Bond Case Briefs

Municipal Finance Law Since 1971

Wall Street Muni-Bond Fees Shrink Fourth Straight Year.

Bank of America Corp. managed the most municipal bond issues for the second-straight year.

Fees that Wall Street charges U.S. cities and states to sell their bonds fell for a fourth straight year in 2013 as dwindling debt issuance intensified competition among banks for underwriting business.

In one example of an issuer that benefited, the New Jersey Turnpike Authority in March paid banks led by JPMorgan Chase & Co. (JPM) about $1.85 million to sell $1.4 billion of bonds backed by tolls, according to an offering statement for the debt. The fee of $1.32 per $1,000 of bonds was one-third of the cost in 2010, said Donna Manuelli, chief financial officer of the agency.

The average expense last year for municipalities to issue long-term, fixed-rate bonds in the $3.7 trillion market fell to $5.42 per $1,000, the lowest since at least 2009, data compiled by Bloomberg show.

"In a declining market, they're trying to pick up market share," Manuelli said in a telephone interview. Other banks proposed similar fees, she said.

More than four years after the longest recession since the 1930s, municipalities are loath to borrow as they are starting to mend their finances, said Bart Mosley, co-president of Trident Municipal Research in New York. Long-term fixed-rate U.S. municipal bond sales fell 15 percent to about $294 billion in 2013, Bloomberg data show.

Scaling Back

U.S. localities also scaled back refinancing as Detroit's record bankruptcy filing in July and speculation that the Federal Reserve will curb its bond buying pushed borrowing costs to the highest in more than two years in September. Interest rates soared from generational lows set at the end of 2012.

Municipal issuers refunded much of their higher-cost debt before 2013 as the Fed kept its benchmark overnight interest rate near zero and purchased long-term bonds to stimulate the economy, Mosley said.

The Federal Open Market Committee in December decided to cut monthly purchases of Treasuries and mortgage debt by $10 billion, to $75 billion, citing improvement in the labor market that pushed the jobless rate to a five-year low of 7 percent in November.

"Issuers know that banks are competing for a dwindling pool of business," Mosley said. "Price becomes the differentiating factor."

The shrinking commissions also reflect decisions by states and local governments to eschew complex deals laden with derivatives, which generated higher fees, in favor of simpler structures, he said.

No. 1

Bank of America Corp. managed the most municipal bond issues for the second-straight year. The Charlotte, North Carolina-based bank handled $42.2 billion of long-term, fixed-rate sales, according to Bloomberg data. New York-based JPMorgan ranked second for the second year in a row, managing about $38 billion.

The New Jersey authority oversees the 148-mile (238-kilometer) turnpike and the 172-mile Garden State Parkway. Its debt carries an A3 rating from Moody's Investors Service, six steps below the top, and an A+ rating from Standard & Poor's, two levels higher.

Demand for the agency's tax-free obligations typically outstrips supply, reducing the chance that underwriters will be left with unsold bonds, said Manuelli, the chief financial officer. New Jersey residents' top income-tax rate ranks fifth among U.S. states that assess the levy, according to the Tax Foundation, a nonprofit research group in Washington.

Excess Orders

"We're always oversubscribed," meaning investors place orders for more bonds than are being offered, she said. Underwriters "view the risk as a minimum."

Manuelli said JPMorgan assured her that the lower fees wouldn't affect the pricing of the bonds and increase borrowing costs. Ten-year Turnpike Authority bonds were priced on March 20 to yield 2.57 percent, or 0.06 percentage point below a Bloomberg index of A rated revenue bonds.

Jessica Francisco, a JPMorgan spokeswoman, declined to comment, as did Zia Ahmed, a Bank of America spokesman.

Colin MacNaught, assistant treasurer of Massachusetts, also said underwriting costs have declined.

In November, fees on long-maturity bonds typically sold with a $5 commission were issued with a $3.75 fee, the lowest in MacNaught's six years with the state and saving taxpayers almost $500,000, he said.

Bank Bids

A September auction of about $800 million of short-dated debt drew 106 bids from 20 banks, MacNaught said. The state paid $6,500 in fees on the deal, he said.

Massachusetts issues 80 percent of its debt by competitive bid, in which underwriters bid against each other for the securities.

Nationwide last year, about 20 percent of the dollar volume of munis were sold with that method.

Localities offered the remaining 80 percent through negotiated sales, in which issuers select a bank and negotiate fees in advance of a sale, comparing qualifications, performance and fees.

The average cost for negotiated offerings in 2013 was $5.37 per $1,000 of debt, compared with $5.71 for competitive offers, Bloomberg data show.

Same Dynamic

States and localities stand to reap the benefits of lower fees for the next few years, Mosley said.

"I don't see anything in the next few years that changes the dynamic," he said.

The borrowing slowdown is extending into 2014, with localities scheduling about $6.5 billion of debt sales in the next 30 days, about 29 percent below the one-year average.

The issuance lull is feeding lower debt costs. Benchmark 10-year munis yield 2.84 percent, the lowest since Dec. 2, and compared with 2.97 percent on similar-maturity Treasuries.

The ratio of the interest rates, a measure of relative value, is about 96 percent, close to the lowest since May, compared with a five-year average of 99 percent. The lower the figure, the more expensive munis are compared with federal securities.

By Martin Z. Braun Jan 9, 2014 5:00 PM PT

To contact the reporter on this story: Martin Z. Braun in New York at mbraun6@bloomberg.net

To contact the editor responsible for this story: Stephen Merelman at smerelman@bloomberg.net