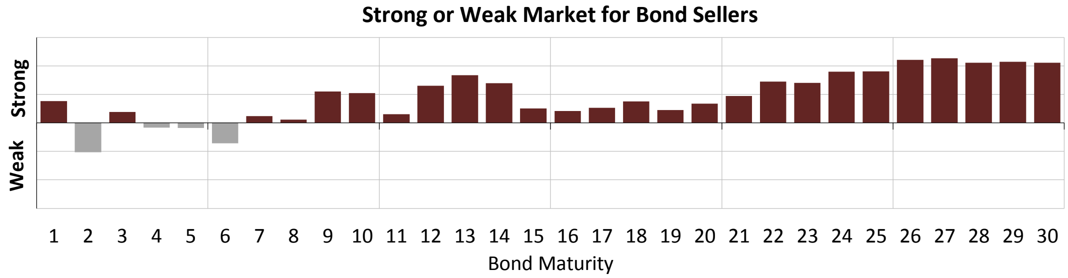
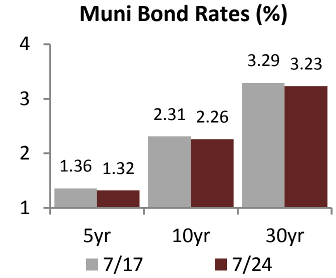
MMA Independent & Data Driven

JULY 27, 2015

MUNICIPAL ISSUER BRIEF





Heading into this week, a decidedly positive dynamic for issuers has emerged in the marketplace. The intermediate and longer parts of the yield curve have rallied after a more tentative market context in the first half of the month. Fewer pricing concessions would be expected among new issues this week.

MARKET UPDATE

JULY CONSISTENT WITH HISTORICAL RECORDS: The month has posted positive returns for municipal bond investors. Issuers' borrowing costs edged lower last week, with the final full week of the month poised to continue this favorable trend.

INVESTORS & ISSUERS: Constructive themes remain in place:

- With worldwide **bond markets moving into lower yield ranges** last week, municipal borrowing costs generally did the same.
- Most of the deals **MMA** tracked last week **had strong retail subscription** (see **page 3** for details) that translated into even larger institutional demand.
- New York issuers in particular did quite well. The strong reception will serve as a **positive for New York City**, which is selling $750 million GOs starting with retail orders on Tuesday.
- There are currently several market dynamics at play that are also helpful to issuers this week: 1) secondary selling pressure has been mitigated as seen through fewer bids-wanted lists; 2) the market is entering a seasonally low supply period (see ***Figure 1*** for more); and 3) **mutual funds experienced inflows into their funds, on a net basis, for the first time *in 10 weeks.***
- Those coming to market this week may want to not only monitor the results of New York City, but also the triple-A Florida Department of Transportation's competitive deal that sold Monday. **Aggressive dealer sponsorship would be a positive sign**.
- Finally, Puerto Rico's electric utility bonds that are currently in forbearance **began to rally late last week** as it appeared a deal had been reached with creditors. This agreement later fell through and negotiations are still ongoing. (See **page 2**).

CHRISTMAS IN JULY: Earlier this month *The Bond Buyer* newspaper published a story about Senate Finance Committee Ranking Minority Member Ron Wyden (D-OR) and his continued interest in the municipal bond market. While giving a nod to direct subsidy bonds that he has championed in the past, he noted that he does not oppose tax-exempt municipal bonds, but that the abuses that exist must be reigned in (see: Stadium Bonds in his opinion). He stressed the importance of infrastructure financings and that most of the country's infrastructure has been built and provided by state and local governments. He also commented that he hopes the day comes when parents give their children municipal bonds as Christmas presents. This is welcomed support for the tax-exemption and comes on the heels of developments for WIFIA-see the **next page** for more.

BUYERS BITES:

WHAT IS TRENDING HOT:
1) New York City issuers
2) Massachusetts GO
3) Puerto Rico electric utility bonds

CURRENTLY HARDER SELLS:
1) Chicago GO underperforming

WHO IS REPORTEDLY BUYING:
Mutual funds, large and mid-sized domestic banks, SMAs, insurance companies

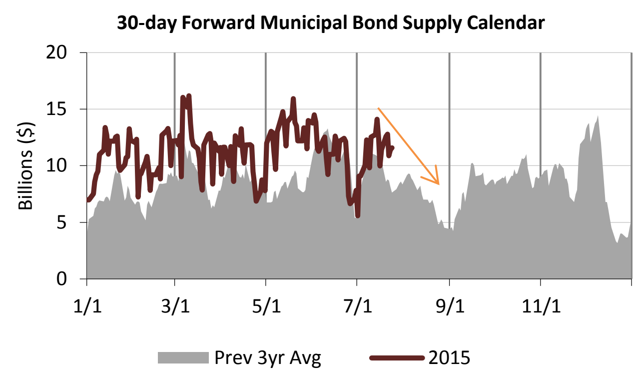


***Figure 1**: Late July and August are historically periods in which issuance declines. In the chart **above**, the shaded grey area, which represents the 3-year average of the 30-day visible supply, falls dramatically during this period. Thus far 2015 (maroon line) has largely outpaced historical averages. **MMA** expects issuance to decline in the next few weeks. This may tip the supply/demand balance in favor of issuers opting to sell during this quieter time period of bond origination.*

TOPIC OF THE WEEK: WIFIA & FUTURE IMPLICATIONS

WIFIA: Earlier this month the U.S. Senate Committee on Environment and Public Works approved a bill that would allow municipal water utilities to use tax-exempt bonds when financing part of a project with Water Infrastructure Finance and Innovation Act (WIFIA) loans. The WIFIA program provides low-interest federal loans for up to 49% of large drinking water, wastewater and water reuse projects. As it was originally written in 2014, it prohibits the use of tax-exempt bonds to pay for the remaining 51% of these capital project costs. **MMA** recently wrote to our institutional investor clients that Congresses' banning of the use of tax-exempt bonds as part of the program "reflected not only the current Federal antipathy toward the tax-exemption but also the difficulty in approving any legislation that includes an unfunded cost like the one Congress chooses to show for the tax-exemption."

WHAT THIS MEANS FOR YOU: While work remains to ensure full Senate and House passage, this is largely a success for the state, local and water groups that advocate for tax-exempt bond policy in Washington. This underscores the impact that public sector groups can have when it comes to Congresses' approach to the tax-exemption; and could serve as a lesson when a broader tax reform debate occurs in Washington. That broader tax reform debate may include hits to specific kinds of programs – water, private activity bonds, etc. – and the full tax-exemption as well. While fortitude in Congress to tackle reform in the near future has waned, issuers and the municipal sector need to remain vigilant against proposals to diminish the benefits of municipal securities.

DEFAULT & IMPAIRMENT UPDATES

PUERTO RICO ADDED TO DEFAULT DATABASE: With **Puerto Rico's** governor telling the *New York Times* of a need for sweeping debt moratoriums on the island, and following a commonwealth presentation to creditors that underscored the potential for bondholder losses across the capital structure, **MMA** has added 13 new PR bond securities to our default database, affecting $53.5 billion of outstanding par bonds. All of the new additions are currently in the OTHER category because no payments to bondholders have actually been missed and no new issuers have used emergency solutions to cover debt service payment. On July 15, Puerto Rico failed to transfer cash to a Public Finance Corporation (PFC) trustee ahead of an August 1 debt service payment. This is a technical default—warranting an OTHER characterization—that could become Puerto Rico's first payment default if sufficient funds aren't advanced by the end of the month. As **MMA** has noted to institutional investor clients, we expect that even a single default anywhere in PR's capital structure enhances the political viability of additional defaults everywhere else, to the detriment of creditors. More directly, a PFC payment default would unleash highly negative media headlines. Note that **MMA** did not include PR securities that appear only remotely reliant on the central government, including refunded bonds, PR housing, tobaccos, etc. However, what **MMA** did add has more than doubled the amount of impaired par in the total database. Puerto Rico issuers now account for 59% of all impaired municipal par across all sectors, states, and categories. This creates a challenge in showing that the municipal industry as a whole has very low default and impairment rates. A summarization of all current, non-Puerto Rico impairment across the industry by sector, rating category, etc., shows that the rest of the municipal industry still has very low default rates. (See **below**.)

Par (and #) of Outstanding Bonds With an Uncured Impairments, Excludes PR Except Where Noted ($M)						Support Detail:
Sector	Last 2 Wks	All Notices	DEFAULT	Support	Other	Bond Reserves
ALL (Including Puerto Rico)	$62,416 (39)	$110,940 (971)	$11,036 (459)	$30,663 (252)	$69,241 (259)	$32,834 (182)
ALL (Excluding Puerto Rico)	$831 (25)	$45,724 (956)	$11,036 (459)	$22,555 (251)	$12,133 (245)	$24,726 (181)
Land Secured	$47 (4)	$4,519 (339)	$3,222 (223)	$985 (99)	$312 (17)	$776 (84)
IDB	none	$3,058 (60)	$2,218 (27)	$568 (19)	$272 (14)	$207 (13)
Retirement	$272 (7)	$3,063 (106)	$993 (41)	$484 (15)	$1,586 (50)	$244 (9)
Local Housing	$9 (1)	$673 (62)	$482 (40)	$17 (6)	$174 (16)	$13 (3)
Tribal	none	$480 (4)	$480 (4)	none	none	none
Hotel	$232 (2)	$4,393 (14)	$478 (11)	$254 (3)	none	$820 (3)
All Risky Sectors	$823 (24)	$38,484 (840)	$10,418 (443)	$19,196 (207)	$8,870 (190)	$13,769 (13)
All Safe Sectors	$8 (1)	$7,240 (116)	$618 (16)	$3,359 (44)	$3,263 (55)	$8,640 (27)
Initially Non-Rated	$599 (18)	$12,090 (690)	$7,398 (416)	$1,970 (143)	$2,722 (131)	
Initially Ins'd/LOC	$97 (3)	$16,911 (119)	$643 (7)	$10,016 (62)	$6,253 (50)	
Initially Rated, Unins'd	$134 (4)	$16,723 (147)	$2,995 (36)	$10,570 (46)	$3,158 (64)	

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

Three large deals that had implications for the broader market (**highlighted below**):

- **The New York Dormitory Authority** was the largest issuer of the week offering $1.5 billion sales tax revenue bonds. The deal received more than $350 million in retail orders that then translated into strong institutional interest allowing the issuer to increase the size of the loan and lower yields as much as 5 basis points as the general market improved.
- **The Metropolitan Government of Nashville, Tennessee** competitively sold bonds on a day when Treasuries were improving as were tax-exempts, which enabled an aggressive bid by Morgan Stanley with subsequent good follow-through.
- **The City and County of Honolulu, Hawaii** – a fairly frequent high-grade issuer – was also able to lower yields 1-2 basis points before closing the account on Tuesday, the busiest new-issue day of last week.

NORTHEAST

7/22: **Morgan Stanley & Co.** priced $1.522 billion sales tax revenue bonds for the **Dormitory Authority of New York**; NR/AAA/AA+; callable at par in 3/15/2025:

Maturity	Coupon	Yield	+/- AAA 5%
2020	5.00	1.31	-3
2025	5.00	2.36	+6
2027	5.00	2.59	+6

Notes: A 6bps spread over MMA Benchmark is on par for rating

MID-ATLANTIC

7/22: **Alexandria, VA** sold $23.2 million general obligation capital improvement bonds to **Citigroup Global Markets Inc.**; Aaa/AAA/NR; callable at par in 7/15/2025:

Maturity	Coupon	Yield	+/- AAA 5%
2020	5.00	1.28	-6
2025	5.00	2.29	-1
2035	3.25	3.38	+32

Notes: Triple-A competitive deal put spreads through Benchmark

MIDWEST

7/22: **Monroe County, WI** sold $10.0 million general obligation corporate purpose bonds to **Wells Fargo Securities**; NR/AA/NR; callable at par in 3/1/2025:

Maturity	Coupon	Yield	+/- AAA 5%
2020	2.00	1.30	-4
2025	2.25	2.15	-15
2028	2.65	2.65	+1

Notes: Bank Qualified enabled low, longer-dated coupon payments

SOUTHEAST

7/21: The **Nashville Metro Government, TN** sold $347 million general obligation bonds to **Morgan Stanley & Co.**; Aa2/AA/NR; callable at par in 7/1/2025:

Maturity	Coupon	Yield	+/- AAA 5%
2020	5.00	1.46	+10
2025	4.00	2.50	+19
2034	4.50	3.43	+41

Notes: Sub-5% coupons out long likely result of P&C Insurance cos

SOUTHWEST

7/21: **BOSC, Inc.** priced $12.3 million waterworks and sewer system revenue refunding bonds for **Rowlett, TX**; Aa3/A+/NR; callable at par in 3/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2016	1.50	0.42	+14
2020	2.50	1.67	+33
2025	5.00	2.83	+53

Notes: Lack of income tax generates wider spreads for TX issuers

FARWEST

7/22: **Bank of America Merrill Lynch** priced $582 million wastewater system revenue bonds for the **City and County of Honolulu, HI**; 1st res Aa2/NR/AA, 2nd res Aa3/NR/AA-; callable at par in 7/1/2025:

Maturity	Coupon	Yield	+/- AAA 5%
2020	5.00	1.48	+14
2025	5.00	2.55	+25
2045	5.00	3.52	+24

Notes: First Resolution bond yields are above (higher-rated)