Muni Bonds Prove a Refuge for Investors Hiding From Rising Rates.

- **The debt posts small March gains as Treasuries see losses**
- **It may be short-lived, with Barclays saying ‘stay defensive’**

For now at least, America’s state and local government bonds are a refuge from the losses piling up in other corners of the debt markets.

Yields on 10-year benchmark tax-exempt bonds edged lower Friday by about one basis point to 1.07%, a 4 basis-point drop since the end of last week, according to Bloomberg’s BVAL indexes. Yet those on comparable Treasuries have jumped about 14 basis points to 1.55% over that time.

The result: municipal bonds have eked out a small gain this month while Treasuries and corporate debt have lost 0.81% and 1.26%, respectively, according to Bloomberg Barclays indexes.

The disconnect shows that the municipal market’s usual ties to Treasuries have weakened somewhat amid speculation that the nation’s recovery from the pandemic will drive interest rates higher. That conviction was reinforced by Friday’s report from the Labor Department that employers added nearly twice as many jobs to payrolls in February than had been expected.

The municipal market’s status as a haven may prove short lived. As Treasury yields started trending higher late last year, those on state and local government bonds continued to fall, opening a record gulf between the two. Then that swiftly changed during the last two weeks of February, when yields surged steeply.

That jump in yields could be helping the municipal market by drawing in investors who may have balked at buying when valuations were at record highs. Yet the market may face pressure in the weeks ahead if investors continue to pull cash out of mutual funds or sell debt to pay tax bills, as they often due around this time of year.

“Munis were able to withstand the Treasury selloff much better, as more attractive valuations brought in buyers, helping tax-exempts outperform,” Barclays municipal analysts Mikhail Foux, Clare Pickering and Mayur Patel wrote in a note Friday. “However, if rates keep rising, coupled with fund outflows and heavier tax-exempt supply, munis will likely follow, and investors should still stay defensive.”

Bloomberg Markets

By Fola Akinnibi

March 5, 2021, 10:34 AM PST