

# **Bond Case Briefs**

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## **Easing Inflation Concerns Spur Jump For Longer-Dated Munis.**

### **Summary**

- **The Black Belt Energy Gas District has surfaced in the municipal bond pipeline with US\$735m worth of gas prepay revenue notes, amid increasing demand for longer-dated debt.**
- **For the week ended April 24, Thomson Reuters/Lipper U.S. Fund Flows reported a net inflow of roughly US\$1.28bn into municipal bond funds - contributing to 16 straight weeks of inflows.**
- **The Bond Buyer's 30-day visible supply - at US\$8.8bn - is the highest in a month.**

### **Black Belt Energy Eyes US\$735m 30-year Gas Prepay Revenue Bonds**

The Black Belt Energy Gas District (BBE) has surfaced in the municipal bond pipeline with US\$735m worth of gas prepay revenue notes, amid increasing demand for longer-dated debt.

The Alabama state-based public corporation serves as the natural gas supply arm of the Clarke-Mobile Counties Gas District, and was formed in 2008 for acquiring, managing and funding natural gas supplies for consumers, among other purposes. It is comprised of three municipal members: The City of Jackson, AL, the City of Thomasville, AL and the Town of Grovehill, AL.

The issuer said it aims to peg the proceeds from the sale of the bonds to prepay the acquisition costs of a fixed quantity of natural gas to be delivered over a 30-year period by Morgan Stanley Energy Structuring (MSES), pursuant to a Prepaid Natural Gas Sales Agreement (GSA).

Among the details of the transaction, BBE aims to enter into a commodity swap with BP Energy Co - guaranteed by BP Corporation North America - to mitigate any difference between the fixed payments owed to bondholders and the variable gas sales revenues received from its project participants.

BBE will also enter into an interest swap arrangement with MSES for the fixed payments it receives, with Morgan Stanley guarantying MSES's payments.

The issuance's series 2019A-1 bonds will be sold with a fixed interest rate, while the 2019A-2, 2019A-3, and 2019A-4 notes will be issued with variable rates.

The deal, rated 'A3' by Moody's Investors Service and 'A' by Fitch Ratings, is being lead-managed by Morgan Stanley, which is also serving as guarantor for payment obligations under the GSA.

Analysts at Fitch highlighted that by "virtue of the sales, hedging and investment agreements," the project is structured to "ensure that monthly net payments to BBE are sufficient to pay scheduled debt service, regardless of changes in natural gas prices, the physical delivery of gas, or the acceptance of delivered gas."

Both Moody's and Fitch base their credit ratings, in large part, on the credit quality of Morgan Stanley.

BBE's bonds are expected to price in May 2019. If successful, it would mark the issuer's fourth debt transaction.

At the start to March 2018, BBE had issued close to US\$687m worth of gas supply revenue bonds to finance an upfront prepayment for the 30-year supply of natural gas under an agreement with commodities broker J. Aron.

### **Alabama's Natural Gas Profile**

According to the U.S. Energy Information Administration, Alabama's natural gas production meets about one-fourth of the state's demand.

The EIA notes that the state's consumers receive the commodity via interstate pipelines, mainly from Mississippi and the Gulf Coast, but a growing share of supplies is also shipped south through Tennessee from Pennsylvania natural gas fields in the Marcellus and Utica shales. More than four-fifths of the natural gas entering Alabama continues through the state, mainly on to markets in Georgia, Florida, and Mississippi.

In terms of BBE's proposed bond issuance, the district will enter into Gas Supply Contracts with one public gas system; the City of Greenwood; as well as two gas and electric joint action agencies, Florida Gas Utility and the Public Energy Authority of Kentucky, which will resell its gas to Philadelphia Gas Works.

The EIA continued that an increasing amount of the natural gas delivered to Alabama customers goes to the electric power sector to fuel electricity generation, and since 2007, that sector has been "the largest natural gas-consuming sector" in the state.

The energy agency added that while the industrial sector consumes the second-largest amount, about 3 out of every 10 households use natural gas for heating. The residential sector typically uses only about 5% of the natural gas delivered to customers, mainly due to the state's mild winters.

In fact, Alabama, which produces natural gas both onshore and offshore in state waters, has seen its annual natural gas production steadily decline from its height in 1996, and currently contributes less than 1% of the nation's total natural gas output.

### **Rising Muni Demand Continues**

Meanwhile, BBE's pipeline bond deal comes amid a surge of investor demand in longer-dated municipal debt.

At 90.9% of comparable U.S. Treasuries Friday, the 30-year AAA municipal bond yield rose to its most expensive in nearly three years, according to data compiled by Bloomberg. The ratio – a key level of relative value – fell to its lowest since late June 2016.

Also, for the week ended April 24, Thomson Reuters/Lipper U.S. Fund Flows reported a net inflow of roughly US\$1.28bn into municipal bond funds – not including ETFs such as the iShares National Muni Bond fund (NYSEARCA: MUB) and the Vanguard Tax-Exempt Bond fund (NYSEARCA: VTEB).

The most recent positive flows contributed to 16 consecutive weeks of inflows, with long-term municipal funds having received more than US\$2bn.

Analysts at Janney Montgomery noted that as “inflation worries recede, longer maturity bonds are attracting increased investor interest.”

They also said that while the Bond Buyer 30-day visible supply – at US\$8.8bn – is the highest in a month, this week’s primary calendar of US\$5bn is “quite manageable, especially in the high demand environment we’ve occupied this year with record inflows to municipal mutual funds fueling municipal sector outperformance.”

Other deals on the radar for the week ahead include issuance from the cities of Philadelphia, Dallas, and Milwaukee.

In the meantime, prices of MUB and VTEB have soared more than 4.5% to 4.8% since their latest 52-week lows set in early November 2018 of US\$106.575 and US\$49.855, respectively, according to the IBKR Trader Workstation.

## **Seeking Alpha**

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