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WSJ: Investors Yank Money from Municipal-Bond Funds.

June's $13.5 Billion Outflow Is Second Largest on Record

Investors yanked $13.5 billion from mutual funds that invest in municipal bonds in June, according to Lipper FMI, a retreat that is making it harder for several cities, states and towns to raise money.

Individual investors are big buyers of municipal bonds for their tax-free status and their usually stable prices. But as Treasury bond prices fell last month, sparking a broad bond market rout, some of the largest mutual fund companies managing municipal bond funds saw huge amounts of money march out their doors.

June's outflow is about 2.2% of the $680.7 billion managed by the funds and the second largest monthly outflow of cash from the market on record, said Matt Lemieux, senior research analyst at Lipper, which has been tracking fund flows since 1992.

The selloff sent borrowing costs higher for municipalities, causing some to delay plans to raise money. The yield on 10-year, triple-A-rated municipal debt rose to 2.74% Tuesday from 2.08% on June 3, according to Thomson Reuters Municipal Market Data. The 2.74% yield is near levels last seen two years ago.

The Coatesville Area School District in Pennsylvania wanted to refinance $25 million of debt about three weeks ago but waited to see if rates would decline, said Tom Kozlik, director at investment bank Janney Montgomery Scott LLC, which is an underwriter of the bond sale. Rates have stabilized somewhat, and the deal is rescheduled for Wednesday. A Coatesville school district representative couldn't immediately be reached for comment.

Health-services company Geisinger Health System of Danville, Pa., has put plans to sell $284.4 million of bonds on a "day-to-day" status, "waiting to determine whether attractive fixed rates will return," said Timothy Fitzgerald, vice president of treasury management at the company.

The pace of redemptions from funds is mellowing as benchmark interest rates pause amid a two-month march higher, said fund managers, but big investor withdrawals mean they must sell bonds quickly, hurting prices further.

Managing investor redemptions was difficult, said Alex Grant, who manages two mutual funds totaling about $700 million in assets for RS Investment Management Co. He got through the end of the month and the end of the second quarter in part because he "was sitting on some cash," he said.

Investors saw returns suffering in June as trading became trying. Barclays's municipal bond index saw a negative return of 2.83% last month, the biggest loss since September 2008, when the index saw a negative total return of 4.69%.

Vanguard Group Inc., which has about $100.6 billion in municipal bond assets, saw the most money exit its municipal bond funds last month, about $2.3 billion, Lipper said. The funds had enough cash reserves to meet investor redemptions, said spokesman John Woerth, adding the company's money-market funds saw money pour in.

OppenheimerFunds Inc., Fidelity Management & Research Co. and Nuveen Fund Advisors Inc. each saw more than $1 billion exit their municipal bond funds, Lipper said.

OppenheimerFunds' municipal bond fund assets total about $33.3 billion, while Fidelity's are $29.3 billion and Nuveen's are about $26.7 billion, according to Lipper.

Christine Thompson, chief investment officer of Fidelity's bond group, said its funds met investors' demands for redemptions, in part because the firm ensured it had cash on hand. Representatives for OppenheimerFunds and Nuveen declined to comment.

The June pullback is only surpassed by a $16.6 billion outflow in December 2010, when investors were spooked by banking analyst Meredith Whitney's predictions of large numbers of defaults by states and municipalities, a projection that so far has been unfounded.

The outflow figure includes weekly and monthly reporting of open-ended municipal bond mutual funds as well as exchange-traded funds. Lipper said more than 95% of the funds it tracks have reported June data.