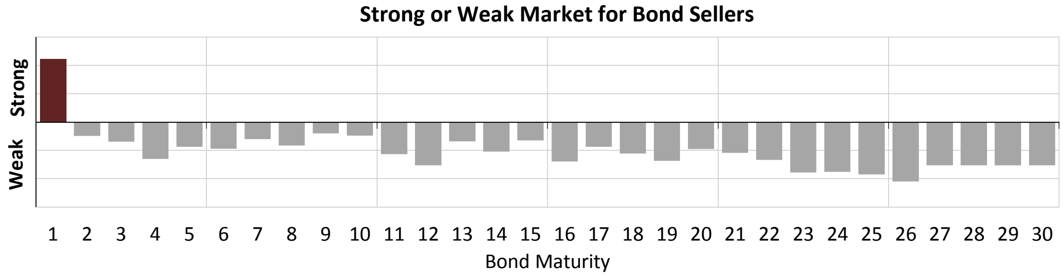
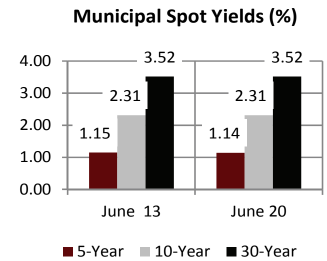
MMA The Power of Independence

JUNE 23, 2014

MUNICIPAL ISSUER BRIEF





Heading into this week, the municipal market's valuations continued to reflect a weaker market context but one where pricing power was improving amid stability. The better improvement remained in the front and intermediate maturities on the curve.

MARKET UPDATE

CAN'T QUITE TURN THE CORNER: In the middle of last week municipals stabilized, suggesting that pricing strength might emerge into the end of the quarter. (**Figure 1**, **below**) Deals generally did well and a reasonably large calendar is expected this week.

- **INVESTORS & ISSUERS:** Deals do well but positive trend still forming.
- **Borrowing rates generally ended where they started off** last week as bond markets around the world responded to not-so-friendly economic data (inflation came in higher). Also, the Fed kept its slightly better economic expectations in tact.
- For a moment mid-week, it looked as though municipal rates were to follow Treasuries to much lower levels, **but by week's end the momentum slowed.**
- Still, **most new municipal deals generally did quite well** as the light supply continued to bolster support for states and localities.
- Exemplifying the support: **Texas Transportation Commission** had more than $5 billion in orders on its $900 million sale and the **New York Metropolitan Transportation Authority** had nearly $400 retail million orders on its $500 million sale—both were re-priced to lower yields.
- Competitive deals also saw **strong dealer bidding** as **Georgia** sold nearly $1 billion of GOs to 4 separate underwriters. Once again pre-sale orders from large banks and insurance companies helped this issuer and others to **secure lower, longer-dated coupon payments.** (**See page 3** for more on regional deals.)
- The demand via the competitive process will be tested once again on Tuesday and Wednesday with large, high-grade issuers out of the **New York Dorm Authority** and **Washington** state, respectively, **all selling within short time periods of each other**.
- **These types of transactions in the recent past have had mixed results** as generally the bonds have been bid aggressively **and then experienced less exuberant distribution in the secondary.**
- Longer bond issuers should track the long-only **New York City Municipal Water Finance** deal Wednesday as it is apt to help dictate the market's tone.

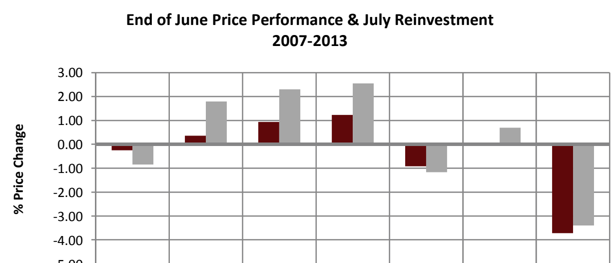
ATTRACTING INVESTORS TO YOUR BOND DEAL: Last week the **Council of Development Finance Agencies** and **BNY Mellon** hosted a webinar for issuers. **MMA** gave a presentation on market conditions, municipal credit and an update on Washington, D.C. You can view it by clicking **here**.

BUYERS BITES:

WHAT IS TRENDING HOT:
1) NY-names—City GO, MTA, PITs
2) Lower-rated GOs outperformed
3) Higher-rated competitive deals aggressive

CURRENTLY HARDER SELLS:
1) Puerto Rico woes continue to make headlines
2) Stanford University did not find a bid in the Street

WHO IS REPORTEDLY BUYING:
Large banks, property & casualty insurance companies, mutual funds



	2007	2008	2009	2010	2011	2012	2013
Municipal	-0.25	0.36	0.94	1.23	-0.92	-0.06	-3.71
Treasury	-0.85	1.80	2.30	2.55	-1.17	0.69	-3.40

Figure 1: *The chart above reflects price performance of municipal and Treasury bonds from June 20 through the July 4 holiday dating back to 2007. Because this is price, the bars reflecting increases are positive and vice-versa. Note that with the exception of the last two years, generally the end of June is a positive one for municipals as they either increase, or do better than their counterpart Treasury bonds. For issuers coming to market in the next two weeks, this could be beneficial to your issue. We note that the last two years of poor performance relative to Treasuries is the result of very specific situations and outliers. The data from 2008 might be of keen interest since the July 4 holiday fell on a Friday as it does this year. Quarter-end is critically important for hedge fund compensation, so that municipals can display greater resilience.*

TOPIC OF THE WEEK: INTERVIEW

*Periodically **MMA** will interview industry officials to share their perspectives on pressing issues in public finance. This week, **MMA** interviewed **Tim Firestine, Chief Administrative Officer for Montgomery County, Maryland**. Tim is also the immediate past president of the **Government Finance Officers Association**. Tim has a long-held interest in the market, as a member of the GFOA's Debt Management Committee who has testified before Congressional, IRS and SEC hearings pertaining to public finance.*

MMA: Tim, this is a very interesting time for the municipal market and especially for issuers. What do you see as the top issues facing governments today?

TF: I think there are many big issues facing our profession, but I will mention what I think are the top three. 1) Governments are still recovering from the financial crisis and that affects everything from their credit ratings to budgetary demands. 2) Changing debt issuance practices due to the *Dodd-Frank Act* and especially the Municipal Advisor Rule. 3) Determining how to address an aggressive regulatory landscape, with programs such as the SEC's Municipal Continuing Disclosure Cooperative (MCDC) initiative.

MMA: You were involved in a lot of conversations that were held by Congress and at the SEC about the MA Rule. How do you think issuers and the market will adjust to implementation of the Rule on July 1?

TF: There will be an adjustment period for all market participants. Education is key to understanding its realities and myths. Most professional organizations have been working to get their members up to speed [see GFOA's efforts here]. I believe a professional with a fiduciary duty should be the one to provide advice to an issuer. This will likely need to be incorporated into many debt management policies and procedures, but it is the right one. I also think that there are unnecessary waves of hysteria that bankers will no longer be able to 'help' and provide issuers with financing ideas. There are plenty of ways that an issuer can continue to receive ideas from bankers, most notably the ability to have bankers respond to issuer RFPs. GFOA has had long-standing policy to use RFPs for both financing ideas and hiring outside professionals. Hopefully this will push governments to use this important practice.

I do think that the industry will need to provide some constructive feedback to the SEC once we've all seen the rule in action. I know one item that some of the larger governments who have a robust debt management staff have mentioned is the possibility of some type of large issuer exemption. While I know this would be difficult to define, it may be something to address down the road.

MMA: With a fiduciary duty, advisors will bear a larger responsibility to the issuer. Do you think advisors will charge more for their work and thus increase the cost of issuance?

TF: I agree that the professional responsibilities of the MA (including new fees and rules imposed upon them by the MSRB) will be greater going forward and that will come at a cost to them, and probably issuers. All of us are going to have to adjust to this new framework and at the beginning costs could rise for issuers, especially those who may now for the first time engage a MA.

MMA: **The geographical diversity, plethora of credit types and massive differences in issuer-size has created a very wide scope of advisors in public finance. Are most MA professionals capable and ready to pick up these additional responsibilities?**

TF: I think they are ready. They've had years to prepare and while some of the specifics still need to be formalized through rulemaking, I know from conversations I have had with many of them that they are ready. One point related to this that I think is important: because of the qualification standards and greater professional responsibilities, similar to that of other professions, this will help weed out any of the bad actors, which I think is positive for issuers.

MMA: It seems issuers are trying to get their arms around the SEC's MCDC. Are you surprised by it?

TF: Yes. The MCDC program is tricky, in that there is a lot of grey area about what should and should not be reported. I think issuers are struggling with how to determine what they should do, especially in the short time frame the SEC has allowed for (and for which I would like to see an extension). I am also concerned about the premise of the program, and whether some of the information that issuers may be self reporting, really constitutes fraud, which seems to be what the SEC is saying. While I understand and respect the need for the SEC to ensure compliance with Rule 15c2-12, and to make sure representations in official statements are correct, I wonder if this program will just end up creating layers of other problems. I know from talking to my colleagues, it is causing a lot of confusion. If you said you filed your annual financials according to your CDA and did not, that seems to be something to self report. But is that fraud? And what about items such as other material events unrelated to an event on an issuer's credit but instead on something such as bond insurance, and filings that occurred prior to the EMMA system being up and running – how best should issuers determine whether to self report? (continued on **page 3**)

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

NORTHEAST

On June 19th, **Jefferies LLC** priced $500 million of transportation revenue bonds for **New York Metropolitan Transportation Authority**; A2/AA-/A; callable in 11/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.62	+48
2024	5.00	2.89	+57
2034	4.00	4.00	+69

Notes: This priced similarly to the City's $1B GO deal from last week

MID-ATLANTIC

On June 19th, **North Penn School District, Pennsylvania** sold $9.9 million of limited tax general obligation bonds to **Janney Montgomery Scott**; Aa2/NR/NR; callable in 9/1/2019:

Maturity	Coupon	Yield	+/- AAA 5%
2019	4.00	1.45	+41
2021	2.00	2.00	+22
2024	2.375	2.45	+13

Notes: The short call option and state aid withholding helped

MIDWEST

On June 18th, **Loop Capital Markets** priced $555 million of sales tax receipts revenue bonds for the **Chicago Transit Authority**; NR/AA/NR; Kroll: AA callable in 12/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2044	5.00	4.03	+49
2044	5.00	4.13	+59
2049	5.25	4.23	NA

Notes: Tied to the state's sales tax avoided Chicago woes

SOUTHEAST

On June 17th, **Goldman, Sachs & Co.** priced $105 million of water revenue and refunding bonds for **New Orleans, Louisiana**; NR/BBB+/BBB; callable at par in 12/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	2.27	+67
2024	5.00	3.51	+120
2034	5.00	4.25	+95

Notes: The issuer did well with high-yield investor demand

SOUTHWEST

On June 19th, **Bank of America Merrill Lynch** priced $977 million of general obligation mobility fund refunding bonds for the **Texas Transportation Commission**; Aaa/AAA/AAA; callable in 4/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.40	+26
2024	5.00	2.45	+13
2034	5.00	3.21	-9

Notes: The issuer had $5 billion of orders across the scale

FARWEST

On June 19th, **RBC Capital Markets Inc** priced $49 million of revenue bonds for the **San Joaquin Transportation Authority, California**; NR/AA/AA; callable in 3/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2020	4.00	1.58	+10
2024	5.00	2.48	+16
2029	5.00	3.04	+14

Notes: Very strong demand in the 10-year portion of this deal

INTERVIEW CONTINUED

MMA: Are you concerned that the regulatory items as well as market trends may be overwhelming smaller governments?

TF: Smaller governments have a lot on their plate especially if they don't have staff dedicated to debt management. It is important to make sure governments understand how the new MA rule will affect them – likely significantly as many small governments probably have relied on their bankers for advice through the years. The SEC's MCDC initiative could really serve a wallop to those governments, since again, it isn't exactly clear what the SEC wants. I'm afraid a lot of governments are going to have to turn to outside professionals – at a cost – to better equip themselves. Then of course, there is the proposed IRS regulation on issue price that could be disruptive to all issuers.

MMA: You mentioned that governments are still recovering from the Financial Crisis. Do you think they are seeing the light at the end of the tunnel?

TF: I do. A lot of governments have had to make difficult choices to weather this storm, but are stronger for it. It exposed a lot of the vulnerabilities in our financial system and I know my colleagues across the country have taken appropriate steps to ensure that public funds are protected and that their exposure to volatile markets is minimized. But we are still adjusting to a new normal. Hiring isn't the same and we are learning to do more with less. One bright spot is that I think finance officers have been able to increase their role in the decision-making process of their governments and with elected officials, because there is a greater awareness of the importance of the finance function. Related to the market, debt issuance is down, which in theory helps those in the market but in the long term, it means that we are not addressing the infrastructure needs of our communities, which is a worrisome trend.