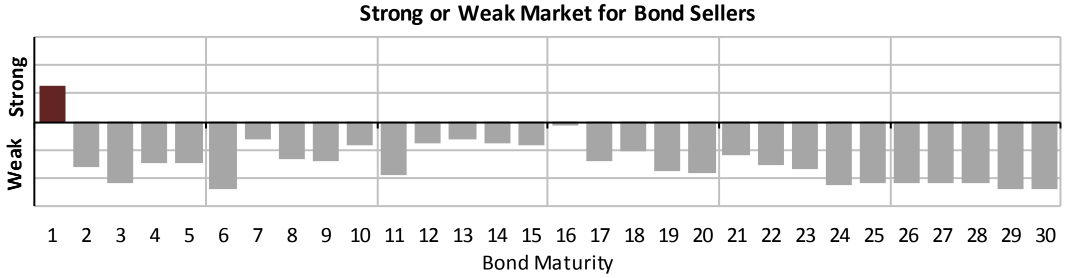
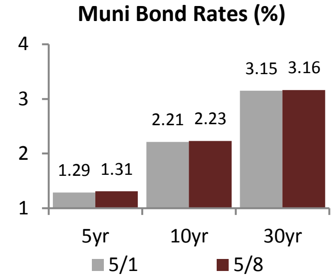
MMA Independent & Data Driven

MAY 11, 2015

# MUNICIPAL ISSUER BRIEF




*Heading into this week, the pricing dynamic is decidedly negative for issuers across the curve after last week's poor performance. Issuers, however, benefit as the 1-year bond continues to be in the 'strong' column. Corporations have recently been buying short-term municipal notes.*

## MARKET UPDATE

**DIFFICULT WEEK ENDS ON A POSITIVE NOTE:** Interest rates continued to slide to higher ranges throughout most of the last week and several municipal bond deals struggled amid the headwinds. Friday's data led to a brief rally in which municipals participated.

**INVESTORS & ISSUERS**: Mixed market themes remain.

- Bond markets **struggled into higher rates** through most of last week and as a result several deals struggled to get done (more details on **page 3**).
- However on the last two days of the week there was a rally in much of investment-grade debt domestically and abroad, which helped bolster municipals and the **week ended with an improved rate environment.**
- Still, two important and potentially negative themes developed as mutual funds saw net outflows and the hefty supply dynamic was maintained as this week's calendar grew to nearly $10 billion—**the largest week of issuance in more than a month**.
- With the rise in interest rates, the **retail networks began to pick up activity** as individuals participated in the retail order periods of leading deals that **MMA** followed (again, **page 3** for more).
- Meantime, **broader market optimism appears to be returning**, boosted by expectations for a strong summer reinvestment season. Between today and July 31st (excluding notes) there are $54.3B of municipals maturing, nearly 20% of which ($10.2B) are in California alone.
- Two big market entities—Puerto Rico and Illinois– both had **potentially negative credit headlines develop last week** and some of the related bonds traded cheaper as a result. The industry has done a good job maintaining the story line how each issuer has unique problems and are not systemic to the entire marketplace.
- **MMA** will keep an eye on **Salt River, AZ**—once a frequent issuer but less so in recent years will refund its debt. The **Pennsylvania Turnpike** Authority, that on its own has strong fundamentals, could suffer from broader state-level fiscal concerns.

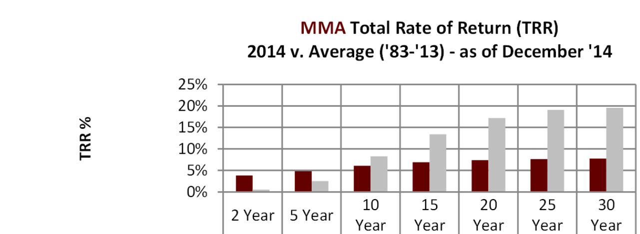
**DISCLOSURE**: Last week the **MSRB,** updated with 2014 data, released its report on *Timing of Annual Financial Disclosures by Issuers*. The report shows that issuers averaged about 200 days past the end of their fiscal year to file their audited financial statements. Additionally the report noted a significant increase in catch-up filings from June-December of 2014, likely due to the effects of the SEC's MCDC program. Click here to view the full report.

### BUYERS BITES:

**WHAT IS TRENDING HOT:**
**1) Variable-rate and 1-year or shorter notes**
**2) New York issuers outperforming**

**CURRENTLY HARDER SELLS:**
**1) Illinois , Chicago credits**
**2) Puerto Rico**

**WHO IS REPORTEDLY BUYING:**
**Tech-oriented corporations, insurance companies, regional and larger banks**




| | 2 Year | 5 Year | 10 Year | 15 Year | 20 Year | 25 Year | 30 Year |
|---|---|---|---|---|---|---|---|
| Average TRR (through last year end) | 3.80% | 4.85% | 6.09% | 6.92% | 7.37% | 7.62% | 7.75% |
| 2014 | 0.53% | 2.47% | 8.30% | 13.40% | 17.19% | 19.11% | 19.58% |

***Figure 1**: After one of the strongest years in recent memory, the market found itself at a cross roads entering 2015. In the chart above we look at the strong rate of return municipal bond investors received for various maturities this year (in grey bars) compared to the 30-year average (maroon bars). While the 1st quarter produced gains for investors (this generally means strong market conditions for issuers), there are mixed themes to take into account heading into the next 4 to 5 months. The **Topic of the Week** on **page 2** delves into some market considerations for issuers planning to sell bonds this summer.*

## TOPIC OF THE WEEK: MARKET TECHNICALS

**CURRENT MARKET DYNAMICS**: How to prioritize key data from the volume of market information is not always easy to ascertain. For those just looking at the first quarter of the year from a broad perspective, the data shows generally strong market conditions (**Figure 2**), however, the bulk of the market strength occurred in the first two weeks of January. Since then, the market has seen increased volatility and a declining price. Today's ***Brief*** will look at the 3 important technical factors for issuers to monitor when planning to sell bonds this summer:

**SUPPLY**: Often in ***MIB*** we make note of whether supply/demand dynamics favor issuers. After seeing supply decrease significantly in the wake of higher borrowing costs throughout 2013 and into 2014, issuance on an aggregate has increased significantly (**Figure 3**). The last 6 months has put the 12-month rolling average at $375 billion with the surge a result of issuers refunding outstanding debt to take advantage of low rates. When coming to market, issuers should take into account how much debt has been sold recently and especially how much is planned for the same week or even day of the proposed sale. This becomes especially important when the market is on pace to digest the most amount of bonds since before the financial crisis.

**INVENTORY**: The amount of bonds an underwriter holds on their balance sheet changes for a variety of reasons and in many ways can influence a bond pricing and/or effect general market conditions. Getting this type of information in a timely manner is nearly impossible but there are a few ways that **MMA** measures how 'heavy' or 'light' the dealer community is holding at any given time. One way is provided by the New York Federal Reserve in the collected balance sheet data from the 21 primary dealers. This way we can see – although with a 1-week delay – that the aggregate positions of the dealers have risen dramatically since the start of March (**Figure 4**). **MMA** also utilizes data from various vendors that measure the amount of bonds dealers are trying to sell each day in the secondary markets via listed offerings. In **Figure 5**, at the start of May the market's offering items rose to the highest amount since the summer of 2013. As that volume increases, it implies that bonds are not being sold to customers as fast as they are being issued. With both of these data-sets put together, the information suggests that dealers on aggregate are heavy with bonds and finding the market a challenging one to sell bonds to customers. These types of factors could make your bond pricing more difficult if they remain in place through the summer.

**MUTUAL FUNDS:** As the 2nd largest holder of municipal bonds, mutual funds investment inflows or outflows are an important element to consider when pricing bonds. There is weekly, and even daily, data that identifies investment flows in and out of mutual funds (including municipals). From a broader perspective, fund flows of cash also provide general insight as to retail and its investment advisors' sentiment. If major brokers are advocating municipal bonds, then there is likely a positive trend for funds – and vice-versa.

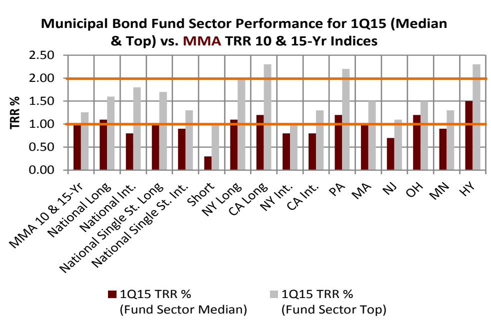



***Figure 2****: Funds saw strong returns in the 1st Quarter*

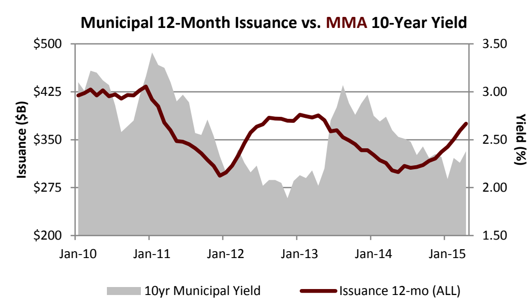



***Figure 3:*** *Issuance is on an annual pace of $375B.*

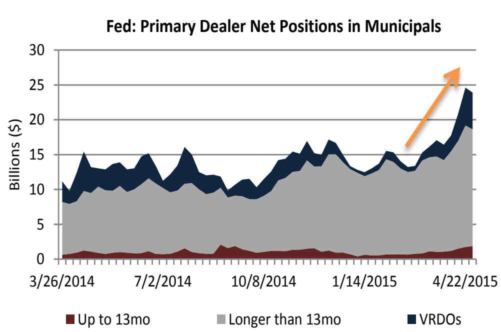



***Figure 4:*** *Dealers have increased their municipal holdings.*

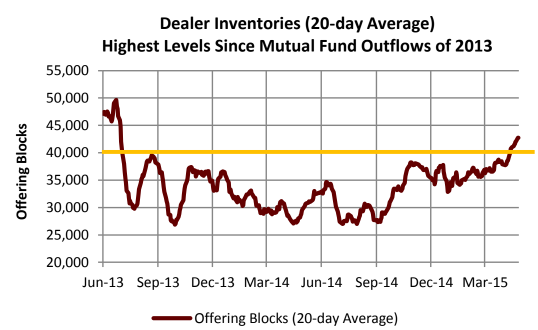



***Figure 5:*** *Offering items at the highest since summer 2013.*

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

Three large deals that moved the market last week and why (highlighted in yellow):

- The **Triborough Bridge and Tunnel Authority** benefited from strong retail interest on its deal, as it received more than $250 million in retail orders on the $225 million offered. The issuer was able to lower borrowing costs substantially. Retail has re-entered the market in a meaningful way as rates have moved higher in the last month.
- **Louisiana** competitively sold its GO credit in the wake of news that the Louisiana State University was expected to see state aid be cut. The revelation regarding LSU did not shed a kind light on the state. As a result the state's borrowing costs increased. For example, similarly rated Los Angeles schools issued bonds the same day at rates at least 15 basis points lower than the Louisiana GO.
- **Seattle, Washington** sold its limited and unlimited tax GO on Wednesday morning via silent auction. The penalty on the recently lower-rated limited tax was negligible—rates were either identical or at most, 5 basis points cheaper.

## NORTHEAST

5/7: **Loop Capital Markets** priced $225 million general revenue bonds for the **Triborough Bridge and Tunnel Authority**; NR/AA-/AA-, Kroll: AA; callable at par in 5/15/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2020 | 5.00 | 1.62 | +29 |
| 2025 | 5.00 | 2.58 | +33 |
| 2045 | 5.25 | 3.50 | +29 |

**Notes:** The 4th rating on credit does not appear to impact pricing

## MID-ATLANTIC

5/5: **Queen Anne's County, MD** sold $12.2 million public facilities bonds of 2015 to **Citigroup Global Markets Inc.**; Aa2/NR/AA+; callable at par in 7/1/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2020 | 5.00 | 1.50 | +20 |
| 2025 | 3.00 | 2.39 | +18 |
| 2035 | 3.375 | 3.52 | +59 |

**Notes:** Sub 4% coupons in 20-years the result of insurance interest

## MIDWEST

5/7: **Goldman, Sachs & Co.** priced $42.8 million lease appropriation refunding bonds for the **Indiana Finance Authority**; Aa2/AA+/AA+; callable at par in 8/1/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2020 | 5.00 | 1.65 | +32 |
| 2025 | 5.00 | 2.69 | +44 |
| 2035 | 5.00 | 3.70 | +71 |

**Notes:** 5% coupon structures perform well in rising rate environment

## SOUTHEAST

5/6: **Louisiana** sold $335 million general obligation bonds to **Wells Fargo Securities**; Aa2/AA/AA; callable at par in 5/1/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2020 | 5.00 | 1.60 | +29 |
| 2025 | 5.00 | 2.50 | +27 |
| 2035 | 4.00 | 3.75 | +79 |

**Notes:** Spreads were wider given state level fiscal concerns

## SOUTHWEST

5/5: **Raymond James & Associates** priced $3.3 million revenue certificates of obligation for **Southlake, TX**; NR/AAA/NR; callable at par in 2/15/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2016 | 4.00 | 0.40 | +17 |
| 2020 | 4.00 | 1.30 | 0 |
| 2035 | 3.25 | 3.10 | +17 |

**Notes:** Legislation to increase BQ levels was proposed last week.

## FARWEST

5/6 **Seattle, WA** sold $166 million limited tax general obligation improvement and refunding bonds to **Citigroup Global Markets Inc.**; Aa1/AAA/AA+; callable at par in 6/1/2025:

| Maturity | Coupon | Yield | +/- AAA 5% |
|---|---|---|---|
| 2020 | 5.00 | 1.55 | +24 |
| 2025 | 5.00 | 2.38 | +15 |
| 2035 | 4.00 | 3.65 | +69 |

**Notes:** The spread of +15 is tight for this credit.