

# MONTHLY REVIEW

February 2013

**MAINLINE WEST**

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M U N I C I P A L   S E C U R I T I E S   •   O P P O R T U N I T Y   F U N D S  
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## MUNICIPAL MARKET REVIEW

The Municipal market is working on finding its "balance". Scales continue to tip back and forth from good to bad due to the following:

- Yield levels are low, with duration risk high, yet, given new tax rates, value versus other fixed income classes is good.
- Potential legislation risk is low, but could be very damaging to the value of municipal bonds.
- Supply & demand prospect in the long-run are very bullish, yet bearish in the short-run due to seasonal effect.

What is an investor to do? Municipal bonds have started out 2013 with very little changes in yields and the market has been quiet. More specifically from January 31, 2013 to February 28, 2013:

- 10 year muni rates decreased 1 bp, underperforming the Libor market which decreased 4 bps.
- 25 year muni rates decreased 4 bps, underperforming the Libor market which decreased 5 bps.

Is this the calm before the storm?

## INVESTMENT STRATEGY REVIEW

MainLine's 2013 Outlook (published last month) highlighted that investors need to be prepared to take advantage of market sell offs to execute their investment strategy during 2013. We feel one of these opportunities is about to occur. There are three things working in a buyers favor over the next 30 to 45 days that we feel will create some value opportunities. More specifically:

1. Seasonal supply and demand factors highlighted in our attached analysis: ***"When to buy and when to sell – The Seasonal Effect on the Municipal Market"***.
2. Budget/sequestration talks could create concerns for municipal bond tax benefits, federal aid cuts and the impact on municipal credit quality.
3. Long-term municipal yields have declined to 30 to 45 bps over the last year. Yield levels are near all time lows, while long-term taxable yields are a bit higher to unchanged. There seems to be a lot of resistance for municipal investors to accept lower yields, going forward.

Please feel free to call us to discuss your cash availability and to review your investment strategy. This can allow us to be prepared for when the right deal is priced at the right value, and we can get your cash put to work.

**SPECIALISTS IN MUNICIPAL BOND INVESTMENTS**



MUNI ADVISORY

**Municipal Bonds - When to buy and When to sell – The Seasonal Effect on the Municipal Market:**

**Introduction:**

This is an update to an analysis first done in 2009, where we used data from 2000 to 2009. The new analysis is for data from 2008 to 2012. We wanted to update the analysis to see if there has been a change in the seasonal effects on the municipal market.

**Background:**

The municipal market is a vehicle used to finance the needs of the public (supply). An investor in muni bonds does so to realize tax-exempt income (demand). This creates a supply that is necessary, countered by a demand that can be controlled.

Supply in this analysis is represented by the issuance of municipal bonds. Municipal issuers sell bonds to fund long-term public projects that are needed and approved by its citizens. The need to finance these projects is not so much market driven (cost versus reward), but is more so for the importance of the services that the project provides. The residents have determined the service is needed and, therefore, the quicker it is provided, the better. Most municipalities' fiscal years begin and end in June/July and/or December/January. This is when most new bond issues are approved and underwritten.

Demand in this analysis is represented by bond maturities and bond refunding payments received by investors. This creates a "natural demand", as long-term municipal investor will have proceeds from these sources to purchase new bonds.

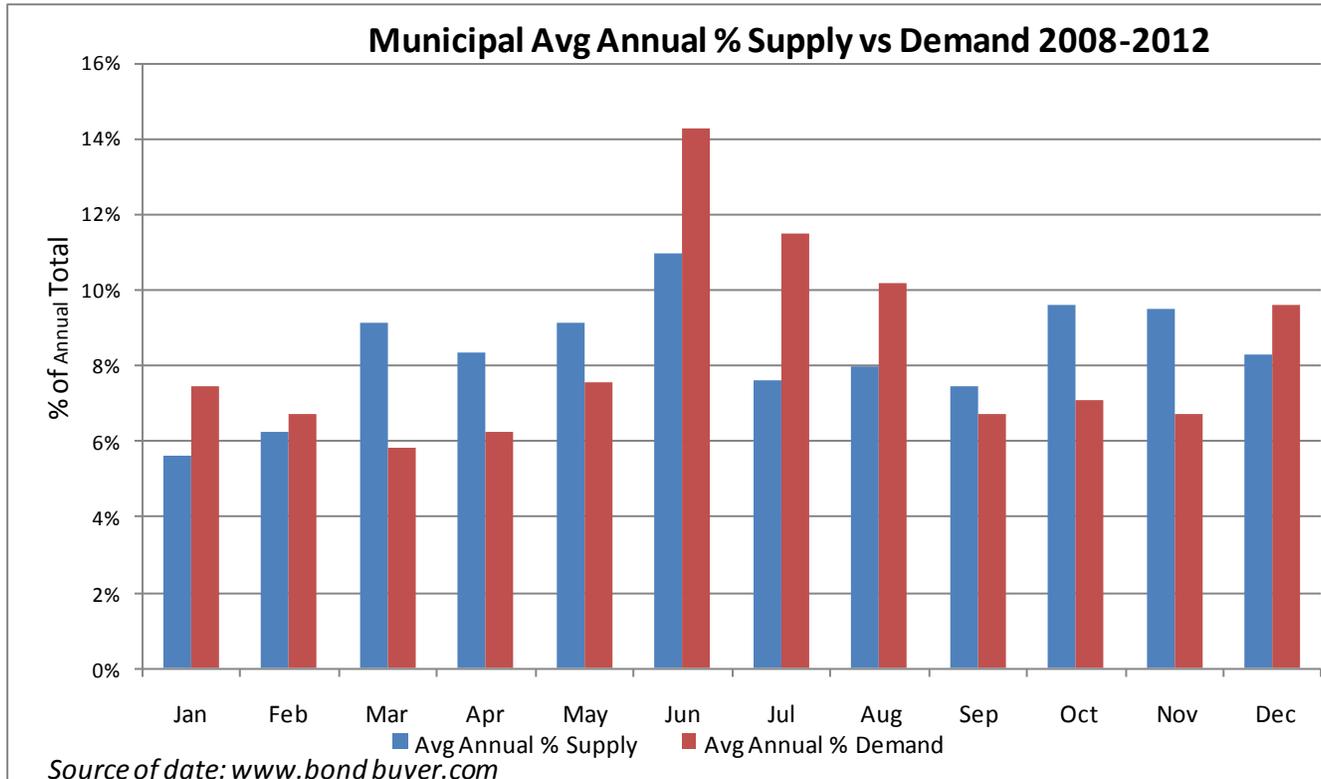
**Supply & Demand Analysis:**

To see what type of seasonal patterns exist with municipal bonds, MainLine analyzed municipal bond issuance (supply) and bond maturities and refunding (demand) from 2008 to 2012 to look at the seasonal patterns of each. Monthly numbers for both sets of data are divided by that year's total to give a monthly percent. For example:

- Roughly 14.3% of annual demand is found in the month of June, while 10.9% of annual municipal issuance is underwritten in June.

*Please see chart on next page...*

## MUNI ADVISORY (CONTINUED)



Let's summarize the data a bit more:

When to Sell	
% Demand in Peak 5 mos of Yr (*)	53%
% of Supply in Same 5 mos of Yr (*)	41%
<b>Difference</b>	<b>12%</b>
(*) Months of Jan, Jul, Aug & Dec	

When to Buy	
% in Demand in Low 5 mos of Yr (*)	32%
% of Supply in Same 5 mos of Yr (*)	41%
<b>Difference</b>	<b>-9%</b>
(*) Months of Feb, Mar, Apr, Sep & Nov	

### Conclusion:

This analysis shows a disparity between supply and demand on a seasonal basis, which can create market opportunities for the patient investor. More specifically:

- June-August, and December, January, demand far outpaces supply (53% versus 41% of annual volumes). This would tend to be a good market to sell bonds as, on average, there is \$27 billion of additional demand (cash) in the market.
- March-May, and October and November, supply outweighs demand (41% versus 32% of annual volumes). This would tend to be a good market to buy bonds as supply outstrips natural demand by over \$45 billion.

## MUNI ADVISORY (CONTINUED)

- The results of 2008-2012 compare almost perfectly to the 2000-2009 analysis. Results from the 2000-2009 analysis were as follows:

When to Sell		When to Buy	
% Demand in Peak 5 mos of Yr (*)	54%	% in Demand in Low 5 mos of Yr (*)	32%
% of Supply in Same 5 mos of Yr (*)	41%	% of Supply in Same 5 mos of Yr (*)	40%
<b>Difference</b>	<b>13%</b>	<b>Difference</b>	<b>-8%</b>
(*) Months of Jan, Jul, Aug & Dec		(*) Months of Feb, Mar, Apr, Sep & Nov	

A patient municipal investor looks to maximize tax-exempt income and, therefore, can be more selective on what bonds are bought and when they buy the bonds. MainLine is not an advocate for timing the market and there are many other variables that can influence decisions to sell or buy bonds. One factor we feel should help with this decision is the long-term proven seasonal demand and supply factors discussed in this analysis. This is a structural anomaly of the market and does not look like it will change anytime in the near future. Picking the right time to buy or sell a bond can provide an investor with a savings that will last the life of the bond through increased buying yield, or higher selling proceeds.

# MONTHLY REVIEW: YIELD & RATE CHANGES

February 2013

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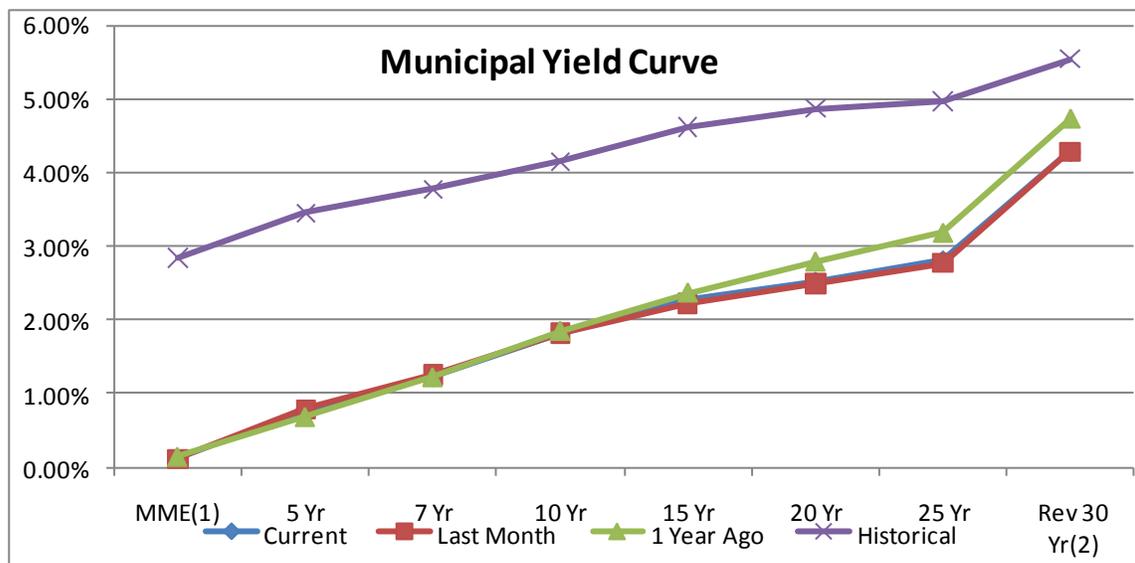
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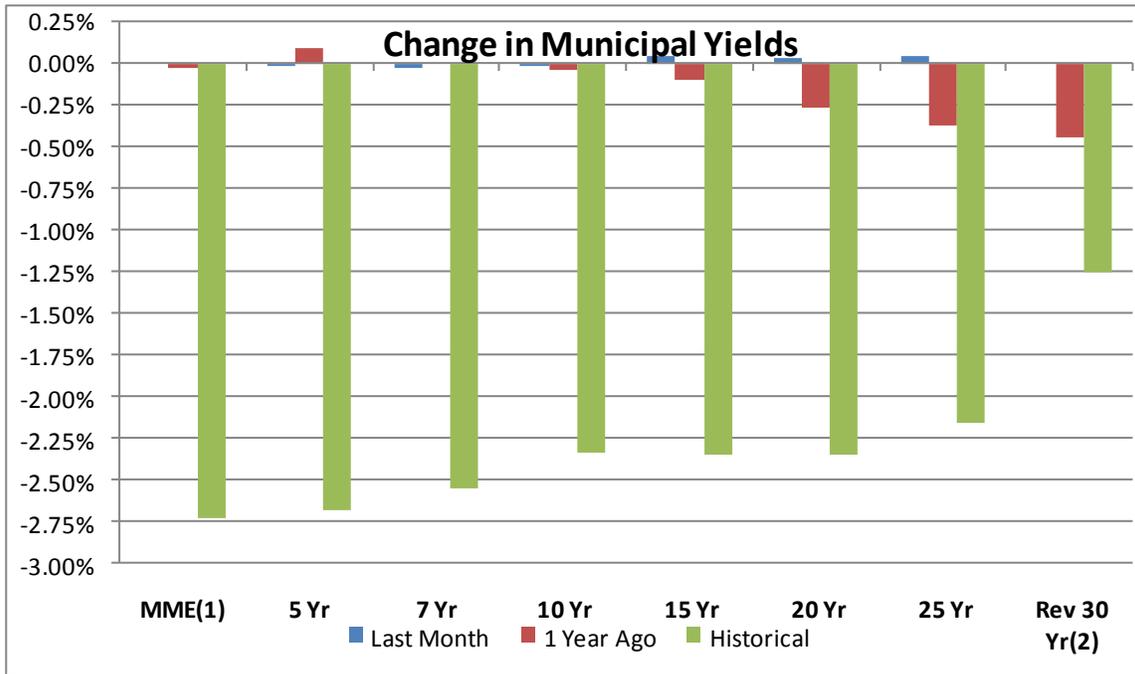
## TAX EXEMPT & TAXABLE YIELD / RATE LEVELS: 2/28/2013

	AAA Rated Municipal Yields				Libor Swap Market Rates			
		Last		Historical		Last		Historical
	Current	Month	1 Year Ago	Avg(3)	Current	Month	1 Year Ago	Avg(3)
MME(1)	0.11%	0.11%	0.14%	2.84%	0.28%	0.30%	0.30%	3.44%
5 Yr	0.77%	0.79%	0.68%	3.45%	0.91%	1.03%	1.11%	4.87%
7 Yr	1.22%	1.25%	1.22%	3.77%	1.39%	1.51%	1.63%	5.16%
10 Yr	1.81%	1.82%	1.85%	4.15%	1.95%	2.06%	2.06%	5.28%
15 Yr	2.27%	2.22%	2.37%	4.62%	2.50%	2.60%	2.54%	5.43%
20 Yr	2.52%	2.49%	2.79%	4.87%	2.75%	2.83%	2.65%	5.53%
25 Yr	2.81%	2.77%	3.18%	4.97%	2.86%	2.94%	2.73%	5.55%
Rev 30 Yr(2)	4.29%	4.29%	4.73%	5.54%	2.92%	3.01%	2.79%	5.58%

- (1) MME = Money Market Equivalent: Tax Exempt = 7 day VRDN Rate, Taxable = 1 Month US Libor Rate.
- (2) = Bond Buyer revenue bond index (BBWK25RV). This index mirrors MainLine West's maximum yield strategy. Index represents the yield on 30 year maturing A1 essential service revenue bonds. Index is priced weekly on Thursdays.
- (3) Data from May 1994.



## CHANGE IN RATES: 2/28/2013



# MAINLINE WEST

MUNICIPAL SECURITIES

OPPORTUNITY FUNDS

RATIO MUNICIPAL / LABOR RATES: 2/28/2013

	AAA Rated Municipal Yields			
	Current	Last Month	1 Year Ago	Historical Avg(3)
MME (1)	38.73%	36.67%	47.46%	82.56%
5 Yr	84.62%	76.70%	61.26%	70.84%
7 Yr	87.77%	82.78%	74.85%	73.06%
10 Yr	92.82%	88.35%	89.81%	78.60%
15 Yr	90.80%	85.38%	93.31%	85.08%
20 Yr	91.64%	87.99%	105.28%	88.07%
25 Yr	98.25%	94.22%	116.48%	89.55%
Rev 30 Yr(2)	146.92%	142.52%	169.53%	99.28%

