# Bond Case Briefs

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## As Puerto Rico's Storm Grows, Muni Market Is Smooth Sailing.

You'd never know from looking at the $3.7 trillion municipal market that the largest restructuring in its history is unfolding in Puerto Rico.

Individuals last week poured more money into tax-exempt mutual funds than at any other time this year, just days ahead of the commonwealth's well-anticipated default on $422 million of Government Development Bank debt. Munis have gained every month this year, only the second time that's happened since 1999. And on the U.S. mainland, prospects are brightening: S&P Global Ratings has upgraded more localities than it has lowered for 13 straight quarters, the longest streak since 2001. Just nine issuers have defaulted in 2016 apart from Puerto Rico, compared with 24 at this time last year.

Much like how Puerto Rico is an island territory off the coast of the U.S., the trends show that investors are treating the commonwealth's debt crisis as separate from the broader municipal market. Monday's default, its largest yet, was a long-time coming: Puerto Rico lost its investment grades over two years ago, and 10 months ago Governor Alejandro Garcia Padilla declared its debt too crippling to pay.

"It was telegraphed," John Miller, who oversees $110 billion of munis as co-head of fixed income at Nuveen Asset Management, said in an interview on Bloomberg Radio with Tom Keene and Michael McKee. "It's a continuation of an ongoing reality that they don't have the revenues to meet all their budgetary expenses and pay debt service at the same time."

Puerto Rico wasn't the only borrower on the precipice of a historic default. Atlantic City, the distressed New Jersey gambling hub, made $1.8 million in interest payments due May 1, after saying it might not. It avoided the first default for a municipality in the Garden State since the Great Depression.

The clearest sign that the market is shrugging off Puerto Rico and Atlantic City is the money pouring into tax-exempt bond funds.

Individuals have added assets to muni funds for 30 straight weeks dating back to October, the longest stretch since March 2010, Lipper US Fund Flows data show. The $1.2 billion inflow in the week through April 27 was the largest of 2016, and came after Moody's Investors Service warned that a Puerto Rico default was inevitable.

"They are unique," Peter Hayes, the head of municipals for BlackRock Inc., the world's largest money manager, said in a Bloomberg Television interview. "It's been coming for the last few years. Investors were either comfortable or not."

"The market is pretty big. It's $3.7 trillion. It's different than other fixed-income asset classes. They don't all have problems."

Part of the reason investors have been so willing to buy munis is because the bonds have gained every month this year, S&P Dow Jones Indices data show. It's just the second time that's happened in the past 18 years.

Also padding returns: improving credit quality for states and cities across the country. S&P said in February that it upgraded nearly twice as many issuers as it downgraded in the fourth quarter of 2015. The 13th-straight quarters of elevating more municipalities than it lowered is the longest streak since 2001.

Fitch Ratings said last week that the trend continued: It upgraded 29 issuers and lowered 19 in the first quarter. Positive outlooks are the highest since at least 2001, when Fitch began tracking that, while negative outlooks are the lowest since the third quarter of 2008.

Defaults, aside from Puerto Rico, are also slowing among municipal borrowers. Just nine issuers missed payments for the first time in the first four months of the year, compared with 24 at this time a year ago and 15 in 2014, according to data from Municipal Market Analytics.

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