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## **U.S. Tobacco Bond Market Shrugs Off Fitch Move to Ditch Ratings.**

Fitch Ratings' announcement that it will pull its ratings on tobacco bonds sold by U.S. states and local governments was not shaking up the market for the high-performing debt on Tuesday.

Billions of dollars of bonds are backed by money from U.S. tobacco companies under a 1998 master settlement agreement (MSA) to compensate 46 states, Washington D.C., and Puerto Rico for the cost of caring for sick smokers.

Fitch on Monday said that recent side agreements between several states and tobacco companies that did not participate in the MSA regarding disputed payments "have eroded Fitch's confidence in the predictability of the calculation of MSA payments going forward."

The tobacco sector has not seen much negative movement since Fitch's announcement, said Chris Taddoni, vice president of municipal evaluated bonds at Markit.

The number of price quotes observed by Markit has remained consistent this week, suggesting that Fitch's action "is not having a huge effect on the market."

States have received more than \$50 billion so far under the MSA, according to the National Association of State Attorneys General, which manages the agreement.

Fitch said it will withdraw its ratings on tobacco bonds issued by Ohio, California, Puerto Rico, Michigan, Illinois, New York, and others on June 15. The credit rating agency did not respond to requests for further comment.

Moody's Investors Service and Standard & Poor's still rate tobacco bonds.

"I think that perhaps it just doesn't fit their process," said John Miller, co-head of fixed income for Nuveen Asset Management, regarding Fitch's action. "I'm a little bit surprised. It kind of looks like it's a lack of commitment to doing the analysis."

He added that tobacco bonds are in their third year of outperformance driven by stabilizing cigarette sales and investor demand for municipal bonds and high yields.

In the first four months of the year high yield tobacco bonds returned 9.4 percent, according to Barclays Capital, nearly three percentage points better than the next sector, transportation, which has returned 6.5 percent for investors.

Yields hit a high of 6.27 percent in some of the \$4.5 million traded in Ohio tobacco bonds with a 5.875 percent coupon maturing in 2047 on Tuesday, according to the Municipal Securities Rulemaking Board.

Dick Larkin, credit analysis director at Stoeber Glass & Co, concurred with Fitch's decision.

“So many side settlements, side negotiations and agreements that affect only handfuls of states have made forecasting issuer settlement payments totally unpredictable,” he said.

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