

## Is Now the Time to Reconsider Municipal Bond Funds?

(NAPS)—Investors continue to demonstrate concern about ongoing volatility in the equity market. In many cases, equity shareholders have received large taxable capital gains distributions after last year's negative returns, compounding the pain. What's an investor to do?

Remember municipal bond funds? While muni bond returns will never rival the highs of equities, munis are generally viewed as less volatile, more conservative investments across different market environments. The Lehman Muni Bond Index was up 13.28% in 2000, versus the S&P 500 Index which was down 9.10% for the year. The Lehman Muni Bond Index was up 2.2% in 2001, versus the S&P 500 Index which was down 4.37% as of May 31, 2001.

Ironically, while volatility in the equity market over the recent past is prompting investors to consider whether other options might make sense for them, the very fact that the bull market was so strong for so long is, in and of itself, a compelling reason to examine the allocation of your portfolio. The decade-plus run of strong equity returns in many cases skewed the mix of individual portfolios, dramatically increasing the portion dedicated to equities. The percentage you may have allocated years back to fixed-income funds may now be much less than what you had intended, with capital appreciation having driven up your exposure to stocks. Thus, your overall risk levels might be far greater than the last time you balanced your portfolio.



For example, a typical asset allocation put together at the end of 1993 might have been 55% equities, 35% bonds, and 10% cash. If that portfolio had not since been "tweaked," on average, the asset allocation would now be far more weighted toward equities—somewhere in the magnitude of 70%, with now only approximately 22% weighted in bonds.

"Asset allocation is extremely important now," stated Robert MacIntosh, vice president and portfolio manager of 12 municipal bond funds at Eaton Vance. "The market is driven by fear and greed. At the bottom of markets like October 1998, people don't want to touch stocks. Give me shelter, so to speak. At the high end, it's a wonderful party and let's enjoy it. That's the precise reason asset allocation makes sense. The current environment represents a classic opportunity for investors to fine-tune a portfolio and add potential value over the next 18 months."

Munis are also an asset class that thrives in an environment of low interest rates, and Mr. Green-

span has made it clear that the Federal Reserve Board's bias will be to continue to cut rates to ward off a recession, in Mr. MacIntosh's opinion. "With layoffs occurring in many key industries and businesses highly reluctant to invest in new plants and equipment, further rate reductions are very likely," he observed.

While muni yields may appear miniscule compared to the eye-popping equity returns of the recent past, remember that munis offer tax-exempt yields—in other words, a portion isn't going to the government in the form of taxes. For investors in the top federal tax bracket, a seemingly small 4.5 percent annual tax-exempt yield on a national municipal bond fund actually translates into a taxable equivalent yield of 7.45 percent. That means an investor would have to earn 7.45 percent in taxable income on an equity fund, in order to derive the same after-tax benefit as earning a tax-free 4.5 percent. For single-state municipal bond fund investors, that return can be even greater because the income from in-state muni bond funds is usually exempt from state and often local taxes.

Eaton Vance, a leader in tax-managed investing, offers the most single-state municipal bond funds of any mutual fund provider. Eaton Vance municipal bond funds are actively managed, with the managers keeping a close eye on the level of capital gains. In fact, Eaton Vance municipal funds paid out very little in capital gains and have an impressive record of tax efficiency.