

# California Debt and Investment Advisory Commission Municipal Debt Essentials: Accessing the Market

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ADVISORY  
COMMISSION



# Fidelity Capital Markets (FCM) Facts

- Customer-focused institutional trading firm under the Fidelity umbrella
- FCM is a full service underwriter with \$2 billion capital base\*
- Conduit to 15 million individual accounts and with \$2 trillion in assets\*\*
- Active in competitive municipal market since 1987
- Active as co-manager since 2007
  
- Debra Saunders
  - Over 20 years as credit analyst at Ambac Assurance
  - Series 7, 63
  - Opened West Region Municipal Underwriting office for Fidelity Capital Markets in 2010

\* December 2014 FOCUS Report

\*\* Fidelity unaudited data as of January 30, 2015

# Who is Buying Your Bonds?

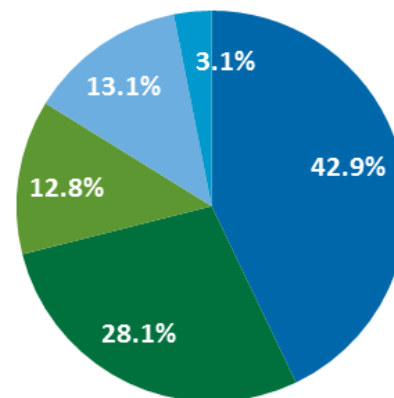
\$3.7 trillion in outstanding municipal bond debt

- There are over 60,000 different municipal bond issuers and over 1.5 million CUSIP's\*\*

Who owns Municipal Bonds and Why?

- Individuals: Preference for tax exempt income, higher relative credit quality and predictability of payments.
- Mutual Funds: Offer tax exempt investment and diversification with greater liquidity.
- Other Institutions: May buy tax exempt bonds for gains or losses, or buy taxable Municipal / Build America Bonds for longer term taxable alternative.
- The corporate bond market, almost three times the size has approximately 1/6<sup>th</sup> the number of issuers

## 2014 Holders of Municipal Bonds\*

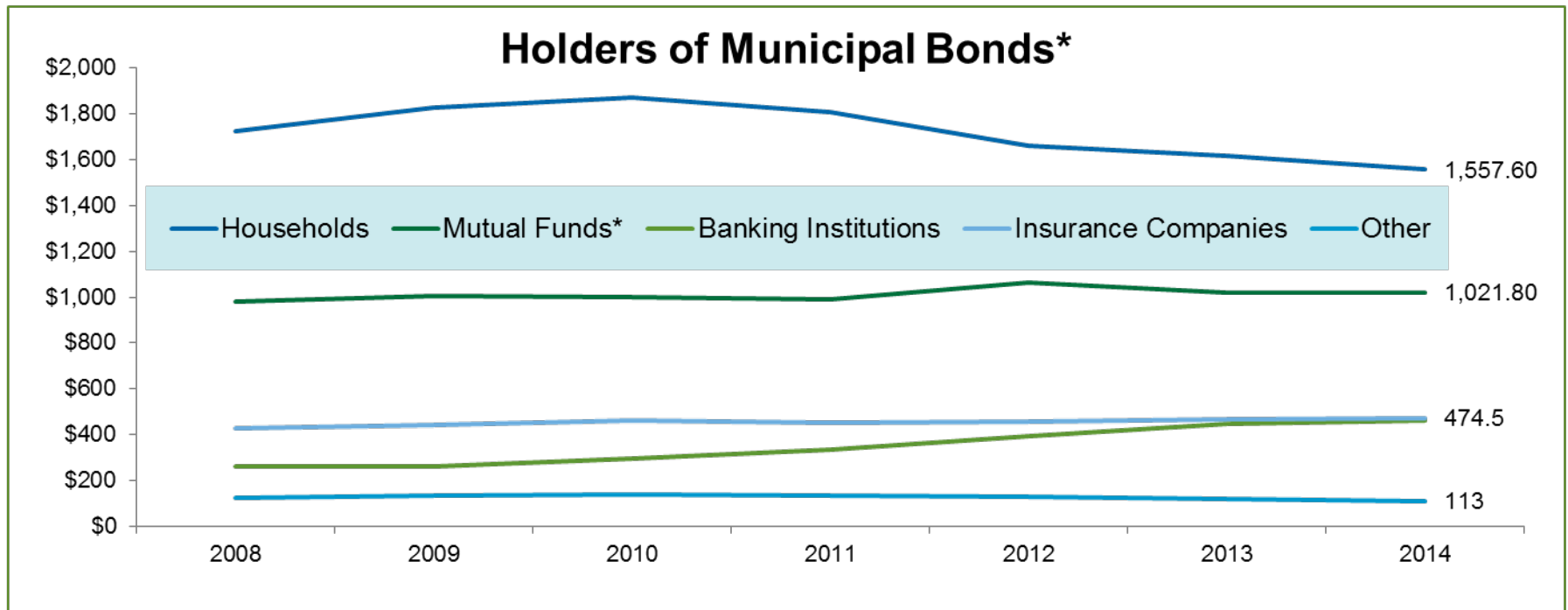


■ Households ■ Mutual Funds\* ■ Banking Institutions ■ Insurance Companies ■ Other

\*Source: SIFMA 3rd Quarter, 2014

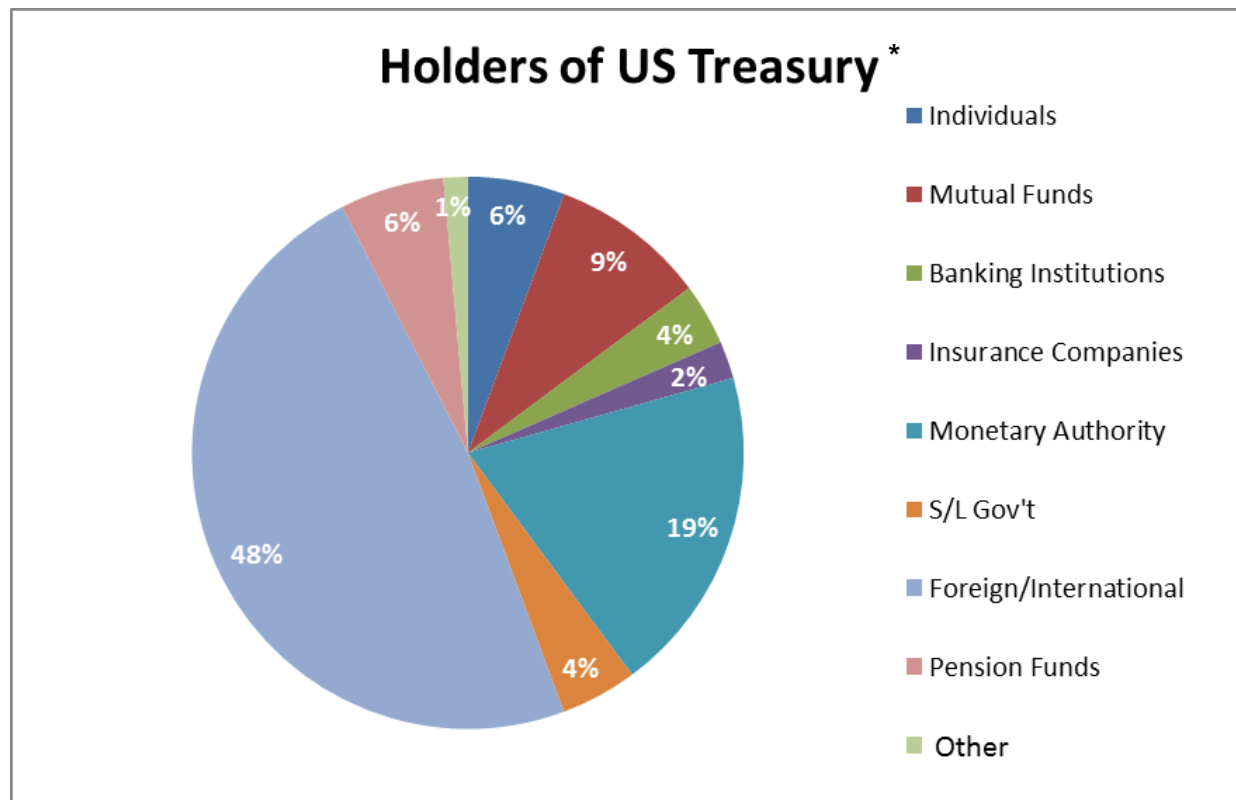
# Distribution of \$3.6 trillion in Municipal Bonds

- Retail domination of the municipal market is unique compared to other asset classes
- Trends: Individual has been shrinking but institutional has been growing
- Tax exemption benefits individual taxpayers more than Corporations
- Direct loans, taxable bonds, BAB's driving increases in banks/insurance company holdings



# Compare: Treasury Bonds

- \$11 Trillion Outstanding
- Global Market
- Individuals hold 6% of Total
- Broad distribution and demand

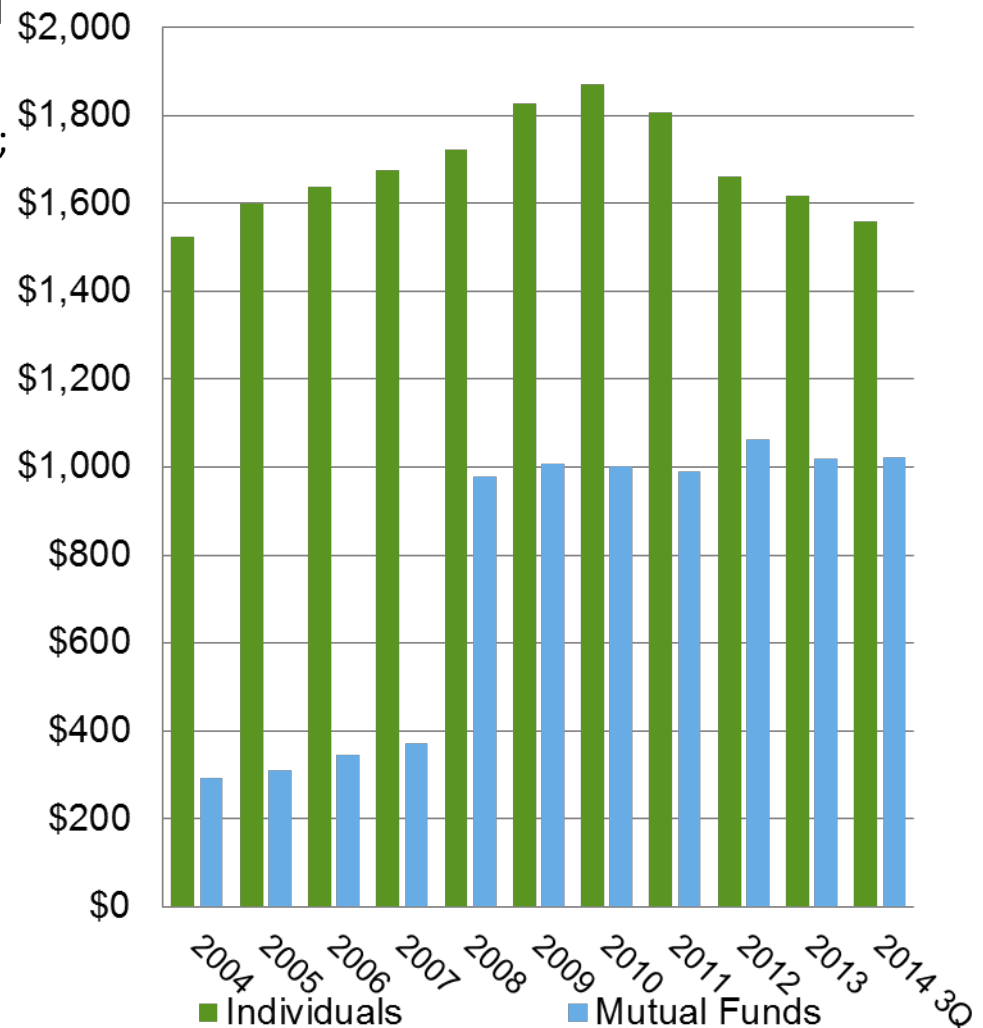


# Retail

- Households hold 42% of outstanding municipal securities; down from 54% in 2004
- Mutual funds own 17% of municipal securities; up from 10% in 2004\*

## The environment:

- Fiscal crisis, credit fears and bond insurance
- Low interest rates, expectation of rising rates
- Rising rates depress mutual fund NAV's



## There are different types of retail investors

Type of Investors	Buying preferences	Structure
Individual retail	Internet, phones, \$5-25K	Par, 10 years
Separately Managed Accounts	Large firms: From lead managers Medium-small: captive	All coupons, 10+ years
High Net Worth	Broker-assisted, \$100K-\$5M	Par, slight premiums, 10-15 years
Family Office	Broker assisted	Par/preservation of capital

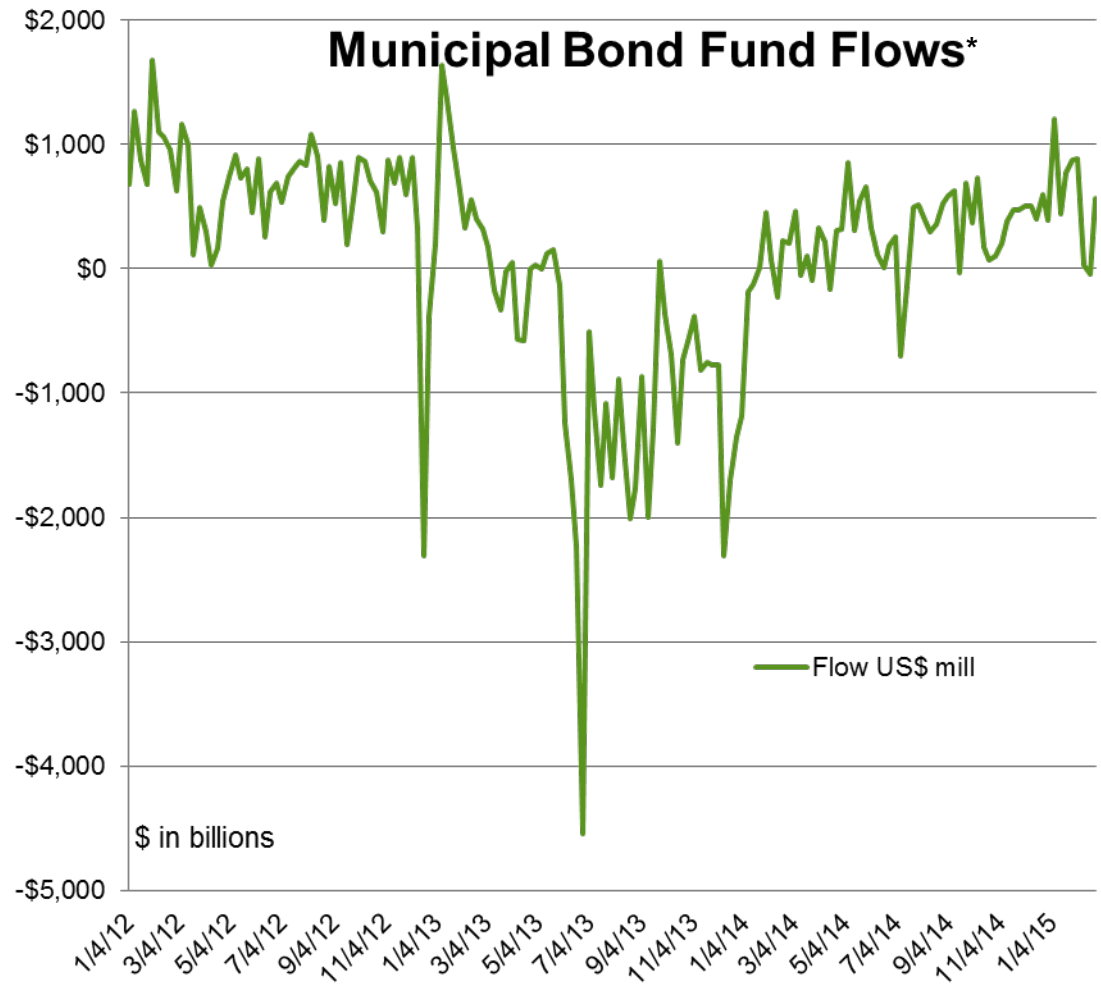
# Professional Retail

- Fee-based tax-exempt portfolios (25 bps and up)
- Tailored portfolios based on duration and maturity guidelines, tax exempt portfolios typically fall into three basic categories; *Short-Term*, *Intermediate*, and *Long-Term*.
- Strategic: State-focused, solution-focused
- Portfolio Management Team has authority to trade within parameters
- Small, specialty firms to very large firms
- Participate strategically – may order during retail order period or wait and order during institutional order period



# Mutual Funds

- Mutual Fund Dynamics:  
Rising rates drive declines in NAV which triggers further selling.
- Major institutions covered by multiple banking firms
- Designate syndicate members for compensation
- Strong demand in short end, money market eligible



# How to Reach Retail Buyers

- Marketing process that is accommodative and can reach all investors
- Retail order periods
  - Negotiated sales only
  - Prior to institutional sales
  - Extended order periods: multiple days, open over weekend
  - Time of day is important
- Engage retail brokers
  - Need reasonable certainty that bonds will be allocated
  - Use retail order period

# Targeting Retail

- The ROP typically occurs during the day or two before the official bond or pricing.
  - Through the end of the ROP, investors can submit orders through their broker if they are a member of the syndicate or selling group.
  - Retail investors are notified of the status of their order and the final pricing. (Note: The ability to fill individual orders depends on the amount of bonds or notes available and the amount of orders. While there is no guarantee, individual orders usually are filled.)
  - Investors who order bonds or notes during the ROP have the right to change, or cancel, their order until the order has been confirmed after final pricing.
- “Retail investors” are defined to include individuals as well as bank trust departments, investment advisors and money managers acting on behalf of individuals.
  - Individual investors purchasing bonds or notes to hold as an investment may purchase during the ROP.
  - Generally, orders may not exceed \$1 million. Larger orders are subject to prior approval by the State, its financial advisor or the senior managing underwriter.

# Advantages to individual investors

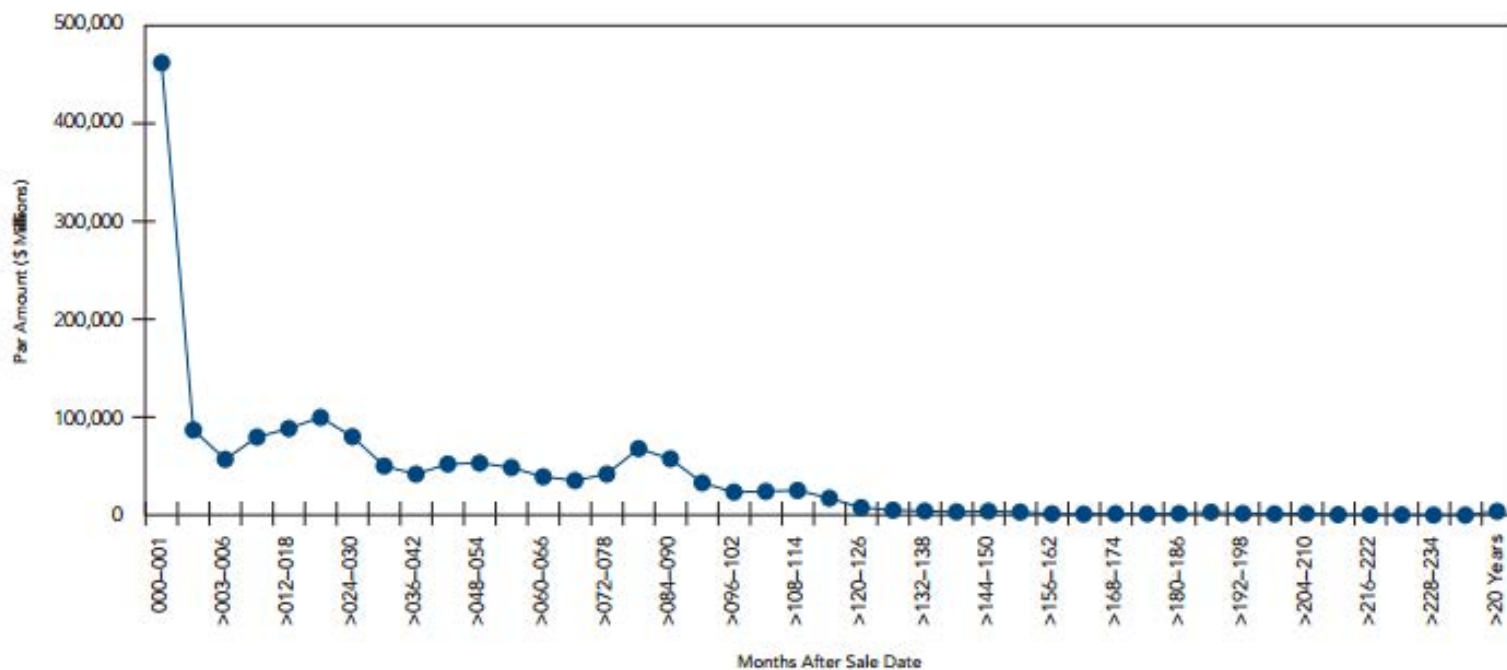
- Purchasing bonds during the ROP provides advantages to investors:
- They get to place orders before institutional investors, such as mutual funds or insurance companies.
- They earn the same return on their investment as other investors who buy bonds or notes with the same maturity date after the early order period.
- They do not pay the upfront brokerage fee/commission. (Individuals should check with their broker to learn about any other transaction or account maintenance fees the firm may charge.)

Plus:

- Disclosure is up to date
- Call Dates are furthest out
- Ratings are fresh

# The Aftermarket: Tracking your bonds on MSRB

Par Amount Traded by Months After Sale Date<sup>1</sup>, 2014

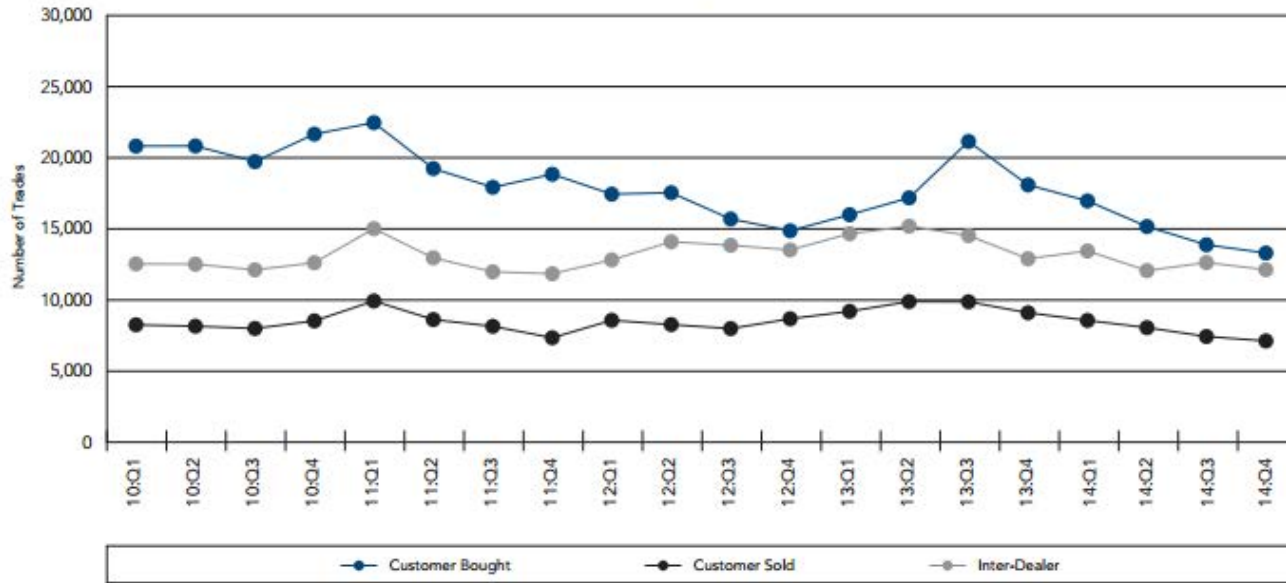


<sup>1</sup> Includes only bonds—securities with maturities of two or more years (maturity date less dated date) with fixed (MSRB 2014 Fact Book)

# Monitoring Activity on EMMA

Average Daily Number of Trades, 2010–2014

By trade type



Quarter	Customer Bought	Customer Sold	Inter-Dealer
10:Q1	20,889	8,328	12,608
10:Q2	20,898	8,230	12,590

# Analyzing MSRB Secondary Market Trading

## Security Details

### NEW YORK STATE HOUSING FINANCE AGENCY STATE PERSONAL INCOME TAX REVENUE BONDS (ECONOMIC DEVELOPMENT AND HOUSING) 2009 SERIES A (NY)

NEW YORK ST HSG FIN AGY ST PERSONAL INCOME TAX REV ECONOMIC DEV & HSG-SER A (NY)\*

CUSIP: 649870LB6\*

Dated Date: 08/27/2009

Maturity Date: 03/15/2024

Interest Rate: 4.0 %

Principal Amount At Issuance: \$2,845,000

Initial Offering Price/Yield: 98.264

Add this security to your alerts.

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Issuer Homepage <sup>Pilot</sup>

STATE OF NEW YORK

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View daily summary of price and yield information for trades in this security, including a graph of trade prices over time. [Learn more about trade prices.](#)

Screen shots are for illustrative purposes only.

View historical price and yield information for trades in this security. [Learn more about trade prices.](#)

Display  results | Find in results:  [First](#) [Previous](#) [1](#) [2](#) [3](#) [4](#) [5](#) [Next](#) [Last](#)

Trade Date/Time	Settlement Date	Price (%)	Yield (%)	Trade Amount (\$)	Trade Type	Special Condition
12/11/2014 12:55 PM	12/16/2014	109.512	1.67	15,000	Inter-dealer trade	
12/11/2014 12:55 PM	12/16/2014	110.512	1.439	15,000	Customer bought	
12/10/2014 02:38 PM	12/15/2014	109.518	1.67	20,000	Inter-dealer trade	
12/10/2014 02:38 PM	12/15/2014	110.618	1.416	20,000	Customer bought	
12/10/2014 11:43 AM	12/15/2014	109.518	1.67	15,000	Inter-dealer trade	
12/10/2014 11:43 AM	12/15/2014	111.434	1.23	15,000	Customer bought	
12/08/2014 02:11 PM	12/11/2014	109.284	1.73	100,000	Inter-dealer trade	
12/08/2014 02:11 PM	12/11/2014	111.196	1.291	100,000	Customer bought	
12/03/2014 02:26 PM	12/08/2014	108.87	1.83	150,000	Inter-dealer trade	
12/03/2014 02:26 PM	12/08/2014	108.37	1.947	150,000	Customer sold	

Displaying 1 to 10 of 166 results [First](#) [Previous](#) [1](#) [2](#) [3](#) [4](#) [5](#) [Next](#) [Last](#)

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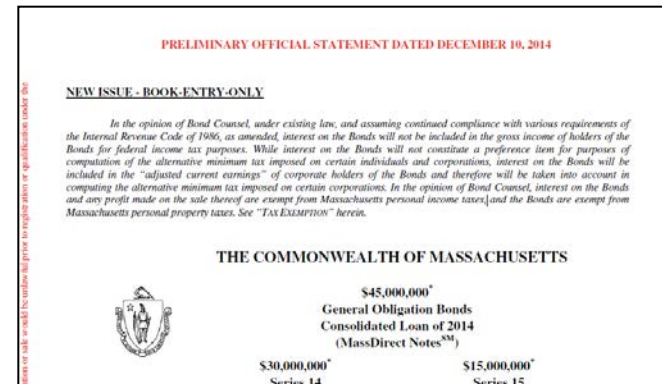
Trade Date	High/Low Price (%)	High/Low Yield (%)	Trade Count	Total Trade Amount (\$)
12/11/2014	110.512 / 109.512	1.67 / 1.439	2	30,000
12/10/2014	111.434 / 109.518	1.67 / 1.23	4	70,000
12/08/2014	111.196 / 109.284	1.73 / 1.291	2	200,000
12/03/2014	108.87 / 108.37	1.947 / 1.83	2	300,000
05/22/2014	109.071 / 109.071	2.007 / 2.007	1	25,000
05/21/2014	108.437 / 105.634	2.742 / 2.141	3	100,000
02/28/2014	105.9 / 105.9	2.736 / 2.736	1	20,000
02/27/2014	102.91 / 102.91	3.366 / 3.366	1	20,000
01/18/2013	111.809 / 111.809	1.95 / 1.95	1	40,000
11/29/2012	112.186 / 109.496	2.364 / 1.93	2	265,000
11/28/2012	111.401 / 111.401	2.056 / 2.056	1	200,000
12/07/2011	104.681 / 104.481	3.3 / 3.27	2	10,000
11/30/2011	104.692 / 104.492	3.3 / 3.27	2	10,000
11/16/2011	105.685 / 105.685	3.124 / 3.124	1	5,000
11/09/2011	105.493 / 104.993	3.229 / 3.155	3	45,000
11/04/2011	102.034 / 102.034	3.681 / 3.681	1	50,000
10/11/2011	106.605 / 106.605	3 / 3	2	20,000
09/29/2011	105.44 / 103	3.538 / 3.174	6	240,000
01/10/2011	98.985 / 98.985	4.1 / 4.1	1	100,000
01/06/2011	96 / 96	4.403 / 4.403	1	100,000
09/22/2010	106.133 / 106.133	3.168 / 3.168	2	30,000

# Rolling Offering / Direct Notes Program



In 2014 the Commonwealth of Massachusetts initiated its “MassDirect Notes Program” in an effort to provide individual investors direct access to new-issue Mass Bonds

- Each month up to six different maturities of fixed-rate tax-exempt general obligation bonds over a two-week period
- The prices/yields of the bonds are expected to change daily
- With the exception of Fidelity Capital Markets, the MassDirect Notes utilized TMC to offer and distribute the Notes – FCM relied on its online platform and IPreo



**\$30,000,000\***  
**General Obligation Bonds**  
**Consolidated Loan of 2014**  
**(MassDirect Notes<sup>SM</sup>, Series 14**

**Dated: Date of Delivery**      **Due: As shown below**

**\$10,000,000\* Series 14 Bonds maturing January 1, 2018\***, % CUSIP No. \_\_\_\_\_ \*\*

Sale Date	Principal Amount	Yield***	Price***
December 15, 2014	\$	%	%
December 16, 2014			
December 17, 2014			
December 18, 2014			
December 19, 2014			

**\$10,000,000\* Series 14 Bonds maturing January 1, 2020\***, % CUSIP No. \_\_\_\_\_ \*\*

Sale Date	Principal Amount	Yield***	Price***
December 15, 2014	\$	%	%
December 16, 2014			
December 17, 2014			
December 18, 2014			
December 19, 2014			

**\$10,000,000\* Series 14 Bonds maturing January 1, 2025\***, % CUSIP No. \_\_\_\_\_ \*\*

Sale Date	Principal Amount	Yield***	Price***
December 15, 2014	\$	%	%
December 16, 2014			
December 17, 2014			
December 18, 2014			
December 19, 2014			



# Meeting Retail Investors on the Web: Secondary Market

## Secondary Market Transparency

- Investor access to pricing and material events may help foster liquidity in the retail driven market

## Support Retail Trading in Secondary Market

- FCM Bids and then puts bid out to the market
- After a period of time, the retail investor is presented with the bids and able to select the best price – which may or may not be Fidelity's
- There are other firms that are developing platforms to speak to secondary market access

The screenshot displays the Fidelity.com website interface. The top navigation bar includes 'Fidelity.com', a search bar, and links for 'Quotes', 'Customer Service', 'Open an Account', and 'Log In'. Below the navigation, there are tabs for 'Accounts & Trade', 'News & Insights', 'Research', 'Guidance & Retirement', and 'Investment Products'. The main content area shows 'Search Results: Municipal (Secondary)' with various filters for Maturity Date, Ask Quantity, Ask Price, State/Territory, Risk/Price Filters, and Ask Yield. A 'Recent Trades' table is highlighted, showing transaction details for 'NEW YORK ST ENVIRONMENTAL FACS 05.25000% 06/15/2016CORP ST CLEAN WTR'. The table includes columns for Price, Quantity, Yield, Date/Time, and Buy/Sell. A green arrow points from the 'Recent Trades' table to the '3rd Party Recent Trades' column in the main search results table below.

**Recent Trades**  
NEW YORK ST ENVIRONMENTAL FACS 05.25000% 06/15/2016CORP ST CLEAN WTR

Price	Quantity	Yield	Date/Time	Buy/Sell
114.854	350	0.480	04/19/2013 12:34:00	Customer Buy
114.65	350	0.560	04/16/2013 02:01:43	Customer Sell
113.699	25	1.224	12/17/2012 04:13:23	Customer Sell
113.949	25	1.156	12/17/2012 04:11:30	Customer Buy
116.358	60	0.800	09/14/2012 04:09:09	Customer Sell
116.358	60	0.800	09/14/2012 04:09:09	Dealer to Dealer
116.358	25	0.800	09/14/2012 04:08:00	Customer Buy
116.358	35	0.800	09/14/2012 04:08:00	Customer Buy
115.717	60	0.963	09/13/2012 03:33:52	Customer Sell
115.917	60	0.913	09/13/2012 03:32:39	Customer Buy
115.917	60	0.912	09/13/2012 03:32:22	Dealer to Dealer

Recent trade information contains actual trade data as reported to the Financial Industry Regulatory Authority (FINRA)'s Trade Reporting and Compliance Engine (TRACE) for Corporate Bonds, and from the Municipal Securities Rulemaking Board (MSRB) for Municipal bonds. The prices quoted provide insight into recent historical transaction levels and are not necessarily reflective of current market value. Fidelity reports TRACE and MSRB information on a real-time basis.

**6 Results Found** As of 07/22/2013 at 12:24:16 PM

Row #	State	Description	Coupon	Maturity Date	Ratings (Moody's / S&P)	Underlying Ratings (Moody's / S&P)	Bid Yield	Bid Price Qty (min)	Ask Price Qty (Min)	Ask Yield	Depth Of Book	3rd Party Recent Trades	Yield Type	Attributes and Issuer Events	Action
1	NY	NEW YORK N Y CITY MUN WTR FIN AUTH WTR04.00000% 06/15/2016 & SWR SYS REV REV BDS SER. 2009 FF1	4.000	06/15/2016	AA2/AA+	AA2/-	--	--	109.583 1,000(50)	0.646	No	108.858 View	M	ME IR CP R SFP	Buy Sell
2	NY	NEW YORK ST ENVIRONMENTAL FACS 03.00000% 02/15/2016CORP REV ST REVOLVING FUND REV NEW YORK N Y GO BDS SER. I 05.00000% 08/01/2015	3.000	02/15/2016	AAA/AAA	AAA/-	--	--	106.603 925(50)	0.4	No	106.031 View	M	ME IR CP R SFP	Buy Sell
3	NY	NEW YORK N Y CITY MUN WTR FIN AUTH	3.000	06/15/2015	AA2/AA+	AA2/-	--	--	109.283 1,255(100)	0.375	No	109.03 View	M	ME IR CP GO SFP	Buy Sell
	NY	NEW YORK N Y CITY MUN WTR FIN AUTH	3.000	06/15/2015	AA2/AA+	AA2/-	--	--	104.848 475(50)	0.42	No	104.739 View	M	ME IR CP	Buy

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Although bonds generally present less short-term risk and volatility than stocks, bonds do contain interest rate risk (as interest rate rise, bond prices usually fall and vice versa) and the risk of default, or the risk that an issuer will be unable to make income or principal payments. Additionally, bonds and short-term investments entail greater inflation risk, or the risk that the return of an investment will not keep up with increases in the prices of goods and services, than stocks.

Interest income generated by municipal bonds and certain securities issued by U.S. territories, possessions, agencies, and instrumentalities is generally exempt from state income tax but is generally subject to federal income and alternative minimum taxes and may be subject to state alternative minimum taxes. Short- and long-term capital gains and gains characterized as market discount recognized when bonds are sold or mature are generally taxable at both the state and federal level.

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