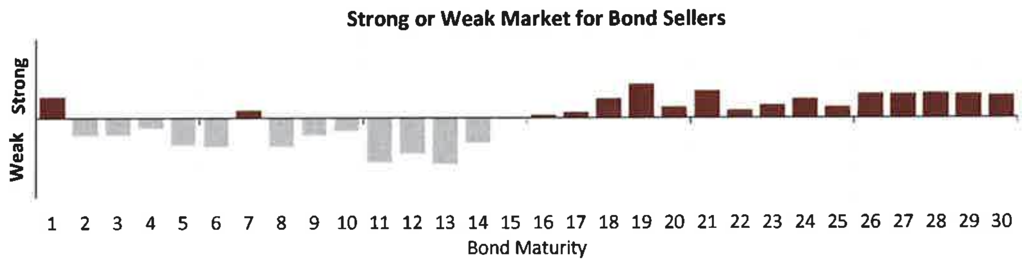
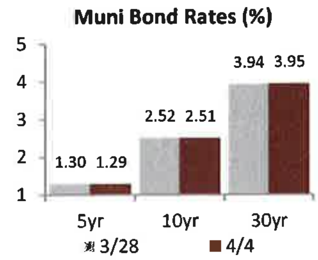
MUNICIPAL ISSUER BRIEF





Heading into this week, the climate for issuers looks better outside of 15 years as that is where the market did best in last week's rally. There continues to be some difficulty on bonds inside of 15 years.

MARKET UPDATE

THE MARKET IMPROVED AFTER JOBS DATA: Momentum shifted last Friday after a slightly weaker March jobs report sparked a rally in Treasuries and municipals followed. In addition, larger global concerns regarding economic growth renewed bond bid.

INVESTORS & ISSUERS: Market direction shifted on Friday.

- The monthly nonfarm jobs report fell short of expectations and **contributed to a rally in many bond markets at the end of last week**. Most Wall Street firms had expected the national jobs report to show an exuberant U.S. economy. When it did not, many investors moved into bonds for their relative safety. The **Municipal bond market joined the Treasury rally.**
- Also in favor of issuers this week is that —once again—the lackluster issuance continued to put the supply/demand imbalance tilted toward issuers. This implies potential for strong pricing.
- **The several higher education issuers in the market place** last week had to re-price to slightly higher yields. The University of California and Texas priced before the Friday economic report and the market was under modest pressure to higher yields at that time. As a result their borrowing costs increased slightly and the bonds subsequently traded at lower yields in secondary market on Friday. **See page 4 for more.**
- **The larger New York issuers that underperformed two weeks ago traded better more recently.** The city's TFA and MTA are selling bonds this week and may take advantage of this new stronger pricing trend. The TFA did well with retail orders on Friday and Monday selling $190 million out of $225 offered.
- **Illinois** is selling its general obligation bonds competitively this week. **The state's GO has outperformed the triple-A market** and tightened as much as 50 basis points since the start of the year.

BUYERS BITES:

WHAT IS TRENDING HOT:

1) Lower investment grade issuers
2) Illinois GO
3) Bonds maturing 20-years and longer
4) Higher education bonds of varying credit quality

CURRENTLY HARDER SELLS:

1) Puerto Rico issuers

WHO IS REPORTEDLY BUYING:

Large banks, separately managed accounts, life insurance companies

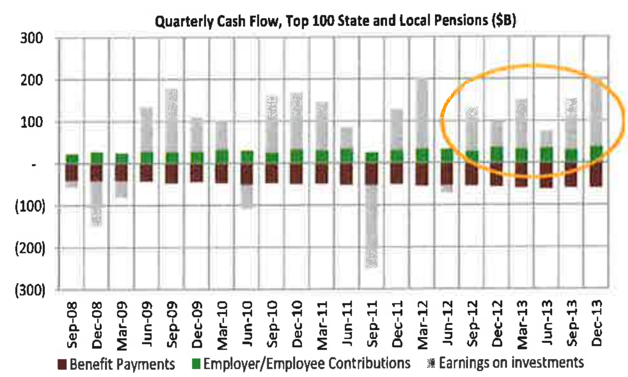


__Figure 1:__ The chart __above__ tracks the quarterly cash flow of the nation's 100 largest state and local pension systems since 2008. The grey bars represent earnings on investments. Circled is the strong performance since 2012 as these gains could entice some states and localities to issue pension obligation bonds, betting on continued good performance. We discuss pension obligation bonds on __page 3__ in this week's __Topic of the Week.__

GASB WON'T DELAY PENSION RULE IMPLEMENTATION: The Governmental Accounting Standards Board (GASB) recently announced it would not delay the implementation date of new GASB pension reporting rules. GASB Statement No. 68, Accounting and Financial Reporting for Pensions, will go into effect for fiscal years beginning after June 15. GASB said the request to delay implementation was denied because the board did not believe that it would benefit its stakeholders. **MMA** examines the issuance of pension obligation bonds in the "Topic of the Week" on **page 3**.

TOPIC OF THE WEEK: PENSION OBLIGATION BONDS

RETURN OF PENSION OBLIGATION BONDS: **MMA** expects pension obligation bond (POB) issuance to re-emerge in the market over the next 2 years as more state and local governments seek capital market solutions for unfunded pensions. Issuance should increase as a result of: **A)** Rising awareness of unfunded pension liabilities in light of new GASB accounting methods being implemented in next year's CAFRs; **B)** Robust pension investment performance of late (see **figure 1 on page 1**) that may lead managers to believe these results can be continued, which is needed to cover the debt service of POBs; **C)** Moody's focus on pension obligation that could make issuers feel impelled to replace liabilities with new POBs and **D)** state and local budgets which remain under material pressure from rising expense budgets and weaker economic recovery making one-time budget savings allowed by POBs more attractive. **To recall**: state and local governments sell taxable POBs, transferring proceeds into one or more employee pension funds but keeping the new debt's liability on their own balance sheet. Not only does this strategy boost the pension fund's funding ratio, but the transfer also can be accounted as satisfying one or more years of the government's employer contribution to the pension system — giving that government temporary budget relief. This is a primary driver for POB issuance but also why it is a symptom of questionable management practices. This is because it is a one-time budget savings wherein issuers can accept enormous market performance and policy risks. For the bonds to project a positive effect on pension funding, securities purchased with POB proceeds must achieve a cumulative net return in excess of the bonds total costs—a challenging investment objective.

WHAT THIS MEANS FOR YOU: Although 2013 was the lowest year for POB issuance since 2006 ($660 million), and YTD issuance is just $50 million (one local MI bond sale), **MMA** expect total par will rise through 2016. The net effects on the municipal market will be negative: POBs are almost always a drag on credit quality. POBs are an aggressive and often imprudent strategy. Governments that use or have used POBs are likely to be viewed with some suspicion by investors as reflective of a gimmick. It is important to note that there needs to be a very sophisticated understanding of POBs by the entity's finance staff as well as elected officials who may entertain the idea of using this as a financing tool. Even then, red flags are raised by rating agencies and investors as to the long-term health of the government. All municipal issuers should be aware of POB issuance in their vicinity as rating agencies will view this as a credit negative and investors may demand increased rates thus increasing borrowing costs. Pensions are already a hot button topic in light of the Detroit bankruptcy, and the role POBs played in the city's finances. Pressure to use one-shot budget fixes like POB issuance are historically viewed with healthy skepticism.

WASHINGTON ROUND-UP

HOUSE OKs BUDGET RESOLUTION: The House passed a FY15 Budget Resolution last week, the day after it was introduced by House Budget Chairman Paul Ryan (R-WI). The non-binding resolution is likely to help shape how the House Committees tackle their work related to federal spending for the coming fiscal year. It should be noted that the resolution will more than likely not see the light of day in the Senate. There are many provisions of interest to state and local governments, including:

- Capping the top individual tax rate at 25%, which in turn means that more than $1 trillion annually must be found in savings through the tax code. Governments should be concerned that this could mean that the exemption on municipal bond interest could be eliminated, as well as the state and local tax deduction.
- The Highway Trust Fund (HTF) would only receive revenues from fuel taxes, therefore creating new restraints on the funding for infrastructure. For many years, the federal government has added funds to the HTF to meet the demands of transportation projects. The proposal would no longer allow the federal government to add to the fund. Additionally, the resolution would allow a state to opt-out of the HTF and pay for their transportation projects solely though state fuel taxes.
- Provide states with greater flexibility for some federal aid programs, yet with reduced funding from the federal government. Additionally, the resolution calls for a "hard look" at many federally backed community and regional programs, including the eligibility criteria for Community Development Block Grants.
- Medicaid reforms and greater flexibility with state programs.

SENATE EXPECTED TO TAKE ON EXTENDERS: Last week the Senate Finance Committee approved the *Expiring Provisions Improvement and Reform Efficient Act (EXPIRE)*, a bill that extends certain non-permanent tax code provisions. Congress did not address these items prior to turning the calendar over for 2014, and many in the House and Senate are hoping that they will do so quickly and have the votes before election season gets into full swing to ensure various programs remain in place. The Act includes provisions that would:

- Allow for taxpayers to deduct their state and local sales taxes instead of their state and local income taxes. This option is important for those who live in states without an income tax. It is worth noting that there have been many efforts in the past to make this provision permanent, a topic that may be addressed in the House Ways and Means Committee this year.
- Provide a $400 million allowance for tax credit Qualified Zone Academy Bonds issued in both 2014 and 2015.
- Allow for unused Empowerment Zone Facility Bonds allocation to issue those bonds through 2015, part of a 2-year extension for empowerment zone tax incentives and does not provide additional funding for these programs.

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

NORTHEAST

On April 3rd, **Citigroup Global Markets Inc.** priced $68 million of refunding bonds for **Suffolk County, New York**; A3/A+/A; callable in 2/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.81	+50
2024	3.00	3.20	+65
2025	3.125	3.32	+65

Notes: Assured insurance allowed for re-pricing to lower yields

MID-ATLANTIC

On April 3rd, **Janney Montgomery Scott** priced $2.6 million of general obligation bonds for the **Johnsonburg Area SD, Pennsylvania**; NR/A/NR; not callable:

Maturity	Coupon	Yield	+/- AAA 5%
2015	0.45	0.45	+4
2016	2.00	0.75	+12
2018	2.00	1.44	+49

Notes: With less Pennsylvania school supply, this deal did well

MIDWEST

On April 3rd, **RBC Capital Markets** priced $89 million of general revenue refunding bonds for **Board of Regents of the University of Oklahoma**; NR/AA-/AA; callable at par in 7/1/2022:

Maturity	Coupon	Yield	+/- AAA 5%
2019	3.00	1.54	+23
2024	5.00	2.89	+34
2029	5.00	3.40	+17

Notes: The shorter call option made for tighter spreads

SOUTHEAST

On April 1st, **Morgan Stanley &Co. LLC** priced $88 million of new facilities project revenue bonds for the **Mississippi State University Educational Building Corporation**; Aa2/NR/AA; callable in 8/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.57	+27
2024	5.00	3.03	+45
2029	5.00	3.67	+30

Notes: The 10-year bond of this deal saw good demand

SOUTHWEST

On April 1st, **Wells Fargo Securities** priced $258 million of system financing revenue bonds for the **Board of Regents of the University of Texas**; Aaa/AAA/AAA; callable in 8/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.43	+13
2024	5.00	2.66	+13
2044	5.00	3.80	+41

Notes: The issuer had to raise yields in a re-pricing

FARWEST

On April 1st, **Goldman Sachs & Co.** priced $211 million of general obligation bonds for the **San Diego Unified School District**; Aa3/AA-/NR; callable 1/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.45	+15
2024	5.00	2.80	+27
2029	5.00	3.39	+19

Notes: With so much higher ed issues, prices were cut slightly