

# 2009-11 Governor's Budget

**Bond Issuance/Capital Construction**

Jack Kenny – January 30, 2009

# 2009-11 Governor's Budget

- Definitions, Legal Framework & Policy
- Recent Developments & Market Conditions
- 2009 Legislation and Governor's Recommended Budget

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- Issuing bonds is a form of borrowing
  - a bond is a certificate that represents a promise to repay investors who loan money.
- As a general rule, tax-exempt borrowing is for capital assets only
- State typically structures transactions to achieve “level debt service”
- Benefits of financing include:
  - inter-generational equity
  - Ability to take advantage of opportunities that might be missed under a strict pay-as-you-go approach
  - Take advantage of unique economic circumstances

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- Constitution prohibits State to be in debt for more than \$50,000 unless an exception has been made. Programs authorized by such exceptions are denoted by an “Article XI” prefix:
  
- Article XI-A                      Veterans’ farm and home loans
- Article XI- F (1)                Higher Education self-supporting
- Article XI- G                     Higher Education/Community College
- Article XI- H                     Pollution Control
- Article XI-I (2)                 Elderly & Disabled Housing
- Article XI-J                      Small Scale Energy Loan Program
- Article XI-L                      Oregon Opportunity Bonds (OHSU)
- Article XI-M/N                 Seismic Rehabilitation Schools/Emergency Services Buildings
- Article XI-O                      Pension Obligation Bonds

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## Revenue Bonds

### Department of Transportation

- Highway User Tax (OTIA)
- Transportation Infrastructure Fund

### Department of Administrative Services

- Lottery Revenue Bonds

### Housing and Community Services

- Single and Multi-family Housing Programs

### Department of Economic Development

- Economic Development Bond Bank

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## Appropriation Credits

- Department of Administrative Services
  - Certificates of Participation
  - Appropriation Bonds

## Conduit Revenue Bonds

- Economic and Community Development
- Housing and Community Services
- Oregon Facilities Authority

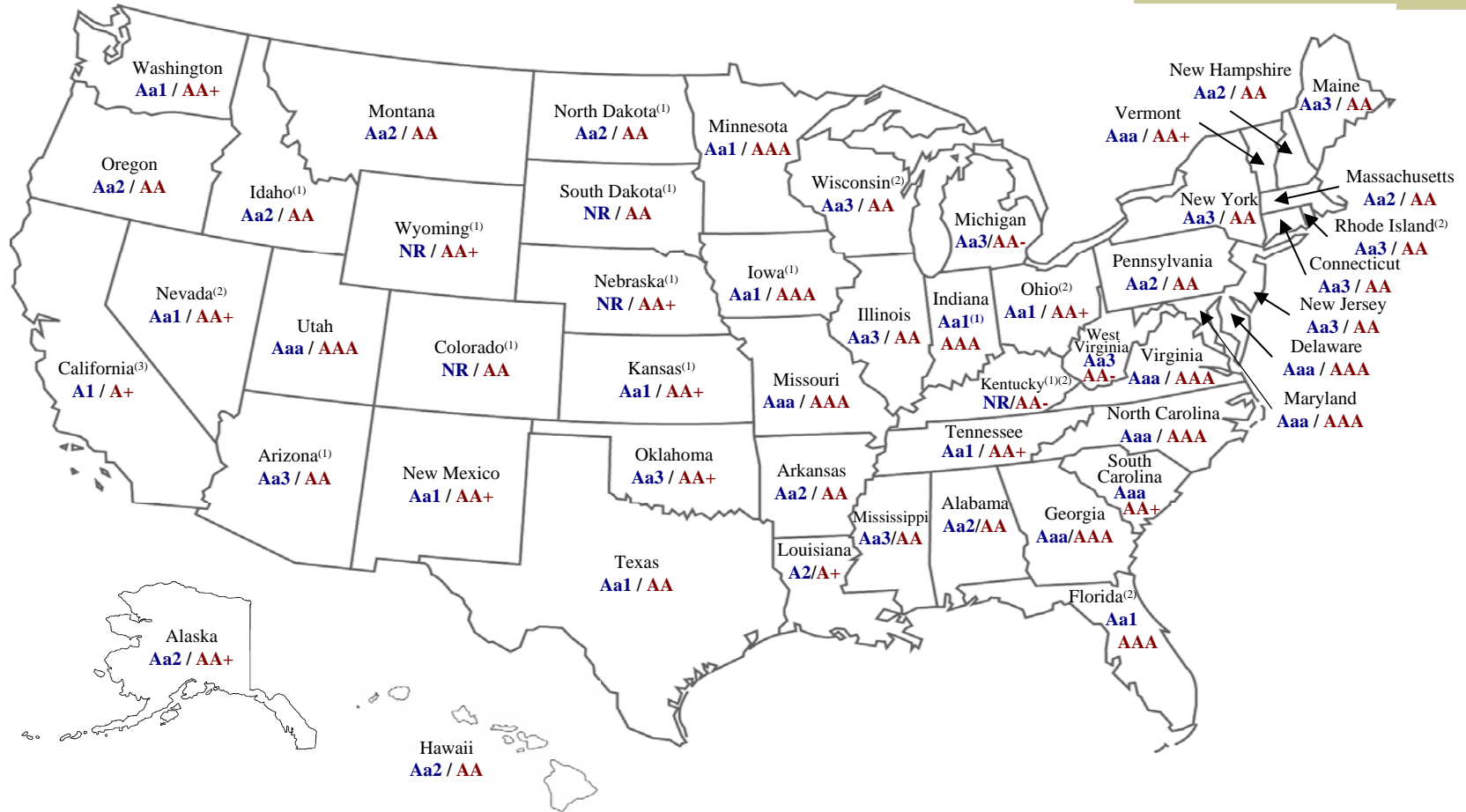
## Tax Anticipation Notes

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*Credit Ratings provide investors with an easily identifiable way to assess the degree of risk relative to a particular security.*

Current Credit Ratings			
	Standard & Poor's	Moody's	Fitch
General Obligation Bonds	AA	Aa2	AA
Highway Revenue Bonds	AAA	Aa2	AA
Lottery Bonds	AAA	Aa3	A+
Certificates of Participation	AA-	Aa3	AA-
Housing Revenue Bonds		Aa2 Single Fam. AAA – Multi-fam	
ECD Infrastructure Bonds	AA	Aa3	AA

# Current State General Obligation Bond Ratings

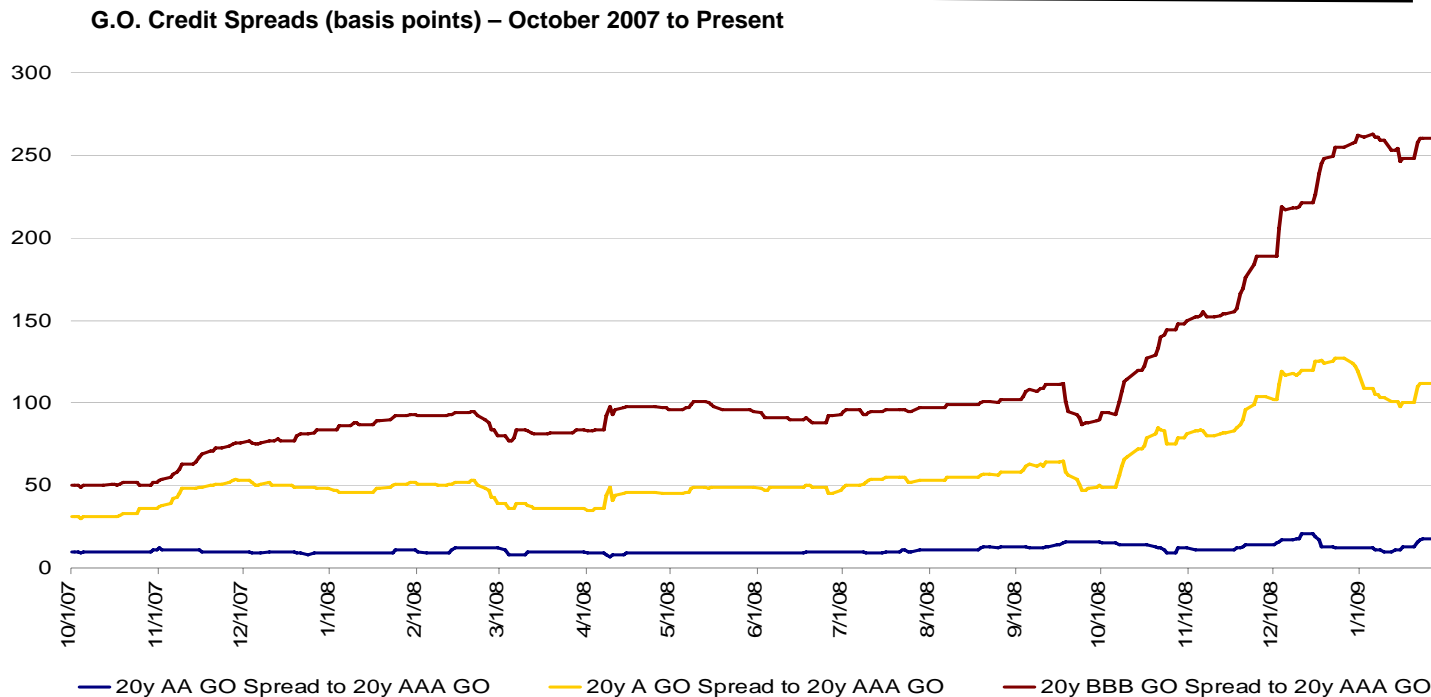


**Moody's Rating / Standard & Poor's Rating**

- (1) Issuer Rating: No General Obligation Debt
- (2) States on Moody's Negative Outlook list: Florida, Kentucky, Nevada, Ohio, Rhode Island, Wisconsin
- (3) Moody's Negative Watch: California

# Credit Spreads Have Widened – A Two Tiered Market

- Municipal issuance is now segmented into the “haves,” “AA” rated and better, and the “have nots,” “A” and below
- The interest rate spreads between “AA” and “AAA” credits as measured by MMD, a General Obligation municipal market index, has remained stable
- However, the interest rate spreads between “BBB” and “A” MMD relative to “AAA” MMD have increased significantly since the credit crisis began



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## Controls on Bond Programs

- State Constitution/Statutes Specific to Programs
- Constitutional and Statutory Limitations on Amounts Outstanding
- Bond Bill(s) limit amount that can be issued in any biennium
- Programs may have limitations based on agreements with bondholders
  - e.g. 4X coverage test in Lottery Bond Program*
- State Treasurer (and financial markets) can limit individual sales
- Internal Revenue Code

# Unprecedented Market Environment for Issuers and Investors

## Reopening of Municipal Market

- Market access for liquid high quality names
- Demand strongest for AA and AAA credits, limited access for A-minus or lower-rated credits
- Market recovery driven by individual retail investor and investment advisor demand, with limited participation from mutual funds
- Property & Casualty company, hedge-fund and total-return investor demand remains weak
- Deal sizes mostly below \$400 million

## Supply

- 2008 new issuance was \$387 billion, down 8.8% from 2007
  - VRDB new issuance at record \$115 billion, up 132%
- Tender option bond funds de-leverage
- Unwind of AIG's municipal portfolios over next two years brings further market uncertainty
- Limited market demand in Q4 2008 has pushed supply into Q1 2009

## Credit

- With demise of bond insurance, investors focused on credit
- Increased trading differentials within ratings categories
- Remaining bank letter of credit and liquidity capacity limited
- Uninsured supply is straining buy-side credit analysis capacity
- Market no longer commoditized; all about credit

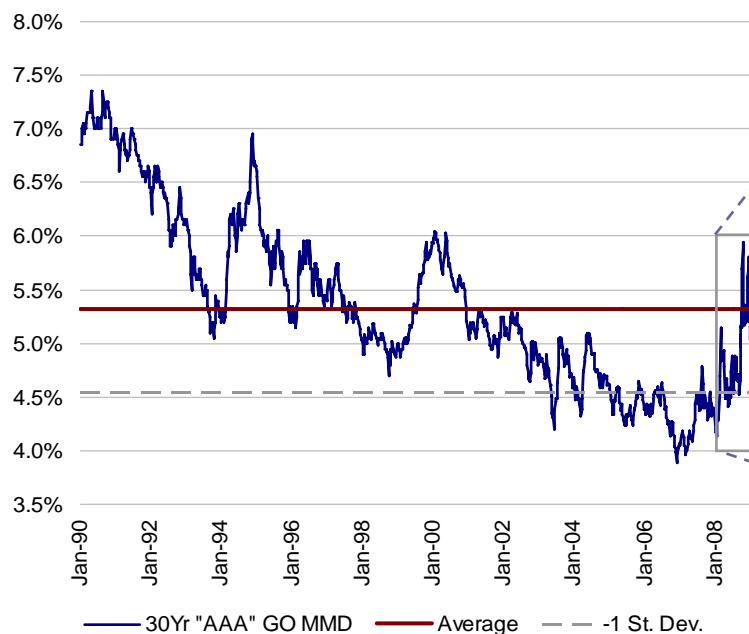
# Ongoing Credit Crisis – Downgrades of the Bond Insurers

MUNICIPAL BOND INSURERS Current Rating Status (1/05/09)			
	Moody's	Standard & Poor's	Fitch
<b>Ambac</b>	Downgraded 11/05/08 to <b>Baa1</b> . Outlook revised to developing.	Downgraded 11/19/08 to <b>A</b> . Outlook remains negative.	Rating withdrawn 6/26/08 6/18/08: <i>Ambac has requested immediate ratings withdrawal</i>
<b>Assured Guaranty</b>	Downgraded 11/21/08 to <b>Aa2</b> . Outlook revised to Stable.	<b>AAA</b> . Stable Outlook	<b>AAA</b> . Stable Outlook
<b>CIFG</b>	Downgraded 10/28/08 to <b>B3</b> . Under review with direction uncertain.	Downgraded 8/22/08 to <b>B</b> . Placed on CreditWatch Developing.	Rating withdrawn 10/21/08.
<b>FGIC</b>	Downgraded 12/19/08 to <b>Caa1</b> . Outlook revised to Negative.	Downgraded 11/24/08 to <b>CCC</b> . Outlook revised to Negative.	Rating withdrawn 11/24/08
<b>FSA</b>	Downgraded 11/21/08 to <b>Aa3</b> . Outlook revised to developing.	<b>AAA</b> . Revised to CreditWatch Negative 10/08/08.	<b>AAA</b> . Revised to Rating Watch Negative on 10/09/08.
<b>MBIA</b>	Downgraded 11/07/08 to <b>Baa1</b> . Outlook revised to developing.	<b>AA</b> . Outlook revised to negative on 8/14/08.	Rating withdrawn 6/26/08 3/7/08: <i>MBIA has requested immediate ratings withdrawal</i>
<b>Syncora Guarantee (previously known as XL Capital)</b>	Downgraded 10/24/08 to <b>Caa1</b> . Placed under review with direction uncertain.	Downgraded 11/18/08 to <b>B</b> . Placed on CreditWatch Developing.	Rating withdrawn 9/05/08 9/03/08: <i>Syncora has requested immediate ratings withdrawal</i>
<b>BHAC</b>	Assigned <b>Aaa</b> on 4/25/08. Stable outlook	Assigned <b>AAA</b> on 4/11/08. Stable outlook.	NR
<b>Radian Asset</b>	<b>A3</b> . Placed Under Review for possible downgrade on 10/10/08.	Downgraded 8/26/08 to <b>BBB+</b> . Outlook changed to Negative.	Rating withdrawn 5/02/08.
<b>ACA</b>	NR	Rating Withdrawn 12/15/08	NR

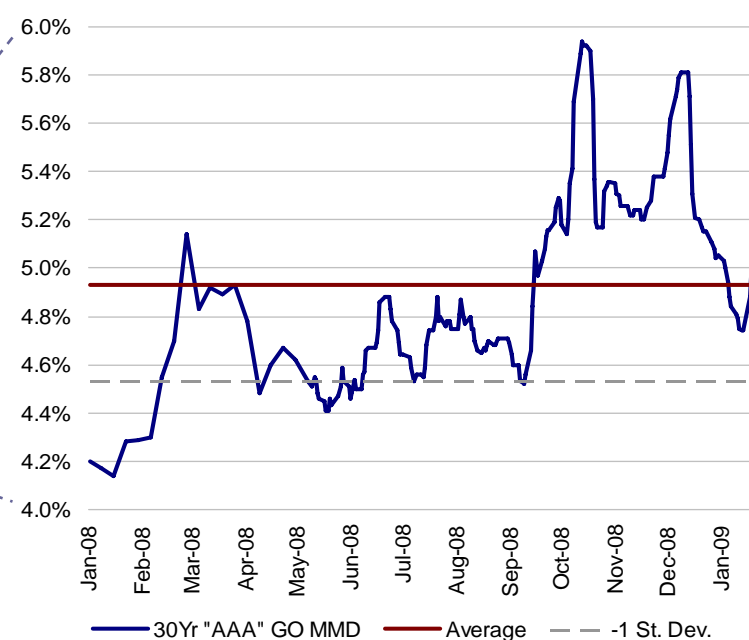
# History of 30-Year AAA MMD

- Following a significant rise in MMD in October 2008 and then again in December, tax-exempt rates have fallen significantly
- The municipal market is now much more receptive to the successful sale of municipal bonds, particularly higher rated credits

30-Year AAA MMD Since 1990



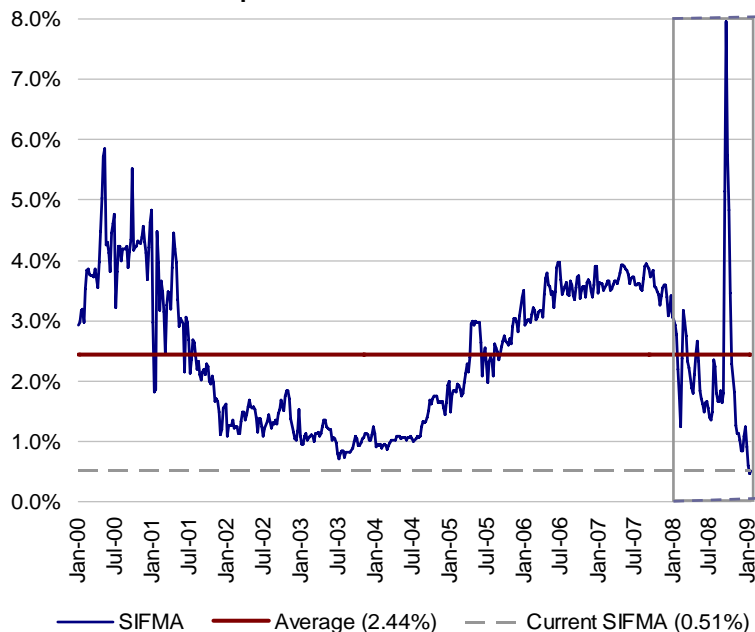
30-Year AAA MMD Since 2008



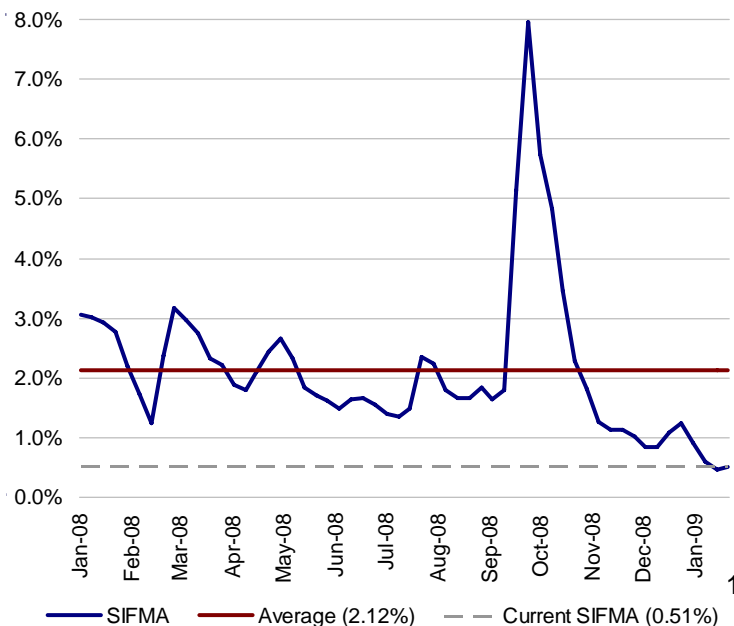
# Variable Rate Bonds Continue to Be Attractive If Strong Credit Support is Available

- Variable rate bonds are currently a source of low-cost funding if highly rated credit facilities are available
  - The average national tax exempt variable rate index (“SIFMA”) was 2.12% for 2008
  - However, credit-worthy letters of credit and liquidity facilities are scarce and cost much more than in the past
- Last year, many issuers were “caught” with remarketing failures and high variable rates based on the poor credit quality of their credit banks
- During September 2008, a lack of liquidity resulted in a significant spike in variable rates with SIFMA increasing to roughly 8% for virtually all issuers, regardless of credit quality

**Historical Tax-Exempt Variable Rates Since 1990**



**Historical Tax-Exempt Variable Rates Since 2008**



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## 2009 Legislation

- SB 5505 – “The Bond Bill”
- SB 5506 – Capital Construction Authorization
- HB 5018 – Higher Education / Community College Capital Construction Authorization
- SB 5535 Lottery Bond Project Authorization
- HB 2120 Jobs and Transportation Act of 2009

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## Highlights of Governor's Capital Construction and Project Initiatives

- \$1 billion in Higher Ed/Community College Construction Projects
- \$279 million - State Hospital Replacement Project
- \$133 million - Junction City Prison
- \$240 million - Wireless Interoperability Network
- \$44 million - Military Armories & Emergency Preparedness
- \$30 million - Seismic Upgrades at Schools/Emergency Services Buildings
- \$150 million - Connect Oregon III – Multi-Modal Transportation
- \$35 million - Amtrak Cascades Train
- \$19 million – Affordable Housing Preservation
- \$ 9 million – OECDD Infrastructure Bond Bank
- \$ 2 million – Water Project (Umatilla Basin Aquifer)

# 2009-11 Governor's Budget

## Expected Commitments Beyond 2009-11

- State Hospital Replacement
- Junction City Prison
- Wireless Interoperability Network
- Measure 57 Construction
- Coos Bay Channel Deepening
- Other Building Needs