

Maryland Leads Municipal Bond Auctions as Yield Spreads Widen

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By Jeremy R. Cooke

Jan. 30 (Bloomberg) -- Maryland plans to sell \$250 million of revenue bonds to fund state transportation projects in today's largest competitive offering of U.S. municipal debt.

Maryland's Department of Transportation will take bids from investment banks for debt due from 2011 through 2023, rated AAA by Standard & Poor's and Aa2 by Moody's Investors Service. State and local governments have sold or plan to sell \$3.3 billion of bonds this week, roughly half last year's average, based on data compiled by Bloomberg.

Even as higher-rated borrowers dominate new issues, investors are demanding yields of 5 percent or more on some existing tax-exempt bonds with lower ratings and with the backing of insurers seen as more at risk. For some buyers, the higher yields are enticing in a market where defaults are low.

"Our retail here sees the volatility that's going on in our market as an opportunity to buy attractively priced bonds," said Jenny Stark, manager of underwriting and sales at Janney Montgomery Scott LLC in Philadelphia. Even with insurers' woes, "you get a GO name and the taxing power is going to bail it out before you ever need the insurance companies."

Yields on top-rated general obligation bonds due in 30 years rose 5 basis points, or 0.05 percentage point, to 4.29 percent yesterday, the highest in almost four weeks, according to Municipal Market Advisors.

Philadelphia city bonds maturing in 23 years and backed by CIFG Assurance North America Inc. yesterday traded dozens of times at prices ranging from 99 to 102 cents on the dollar.

Spreads Double

Customers got yields as high as 5.04 percent, or 76 basis points more than the AAA uninsured scale. The spread at issue in July 2006 was 1 basis point.

Philadelphia is rated Baa1 by Moody's and BBB by S&P, both of which have also negative outlooks on CIFG's AAA grades.

The average yield spread between tax-exempt securities at the lowest- and highest-rated investment grades have more than doubled in the past six months to about 160 basis points,

according to indexes from Merrill Lynch & Co.

While buy-and-hold investors might find solace in municipal bonds' relatively low default rate, buyers more focused on fluctuating market values are questioning the wisdom of judging their attractiveness by traditional measures of relative value, such as the ratio to Treasury yields.

"Are they cheap or are they a 'value trap'?" Bennet Sedacca, president of money manager Atlantic Advisors LLC in Winter Park, Florida, said in a Jan. 28 report. "Value traps are known for looking cheap, only to get cheaper."

Yield Ratios

Ten-year municipal yields tracked by independent research firm Municipal Market Advisors represent about 93 percent of the 10-year Treasury note. During the past three years, the ratio has averaged 85 percent; in the past three months, 91 percent.

Treasuries gained 2.7 percent this month as investors sought a heaven from credit-market losses in the safest government-backed debt and anticipated more interest-rate cuts by the Federal Reserve, according to Merrill's total-return indexes. Municipal bonds gained 1.6 percent through yesterday.

Fed policy makers will probably cut their benchmark rate for overnight lending between banks by 50 basis points to 3 percent at their meeting today, based on the median forecast of economists polled by Bloomberg. They cut the federal funds rate by 75 basis points last week, acting between regularly scheduled meetings for the first time since 2001, as they look to boost economic growth amid fears of a recession.

In new municipal issues today, Maryland is offering consolidated transportation bonds that are backed by motor-fuel and vehicle taxes, federal aid, and airport and transit revenue.

The San Francisco Airport Commission, which planned to sell as much as \$300 million of fixed-rate bonds as soon as today, placed its deal on the day-to-day calendar, while underwriters led by Citigroup Inc. monitor market conditions.

The proposed refinancing, hurt by rising yields, would feature underlying ratings of A1 from Moody's and A from S&P as well as AAA insurance from Assured Guaranty Corp., one of two bond insurers to maintain stable outlooks on its top grades. Financial Security Assurance Inc. is the other.

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