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Relax and Unwind: Volcker Rule Delayed.

Last month, regulators announced they were extending by two years the effective date of the Volcker Rule, which was supposed to go into effect in July. This is good news for the municipal market, which otherwise would have seen some concentrated selling-off activity during the first half of this year.

The Volcker Rule, finalized in late 2013, limits banks' investments in hedge funds and other high risk vehicles, including what are called Tender Option Bonds, or TOBs. These bonds represent a small fraction of the municipal market (about $90 billion of the $3.7 trillion market) and are used to cover long term investments.

Banks and hedge funds get cash from a money market fund (a short term borrow) then turn around and invest that in a municipal bond. Because short term borrowing has typically yielded very low interest rates while rates on longer-term bonds has been higher, banks hope to pocket the difference between the two rates as profit.

Without the delay, managers would have had to unwind up to $90 billion in bonds currently held in TOB trusts during the first half of the year, which is equivalent to 60 percent of the expected $150 billion of new issuance in that same period, according to a Jan. 26 analysis by Moody's Investors Service. "Postponement of that liquidation relieves pressure on the overall market," Moody's added.

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