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## Everything Is Great in Muni-Bond Market. That's the Big Worry.

- **If everyone is on same side, it topples over 'pretty easily'**
- **Money managers discuss outlook at Bloomberg News event**

In the municipal-bond market, everything's going strongly in the right direction: prices have been rising, mutual funds have received new cash from investors for the past 57 weeks, and new debt sales have been gobbled up.

But Guy Davidson, chief investment officer of the municipal-debt business for AllianceBernstein, is still preparing for the risk that his firm's outlook is wrong, given that he and other money-managers are largely in lockstep with expectations for another year of positive returns.

"When everyone's on one side, it gets toppled over pretty easily," he said at a panel hosted by Bloomberg News on Wednesday.

The $3.8 trillion municipal market returned 7.5% last year, the biggest annual gain since 2014, and in January posted its biggest monthly gain in six years. The run-up has pushed yields to the lowest in over six decades, leaving some analysts skeptical of how much more prices can rise.

Davidson said his firm expects "decent" economic growth and isn't anticipating any big moves in yields. But he said he has taken some steps to prepare for a surprise economic downturn, such as adding U.S. Treasuries to portfolios because they tend to outperform during a recession.

At the Wednesday panel, investors from Macquarie Investment Management, Parametric Portfolio Associates, and Columbia Threadneedle Investments expressed similar outlooks for the coming year.

Catherine Stienstra, head of municipal investments at Columbia Threadneedle, said 2020 may be more of a "coupon-clipping" year for investors, meaning returns will be driven more by interest payments than price gains. Still, she said the individual investors who flocked to the municipal market in record numbers last year will likely keep buying the securities to gain the tax breaks or avoid stock-market volatility.

She said she expects such demand to keep supporting the market, even if it isn't as strong as last year. "What drove the strong returns in 2019 are still in place," she said.

Nisha Patel, a director at Parametric, also said the weekly cash influx into mutual funds could slow if investors are deterred by the low yields. Municipal bonds maturing in 10 years yield just 1.2%, half what it was in late 2018, according to the Bloomberg BVAL index. The Bond Buyer's 20-year index is hovering near the lowest since the 1950s.

Patel said she noticed that some new municipal-bond deals this week weren't met with the overwhelming demand that's become routine and left deals far oversubscribed. A move higher in rates would likely lure investors who have been sitting on the sidelines, Patel said.

“The market staying stagnant, where it is, is probably something that we would be concerned about,” she said.

Not all muni-bond investors are discouraged. Steve Czepiel, who leads municipal bond portfolio management for Macquarie, said he expects another strong year of returns, saying that rates have room to go lower and that credit spreads can tighten more.

Macquarie is still favorable on high-yield municipals — which last year rallied the most since 2014 — and is being “selective” in what it buys, Czepiel said. He said they prefer deals where there’s a lot of issuance to choose from, like health care, so the firm can be choosy.

“The credit markets are in good shape and they will continue to perform due to that technical demand,” he said.

**Bloomberg Markets**

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