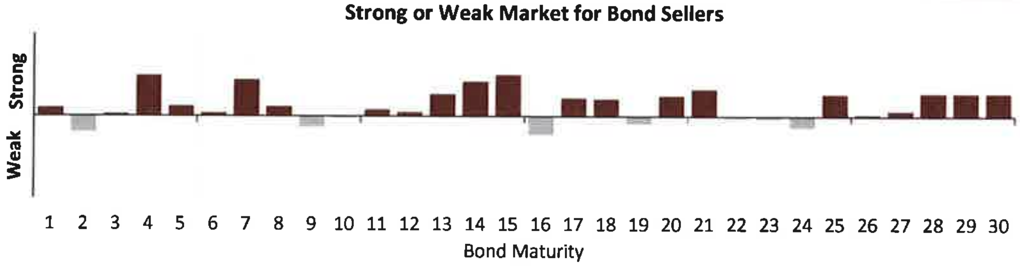
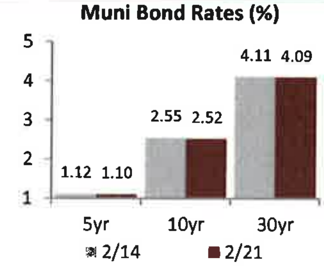
MMA The Power of Independence

FEBRUARY 24, 2014

MUNICIPAL ISSUER BRIEF





Heading into the week, while not as evident as it was to start the month, most maturities continue to be in the 'strong' column—where issuers may experience a more aggressive pricing for their bonds. The few areas that are on the weak side are one-offs and trending better than the previous week.

MARKET UPDATE

SUPPLY STILL LACKING: Issuance, or the lack thereof, continues to be a driving force in this market. Borrowing rates for municipalities continue to be lower than borrowers in other markets principally for this reason. This week the trend keeps on.

INVESTORS & ISSUERS: The market continues to favor issuers.

- **The municipal market is again lacking bonds for investors to purchase.** At this point, 2014 looks to be going at a pace in which there would be a drop in issuance of 33% compared to last year. We look more at issuance this year and what it means for you in our **Topic of the Week** on **page 2**.
- **Keep an eye on Delaware and the California Department of Water Resources, which will sell competitively later this week.** Last week, the Florida Board of Education and Oyster Bay Township of New York both had very strong bids from Morgan Stanley and Citi, respectively, as dealers continue to pay more for your bonds on the lack of overall supply. If this happens again on Thursday it will bode well for all issuers heading into the first week of March.
- The University of Texas decided **to come to market on short-notice to take advantage of the current tone** and where borrowing rates stand. This happened a few times the previous week with other issuers as well.
- The New York Metropolitan Transportation Authority found **very strong interest by retail investors in its sale last week.** In a single day the Authority sold 75% of its deal to retail. Issuers in the state of New York and other high-tax areas should consider marketing bonds to retail in a more concerted fashion.
- This week **MMA** expects Rep. Dave Camp (R-MI) to release his version of tax-reform. The possible legislations is apt to have provisions on the municipal industry and impact market activity.

DETROIT UPDATE: On Friday morning last week, the city of Detroit filed its plan of how to handle its bankruptcy with a Federal Court. The plan—which has not been approved—would give its bondholders 20% of the value of their investments. This would alter the strength of all general obligation bond pledges by many issuers in the entire marketplace and especially for those in Michigan. **MMA** anticipates borrowing rates to rise for issuers in Michigan and in other states that do not provide a statutory lien that benefits GO bond holders. To learn more about Detroit and you click here.

BUYER BITES:

WHAT IS TRENDING HOT:
1) New York retail
2) The 5 to 15-year part of the curve
3) Short-call options continue to rally

CURRENTLY HARDER SELLS:
1) Long maturities lagging shorter ones
2) Detroit and MI GO issuers

WHO IS REPORTEDLY BUYING:
Regional banks, short maturing mutual funds, separately managed accounts

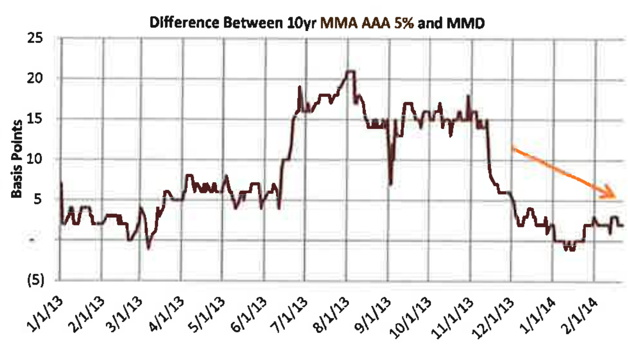


Figure 1: *This chart shows the basis point difference between where the 5 largest municipal underwriters identify a triple-A GO municipal bond is valued versus the Thomson Reuters MMD data-set (taken from the Bond Buyer).* ***MMA*** *prefers to ask municipal dealers where they value the market as they understand the intent of investors. Note that the difference between the two data-sets has declined since last Fall (yellow arrow) in the 10-year area. This is a technical positive for issuers that want to borrow in this maturity range as there is broader acceptance of interest rate levels.*

TOPIC OF THE WEEK: ISSUANCE

ISSUANCE: The principal story line in 2014 for most municipal market participants thus far has been the lack of supply. The data is very clear: in January of 2013 the amount of municipal bonds sold was $27.0 billion compared to this year's January that saw $18.8 billion issued. February of 2013 saw $24.6 billion. **MMA** projects this February to have roughly $15.0 billion, which would mean that there is one-third less issuance this year versus last. One way to quantify just how low issuance has been is by looking at the *Bond Buyer's* 30-day Visible Supply. In **Figure 2 below** we chart the 30-day supply versus its average of the last 3 years. Historically, March sees an uptick in bonds sold, which is quantified by **Figure 3 below**—though in 1991 and 2003, Marchs' totals were less than February, **Figure 4**. However, **MMA** is expecting the historical bias to repeat as several large deals are scheduled for next month.

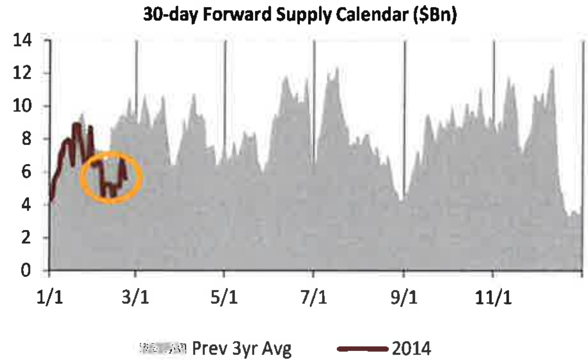


Figure 2: *This year's forward supply has been below recent averages.*

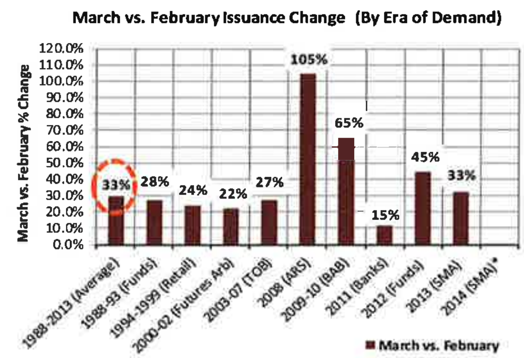


Figure 3: *March consistently sees more issuance than February.*

WHAT THIS MEANS FOR YOU: There are several ways to slice this topic. First, for issuers looking to come to market in the short-term, your borrowing costs should be lower as the supply/demand dynamic is tipped heavily in your favor. If issuance continues to be on the lighter side this year it may have a negative impact on the outside professionals that help you come to market. Bankers, underwriters and financial advisors (among others) are somewhat at risk as their business models rely on a certain amount of issuance annually. If this year were to see less than $250 billion issued (the average since 2005 has been $384 billion) it would seriously undermine some firms' profitability. Their service costs could potentially increase as a result, which could be passed on to issuers. Next, the lack of issuance underscores the austerity that many state and local governments are adhering to in the wake of the financial crisis and financial burdens set upon many governments. Generally, this is a credit positive as many issuers are borrowing less and "tightening their belts." Still, it is evident that the country's infrastructure needs are growing. Historically, these needs have been met by accessing the municipal market. If the infrastructure needs of the country are ignored, it is likely to make headlines in major media outlets, as was reported in the *New York Times* last week. Finally, turning back to the near-term, **Figure 4** looks at just how rare it is that the month of March sees less issuance than February (just two times since 1988). While unlikely, if it were to be a similar scenario, issuers that do need to come to market in March should consider **Figure 5**. Several state and local governments adhere to **MMA**'s municipal price performance indicators to help them come to market at the best time possible to lower their borrowing costs. Note that during these rare years, March 24th was a turning point for borrowing costs to become more positive for issuers as prices improved through April.

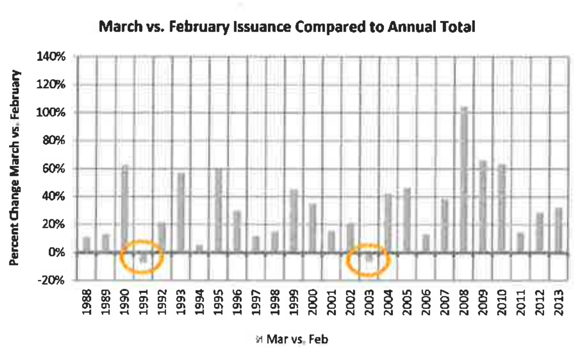


Figure 4: *Since 1988 only two years have seen a decrease in issuance.*

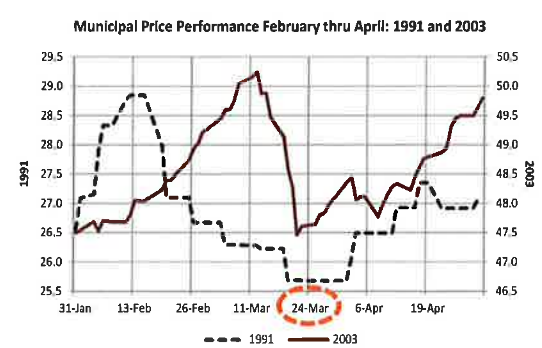


Figure 5: *In those years the market shifted direction on March 24.*

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

NORTHEAST

On February 20th, **Morgan Stanley** priced $400 million of transportation revenue bonds for the **Metropolitan Transportation Authority of New York**; A2/NR/A; callable at par in 11/15/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2015	0.30	0.30	+11
2039	4.65	4.65	+64
2044	4.80	4.80	+70

Notes: This deal saw strong retail investor demand.

MID-ATLANTIC

On February 19th, **RBC Capital Markets** priced $8 million of unlimited tax general obligation bonds for **Lancaster County, Pennsylvania;** A1/NR/NR; callable at par in 5/1/2019:

Maturity	Coupon	Yield	+/- AAA 5%
2015	1.00	0.45	+26
2019	1.60	1.65	+55
2023	2.80	2.90	+54

Notes: Bank-qualified and BAM insurance helped.

MIDWEST

On February 19th, **Stifel, Nicolaus & Co.** priced $51 million of sales tax appropriation bonds for the **Great Rivers Greenway District, Missouri**; A1/A+/NR; callable in 12/30/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2019	3.00	1.65	+54
2024	3.00	3.22	+59
2029	5.00	3.78	+48

Notes: These Gateway Arch Project bonds saw good demand.

SOUTHEAST

On February 19th, the **Florida State Board of Education** sold $188 million of lottery revenue refunding bonds to **Morgan Stanley**; A1/AAA/A+; callable in 7/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.30	+19
2024	5.00	2.82	+29
2025	3.00	3.10	+40

Notes: This competitive loan had 8 different bidders.

SOUTHWEST

On February 18th, **Wells Fargo Securities** priced $50 million of water system revenue bonds for the **Bell County Water Control and Improvement District No. 1, Texas**; A2/AA/NR; callable in 7/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2020	5.00	2.03	+58
2024	5.00	3.18	+63
2034	5.00	4.23	+45

Notes: BAM-insured, this deal was re-priced to lower yields.

FARWEST

On February 19th, **De La Rosa & Co.** priced $65 million of general obligation bonds for the **Stockton Unified School District San Joaquin County, California**; A2/AA-/NR; callable 8/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2024	5.00	3.37	+84
2029	4.00	4.18	+88
2038	5.00	4.65	+67

Notes: Assured Guaranty; it was re-priced 5 & 6 bps to lower yields.