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WSJ: Detroit Has Wiped $13.8 Billion From S&P's Muni Index.

Since Detroit filed the biggest municipal bankruptcy ever on July 18, the S&P Municipal Bond Index—a proxy for the broader municipal-bond market—has dropped 0.97%, as of Aug. 7. The index tracks about $1.4 trillion worth of bonds, so the nearly 1% in negative return represents lost value of about $13.8 billion.

The true lost value is likely larger, given that the index tracks only a portion of the $3.7 trillion muni market.

J.R. Rieger, vice president of fixed-income indexes at S&P Dow Jones Indices, says the sharp drop cannot be attributed to only fears about rising interest rates, should the Fed wind down its bond-buying program as expected. Detroit's problems, and the ramifications it may have for the wider muni market, are a main factor, he said.

Rieger pointed out that the S&P U.S. Issued Investment Grade Corporate Bond Index actually recorded a modest 0.07% positive return since Detroit's bankruptcy filing.

Concerns have also been reflected in cash flows out of mutual funds: Investors have yanked about $17 billion from weekly-reporting muni-mutual funds and exchange-traded funds over the past 10 weeks, according to Thomson Reuters unit Lipper.

Detroit's state-appointed emergency manager, Kevyn Orr, has proposed saddling some bondholders with significant losses, a somewhat alarming proposition in what is usually a safe and relatively sleepy market. Only a handful of major municipalities are in bankruptcy out of tens of thousands of towns, cities, counties and other units of government in the U.S.

"These are big distressed situations, and the bankruptcy cases are posing uncertainty in regard to how they will be resolved," Rieger said. "That could impact municipal investors nationwide."

Even so, Rieger said he was surprised at how poorly the index has performed since the city's bankruptcy. The index actually posted a positive return in the approximately two months after Jefferson County, Ala., filed a large bankruptcy case in November 2011.

"Detroit has been a distressed credit for quite some time," he said. "It's the power of that repetitive negative news that retail investors must be reacting to."