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Mortgage Crisis Forces the Closing of a Fund

By MICHAEL M. GRYNBAUM

Losses on investments weakened by the deepening housing crisis have forced Bank of America to close a multibillion-dollar high-yield fund, the largest of its kind, after wealthy investors withdrew billions of dollars in assets.

The losses, while small, have added to concerns about the safety of other so-called enhanced cash funds, which offer higher returns but greater risk than ordinary money market accounts.

The fund, run by Columbia Management, had $40 billion in assets last month, but that began to shrink after some of its investments were devalued or frozen, a bank spokesman said. The bank briefly shut off withdrawals after the fund dropped to about $12 billion last week.

The closing will cost investors still in the fund about half a cent on the dollar.

“There’s no question that a number of clients aren’t happy that they don’t get back the dollar,” said Robert Stickler, a Bank of America spokesman. “That was the expectation. But it’s not like they’re losing 5 or 10 percent here. We’re talking about one half of 1 percent.”

The Bank of America fund is by far the most prominent fund of its type to face losses related to the subprime crisis.

“It’s hard to see how the sector could get any chillier,” said Peter Crane, president of Crane Data, which tracks the money fund industry. “This is a crippling blow.”

Mr. Crane said the Bank of America fund, called the Columbia Strategic Cash Portfolio, was by far the biggest of its kind. He estimated that before its devaluation, the fund accounted for one-fifth of the total assets invested in enhanced cash funds.

Mr. Crane based that number on his estimate that $200 billion is currently invested in 15 enhanced cash funds.

A separate firm that tracks money market data, iMoneyNet, said the figure may be as high as $850 billion, spread across several dozen funds.

Unlike money market accounts, which typically invest in relatively stable securities like Treasury bonds, enhanced cash funds cater to wealthy individuals and institutions that are willing to accept a riskier portfolio and can afford the entrance fee. Bank of America's fund required institutional investors to have at least $25 million in assets.

But in several instances, those riskier investments included vehicles hurt by recent problems in the credit market. Bank of America's fund invested in structured investment vehicles, or SIVs, which issue short-term debt tied to home loans; some of the SIVs were later downgraded by ratings agencies, Mr. Stickler said.

Other enhanced cash funds made similar investments and faced a similar fate. Federated Investors, the money management firm this is based in Pittsburgh, took a $4.9 million charge last month to unwind its Enhanced Reserve cash fund at full value after it was hurt by credit market problems, Bloomberg News reported.

Investors in a similar high-yield fund run by General Electric's asset management arm were not as lucky. The fund paid 96 cents on the dollar after losing hundreds of millions in bets on mortgage-backed securities.

Bank of America decided to freeze its fund after receiving a request for a substantial withdrawal from a single large investor. "That's what finally broke the camel's back," said Mr. Stickler, the spokesman. He declined to identify the investor, but said the withdrawal was for financial need and not because of a lack of confidence in the fund.

Bank of America's fund accepted only institutional investors, who will receive their share of the securities "in kind," Mr. Stickler said. Smaller investors may receive cash, he said.

Despite the gloomy news, Mr. Crane said he believed that the urge to make money would eventually lure investors back to higher-risk portfolios.

"I don't think this means the death of enhanced cash funds," he said. "The seeds to their rebirth are being sown in all this destruction. Everyone wants to say they're in Treasury bills and their portfolios are supersafe — but they'll be back."