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BlackRock Says the Key Gauge of Muni Bond Prices May Be Broken.

- **The ratio of muni yields to Treasuries is closely watched**
- **But firm's strategist says main buyers aren't driven by it**

The world's largest money manager says one of the most meaningful measures in the municipal-bond market is starting to mean a lot less.

That's because a steady influx of cash earlier this year pushed some state and local government debt yields to record lows relative to U.S. Treasuries. In normal times, the decline of that ratio — which is closely watched by professional investors — would signal that the securities had become significantly overpriced.

But Sean Carney, the head of municipal strategy at BlackRock Inc., which oversees nearly $7 trillion in assets, said in an interview that the buy-and-hold investors who dominate the municipal market are more interested in the tax breaks and the protection the securities offer from stock market swings. That may help explain why retail buyers have poured more than $43 billion into municipal-bond mutual funds even as prices hit record highs against Treasuries this year.

"There's less predictive power to muni-Treasury ratios today," said Carney, who like others on Wall Street still watches it.

Corporations like banks and insurance companies do pay attention to the gauge, Carney said. But those companies aren't driving the municipal-bond market rally right now. Some have even slashed their holdings because the 2017 tax overhaul that reduced corporate tax rates, which makes tax-exempt debt less attractive compared with other securities.

"Everybody likes to get caught up in muni-Treasury ratios," Carney said. "They mean a lot when you're looking for a non-traditional buyer to buy munis. When it's retail that's driving it — and it's retail driving this rally — they tend not to care as much about ratios."

This may mean that tax-exempt bonds have more room to run regardless of whether municipals are considered cheap or expensive, Carney said. Tax-exempt debt has returned about 7.7% this year, according to the Bloomberg Barclays index. While that's less than Treasuries or corporate bonds, it's still the biggest gain since 2014.

For those who do still care about the gauge, the ratio of 10-year municipal yields to Treasuries is hovering around 86%, up from as little as 72% in May.

Maybe that means they're cheap. Or maybe not.

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