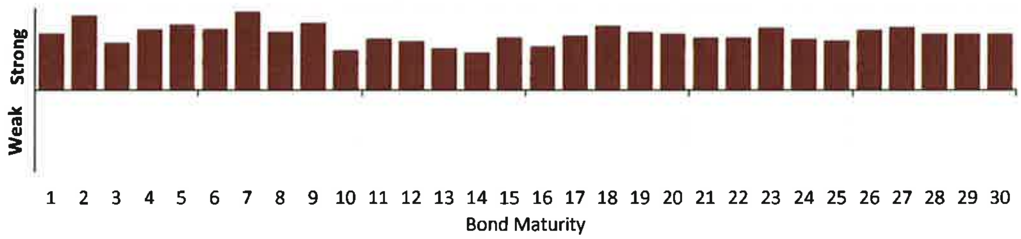
MMA The Power of Independence

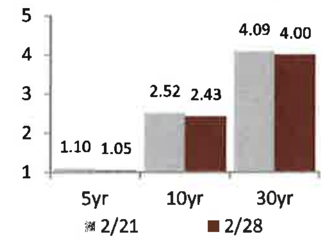
MARCH 3, 2014

MUNICIPAL ISSUER BRIEF

Strong or Weak Market for Bond Sellers



Muni Bond Rates (%)



Heading into this week, the market dynamic has turned universally stronger for issuers. All across the curve, issuers should be able to achieve relatively strong prices compared to recent averages. This is an overwhelmingly strong dynamic and issuers that can, should take advantage of current conditions.

MARKET UPDATE

WEEK STARTS OFF ON STRONG FOOTING: Last week ended on a strong note, setting up a good dynamic for issuers coming to market this week.

INVESTORS & ISSUERS: March is historically a difficult month.

- This month is traditionally a bad one as borrowing costs tend to increase. That being said, the **dynamics in place strongly favor issuers as supply remains limited.**
- For the first time in five weeks, the new-issue calendar surpasses $5 billion. While an increase, **this remains below historical averages.**
- **There are a few sales of nearly $1 billion from Texas, New York City and Maryland that MMA will be closely watching.**
- Maryland is a triple-A state and is selling competitively on Wednesday. Lately, competitive deals have seen very aggressive bidding by dealer firms. Any issuers coming to market should watch how this deal fares as **it is likely to influence the broader market direction.**
- Last week, triple-A Delaware and the California Department of Water Resources were bid so aggressively by dealer firms that they **traded them at weaker levels afterward**. This is indicative of just how willing dealers are going to be to buy your bonds and other issuers can take advantage of this dynamic.
- Fordham University of New York had a $62 million dollar last week that within an hour of pricing had more than $500 million in orders. **There is currently a very high demand for New York** bonds and other issues of the state should take note (**see page 3 for more regional deal details from last week**).
- The unfolding situation in Ukraine is also affecting borrowing rates. As the conflict escalates, investors purchase U.S. Treasury bonds for their perceived safety. **Municipal borrowing rates tend to follow Treasuries and as a result the situation will keep interests lower.**

MSRB 2013 FACT BOOK: The Municipal Securities Rulemaking Board (MSRB) last week released its 2013 Fact Book, which analyzed trading data and other statistics. It examined more than 50 million trades during the last five years. The MSRB stated it received 12,708 primary market document submissions, 14% less than the 14,716 it received in 2012, but the number of continuing disclosures submitted increased 6% in 2013.

BUYER BITES:

WHAT IS TRENDING HOT:

1) Shorter call options in the 2019-2021 range
2) New York issuers
3) Maturities of 20-years and longer

CURRENTLY HARDER SELLS:

1) Michigan issuers

WHO IS REPORTEDLY BUYING:

Property & casualty insurance companies, direct retail, SMAs

Weekly 2014 Issuance v. Previous Three Year Average

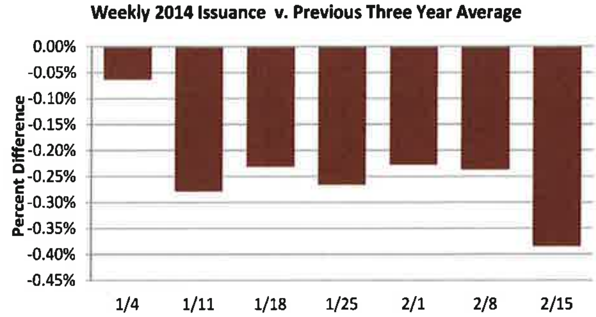


***Figure 1:** As discussed in last week's topic of the week, the lack of issuance in 2014 has been a driving influence in the marketplace. With the data in for February, The Bond Buyer reported it was the slowest month in 13 years. The chart above shows week-by-week how much less was issued compared to the 3-year average. This is a dynamic that issuers can take advantage of for new-issues and refundings.*

TOPIC OF THE WEEK: MOTOR CITY

DETROIT ON GO BONDS: Last week, Detroit released its much-anticipated Plan of Adjustment (POA), which was developed to help the city as it grapples with its bankruptcy. The plan includes significant changes to payments made to investors holding an unlimited tax (ULT) and limited tax (LT) GO pledged bonds. The Plan's call for a haircut of 80% on an ULT and LT GO pledges would be an extreme deviation from the recovery rates traditionally associated with these types of municipal securities. The Plan would also mandate cuts to the city's pension program.

WHAT IT MEANS FOR YOU: If the plan is approved "as is" it **would likely alter the perceived strength of the GO pledge for all issuers**, negatively affect pricing and upset the existing ratings framework for tax-backed securities. In short, if you issue GO bonds, your borrowing costs could increase as investors demand more compensation (i.e. higher interest rate) in light of such a large penalty put on Detroit bondholders. Assuming that the proposed POA is approved, the rating agencies are apt to feel compelled to respond by adjusting their GO rating methodologies across the board. **MMA** believes the ratings agencies would have to make their ratings regime much more state-specific, differentiating between states *that allow* access to bankruptcy protection and lack a statutory lien to bondholders from states *that bar* access bankruptcy protection or provide a clear statutory lien for GOs. This likely **would imply higher borrowing costs those states that do allow access to bankruptcy protection and those without a legal protection of its GOs**, in particular for issuers that have lower credit profiles and those seeking new capital infusions. States with a clear statutory lien benefitting GO bonds include, but may not be limited to: CA, CO, FL, LA and RI. In theory, issuers in these states would receive a better rating under a new regime and would benefit from more investor interest. Those states that do not have a clear statutory lien would be at risk if a new methodology were put in place.

WASHINGTON UPDATE

U.S. House of Representatives Ways and Means Committee Chairman, David Camp (R-MI), released a discussion draft of his Tax Reform Act of 2014 on February 26. There are numerous provisions related to municipal securities, which are highlighted **below.** This is the first major draft of comprehensive tax reform from a Republican to hit the Beltway, however, it is very unlikely that there is traction in 2014 (or even thereafter) for Congress to begin seriously debating these issues.

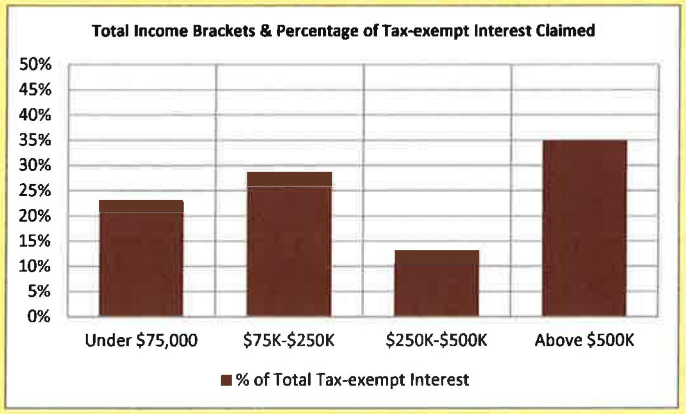
<u>While the majority of the municipal exemption remains intact, there are numerous areas that would limit the ability for state and local governments to continue to access capital markets in a cost efficient manner</u>. State and local governments should take time to comment to their elected officials about the concerns with these provisions as they would limit access to capital markets and increase debt issuance and other costs.

<u>Municipal securities provisions</u>

- The exemption for governmental bonds remains intact. The summary report specifically makes this statement: "[The Reform Act] maintains the current-law tax exemption for public purpose bonds issued by state and local governments (i.e. 'muni bonds')."
- A new 10% surtax on municipal bond interest would be in place for taxpayers who make more than $400,000 (or $450,000 for joint payers). The **chart to the right** breaks down different income brackets into the amount of tax-exempt interest claimed. Note that those above $500,000, or 35% of those claiming exempt municipal bonds, will now be charged an additional 10% on the bond holdings.
- Eliminates the ability for future issuance of private activity bonds.
- Repeals ability for issuers to do future advance refundings.
- Eliminates bank qualified debt by taking away the tax advantages for banks to enter into these transactions.
- Eliminates corporate tax incentives for non-banks and property and casualty companies to purchase municipal bonds.
- Repeals new issues of tax-credit bonds such as qualified zone academy bonds (QZABs) or clean renewable energy bonds (CREBs). However, current holders of these bonds would continue receiving tax credits.

<u>Other Provisions of Interest to State and Local Governments</u>

- Eliminates the ability for taxpayers to deduct state and local taxes on their federal returns.
- Dedicates $126.5 billion to Highway Trust Fund over eight years.
- Eliminates the alternative minimum tax (AMT).



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

NORTHEAST

On February 27th, **Bank of America Merrill Lynch** priced $62 million of Fordham University revenue bonds for the **Dormitory Authority of New York**; A2/A/NR; callable at par in 7/1/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2015	3.00	0.25	+6
2024	5.00	3.00	+52
2044	5.00	4.31	+26

Notes: This deal was 10-times oversubscribed.

MID-ATLANTIC

On February 27th, **Delaware** sold $225 million of general obligation bonds to **Wells Fargo Securities;** Aaa/AAA/AAA; callable at par in 3/1/2022:

Maturity	Coupon	Yield	+/- AAA 5%
2015	5.00	0.14	-5
2019	5.00	0.95	-13
2034	3.50	3.60	-13

Notes: The short call option and competitive bid lowered yields.

MIDWEST

On February 26th, **Mesirow Financial Inc.** priced $3 million of general obligation bonds for the **Grayslake Community Park District, IL**; NR/A/NR; callable in 12/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2019	2.00	1.85	+80
2025	4.00	3.40	+79
2037	4.50	4.60	+76

Notes: Bank interest kept rates lower for this single-A Park District.

SOUTHEAST

On February 26th, **Raymond James** priced $9.8 million of revenue bonds for the **Cullman City Board of Education, Alabama**; Aa3/NR/NR; callable in 7/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2024	3.00	2.63	+21
2029	4.00	3.35	+14
2042	5.00	4.40	+42

Notes: A bank-qualified designation spurred demand.

SOUTHWEST

On February 24th, **RBC Capital Markets** priced $70 million of revenue bonds for the **New Mexico Finance Authority**; Aa2/AA/NR; callable in 6/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.24	+19
2025	5.00	2.92	+31
2032	5.00	3.69	+17

Notes: New Mexico credits benefit from scarcity of issuance.

FARWEST

On February 27th, **Goldman Sachs & Co.** priced $65 million of Peace-Health Project refunding revenue bonds for the **Oregon Facilities Authority**; NR/A/A+; callable 5/15/2024:

Maturity	Coupon	Yield	+/- AAA 5%
2019	5.00	1.79	+71
2024	5.00	3.38	+90
2029	5.00	4.00	+74

Notes: This deal was re-priced 7 to 14 bps to lower yields.