APPLETON PARTNERS, INC.

This Week in the Bond Market 10/30/2017

Connecticut & Pennsylvania End Budget Impasses

- The last two states left to agree on budgets for the current fiscal year have finally ended their more than four months of gridlock. Connecticut lawmakers overwhelmingly passed a bipartisan budget that closes a $3.5 billion budget gap over the next two years. The budget agreement awaits the Governor's approval, but the strong support in the legislature indicates that the Governor's approval or disapproval is largely irrelevant at this point. Pennsylvania's House of Representatives approved a revenue package that closes a $2 billion deficit primarily through borrowing $1.5 billion against annual tobacco settlement payments. Notably, neither state was able to make progress on their most pressing issues; long-term liabilities associated with pensions and healthcare.

State Budget Bails Out Hartford

- The budget agreement agreed to last week by Connecticut lawmakers includes a number of provisions that should help Hartford in the short-term avoid a potential default on debt.
- Once the budget becomes law, Connecticut will immediately provide Hartford with $20 million in additional state aid, a move that will provide sufficient liquidity to keep the City's operations continuing. Connecticut will also cover $20 million in interest payments on Hartford's new debt, as well as providing a backstop in the form of a guaranteed debt service reserve. The debt refinancing will extend maturities and level out annual costs.
- The assistance does come with strings attached, as Hartford will be subject to increased oversight under the Municipal Accountability Review Board. In addition, the budget included a clause that the State's debt service assistance would terminate upon any local government attempting to file for Chapter 9 bankruptcy.
- Hartford is not in the clear, even with Connecticut's help and a debt refinancing. Mayor Bronin has stated that the City's labor unions will have to shoulder a portion of the burden, presumably with contract concessions. We also note that Hartford finds itself in this fiscally distressed position largely due to economic issues, primarily a large tax-exempt presence but also an inability to attract businesses. The recent developments provide Hartford with some breathing room, but structural changes are necessary to ensure a long-term, sustainable path to fiscal balance.

FIXED INCOME INDEX RETURNS AS OF 10/27/2017

	MTD	YTD
Barclays 3Yr	-0.04	2.31
Barclays 5Yr	-0.06	3.81
Barclays 7Yr	0.02	4.74
Barclays MM Short 1-5Yr	-0.06	2.33
Barclays MM 1-10Yr	-0.02	3.80
ML US Gov/Corp 1-10 Yr	-0.18	1.70

Source: Interactive Data

Muni Market Overview

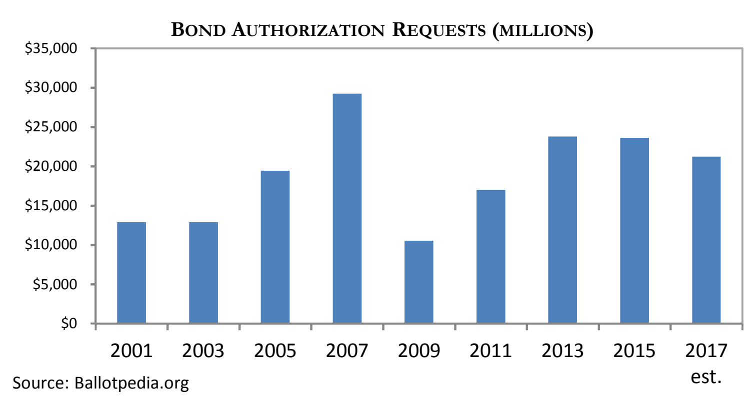
- Munis were cheaper over the week by 4-8bps along the curve through 10Yrs. Munis underperformed Treasuries, and the 10Yr Muni/Treasury ratio rose to about 83.5% from 81.5% last week. The ratio is below the 52-week moving average of about 90%.
- Last week's elevated issuance at $10.2 billion was digested by the market, but total year-to-date issuance is down almost 19% from last year. Expected issuance this week is just under $7 billion, which is below the year-to-date weekly average.

Taxable Market Overview

- The financial sector dominated the $48.7 billion of Investment Grade issuance last week as several institutions came to market after earnings releases. Citigroup's (C Baa1/BBB+/A) $4.4 billion Monday afternoon deal kicked off the week. The deal was spread across three maturities, and the $2.25 billion in 10Yrs priced at +115. A slightly softer market sentiment prevailed as we closed out the week even though credit spreads remain at year to date tight levels.
- The week ahead will be a busy one as the president is slated to announce his appointment of the next Fed chair, tax reform legislation is expected to be announced by the House of Representatives, a Fed rate decision on Wednesday, and jobs data is reported on Friday. With that said, we have seen a slight increase in market volatility and, given all the headlines, this week could prove to be a volatile one. US Treasuries were largely unchanged last week. The 10Yr and 30Yr were both up 2bps to 2.41% and 2.92%, respectively.

Bond Authorization Requests Down in 2017

- According to data collected from Ballotpedia.org by Bank of America Merrill Lynch, on November 7th voters across the country will be asked to authorize roughly $21.2 billion in municipal bonds. This is down 10.7% and 10.2% compared to the last off-year elections in 2013 and 2015, respectively.
- We note that authorizations in off-years are typically much lower than presidential or mid-term elections, so its difficult to say this year's numbers indicate a trend. However given a 10% decline from the last two off-cycle elections, it could reflect some reluctance on the part of issuers to take on large capital projects. Uncertainty at the federal level in regards to infrastructure, tax reform and other policies may play a role.



Source: Ballotpedia.org

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