

CDIAC MUNICIPAL DEBT ESSENTIALS SEMINAR

Introduction: Evolution of the Bond Market

October 2016

The Birth of the Municipal Bond Market

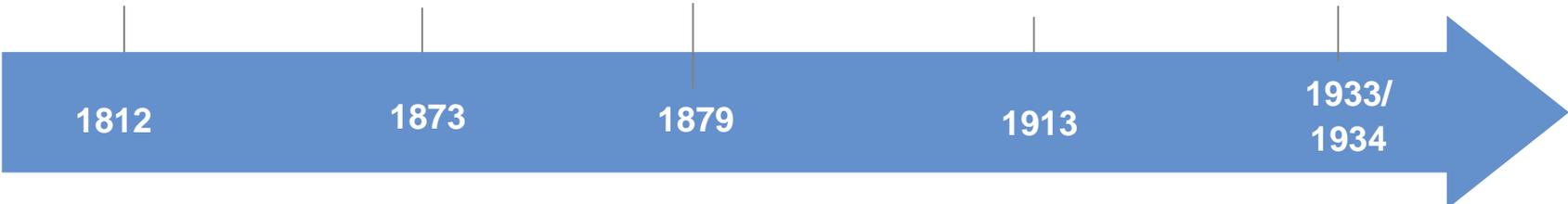
**New York City
Issues First
Municipal
Bonds**

Panic of 1873

**California
Constitution
Places Limits
on Debt**

**Revenue Act
of 1913
codified
exemption of
muni interest**

**1933 and 1934
Securities Act**



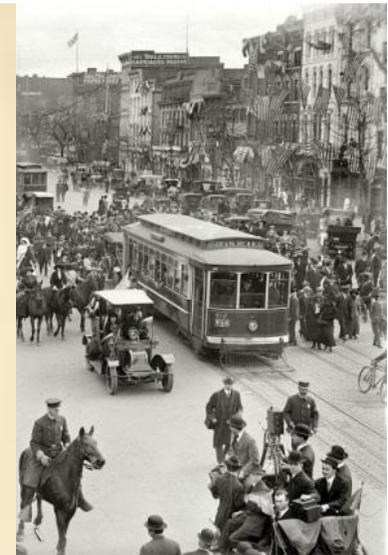
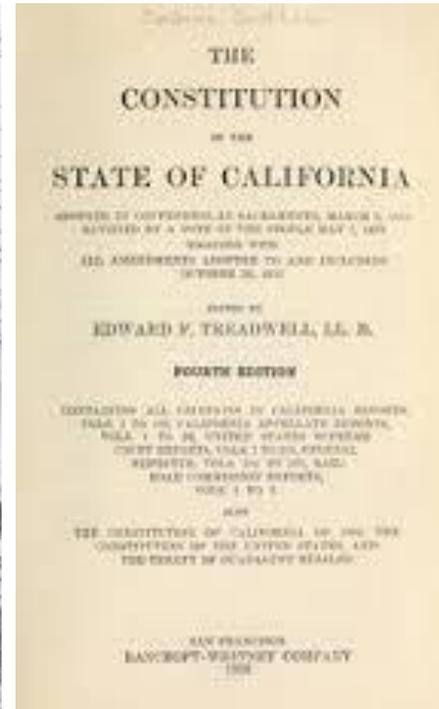
1812

1873

1879

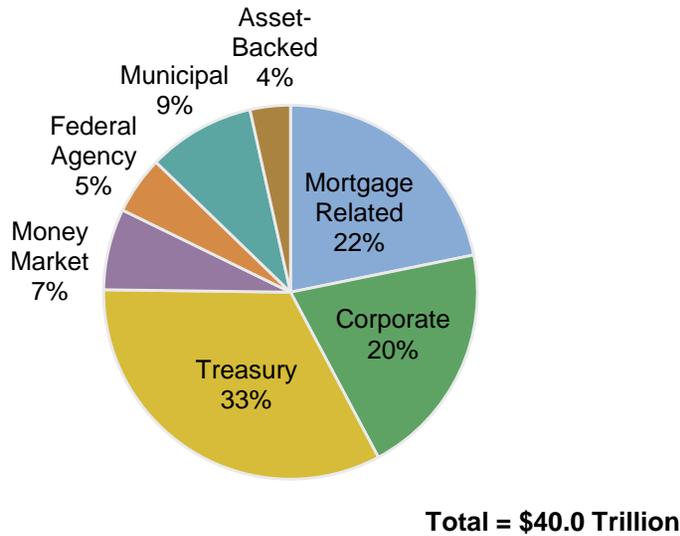
1913

1933/
1934



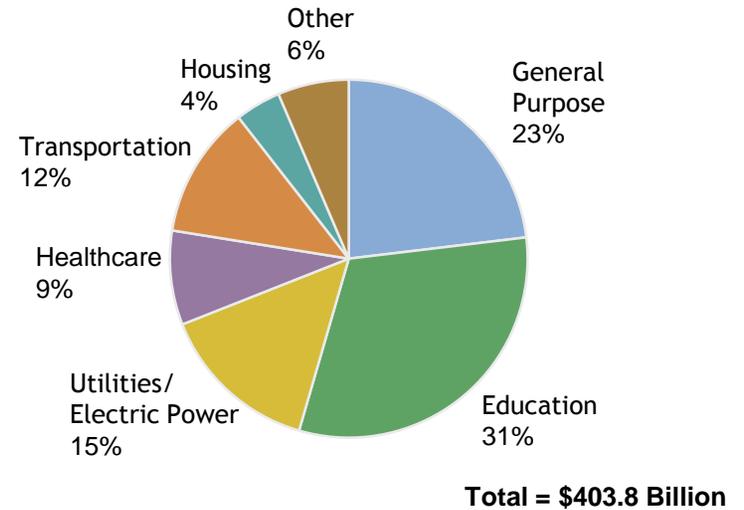
Today's Municipal Market Characteristics

US Bond Market Debt Outstanding (4Q 2015)



Source: SIFMA

2015 Municipal Issuance by Sector



Source: Bond Buyer

How Does the Municipal Market Compare to Other Markets

Key market statistics							
Market	Market Size	# of Issuers	# of CUSIPs	% Direct Retail	Avg Daily Volume	Avg Daily # of Trades	Avg \$ / Trade
Equities	\$50.0 T	5,700	10,000	35%	\$76.8 BN	9,800,000	\$8,000
Corporate Bonds	\$7.7 T	5,000	20,000	10%	\$19.2 BN	37,000	\$519,000
Municipal Bonds	\$3.7 T	46,000	1,100,000	51%	\$6.9 BN	38,000	\$161,000

Source: EMMA, SIFMA, Bloomberg, NYSE/NASDAQ, TRACE, GAO
 Note: Data reflects U.S. market only, bond data excludes money market activity

- Individual municipal bonds trade on average once every 27 days while an individual equity trades on average ~980 times per day
- Municipal bonds are not registered with the SEC: the SEC cannot directly enforce continuing disclosure practices of municipal entities

What is Considered Debt in California?

California's Constitutional Debt Limit

- Article XVI, section 18, provides in part: "No county, city, town, township, board of education, or school district, shall incur any indebtedness or liability in any manner or for any purpose exceeding in any year the income and revenue provided for such year, without the assent of two-thirds of the qualified electors thereof, voting at an election to be held for that purpose"
- In 2015 California municipalities issued \$57 billion in debt, 38% was voter approved

1

Leases

Dean v. Duchel
(1950)

City of Los Angeles v.
Offner
(1942)

2

Special Fund

San Francisco S. Co. v.
Contra Costa Co.
(1929).

City of Oxnard v. Dale
(1955)

3

Imposed by Law

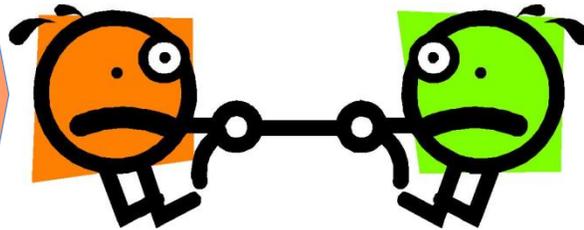
County of Los Angeles v.
Byram
(1951)

Lewis v. Widber
(1893)

During the 20th Century, Californians and the Courts Redefined Voter Approval

The People Fight Back

- Proposition 13
- Proposition 62
- Guardino decision
- Proposition 218
- Proposition 26
- Proposition 53?



New Approaches

- Mello-Roos
- Use of assessments
- Use of fees
- General tax

The Financial Crisis Changed the Municipal Debt Market Landscape

Casualties of the Financial Crisis

Variable Rate Debt

- Auction Rate Securities
- Synthetic Fixed Rate Debt

Receivership of Fannie Mae and Freddie Mac

Bond Insurers

- Insurance for debt service
- Surety Bonds

Consolidation/Elimination of Firms

- Bear Stearns bought by J.P. Morgan
- Bankruptcy of Lehman
- Sale of Merrill Lynch to Bank of America



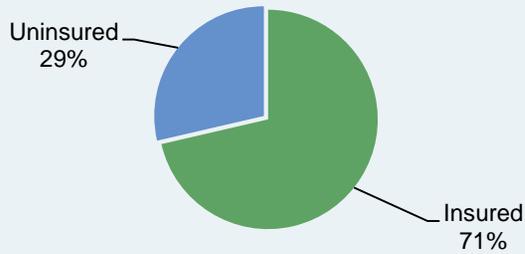
J.P.Morgan

Investor Alerts

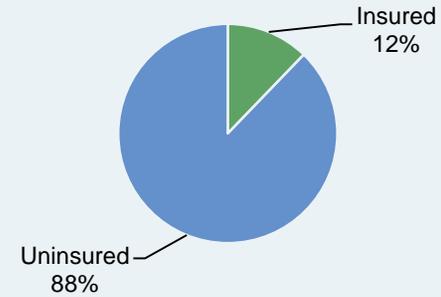
Auction Rate Securities: What Happens When Auctions Fail

California's Municipal Market Trends Before and After the Financial Crisis

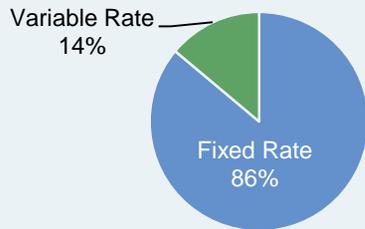
California 2006 Insured vs. Uninsured



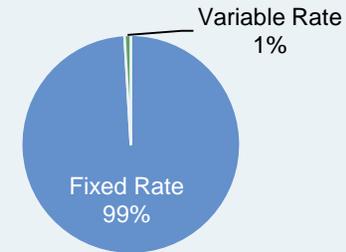
California 2015 Insured vs. Uninsured



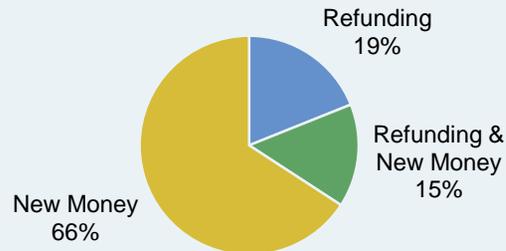
California 2006 Fixed vs. Variable Rate



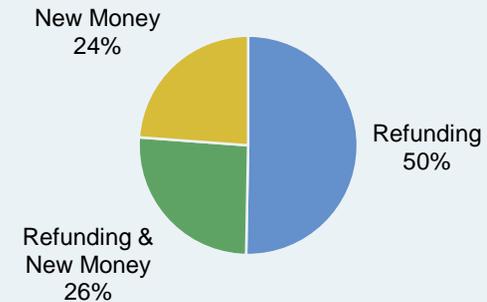
California 2015 Fixed vs. Variable Rate



California 2006 New Money vs. Refunding



California 2015 New Money vs. Refunding



Source: SDC as of October 6, 2016

Enforcement, Regulation, Disclosure

15c2-12	<ul style="list-style-type: none">■ Enacted in 1989 in response to WPPSS default■ Governed disclosure for municipal bonds by regulating underwriters
Amendment of 15c2-12	<ul style="list-style-type: none">■ Enacted in 1995 in response to Orange County bankruptcy■ Requires continuing disclosure
Pension	<ul style="list-style-type: none">■ SEC Enforcement Actions for inadequate pension disclosures■ City of San Diego (2006), States of New Jersey (2010), Illinois (2013), Kansas (2014)
Enforcement Actions	<ul style="list-style-type: none">■ Enforcement Division Unit created in 2010■ Dodd-Frank Act gave SEC new power to obtain fines in administrative (“cease and desist”) actions
MCDC	<ul style="list-style-type: none">■ Announced in March 2014 by SEC■ Focus on whether an offering document was materially accurate with respect to compliance with continuing disclosure undertakings

SEC MCDC Program

- SEC enforcement program aimed at public agencies which made material misstatements about their continuing disclosure compliance
- Program involves public agencies and underwriters self-reporting prior material misstatements
- Consent agreements with underwriters were issued in 2015
- Enforcement actions against municipal issuers announced in 2016; agreements with issuers are expected in 2016

SEC Charges 71 Municipal Issuers in Muni Bond Disclosure Initiative

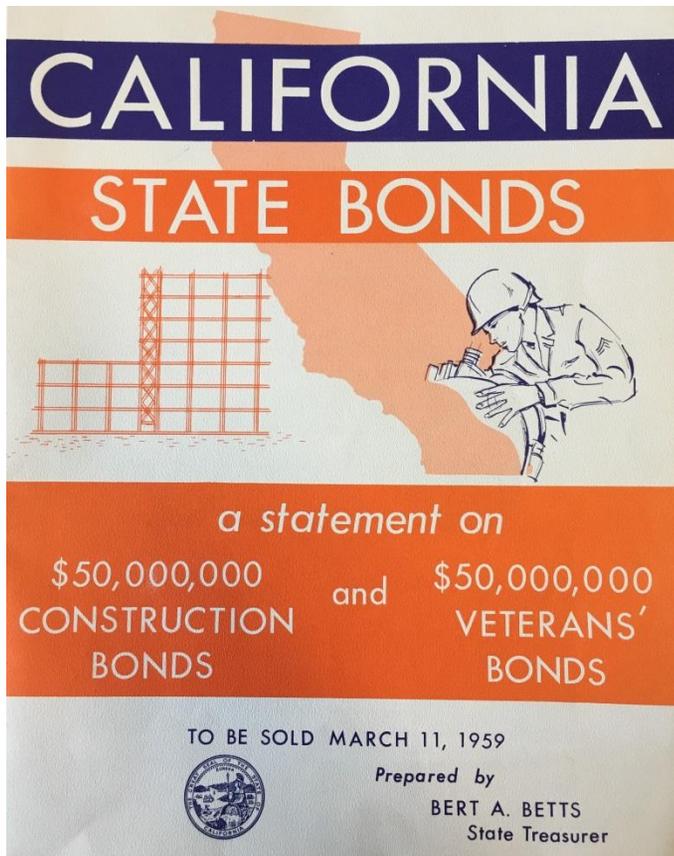
08/24/2016 11:00 AM EDT

The Securities and Exchange Commission today announced enforcement actions against 71 municipal issuers and other obligated persons for violations in municipal bond offerings.

An Illustration of the Changes in Disclosure Practices

California GO 1959

- 14 Total Pages
- 3 Pages Describing Current Budget
- Outstanding GO Debt of \$1.4 billion



California GO 2016

- 396 Total Pages
- 12 Pages Describing Current Budget
- Outstanding Debt of \$75.7 billion

