

Bond Case Briefs

Municipal Finance Law Since 1971

What's the Outlook for Munis as HQLA?

PHOENIX - A bill that would allow banks to count municipal bonds among their high-quality liquid assets appears to be headed towards eventual passage, potentially alleviating a situation that some market participants have said has hurt demand for munis.

Provisions that would allow banks to treat readily-marketable, investment-grade municipal securities as high-quality liquid assets under federal banking rules is included in S. 2155, the Economic Growth, Regulatory Relief, and Consumer Protection Act sponsored by Sen. Mike Crapo, R-Idaho. The provisions, the same as were included in a previously-introduced bill backed by Sen. Mike Rounds, R-S.D., is a response to rules adopted in 2014 by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corp.

These rules require banks with at least \$250 billion of total assets or consolidated on-balance sheet foreign exposures of at least \$10 billion to have a high enough liquidity coverage ratio - the amount of HQLA to total net cash outflows - to deal with periods of financial stress.

The regulators did not include munis as HQLA under the rule because they felt the securities were not liquid enough. The Fed later amended its rules to include some munis as HQLA but muni market participants said the amendments were still too restrictive and, in any case, would mean little if the other banking regulators did not follow suit.

Banks have emerged as major buyers of munis in recent years, with their holdings rising to about \$537 billion in 2016 from about \$191 billion in 2006 according to the Municipal Securities Rulemaking Board, a trend many in the market were concerned would be curtailed by the rules.

If passed into law, banks would be able to treat some munis as level 2B HQLA, the same level as for mortgage backed securities. That's a level down from the level 2A securities the market was hoping munis could belong to, the same level applied to sovereign debt.

The Senate voted March 6 to proceed to debate on the bill, which is broad and touches on not only munis but also mortgage lending and credit standards. The bill has 12 Democrat cosponsors and should be able to pass through the Senate and the House fairly smoothly and be signed into law within a few weeks, according to a source on Capitol Hill.

Emily Brock, director of the Government Finance Officers Association's federal liaison center, said she is "confident in the bill's progress."

"It's the bottom of the totem pole of what issuers could support," she said, noting that issuers had really hoped for a level 2A classification. "It's time to have a bipartisan, bicameral conversation about keeping the bond market strong," she added.

John Mousseau, executive vice president and director of fixed income at Sarasota, Fla.-based Cumberland Advisors said he believes the bill would be a win for the muni market if it becomes law, because it would help cement banks' important place as buyers of municipal debt.

The bill is unpopular with the more progressive Senate Democrats, who view it as largely a rollback of the Dodd-Frank provisions enacted in the wake of the 2007/2008 financial crisis rather than the effort to help the smaller regional and community banks that Republicans say the bill will help. Sen. Elizabeth Warren, D-Mass., has criticized her colleagues for supporting the bill and vowed to fight it.

By Kyle Glazier

BY SOURCEMEDIA | MUNICIPAL | 03/08/18 06:52 PM EST

Copyright © 2024 Bond Case Briefs | bondcasebriefs.com