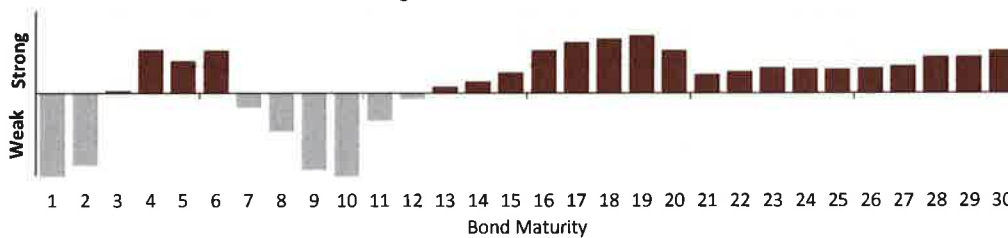
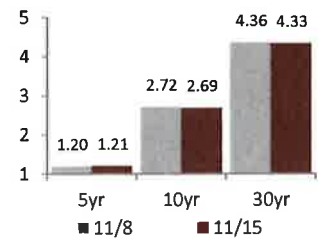


# MUNICIPAL ISSUER BRIEF

Strong or Weak Market for Bond Sellers



Muni Bond Rates (%)



Heading into this week, while still generally in favor of issuers, the market dynamic has changed 12-years and in. Here we see columns in the 'weak' portion meaning it could be more difficult to achieve as aggressive levels. Longer-dated maturities continue to appear more advantageous for issuers.

## MARKET UPDATE

**MUNICIPALS FOUGHT THROUGH HEADWINDS:** Last week started out slow as all markets adjusted to new economic expectations. As the week progressed, though, municipals found stronger investor interest in most new deals and ended on a good note.

**INVESTORS & ISSUERS:** Macro events helped municipalities.

- **When other bond markets improved in the middle of last week, the tone also improved for municipals.** The market started out shaky but when the incoming Federal Reserve Chairman Janet Yellen testified before Congress and appeared supportive of the current Fed bond buying program, municipals improved.
- **The week's new-deal calendar is the largest we've seen in about a month.** It also has some interesting, larger, partially junk-rated entities, such as Jefferson County and Guam. The overall increase in size could pose a problem for issuers as the demand/supply metric won't work in their favor, but counteracting this is that lower-rated bonds in general have done well recently.
- **There were at least two household-name insurance companies and large banks that have been buying high-grade municipal bonds.** These investors were particularly active in last week's larger competitive loan from Georgia and Montgomery County, MD, but also several smaller, infrequent issuers like North Dakota. If you are rated double-A or better and can issue in the 15- to 20-year maturity range, you could take advantage of this trend.
- **Last week retail orders periods were hit-or-miss.** Note in **Buyers Bites** where we saw interest in specific states.

**TAX REFORM UNLIKELY:** The Chairman of the House Ways and Means Committee, **Dave Camp** (R-MI), hinted last week that his efforts to move forward with comprehensive tax reform have stalled. Still, Congress may look at smaller pieces of tax reform in the near future, such as international, corporate, or individual tax reform. These initiatives could still impact the status quo and we understand there is still interest in changing the rules for private activity bonds. Still, it does seem unlikely anything happens through 2014.

### BUYER BITES:

**WHAT IS TRENDING HOT:**

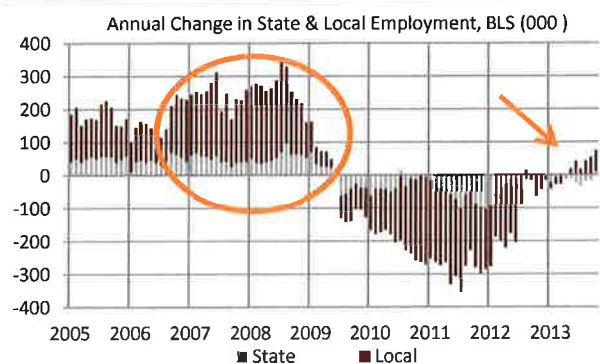
- 1) 15 to 20 year maturity range
- 2) New Jersey, California retail
- 3) Lower-rated issuers

**CURRENTLY HARDER SELLS:**

- 1) Mutual funds purchases
- 2) New York, Virginia retail

**WHO IS REPORTEDLY BUYING:**

Separately managed accounts, insurance companies, large banks



**Figure 1:** The latest state and local government employment figures show a continued rebound from the Great Recession. This is a convincing increase and the highest year-over-year since 2009. Note that localities were still hiring in 2007 to 2009 when the national economy was faltering. We talk more about local economies on page 3.

## TOPIC OF THE WEEK: STATE & LOCAL ECONOMIES

**LOCAL ECONOMIES:** History has shown that negative effects of a national recession tend to hit state and local governments later, but also that state and local governments have a harder time recovering even when the broader economy is improving. Recently, several associations and foundations have released research on how municipalities are moving past the Great Recession and the implications for their budgets going forward. First, we note that in October, state and local government jobs rose to 19.5 million across the United States. While this level is still well below the peak in 2008 (see **Figure 1** on page 1), this is the largest year-over-year increase since February 2009, meaning that government jobs are trending higher. This is in line with data showing an improvement in state and local revenue production. Last month the **National League of Cities (NLC)** released the City Fiscal Conditions Report in which they found that 72% of city finance officers believe their cities are better able to meet their financial needs in 2013 versus in 2012, the most positive reading since the year 2000. They also found that general fund revenues showed small improvements in 2013. With these themes in mind, the **Pew Charitable Trusts** recently put out a [report](#) that looked at how thirty large U.S. cities fared through the latest recession. We look at the major themes from the report that have direct or indirect implications for all municipal issuers below.

**WHAT THIS MEANS TO YOU:** While much of the data is trending better for governments, there are still localities that clearly continue to struggle. The Pew report emphasized the role of intergovernmental aid — funds from the state or Federal level — and found that governments that are more reliant on these funds saw their financial flexibility greatly strained during downturns. In their study of 30 cities, they found that for 80% of these cities, intergovernmental aid played a leading role in whether they achieved or exceeded pre-recession revenues in the 2007 to 2011 timeframe. This is especially important as leaders in Washington continue to tinker with the budget and discretionary spending, all of which have direct effects on state and local governments. Additionally, the types of revenue sources that a government relies on can influence the timing of recessionary effects. Sales or income taxes were negatively affected more acutely during the recession because they responded quickly to the changes in economic conditions. Conversely, property taxes tended to continue to grow during the recession as the assessed taxes lag the housing market. For governments that benefitted from continued growing property taxes over the last 5 years, you may want to monitor if in fact your community could be subject to similar scenarios, as taxes begin to calibrate to housing price declines. **Pew believes that some governments will continue to face additional challenges in the years to come because property tax revenues may underperform, fiscal austerity will lower the amount of intergovernmental aid, and pension and health care costs are likely to escalate.** Pew notes that the most important levers a city can pull to help stabilize finances include: spending reductions, revenue increases, reserve draws and aid from higher levels of government. Bond investors and rating agencies have increased their scrutiny of how issuer's plan ahead. The above trends could impact your rating and borrowing rates. Additionally, **MMA** expects with the increased revenues and infrastructure needs that issuers will borrow more in the coming future. In 2013, municipal issuance for new projects was at 1997 levels—an extremely low amount that does not meet future needs.

## ISSUER GROUP NEWS

**TAX REFORM IMPACT STUDY:** Following several proposals in recent years to alter or repeal the tax-exemption of municipal bonds, industry groups have conducted studies on the effects of those proposals on state and local government borrowing costs. The most recent of those studies comes from the **National Governors Association** and the **Council of State Governments**, which last week released a [study](#) on several tax provisions that have been considered on the Federal level.

The study, *Macroeconomic Analysis of Federal Tax Proposals Affecting State and Local Budgets*, was prepared by Moody's Analytics. It analyzed the impact of a 28% cap on the value of both state and local deductions and the earned interest exclusion for municipal bonds. It also considered the effect of a full repeal of the exemption. The report concluded that:

- The proposals would result in a net loss of about 417,000

jobs and \$71 billion in real gross domestic product (GDP) over the next 10 years.

- Both the cap and repeal scenarios would increase the interest rates that state and local governments pay on issuing municipal bonds with borrowing costs increasing as much as \$33 billion over the next decade.
- In capped and repeal scenarios, there would be a 10-year tax increase of \$187 billion and \$1.1 trillion, respectively.
- The construction and manufacturing industries would see a decrease in demand under a full repeal scenario, with 125,000 fewer jobs by 2023.
- The study also looked at the effects of the proposed America Fast Forward Bond program, which would provide direct-pay subsidies similar to BABs. The report noted that recent BABs subsidy payment reductions because of sequestration raises many questions about direct-pay options.

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

**NORTHEAST**

On November 13th, **M.R. Beal & Co.** priced \$375 million of revenue bonds for the **New York City Municipal Water Financing Authority**; Aa2/AA+/AA+; par call in 6/15/2023:

Maturity	Coupon	Yield
2046	4.625	4.80
2046	5.00	4.75

**Notes:** This issuer struggled to get retail interest and was forced to cheapen significantly when it offered bonds to institutions.

**MID-ATLANTIC**

On November 13th, **Citigroup Global Markets Inc.** bought \$295 million of general obligation bonds from **Montgomery County, Maryland**; Aaa/AAA/AAA; callable in 6/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2018	5.00	1.13	-11
2023	3.00	2.62	-15
2033	4.00	4.04	+3

**Notes:** This triple-A county helped to stabilize the broader market.

**MIDWEST**

On November 12th, **Piper Jaffray** bought \$40 million of general obligation alternative facility bonds from the **Special School District No. 1 Minneapolis, Minnesota**; Aa1/AA/AA; callable in 2/1/2022:

Maturity	Coupon	Yield	+/- AAA 5%
2018	4.00	1.02	-18
2023	5.00	2.73	+1
2028	4.00	3.78	+20

**Notes:** This double-A school benefited from having a regional dealer

**SOUTHEAST**

On November 13th, **Wells Fargo Securities** priced \$83 million of general obligation bonds for **Charleston County, South Carolina**; NR/AA+/AA; callable in 12/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2018	5.00	1.38	+18
2023	5.00	3.13	+39
2033	5.00	3.39	+60

**Notes:** This deal found very strong interest inside of 10-years.

**SOUTHWEST**

On November 13th, **Raymond James & Co.** priced \$60 million of revenue bonds for the **Hidalgo Texas Regional Mobility Authority**; NR/AA-/NR; callable in 12/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2018	4.00	1.60	+40
2023	5.00	3.37	+63
2028	5.00	4.16	+57

**Notes:** This Authority had to offer concessions with only 1 rating.

**NORTHWEST**

On November 14th, **Citigroup Global Markets Inc.** priced \$54 million of revenue bonds for the **Stockton Public Finance Authority**; Ba1/A-/BBB; callable at par in 10/1/2023:

Maturity	Coupon	Yield	+/- AAA 5%
2023	4.00	4.12	+138
2028	5.00	5.00	+141
2038	6.25	5.35	+107

**Notes:** Bankrupt Stockton saw strong demand for its revenue bonds