SECTOR DRIVERS FOR 2014

While we do not construct municipal portfolios with specific sector weightings, we do conduct top-down industry analysis as part of our fundamental credit research process. Annually, we identify the leading drivers that we believe will affect each specific sector and update those views throughout the year as necessary. Our thoughts on the major segments of the market as we begin 2014 are summarized below:

STATE GENERAL OBLIGATIONS	States remain a stable sector based on growing revenues, continued cost constraint, and limited debt issuance. Fifteen consecutive quarters of increased tax collections and restrained expenses have resulted in the lowest combined budget gap in years for FY2015. A federal budget deal will remove uncertainty, benefiting upcoming FY2015 budget proposals.
LOCAL GENERAL OBLIGATIONS	Our outlook for local governments remains cautious, with positive underlying trends. Driven by stronger state budgets, an improving housing market, and moderate economic growth, most local governments should see credit stabilization in 2014. Pensions and long-term liabilities remain a strain and a focus on reform efforts continues. Uneven economic growth has resulted in pockets of stress, increasing the importance of credit selection.
WATER & SEWER	We continue to have a stable outlook for the water and sewer sector based on the essentiality of services provided, the independent rate setting authority, the quasi-monopolistic business position that many systems enjoy, and a modestly improving economy.
PUBLIC POWER	We continue to have a stable outlook on the public power sector based on the rate-setting autonomy, relatively low power costs, and improving economic conditions. Regulatory mandates for lower coal and increased renewable usage will increase capital spending and customer rates for some utilities. Systems that serve regions experiencing economic growth will have greater flexibility to pass on rate increases, if necessary.
HEALTHCARE	Challenges and uncertainty related to the rollout of the Affordable Care Act warrants a continued cautious outlook for the healthcare sector. It remains to be seen if the increase in the insured population is sufficient to offset the expected weakness in reimbursement rates from all payers. We expect a continuation of our main theme from last year: the strong get stronger and the weak get weaker.
TRANSPORTATION	Our outlook for the transportation sector remains stable, as the sector's cyclicality should benefit from improved economic growth. Operating margins may be pressured by states and local governments that leverage transportation revenues to subsidize non-transportation projects and their own budgets. The most significant challenge going forward is identifying financing sources for a large backlog of infrastructure improvements and renovations.
AIRPORT	Our outlook for the airport sector is stable as economic improvements should benefit already healthy financial profiles. Airports have recovered faster than other sectors as enplanements and revenues have experienced steady annual growth. Airline consolidation poses a risk to airports with weaker market positions, as carrier diversity decreases and some overlapping and non-essential routes are cut.
HIGHER EDUCATION	We maintain our cautious outlook on the higher education sector as difficulty in growing top-line revenue is coupled with increasing expenses. The ability to increase tuition and fees is being pressured by public and political scrutiny of affordability issues. Meanwhile, competition for students, faculty and government funds has led many institutions to invest heavily in programs and facilities, both academic and non-academic. Similar to the healthcare sector, consolidation will be a trend and we expect a growing distinction between strong and weak credits.
SPECIAL TAX	Special tax credits have a number of different characteristics, making a broad sector opinion difficult to make. However, those credits that rely on economically-sensitive revenues should see collections improve with modest economic growth.

APPLETON PARTNERS, INC ONE POST OFFICE SQ. BOSTON, MA 02109 TEL. 617.338.0700 WWW.APPLETONPARTNERS.COM