in nine of the past 10 years.

“When investors are looking at alternatives, there are very few in the fixed-income market that have as many positive aspects as the municipal market,” Heckman said.

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