
Muni Bonds Now Yield Next to Nothing, But Americans Keep Buying.

- **Cash keeps flowing in as rally pushes prices to heady levels**
- **Yields in secondary market driven by past gains, havens**

In theory, the swiftly disappearing yields on municipal bonds should be deterring the little buyers like Greg Fazakerley who dominate the $3.8 trillion market.

That's not happening in practice. Even before the coronavirus set off a stampede into financial havens, American state and local government debt prices had pushed past the levels once seen as triggers for an investor revolt. The latest panic has given the market a further jolt, with about $2.3 billion sent to municipal-securities mutual funds last week even as benchmark yields breached the psychological threshold of 1%.

"Taking a look at the monthly statement in municipals, your manager is talking about basis points," said Fazakerley, a 72-year-old real-estate developer who is continuing to buy municipal securities. "We kind of chuckle over a cup of coffee. That's not where we're squeezing the lemon to get more juice."

Americans who already held about $1.9 trillion of state and local debt poured another $113 billion into mutual funds focused on the securities since early 2019, according to Investment Company Institute and Federal Reserve figures. That stepped up buying came even as prices hit new highs relative to Treasuries, yields slid toward more than 60-year lows and fixtures tailored to such buyers — like 5% coupons — were jettisoned, leaving some money managers questioning what threshold, if any, will cause individual investors to retreat.

Nicholos Venditti, a portfolio manager for mutual fund company Thornburg Investment Management, said it's difficult to currently make the case for buying municipal debt. He said one client gave push-back on a 10-year bond he bought that yielded just under 1.4%.

"If enough people scratch their heads and ask that question, that's where you start to see a little bit of a break in the asset class," he said.

The fidelity can be explained by the steady returns the securities have delivered as prices continue to rise, causing buyers to keep stepping up their investments. Overall, municipal securities haven't lost money since 2013 and last year returned 7.5%, the biggest gain since 2014. Citigroup Inc. analysts said the market has benefited from a self-reinforcing cycle, with positive returns drawing in more cash from individuals.

Starting in early 2018, the demand was increased by the cap President Donald Trump placed on state and local tax deductions. As a consequence, many Americans began using tax-exempt securities as an alternative way to drive down what they owe. The demand received an additional spur this year from a flight-to-quality movement in markets given that defaults by state and local governments were extremely rare even during the last recession. That has driven the yield on 10-

year benchmark bonds to about 0.94%, less than one-third of what it was in 2013.

J.R. Rieger, who invests in municipals and runs a blog about bond investing called the Rieger Report, said the securities make sense as a risk-off trade. “The problem is you’re not going to earn any yield at all,” he said.

Nevertheless, buyers haven’t been turned off yet. Los Angeles International Airport, rated AA, last week borrowed at below AAA yields, with bonds maturing in 2021 yielding just 0.63%. Even risky debt is paying only what top-rated securities once did. An Ohio agency sold a massive tobacco-settlement bond sale with unrated debt due in 2055 trading at an average of 3.4% yields on Friday.

Lewis Appelbaum, a retiree who invests in municipal bonds, said he’s not worried about the sub-1% yields. He estimates he has about 30% of his assets in municipals.

“It’s certainly unattractive, but where would you go?” he said. “Where would you put your money that’s going to be more attractive?”

Retail investors are notoriously bad at timing the market and often move like a herd, plowing in money when the market is going up and pulling back when it falls.

Debra Taylor, who advises high net-worth individuals at Taylor Financial Group in New Jersey, said she isn’t a “fan” of the municipal market given where yields are, but they still make sense for clients who don’t have the right temperament for risk.

Even a 30% or 40% allocation to municipals can make sense for some. “Part of it is a factor of what the alternatives are — not that munis are this incredible, screaming opportunity,” she said.

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