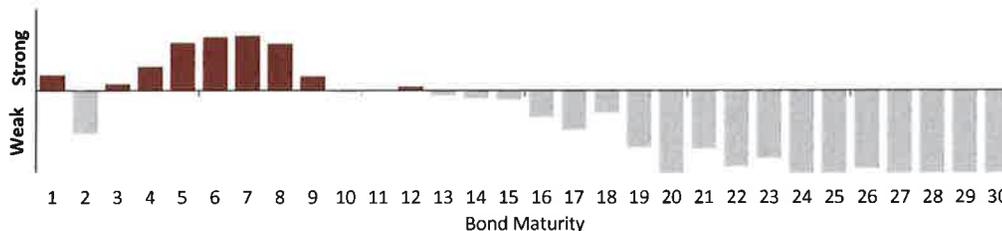
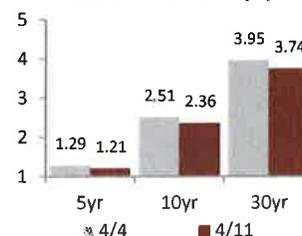


MUNICIPAL ISSUER BRIEF

Strong or Weak Market for Bond Sellers



Muni Bond Rates (%)



Heading into this week, the swift move to lower yields 10-years and out on Thursday and Friday last week left much of the curve in the "weak" dynamic for issuers. While bond evaluations are now not as aggressive after the rally, the momentum continues to generally benefit issuers.

MARKET UPDATE

BORROWING RATES LOWERED YET AGAIN: Most bonds in the municipal market rallied late last week and benchmark yields touched 2014 lows. This is an excellent time for issuers to come to market.

INVESTORS & ISSUERS: Holiday week puts issuance on back burner.

- Issuance this week is half of the already light weekly average for 2014.
- This dearth of issuance could encourage strong bidding by dealers in competitive deals, and investors to seek negotiated deals.
- Illinois—one of the lowest-rated states or territories in the union—competitively sold bonds last week and **received the lowest borrowing rate in at least 3 years and investors continue to seek out lower-rated investment grade issuers.**
- New Jersey GO and appropriation-backed bonds were downgraded one notch by Standard & Poor's last week and **the market for these bonds actually improved as a result.** This is atypical but it was a well telegraphed downgrade and it occurred while the general market was stronger.
- The new Puerto Rico GO issue from March sold-off as much as 75 basis points in secondary activity after an initial investor sold \$50 million of its stake. **Puerto Rico continues to operate in isolation not connected to the rest of the municipal market—a positive trend for other issuers.**
- Mutual funds reported an increase in cash investments, **particularly in the high-yield oriented funds.** Funds that invest in longer-dated bonds did not see as much interest.
- However, the lack of cash here has been made up by non-traditional investors, such as **insurance companies and asset-management arms of large corporations looking for relative value.**

BUYERS BITES:

WHAT IS TRENDING HOT:

- 1) Lower investment grade issuers
- 2) Healthcare, continuing care facilities
- 3) New Jersey GO, appropriation bonds

CURRENTLY HARDER SELLS:

- 1) Puerto Rico GO, utilities

WHO IS REPORTEDLY BUYING:

Large banks, separately managed accounts, high-yield mutual funds

Recent Trends in Fixed Income Yields (%)



Figure 1: The chart above tracks the **MMA 5% AAA** and U.S. Treasury 10-year yields since January of 2013. The low tax-exempt issuance along with Treasury market strength has generated strong returns in 2014. For issuers, we point out that the Benchmark ended last Friday at the low yield of the year. The momentum and seasonality favors a continuation toward lower yields.

ANOTHER BABS BILL: A Massachusetts Senator introduced a bill that would bring back the Build America Bond (BABs) program with lower subsidy rates and a provision that protects the subsidies from sequestration cuts. Sen. Edward Markey (D-MA) introduced the Bolstering Our Nation's Deficient Structures Act of 2014 or BONDS Act, last week and it was referred to the Senate Finance Committee. The subsidy rate would be 31% for BABs issued in 2014 and lowered by 1% each successive year, stopping at 28% for BABs issued in 2017. The legislation also would allow qualified BABs to be current refunded. BABs put issuers at risk of seeing subsidy cuts in the future.

TOPIC OF THE WEEK: LATEST CHAPTER IN DETROIT’S BANKRUPTCY SAGA

DETROIT: Last week, the city of Detroit came to an agreement with the three insurers of the city’s now defaulted general obligation bonds. In the proposed settlement, the city will cover debt service on 74% of the \$388 million of unlimited tax general obligation bonds (ULT GO). This is substantially higher than the city’s last plan to pay a mere 15% to bondholders.

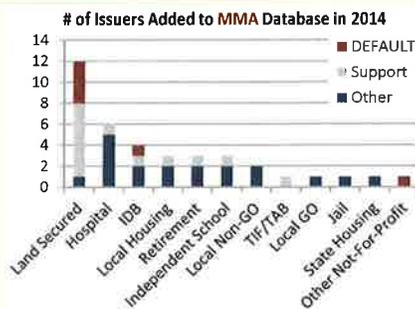
WHAT THIS MEANS FOR YOU: If approved, the settlement positively resolves much of the market’s worry about precedents that could have been set for other ULT GOs. Meaning, while Detroit’s problems are unique, how this bankruptcy proceeds has implications for all issuers of general obligation bonds. **MMA** last wrote about these implications in the December 10th edition of MIB that can be found [here](#). The widely held view in the investment community is that ULT GO bonds are stronger than limited tax or general fund obligations. The Detroit bankruptcy resolution could challenge this view and possibly raise the borrowing costs of other issuers of these bonds. In this latest settlement **MMA** points out that:

- 1) The principal recovery of 74% is only slightly below market expectations and significantly better than the plan of 15%; and
- 2) The settlement attempts to mitigate concerns over the strength of the ULT GO pledge through recognition by the court that the bonds have a lien on the pledged ad valorem taxes and that the levy constitutes special revenues in the US Bankruptcy code. This would give investors in ULT GOs in MI a better argument for par recovery in a future Chapter 9. Consequently, ULT GO issuers in MI could see a lower cost of capital in future bond issues, effectively ending the “Michigan penalty” now being paid in the state.

If this settlement is approved by the Court, the remaining market-moving issues in the city’s bankruptcy will be: 1) whether or not revenue bond issuers can use Chapter 9 to reduce the interest rate paid to bondholders; 2) whether the courts will actually allow pension benefits to be cut; and 3) if this case provides room for more cities—whether in Michigan or not—to pursue strategic bankruptcy to eliminate their debts. These are all major issues, but, arguably, are of less direct importance than the treatment of the city’s ULT GO security.

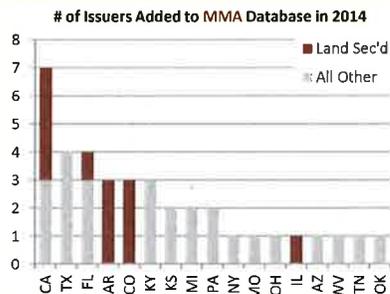
DEFAULT TRENDS AND A BIT ON DC

DEFAULT TRENDS MOSTLY IMPROVE: First-time payment default trends continue their constructive tone, with just 6 first-time defaulters so far in 2014. The number of newly impaired credits (meaning, disclosing technical and payment defaults) is rising, however, with 38 additions to the database so far in 2014, versus 33 during the same period in 2013. The mix this year is diverse: land-secured issuers are still the largest component ([see chart to the right](#)), but **MMA** counts 11 other sectors providing new impairments. And by geography, CA has been the biggest contributor (with 7 issuers overall, 4 of which are land-secured) but there are 16 other states with newly troubled projects ([see chart below](#)). **MMA** interprets this finding—that more projects are suffering but fewer are defaulting—as a sign of how dependent past municipal payment default incidence has been on just a few, catastrophically troubled sectors: FL CDDs, CO Met Districts, TX Jails, MI charter schools, etc. The recent improvements in default trends are certainly encouraging, however caution remains warranted in non-rated credit selection and surveillance. These trends are important as potential investors can become hesitant amid adverse credit headlines and an adverse context can negatively impact the demand and interest rates for a deal.



PRIVATE ACTIVITY BOND DATA: The Joint Committee on Taxation (JCT) recently released data on private activity bond issuance (PAB) and use of PAB proceeds, which shows that 61.5% of total dollar volume of PABs were used for hospitals and other projects.

Chair Dave Camp’s tax reform proposal would eliminate tax-exempt PABs. JCT’s work using 5-year data (2007-2011) indicates: Over 5 years, there was \$273 billion in total PAB issuance, with the following breakdown:



- 34.1% 501(c)3 non-hospital projects
- 27.4% 501(c)3 hospital projects
- 12% qualified mortgage bonds
- 8.4% qualified residential rental bonds
- 6.4% airport bonds
- 4.9% water, sewer, solid waste bonds
- 3.2% qualified student loan bonds
- 1.8% smaller issuer bonds

REGIONAL BOND ISSUES (Moody's/S&P/Fitch)

NORTHEAST

On April 9th, **Wells Fargo Securities** priced \$500 million of transportation revenue bonds for the **New York Metropolitan Transportation Authority**; A2/A+/A; callable in 5/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.74	+47
2024	3.00	3.06	+61
2044	5.00	4.27	+38

Notes: New York issuers led performance last week.

MID-ATLANTIC

On April 10th, **Wells Fargo** priced \$131 million of general obligation refunding bonds for **Charlotte, North Carolina**; Aaa/AAA/AAA; callable in 7/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.31	+4
2024	5.00	2.49	+4
2029	5.00	2.98	-15

Notes: The 20-yr maturity benefited by insurance company interest

MIDWEST

On April 10th, **Illinois** sold \$250 million of general obligation bonds to **Bank of America Merrill Lynch**; A3/A-/A-; callable at par in 4/1/2022:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	2.06	+79
2024	5.00	3.42	+97
2039	5.00	4.54	+64

Notes: The issuer chose insurance on bonds in 2033-2035

SOUTHEAST

On April 8th, **Beaufort County SD South Carolina** sold \$25 million of general obligation bonds to **PNC Capital markets**; Aa1/AA/NR; callable in 3/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.33	+6
2024	4.00	2.54	+9
2029	4.00	3.23	+10

Notes: An infrequent issuer, the deal saw good demand

SOUTHWEST

On April 7th, **BOSC, Inc.** priced \$43 million of unlimited tax school-house bonds for the **Lamar Consolidated Independent School District, Texas**; Aaa/AAA/NR; callable in 2/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2021	4.00	2.04	+10
2024	5.00	2.60	+9
2029	5.00	3.16	-3

Notes: Pricing through the AAA Benchmark is rare for Texas issuers.

FARWEST

On April 10th, **Siebert Brandford Shank & Co.** priced \$409 million of lease revenue bonds for the **State Public Works Board of California**; A2/A-/A-; callable 10/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.70	+43
2024	5.00	3.00	+55
2039	5.00	4.19	+39

Notes: The issuer saw strong demand, especially in 10-years