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Muni Bonds Having Strong May, But Are They A Good Long-Term Investment Amid Budget Deficits?

KEY POINTS

- **Cities and state across the country hurtle towards the worst fiscal crisis in decades**
- **The bond rally in May offset the big loss the asset class suffered in March**
- **State and city governments will balance budgets which were hammered by a plunge in tax collections**
- **Municipal bonds — debt securities issued by state, municipality or county governments to finance capital expenditures — are poised to deliver their best monthly performance in more than a decade in May 2020 – despite the chaos triggered by the coronavirus pandemic and business shutdowns.**

As cities and state across the country hurtle towards the worst fiscal crisis in decades amid an unprecedented economic collapse, the $3.9 trillion muni bond market has gained 2.96% for the month through Friday, according to the Bloomberg Barclays Muni Bond index.

The bond rally in May offset the big loss the asset class suffered in March – as yields fell to 60-plus year lows (yields drop when bond prices rise). On Friday, the yield on the benchmark 10-year tax-exempt muni debt tumbled 5 basis points to 0.83%.

In May through Friday, the iShares National Muni Bond ETF (MUB), the largest exchange-traded fund tracking muni-bond markets, gained 1.03%.

In April, MUB dropped 1.38%; while in March, the ETF plunged 2.98%.

Bloomberg reported that the May rally has been facilitated by an inflow of cash into muni bond funds – even the riskiest ones – due to efforts by the Federal Reserve to protect the markets from another liquidity crisis.

In addition, as more states start to reopen some businesses and coronavirus deaths appear to be leveling off, investor sentiment has improved.

Patrick Luby, a muni bond analyst with CreditSights Inc., a financial research firm, said, state and city governments are expected to seek to balance budgets which were hammered by a plunge in tax collections.

“The serious and thoughtful way in which many [muni bond] issuers are beginning to wrestle with what are going to be really painful decisions from a financial and human perspective is constructive to the [bond] market,” Luby said.

Most state governments are predicting significant budget shortfalls in the coming years, which will no doubt mean massive layoffs to cut costs.

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By Palash Ghosh

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