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Market Close: 2014 - What's Not To Like?

A VERY GOOD YEAR

For many municipal market participations, this year turned out to be a good year in the end, although that's not the way it looked in January.

"There was a lot to like about 2014," says James Colby, senior municipal strategist and portfolio manager at Van Eck Global, summing up the way he views the year. "It was surprising in terms of the returns we have seen in the muni space."

He said that at beginning of the year the municipal community – the sales people, traders and portfolio managers — didn't expect to see anything more in the way of returns than the average coupon.

"What the Federal Reserve would do tempered our expectations – and then that didn't happen."

He says the weakened supply landscape was overtaken by basic demand. "All that reinvestment money found its way back into the asset class."

And he cites March as the turning point for the muni market.

"It was the inflection point. March was a strong signal for a move forward. The big Puerto Rico bond issue came to market then – and the deal was effectively placed. And those Puerto Rico bonds then traded up afterwards in a meaningful way."

Puerto Rico issued $3.5 billion of general obligation bonds on March 11. The junk-rated bonds were priced with an 8% coupon to yield 8.727% in 2035 and saw strong demand from investors.

Other things broke right for munis amid all the uncertainty about the Fed's intentions, he said.

"On the heels of a terrible 2013, when $60 billion in assets left the muni space in all categories and sectors. Even with 8% returns in 2014 we didn't recover all of those assets that left in 2013. This suggests that the rest may come back in 2015 if all goes well."

He sees no change in the supply/demand picture for 2015. "The same story is in place."

"The thing that could work against munis is the economy – the GDP," he asserts. "If the economy really is as strong as 5%, then expect equities and corporates to surge and if Treasury yields rise, then munis would underperform."

Oil could be a market factor in 2015. If crude prices stay in the $50-a-barrel range "more people will drive and they will feel better about things and that could cause a pickup in consumption and economic performance."

That has both good and bad consequences for munis.

"It's a two-edged sword – it's good news for some issuers like toll roads and airlines and industrial, but if rates rise sooner rather than later it would likely put a damper on overall muni performance," he says.

As for the rest of 2015, the scenario is still unclear.

"It's like a two-act play with an uncertain ending," Colby says. "My guess is that investors will take a cautious approach as to when and where they will place their bets in the muni space. But credit quality is a plus and it will remain strong."

A CHRISTMAS PRESENT FOR A.C.

Elsewhere, New Jersey is giving Atlantic City a $40 million short-term loan so the city won't have to sell notes in the municipal market, according to a published report.

The city had originally planned a $140 million bond sale for November, then scaled it back to a smaller note sale, which was delayed because of concerns about the city's finances in the wake of the casino closures.

The city must repay the 0.75% interest loan by March 31, according to an agreement signed by the city and the state, Reuters reported.

PRIMARY MARKET

No bond issues are scheduled for negotiated or competitive sale until after the start of the new year.

Looking ahead to January, Miami-Dade County, Fla., will put out for bid on Jan. 6 three separate competitive sales of general obligation bonds totaling about $372 million. Proceeds from the sales will be used for parks, public health and its "Building Better Communities" program.

SECONDARY MARKET

High-grade municipal bond prices were lower on Wednesday. The yield on the benchmark 10-year general obligation scale rose one basis point to 2.10% from to 2.09% on Tuesday, while the yield on 30-year GOs was up one basis point to 2.95% from 2.94% on Tuesday, according to the final read of Municipal Market Data's triple-A scale.

Treasury prices were lower, with the two-year note yield rising to 0.74% on Wednesday from 0.73% on Tuesday. The 10-year yield increased to 2.27% from 2.25% while the 30-year rose to 2.85%, from 2.83% on Tuesday.

The 10-year muni-to-Treasury ratio was calculated at 92.5% on Tuesday versus 92.5% on Tuesday; the 30-year muni to Treasury ratio was at 104.2%, compared with 103.1% on Tuesday.

"Heavier than anticipated year-end new issue volume contributed to elevated municipal to Treasury ratios in recent weeks," Alan Schankel, managing director at Janney Capital Markets, wrote in a research report. "A strong burst of new issuance in early December may be responsible for the higher municipal to Treasury ratios we've experienced in recent weeks."

But the over the longer term, Janney sees ratios as heading down.

THE BOND BUYER

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