

# **Bond Case Briefs**

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## **Credit Concerns Overhang the Latest Muni Industry Conference: MuniNetGuide.**

Notes from the Bloomberg State & Muni Finance Conference

As previously mentioned in this column, Bloomberg held their State and Muni Conference on November 6th in New York City. Right at the outset, the choice of venue was rather unconventional: the proceedings were held at The Cutting Room, a small rock and blues club owned by “Mr. Big” himself, Actor Chris Noth. Certainly, it was quite interesting for the panelists to be on the same stage where the likes of Ron Wood, Mick Ronson and Marty Balin will be performing.

The 300-pound gorilla in the room was, of course, Puerto Rico (PR).

Since video clips for most of the panels are available for viewing on the Bloomberg conference site, we’ll just go over a few things we found noteworthy.

Perhaps to no one’s surprise, credit topics dominated the discussions at the Conference, particularly those issues with potential “systemic” implications (I sat next to a representative from the FDIC, there to ferret out any and all systemic risks to our banking system!)

The Detroit situation was touched upon by several panels but no new information really emerged from the various discussions.

The 300-pound gorilla in the room was, of course, Puerto Rico (PR). In the very first session, U.S. Treasury Under-Secretary Mary Miller (a brilliant investment professional whom I’ve had the chance to know since her days as a muni analyst at T. Rowe Price) struck a very cautious note regarding potential Federal assistance to Puerto Rico. On the positive side, Mary confirmed that the Administration is closely monitoring the situation and is in close communication with the Padilla financial team. However, she also warned there is no existing Congressional authority for any kind of direct financial assistance to the troubled island. The Fed’s role is currently limited to providing input regarding fiscal management practices and ensure that all federal monies that are due the Commonwealth be expended in the most effective manner possible.

From PR’s side, Treasurer Melba Acosta and Chairman of the GDB David Chaffey were also on hand to hammer home their message to investors: default is not in the cards for now. Of note, after putting out press releases trumpeting stronger revenue collections in October, Treasurer Acosta appeared to back-track a little: she noted there was a special corporate tax payment due in October that could have inflated the numbers somewhat.

The second panel on PR featured Dick Larkin from H J Sims, Hector Negroni from Fundamental Advisors and Emily Raimes from Moody’s. In response to Dick’s unflinchingly strong defense of the PR credit, Hector observed that hedge funds should not be viewed as the “enemy”, since they stepped in to provide liquidity to the market when the traditional buyers could no longer handle the risk. We could not agree more. Like Hector, we feel the muni market should welcome the participation from the hedge funds, as providers of liquidity at a time when the broker-dealer

community is retrenching. Crossover distressed players are also more experienced than muni analysts, we believe, in evaluating trading opportunities related to capital structure. Broadening the audience for municipals can only benefit our asset class over the long run, in our view.

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Being Chicago-based, we were also interested in the panel on the State of Illinois, featuring our local pundit Chris Mier from Loop Capital. Chris pinned Illinois' fiscal problems on the One-Party rule and the high degree of work force unionization. All the panelists agreed that pension reform is the biggest issue facing the Prairie State, and one that won't be resolved any time soon. There was a feeling that the legislators in Springfield needed to be shocked by a real crisis - perhaps a failed State bond financing - in order to get off the dime. All noted the wider spreads on Illinois paper, close to +175, but none was willing to declare the credit a "buy" quite yet.

We were somewhat surprised by the lack of focus on the gubernatorial race, aside from a cursory comment from Chris. Surely, much of the legislative foot-dragging on pension reform must be attributable to the political maneuverings surrounding the election. As reported by the Chicago Tribune, "the two-week fall session that starts Tuesday will unfold just weeks ahead of the deadline for candidacy petitions to be filed for next year's elections. Taking a tough vote on pension reform before then risks drawing a challenger next year." So, even some clarity as to who might emerge as a strong contender in this electoral season could become a catalyst for progress on pension reform.

In the context of Illinois, Chicago's fiscal condition also came up and was deemed much more tenuous than the State's. The Windy City is currently held hostage by the lack of pension progress at the state level, and Mayor Emanuel is viewed as running out of options. Chris Mier pointed out that, although traditionally trading at tighter spreads than Illinois, Chicago bonds have flipped over and now trade at much wider spreads. To that extent, they may eventually become a more interesting credit play than Illinois.

In summary, the overwhelming message we got from the Conference is that the muni credit landscape remains quite unsettled. This should translate into an abundance of muni credit opportunities, as long as you do your homework.

#### About the Author

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Over his 32-year career as a high yield/distressed municipal bond expert, Nguyen has designed, marketed and managed every type of buy-side investment product, from mutual funds to managed accounts and hedge funds.