BARRON'S

August 31, 2020

# Muni Bond Insurance Makes a Comeback

Insurance for municipal bonds, out of favor for years, has started to make a comeback as the market grapples with extraordinary risks.

The portion of municipal bonds sold with this downside protection jumped to 10% in May and has remained elevated since, after hovering below 6% for most of the past decade, according to The Bond Buyer newspaper.

Lower-rated issuers, with ratings of, say, A or triple-B, buy the protection for their bonds to lower the yields they have to pay to investors. The insurers “wrap” the bond with their own double-A ratings, guaranteeing that interest and principal payments will continue to flow to investors even if the issuer can’t pay.

Insured Puerto Rico bonds have continued to trade near 100 cents on the dollar, while uninsured bonds plunged amid the territory’s historic debt restructuring.

“Retail and institutional investors are showing increased selectivity or awareness of credit,” says Sean W. McCarthy, chief executive of Build America Mutual, one of only two insurers in the field. “That’s why we’ve seen a tectonic shift,” he adds.

Assured Guaranty, the larger of the two, recently wrapped a $385 million school-district financing for the Dormitory Authority of New York, one of the nation’s largest issuers of municipal bonds.

Still, there’s a long way to go. Before the financial crisis of 2007 and 2008, more than half of municipal bonds carried coverage, with seven companies providing most of it.

Many of those firms retreated because of losses on mortgage-backed securities.