# Bond Case Briefs

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## WJS: Municipal Bonds Wrap Up Tough Year.

Municipal bonds are on track to post their worst annual performance in nearly two decades as 2013 ushered in more financial woes for U.S. cities.

Municipal debt is down 2.58% so far this year after handing investors a 6.78% return in 2012 and a 10.70% return in 2011, according to Barclays's municipal-bond index.

"We've had these high-profile credit problems that have caught the attention of investors," said Jim Grabovac, senior portfolio manager at McDonnell Investment Management, which oversees about $8 billion in municipal debt.

Bonds from states, cities and counties are having their worst year since 1994, when interest rates spiked. Bond markets have sold off broadly this year as investors braced for the Federal Reserve to start dialing back easy-money policies that had supported credit markets since the financial crisis. The Fed last week said it would begin paring its bond purchases in January.

The yields on the benchmark 10-year Treasury note hit a three-month high of 2.985% on Tuesday, up from 1.78% at the end of 2012. Bond yields move in the opposite direction as prices.

But municipal bonds, long coveted by mom-and-pop investors for their relative safety and tax benefits, took a bigger hit than many other bond markets after a number of negative headlines out of places such as Detroit, Chicago and Puerto Rico.

Munis were "the one fixed-income class that didn't stabilize," said Tom Weyl, municipal strategist at Barclays. Mr. Weyl cited Detroit's filing for bankruptcy protection, concerns about Chicago and Illinois pension costs and economic worries in Puerto Rico. Highly rated U.S. corporate debt is down just 1.57% in comparison, according to Barclays data.

Some investors say 2014 is likely to be brighter for munis. Barclays still projects losses, but not as severe: a negative return of 1.45%. It also expects municipal bonds to post better returns next year than U.S. Treasury debt. New bond sales are forecast to decline 16%, to about $270 billion, which could help prop up prices.

And some tax revenues are recovering from the economic downturn. States have reported growth in tax collections for 15 consecutive quarters, according to the Rockefeller Institute of Government.

Detroit's bankruptcy filing contributed to the negative headlines in 2013 that helped push down municipal bonds for the year. European Pressphoto Agency

The municipal-bond market was last roiled in late 2010, when analyst Meredith Whitney predicted widespread municipal defaults.

There hasn't been a wave of defaults, although a smattering of cities have stumbled. Stockton, Calif., and Jefferson County, Ala., sought protection from creditors in recent years. Detroit's filing is the largest municipal bankruptcy in U.S. history.

"All these defaults you see in the muni market are demographic problems or just bad deals," said Gene Gard, a portfolio manager at Dupree Mutual Funds, which oversees $1.3 billion and invests in highly rated municipal bonds. "We don't think there's a big day of reckoning happening in the muni market."

By MIKE CHERNEY

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