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This Week in the Bond Market 05/08/2017

Puerto Rico Seeks Court-Supervised Restructuring

- Puerto Rico's federal oversight committee approved Governor Rossello's request to seek a court-supervised restructuring of the Commonwealth's nearly $70 billion in debt. Utilizing what is known as Title III under the PROMESA law, Puerto Rico requested the action after a previous protection from creditor lawsuits expired last Monday.
- Although Puerto Rico is not entitled to protection under Chapter 9 of the U.S. Bankruptcy Code and Title III is not technically a bankruptcy declaration, the path forward will be very much akin to what an insolvent creditor would experience in a bankruptcy proceeding.
- While the court supervision will provide a more streamlined restructuring process than multiple, often contrasting, legal battles, Puerto Rico's restructuring will still be a difficult and arduous process. With $70 billion in debt spread among 20 agencies and numerous security provisions, reaching a broad-based outcome will most likely take years rather than months.
- We also note that federal legislation passed last summer that allows Puerto Rico to restructure, PROMESA, has never been tested in court and a judge's legal interpretation of certain provisions may be very different than what Congress intended and what the market is currently anticipating.
- Puerto Rico bond prices have dropped precipitously over the last few years and reflect the market's assumption that all debt was on the table when it came to impairment. However, despite what may seem like low prices, there is no guarantee that bondholder recoveries will be at or near current market values.

Puerto Rico Debt Outstanding ($bns)	
GO	12.6
COFINA Subordinate	9.4
PREPA	8.5
GDB	7.7
COFINA Senior	6.6
PRASA	3.8
Other	21.6
Total	**$70.2**

Insured Debt ($bns)	
COFINA Senior	1.6
GO	2.5
PREPA	3.2
Other	6.7
Total	**$14.0**

Source: J.P. Morgan

FIXED INCOME INDEX RETURNS AS OF 05/05/2017

	MTD	YTD
Barclays 3Yr	0.09	1.66
Barclays 5Yr	0.17	2.77
Barclays 7Yr	0.18	3.09
Barclays MM Short 1-5Yr	0.10	1.85
Barclays MM 1-10Yr	0.14	2.63
ML US Gov/Corp 1-10 Yr	-0.18	0.98

Source: Interactive Data

House Approves Healthcare Reform Bill

- A revamped version of the American Health Care Act garnered enough support among Republicans to pass through the House of Representatives last week. After faltering earlier in the year, the legislation was barely approved with 217 votes for and 213 against.
- Changes to the legislation include: state waivers to opt out of coverage mandates; additional funding for people with pre-existing conditions; and increased funding to offset increases in premiums.
- The bill now moves to the Senate, where the current form of the legislation may face significant hurdles. Many Senate Republicans have already voiced concerns about the bill, opening the door for significant changes to the House's version or a complete re-write. The GOP controls 52 of the Senate's 100 seats, which means that opposition from two or more Republicans (assuming no Democratic support) could derail approval.

Muni Market Overview

- The muni curve did not move significantly over the week, with the 5Yr at 1.41% and the 7Yr remaining at 1.71%.
- This week's calendar is expected to be large, at $10.5 billion, which bests the YTD non holiday average of about $7.3 billion. During the first quarter of the year, municipal bond sales came in at $91.7 billion, which is almost 10% lower than the same time period last year. Partially responsible for this decrease is the reduction in refunding issuance. New money issuance marked its high since the first quarter of 2014, at 46%.

Corporate Market Overview

- With earnings season behind us, issuers exited the blackout period and returned to the new issuance market with a total of just over $39 billion on the week. It was the highest volume we have seen in several weeks, and the market absorbed the new debt with relative ease. The two most notable deals on the week began with Apple's (AAPL Aa1/AA+) return to the market for the second time this year with $7 billion and Eli Lilly (LLY A2/AA-) with $2.25 billion. The LLY deal had 5 times more in orders than was offered. The spread on that deal in 5Yrs was initially whispered to be +75, but tightened 25 bps to 50 by the time it was released. Demand for Investment grade continue to be very strong, which is continuing to keep spreads range bound.
- News out of last week's Fed meeting was consistent with the messaging they have been sending for the last several months, and they are seemingly on track for a rate hike in June. With that said, the economic data as of late has been somewhat weak. First quarter GDP and inflation was lower than expected, but the Fed sees Q1 as a "transitory" blip in the forcasted normalization of future rates hikes and balance sheet normalization. The US 10Yr benchmark rose 7bps on the week to 2.35%

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