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## We are Seeing Cracks in the U.S. State Sector and an Unprecedented Multi-Year Run of Credit Deterioration by Some Local Governments

- The Janney outlook for state credit remains “Stable” although some indicators are mixed. Ratings are still high but, we expect slow growth to hinder economic expansion and believe more downgrades are lurking for a select few.
- Some states were upgraded recently but others were downgraded, some for reasons that are not easily repairable. Mostly structural and not cyclical factors are eating away at the credit quality of states such as IL, NJ and PA.
- U.S. state government tax revenues (YoY) were reported lower in 1Q14 and are expected to be lower again in 2Q14. Uneven collections due to the fiscal cliff are partly to blame but this data is something to watch going forward.
- A Short Tale of Three States: California’s fiscal metrics have improved, leading to rating upgrades and spread narrowing. Illinois’ pension burden makes fiscal improvement a challenge, with wide spreads continuing. New Jersey’s relatively tight trading spreads belie its lagging economic recovery and growing debt and pension liabilities.
- The Janney Local Government sector outlook is still “Cautious”. Ratings in this sector are also generally high but, some locals are still dealing with structurally imbalanced budgets, lower reserve funds or both.
- Credit conditions for local governments have not improved sector-wide. There are some laggards.
- Downgrades have continued to outpace upgrades (and have for 22 straight quarters- an unprecedented multi-year run of credit deterioration) in the public finance sector, per Moody’s data.
- Our analysis shows over 50% of the local governments downgraded by Moody’s in 2Q14 suffer from structurally imbalanced budgets. This is not an easy situation to recover from and the condition will lead to more downgrades.

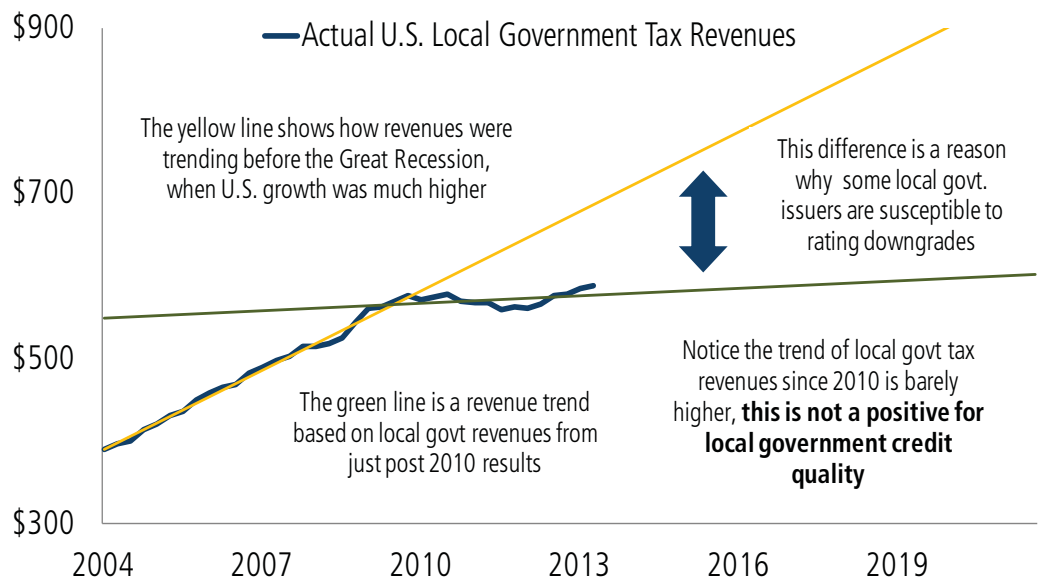
**TOM KOZLIK**  
Municipal Credit Analyst  
215.665.4422  
tkozlik@janney.com

**ALAN SCHANKEL**  
Managing Director  
215.665.6088  
aschankel@janney.com

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### Overspending, Multi-Year Structural Imbalances Lead to Persistent Downgrades



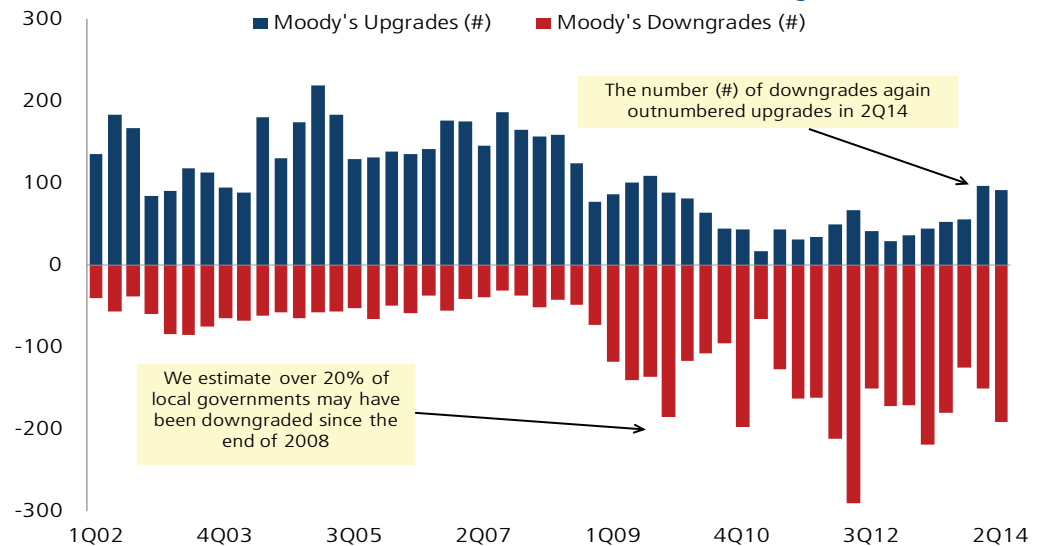
Source: U.S. Census Bureau and Janney FIS. \$ in billions.

Rising fixed costs such as pensions are creating problems for some local governments.

But, downgrades are generally occurring because all spending is outpacing revenues.

We do not see the upgrade to downgrade ratio reversing itself anytime soon.

## We Estimate Over 20% of Local Governments Have Been Downgraded



Source: Moody's and Janney FIS.

- There have been 1,900 tax backed Moody's downgrades since 2008. That amounts to about 22% of the 8,300 local government Moody's rated universe.
- We do not see the upgrade to downgrade ratio reversing itself anytime soon.
- We reiterate our recommendation that credit selection is very important and investors consider only high quality municipal bonds, especially in the local government sector.
- New Jersey was downgraded by S&P and Fitch; and Los Angeles' outlook upped by S&P.

## MUNICIPAL SECTOR CREDIT OUTLOOKS

### Trends to Watch

We conveyed the idea that although credit quality is currently high in the municipal bond market, negative credit factors have caused it to decline in recent years in our August 27, 2014 Janney Municipal Bond Market Monthly. There are some important trends negatively stressing the municipal

### Janney Municipal Sector Credit Outlook and Review

Sector	Janney Credit Outlook	Last Month Change	Barclay's 12 Month Return	Key Sector Trends	Recent Janney Sector Review
Municipal Bond Index	-	-	10.14%	Barclay's Muni Index, 46k issues	-
State Government	Stable	Same	8.76%	Tax revs are falling, Structural imbalances IL, PA, NJ	Sept 2014 MBMM
Local Government	Cautious	Same	9.95%	Downgrades outpace upgrades, structural imbalances	Sept 2014 MBMM
School Districts	Cautious	Same	-	Credit deterioration will continue, budgets squeezed	Sept 2014 MBMM
Airports	Stable	Same	12.04%	Sector stabilizing, consolidations largely finished	May 2014 Note
Health Care	Cautious	Same	13.38%	Reimbursement uncertainty, margins pressured	Feb 2014 MBMM
Higher Education	Cautious	Same	10.72%	Slow rev growth, lower support, spending pressures	Feb 2014 MBMM
Housing	Stable	Same	9.58%	Benefits for HFAs from higher rates, if & when	Feb 2014 MBMM
Public Power (Elec.)	Stable	Same	8.88%	Essential purpose nature enhances stability	Feb 2014 MBMM
Tobacco	Cautious	Same	N/A	More downgrades, consumption dropping	May 2014 MBMM
Toll Facilities	Cautious	Same	12.04%	Demand shifting & activity still near 2004 levels	Feb 2014 MBMM
Water and Sewer	Stable	Same	11.14%	Essentiality factor, system upgrades looming	Feb 2014 MBMM

Source: Barclay's Capital as of September 3rd and Janney FIS.

The Janney outlook for state credit remains "Stable" although some indicators are mixed.

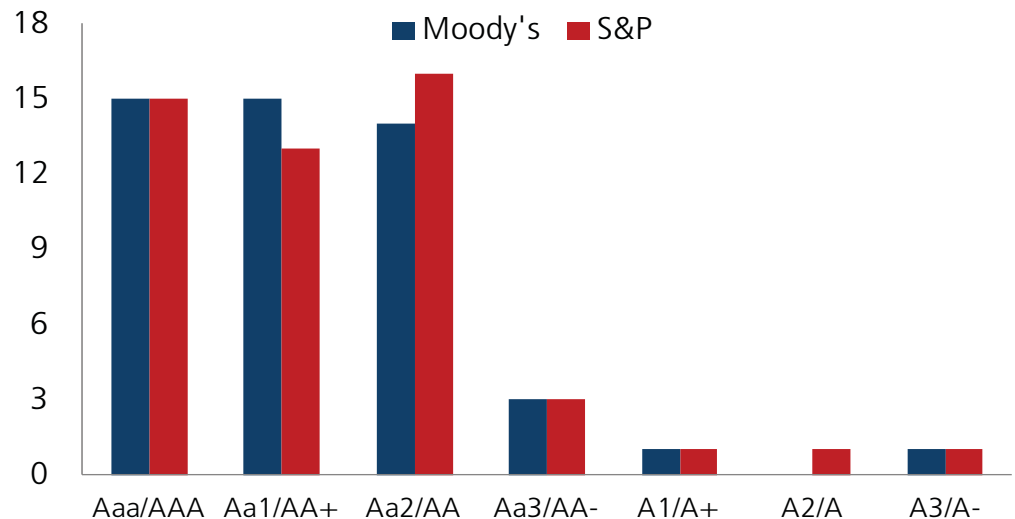
bond sector. Municipal bond investors should be paying attention to these- we expect the stresses to continue despite broader optimism and lack of understanding of current credit conditions. There are "cracks" in the state sector, which are concentrated in a few states, especially Illinois, New Jersey, and even Pennsylvania although to a somewhat lesser degree in the Keystone State. Local governments are being hit hard by downgrades from Moody's, and rightfully so. We have calculated that over 50% of the downgrades in 2Q14 were a result of structurally imbalanced budgets. In this new monthly installment we: update our U.S. State Government sector outlook (Stable), bring investors up to date on the condition of CA, IL and NJ specifically, and renew the factors that cause us to keep a "Cautious" outlook on the Local Government sector. **Tom Kozlik**

## U.S. STATE GOVERNMENT CREDIT UPDATE

### Janney Credit Outlook for U.S. State Government Sector Remains "Stable"

Evolving credit conditions will make budget decisions more difficult for states, and these decisions are likely to further affect issuers in other sectors. States still have many levers at their disposal and possess the sovereign ability to raise revenues and generally cut spending as necessary. For the most part state government credit quality remains in the higher rated categories according to Moody's and S&P, with only a select few experiencing a downward trend, for now. Therefore, we still believe the U.S. State Government Sector deserves a "Stable" credit outlook. However, there are some "cracks" starting to form in the state sector credit quality foundation.

#### U.S. State Ratings Distribution- Mostly in the Higher Categories



Source: Moody's, S&P and Janney FIS.

Some states were upgraded recently but others were downgraded, some for reasons that are not easily repairable.

Mostly structural and not cyclical factors are eating away at the credit quality of states such as IL, NJ and PA.

There was important data released for the state government sector at the end of August. State government tax revenues fell 0.3% in 1Q14 after four years of choppy, but positive, growth, as reported by the Rockefeller Institute. Preliminary data for 2Q14 does not look promising either. Rockefeller sees a 0.8% decline there as well. There is often an uneven relationship between state tax revenues and G.D.P. growth. Falling state revenues do not necessarily mean that the U.S. economy is slowing. In fact, for several quarters the Rockefeller Institute has been warning that declines in recent quarters could very well be attributed to, at least partially, "to the disappearance of the temporary shifts in income tax collection driven by the fiscal cliff." That being said, while the post-recession time period has had its share of ups for some states, others are still facing a mountain of a climb.

#### There Has Been Some Positive State Government Rating Actions Recently

Some favorable momentum has resulted in positive movement for several state credits. Also, we highlight some credit positive insights and drivers as related to the state of California below.

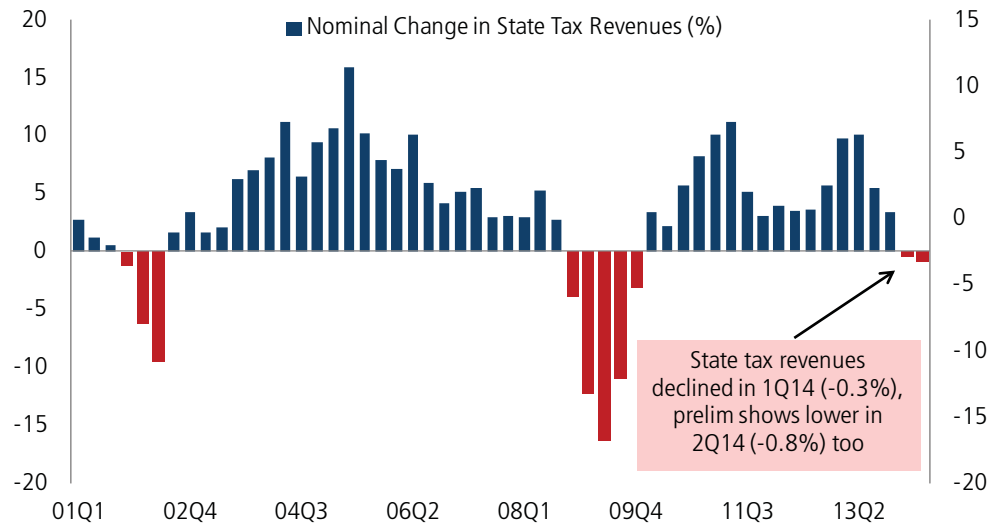
- Recently South Dakota's (Aa2/AA+/AA) outlook was raised to "Positive" from "Stable" by S&P.
- New York was upgraded by all three rating agencies to Aa1/AA+/AA+;

CA and NY were two notable state sector upgrades recently.

State government tax revenues fell 0.3% in 1Q14 after four years of choppy, but positive, growth, as reported by the Rockefeller Institute.

Preliminary data for 2Q14 does not look promising either.

## State Tax Revenues Fell in 1Q14 and Prelim Data Shows Lower Still in 2Q14



Source: Rockefeller Institute and Janney FIS. (Year over year change by quarter)

- California (Aa3/A/A) was upgraded to Aa3 from A1 by Moody's;
- Rhode Island's (Aa2/AA/AA) outlook was raised to "Stable" from "Negative" by S&P;
- Maine's (Aa2/AA/AA) outlook was raised to "Stable" from Negative" by Moody's; and
- Kentucky's (Aa2/AA-/A+) outlook was also raised to "Stable" from Negative" by Moody's.

### Positive Recent State Rating/Outlook Actions

State	Action	Notes	Date	Agency
South Dakota	Outlook raised Positive from Stable	Improved budget planning and results	8/1/2014	S&P
New York	Upgraded to AA+ from AA	Improved budgetary management	7/23/2014	S&P
California	Upgraded to Aa3 from A1	Improved governance and better finances	6/25/2014	Moody's
New York	Upgraded to AA+ from AA	Improved fiscal management practices	6/20/2014	Fitch
Rhode Island	Outlook raised to Stable from Neg	On budgetary approval for 38 Studios debt	6/18/2014	S&P
New York	Upgraded to Aa1 from Aa2	Improved governance and spending restraint	6/16/2014	Moody's
Maine	Outlook raised to Stable from Neg	Stable economy and revenues drive outlook	6/4/2014	Moody's
Kentucky	Outlook raised to Stable from Neg	Fiscal discipline & auto sector recovery	6/2/2014	Moody's

Source: Moody's, S&P, Fitch and Janney FIS.

### Troubling Trends Resulted in Downgrades (and More are Very Likely)

Despite the favorable momentum noted above, and state government's sovereign ability to raise revenue and cut spending, there have been several downgrades in the U.S. state sector recently. This

### Negative Recent State Rating/Outlook Actions

State	Action	Notes	Date	Agency
New Jersey	Downgraded to A from A+	Structural imbalance, pension liabilities	9/10/2014	S&P
New Jersey	Downgraded to A from A+	Absence of long term solutions, still neg outlook	9/5/2014	Fitch
Kansas	Downgraded to AA from AA+, Neg Out	Structural imbalance and tax cuts	8/6/2014	S&P
Pennsylvania	Downgraded to Aa3 from Aa2	Structural budget imbalance & pensions	7/21/2014	Moody's
Illinois	Lowered outlook to Neg from Developing	Structurally imbalanced FY15 budget	6/23/2014	S&P
Michigan	Lowered outlook to Stable from Positive	Lower in response to softening revenues	6/17/2014	S&P
New Jersey	Outlook to Watch Neg from Stable	Continuing structural imbalance	6/2/2014	S&P
New Jersey	Downgraded to A1 from Aa3	Budget imbalance, rev shortfalls, pensions	5/13/2014	Moody's
New Jersey	Downgraded to A+ from AA-	Ongoing budget strain, still neg outlook	5/1/2014	Fitch
Kansas	Downgraded to Aa2 from Aa1	Slow economic pace, structural imbalance	4/30/2014	Moody's

Source: Moody's, S&P, Fitch and Janney FIS.

New Jersey has been hit hard by all three rating agencies.

Pennsylvania was downgraded to Aa3 from Aa2 by Moody's.

Illinois' (A3/A-/A-) outlook was lowered to "Negative" from "Developing" by S&P.

is because there are several mostly structural and not cyclical factors eating away at some states' credit quality. Most notable are the downgrades to New Jersey and Pennsylvania ratings because the factors ailing these states are not easily repairable. Credit stresses are still large in Illinois too.

- New Jersey (A1/A/A) was hit hard by all three rating agencies as a result of the state's structurally imbalanced budget and significant amount (and growing) of unfunded pension liabilities;
- Kansas (Aa2/AA) was downgraded to AA and assigned a "Negative" outlook by S&P and downgraded to a Aa2 by Moody's- both rating agencies cited the states' structural imbalance and tax cuts as reasons for the downgrades;
- Pennsylvania (Aa3/AA/AA) was downgraded to Aa3 from Aa2 by Moody's who cited the Commonwealth's structurally imbalanced budget and growing pension liabilities as key reasons for the downgrade;
- Illinois' (A3/A-/A-) outlook was lowered to "Negative" from "Developing" by S&P; and
- Michigan's (Aa2/AA-/AA) outlook was lowered to "Stable" from "Positive" by S&P.

Overall, the Janney outlook for state credit remains "Stable" although indicators are mixed. We expect slow growth to hinder economic expansion and we believe more downgrades are lurking for a select few. Please see our [U.S. State Fiscal Health Update](#), published on August 12, 2014 for more details and state spread comparisons to the AAA municipal benchmark. **Tom Kozlik**

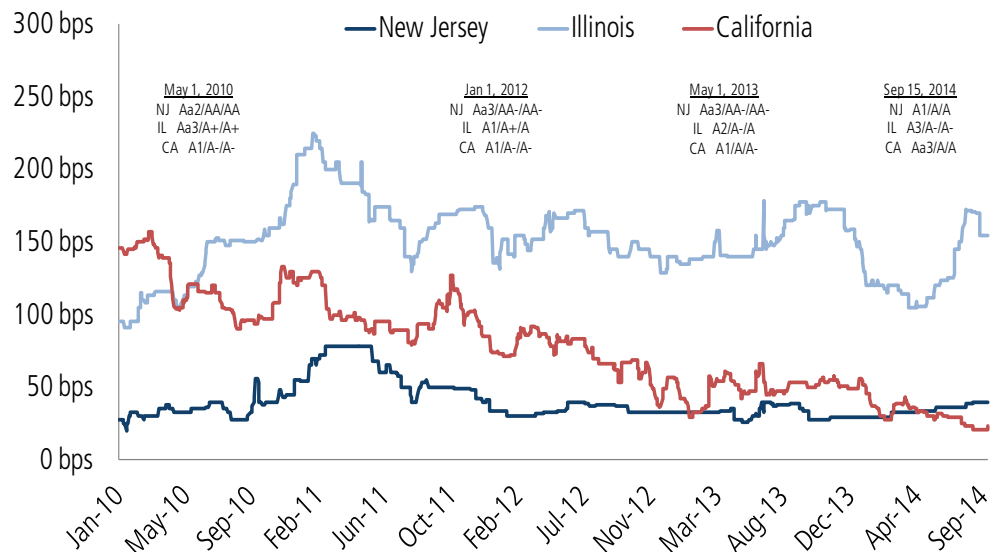
## A SHORT TALE OF THREE STATES

### Summary of Rating Actions and Credit Spreads to AAA Benchmark

After significant recession induced stress, California's fiscal metrics have improved, leading to rating upgrades and spread narrowing. Illinois' pension burden makes fiscal improvement a challenge, with wide spreads continuing. New Jersey's relatively tight trading spreads belie its lagging economic recovery and growing debt and pension liabilities.

Among various sectors in the municipal bond universe, the state sector exhibits the strongest credit quality characteristics. As sovereign entities, states have the ability to raise taxes and reduce expenditures as needed to achieve fiscal balance. States are generally highly rated and as this year began only two states, Illinois and California, carried ratings below the AA category. With Spring downgrades from all three rating agencies, and further downgrades from S&P and Fitch in recent weeks, the Garden State joins the club of A rated states.

### Credit Spreads Not reflective of New Jersey's Recent Credit Deterioration



Source: Thomson Reuters MMD and Janney. Spread to AAA Benchmark.

Exemplified by a June upgrade to Aa3 from A1 by Moody's, California is an improving credit.

## California

Exemplified by a June upgrade to Aa3 from A1 by Moody's, California is an improving credit. Although its recovery from the Great Recession has been uneven across localities, a combination of stronger than anticipated tax receipts and solid budgetary discipline have allowed state finances to rebound. The market's perception of California's improving fiscal stability is evident in the persistent narrowing of spreads in recent years. In January 2010, California 10 year yields were 146 basis points over the 10 year MMD AAA benchmark yield, well wider than Illinois' 95 basis points and New Jersey's tight 28 basis point spread.

## Illinois

Based on spreads, the market perception of Illinois' credit quality has been volatile and has generally deteriorated over the past 4 ½ years, with 10 year spreads currently at 155 basis points. Illinois' largest challenge is poorly funded pension plans, with Fitch adjusted funding levels for the state's three plans ranging from 32% to 38%. Comprehensive pension reform legislation enacted last December has run into legal challenges with the outcome unresolved. Personal and corporate income tax rates, which were increased in early 2011, are scheduled to decline on January 1, potentially reducing annual state income by about \$1.7 billion equal to about 5% of expenditures.

### Liabilities as a % of Personal Income

State	Debt	Pension	Total
New Jersey	7.4%	9.1%	16.5%
Illinois	5.6%	19.3%	24.9%
California	5.0%	3.3%	8.3%

Source: Fitch and Janney.

Based on spreads, the market perception of Illinois' credit quality has been volatile and has generally deteriorated over the past 4 ½ years, with 10 year spreads currently at 155 basis points.

## New Jersey

New Jersey is impacted by both lower than budgeted levels of tax income as well as high debt levels and growing pension liabilities. Despite two rounds of rating downgrades this year, New Jersey spreads have been relatively stable, widening by only 11 basis points since January 1st.

Although the state has only \$2.4 billion of general obligation debt, the appropriation backed debt load exceeds \$32 billion, with yields about 50 basis points higher than GO yields in 10 year maturities (MMD). Given the recent proposal to close budget gaps in FY 2014 and 2015 by reducing contributions to pension plans we believe New Jersey credit deterioration will continue near term, and expect this to be reflected by wider spreads in coming months. **Alan Schankel**

## LOCAL GOVERNMENT SECTOR CREDIT UPDATE

### Janney Retains a "Cautious" Outlook on Local Governments

We are not as encouraged with trends in the Local Government sector as we are with states. Credit conditions in the local government sector have not improved sector-wide. That is largely because many local governments have not had an easy time adjusting to the post-Great Recession time period. There are several factors often out of the control of local governments that make it difficult for them to quickly adjust spending.

We are still seeing many local governments that have not adjusted to the new revenue reality that exists in the post-Great Recession time period (see line chart on next page). One forecast we made at the end of 2013 for 2014 is that we expected downgrades would continue to outpace upgrades in the sector according to Moody's. We were dead right with this expectation. We predicted downgrades would outpace upgrades and they have been in 2014 to date. More details about the upgrade to downgrade experience below.

Much has been made about pension liabilities (rightfully so in our opinion) and the level at which they are funded by states and local governments. This is an important detail to consider. However, fixed costs in the form of pensions are just one spending line item investors need to consider. We recommend investors (and analysts) concentrate on the entire revenue and spending picture and be-

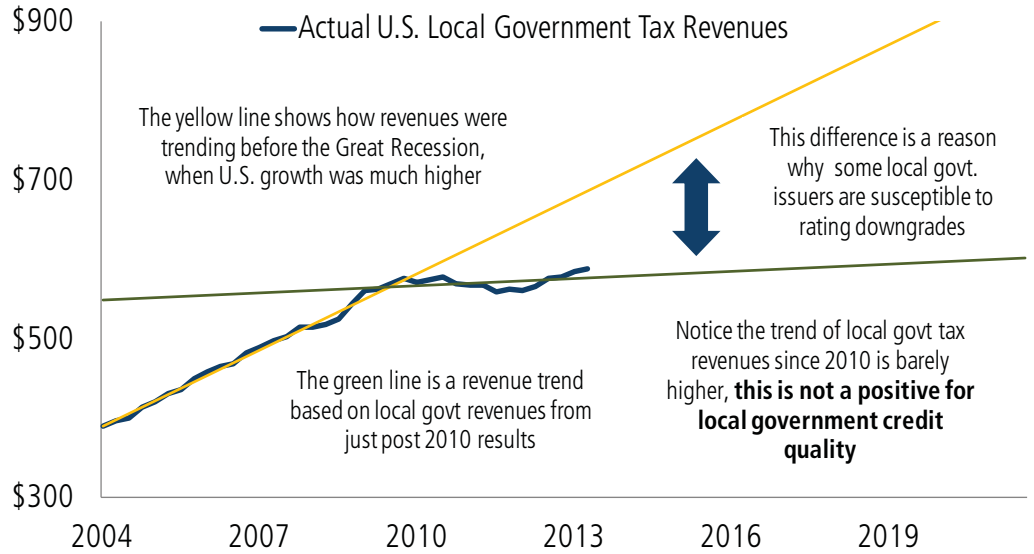
Despite two rounds of rating downgrades this year, New Jersey spreads have been relatively stable, widening by only 11 basis points since January 1st.

We are still seeing many local governments that have not adjusted to the new revenue reality that exists in the post-Great Recession time period.

There is oftentimes a significant disparity between actual revenues and expenditure demands at both the state and local level, as we noted above for local governments.

This is resulting in a significant build-up of structurally imbalanced budgets.

## Many Local Governments Still Want to Spend Like it is Pre-2010



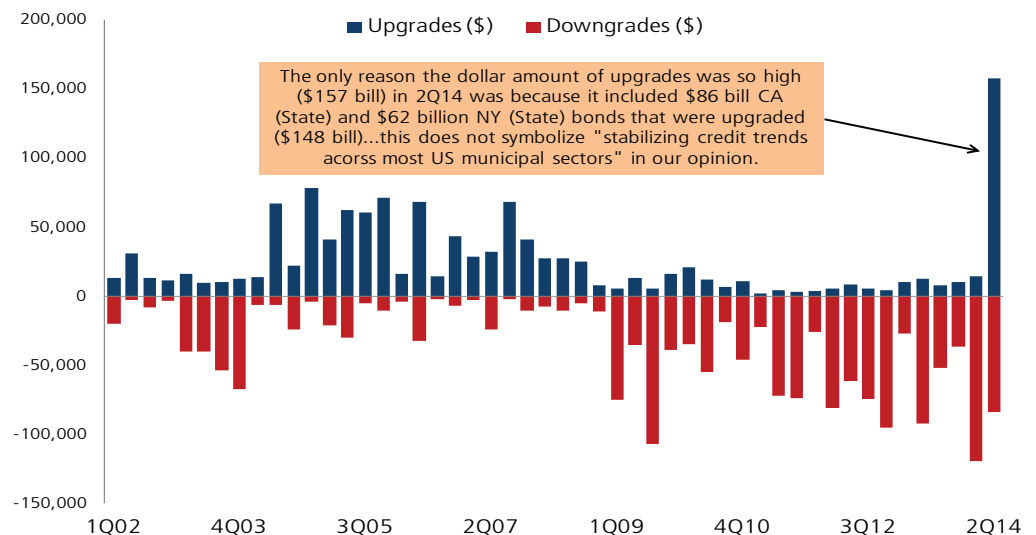
Source: U.S. Census Bureau and Janney FIS. (\$ in billions)

behavior of state and local governments. There is oftentimes a significant disparity between actual revenues and expenditure demands at both the state and local level, as we noted above for local governments. This is resulting in a significant build-up of structurally imbalanced budgets. Our analysis shows that over 50% of the local governments downgraded by Moody's in 2Q14 suffer from structurally imbalanced budgets. This is a financial condition that is difficult to mend, and is likely to result in further future rating downgrades.

## Moody's 2Q14 Upgrade to Downgrade Results

At the end of July Moody's released its quarterly rating revision update. We were a little surprised at the headline, "Stabilizing Credit Trends Across Most US Municipal Sectors," with a sub-title, "More Debt Upgraded than Downgraded for the First Time in Six Years" and we read on with interest because we were becoming more optimistic that maybe there was some data Moody's collected that showed municipal market credits, and especially US local government credits, were finally turning a corner in favor of recovery. But, large dollar amounts are skewing the data. We advise investors to not fall into a view of the sector that is overly optimistic. Downgrades (or the color red) are still the norm it turns out. There were 191 downgrades and 91 upgrades. As far as dollar amount there

## \$148 Billion of the \$157 Billion of Upgrades Was Due to California and New York



Source: Moody's and Janney FIS.

A focus on this slanted data hardly represents “stabilizing credit trends across most municipal sectors,” in our opinion.

“For the remainder of 2014, we expect the number of downgrades to outpace upgrades across US public finance,” Moody’s

There are some powerful forces at work.

was \$84 billion downgraded and \$157 billion upgraded. But, \$148 billion of the total dollar amount was from California (State of) and New York (State of) upgrades. A focus on this slanted data hardly represents “stabilizing credit trends across most municipal sectors,” in our opinion.

We do not think that credit conditions are anywhere close to the point where upgrades will outpace downgrades, and this is especially true for the local government sector, which makes up the majority of the data. Downgrades continued to outpace upgrades in the local government sector (the largest sector by far) and downgrades outpace upgrades when looking at the number (#) not the dollar (\$) amount of rating actions. The 2Q14 dollar amount data is grossly skewed because of the CA and NY upgrades. The actual story is that there were a total of 91 public finance upgrades and 191 public finance downgrades in 2Q14. That makes six fewer upgrades compared to 1Q14 and 41 more downgrades. Another factor skewing the number (#) of downgrades is related to Moody’s new methodology (or new rating criteria). 50% of upgrades, or 90 of the 188 were a result of the new methodologies / or criteria. The new methodology accounted for only 20% of the downgrades.

### Recent Moody’s Rating Movement Summarized (All Public Finance)

Time Period	Total Rating Movement			Rating Movement Excluding Methodology Changes		
	Upgrades (#)	Downgrades (#)	Downgrades % All Actions	Upgrades (#)	Downgrades (#)	Downgrades % All Actions
Q214	91	191	68%	45	155	78%
Q114	97	150	61%	48	118	71%
YTD 2014	188	341	64%	93	273	75%
Total 2013	190	695	79%	190	695	79%

Source: Moody’s and Janney FIS.

We think Moody’s actual expectation for near term credit performance is better described, in the firm’s own words, as noted below in the above referenced July report. The rating agency indicated:

“Most public finance ratings will remain stable as improving revenues and sound management practices support stable credit profiles. However, some issuers across multiple sectors have not recovered all the ground lost during the recession...For the remainder of 2014, we expect the number of downgrades to outpace upgrades across US public finance.”

### Multi-Year Cumulative Downgrade Results are Not So Minor

It is important to point out that there are about 8,300 rated local governments by Moody’s. The market should take comfort in the fact that quarter by quarter and even year by year the overall number of downgrades has been a very small percentage of the total number of local government ratings. The largest annual percentage was in 2013 when 437 entities were downgraded or 5% of local government issues. While the percentage of the sector that has been downgraded on this basis has been rather low, another important point about this data should be considered, and that has to do with the cumulative results of the downgrades. Since 2008 there have been almost 1,900 tax backed downgrades. That number is a much larger percentage of the overall number of local government credits- we get almost 23%. Granted, some issues would have been downgrades multiple times, and 23% is still not a majority of the entire sector. But, it goes to show that there are some powerful forces at work in this sector investors should continue to watch.

### The Total # of Local Government Downgrades is Building

Year	Moody’s Tax Backed Downgrades (#)	% of Local Govt. (8,300)
2008	81	0.98%
2009	279	3.36%
2010	259	3.12%
2011	296	3.57%
2012	344	4.14%
2013	437	5.27%
20141H	198	2.39%
Total	1,894	22.82%

Source: Moody’s and Janney FIS.



What we are seeing is that since 4Q08, or for 22 straight quarters, Moody's public finance rating downgrades have outpaced upgrades.

This trend will continue in the immediate future and we see no indications that it will reverse anytime soon.

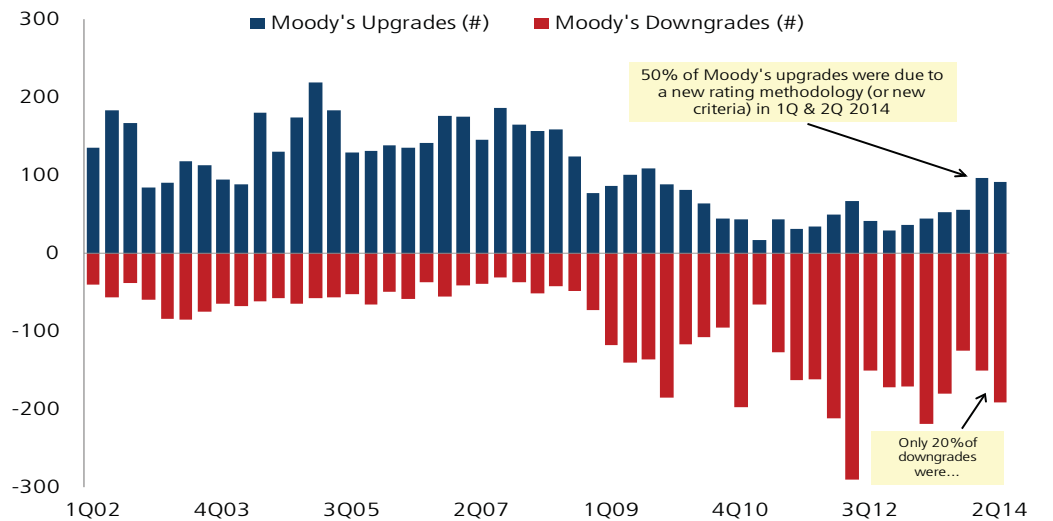
Investors should stay away from deteriorating credits.

What we are seeing is that since 4Q08, or for 22 straight quarters, Moody's public finance rating downgrades have outpaced upgrades. This trend will continue in the immediate future and we see no indications that it will reverse anytime soon. In fact, as one looks at the specifics of the local governments that have been downgraded this year for example, the future does not seem brighter. Of those downgraded this year most have been moved lower because of:

- Multi-year structural budget imbalances (this refers to a budget that is not fiscally sustainable and cannot fund ongoing expenditures with recurring revenues);
- Significant revenue decreases usually over a multi-year period;
- Drops in reserve levels (issuers usually dip into reserves to get through a bad year or two);
- Often the downgraded issuers suffer from all listed above ailments.

What is most problematic is that there are still some in the double "A" category that are suffering from one or more of the noted credit stresses. These are examples of credits we advise investors to stay away from when allocating funds.

### Downgrades are Still Outpacing Upgrades Despite the Mixed Message



Source: Moody's and Janney FIS.

### Investor Recommendation: Stick to Issuers With High Quality Credit Profiles

We are reiterating our recommendation for fixed income investors interested in allocating funds to the municipal market: We recommend fixed income investors stick to high quality municipal bonds. In the local government sector that means entities that have stable or improving credit profiles. One would think that would be easy enough to find in the local government sector, especially because it includes so many issuers. But, it is not as easy as it might have seemed in past years. The Moody's upgrade to downgrades ratios illustrates this. **Tom Kozlik**

# MUNICIPAL BOND MARKET MONTHLY

September 16, 2014



## Select Recent Changes to Ratings & Outlooks (as of Sept 15, 2014)

Issuer	State	Recent Rating Action	Date	Underlying Rating(s)	Notes
New Jersey (State of)	NJ	Downgraded to A from A+ by S&P	10-Sep-2014	A1/A/A	Budget pressures and unfunded pensions
New Jersey (State of)	NJ	Downgraded to A from A+ by Fitch	5-Sep-2014	A1/A/A	Absence of fiscally sustainable budget
Los Angeles (City of)	CA	Raised outlook to Positive from Stable by S&P	1-Sep-2014	Aa2/AA-/AA-	Improving metrics and financial position
N Shore LI Jewish Health	NY	Upgraded to A from A- bby Fitch	28-Aug-2014	A3/A-/A	Growing presence and stability
Orange County	NY	Downgraded to Aa3 from Aa2 by Moody's	26-Aug-2014	Aa3	Multi-year deficits, draws on reserves

Source: Moody's; S&P; Fitch and Janney FIS.

# MUNICIPAL BOND MARKET MONTHLY

September 16, 2014



## State and Other Select Issuer Ratings (Sept 15, 2014)

State	Moody's			S&P			Fitch		
	Rating	Outlook	Last	Rating	Outlook	Last	Rating	Outlook	Last
Alabama	Aa1	Stable	4/16/2010	AA	Positive	11/27/2013	AA+	Stable	5/3/2010
Alaska	Aaa	Stable	11/22/2010	AAA	Stable	1/5/2012	AAA	Stable	1/7/2013
Arizona (*)	Aa3	Positive	11/26/2013	AA-	Stable	12/23/2011	NR	-	-
Arkansas	Aa1	Stable	4/16/2010	AA	Stable	1/10/2003	NR	-	-
California	Aa3	Stable	6/25/2014	A	Positive	1/14/2014	A	Stable	8/5/2013
Colorado (*)	Aa1	Stable	4/16/2010	AA	Stable	7/10/2007	NR	-	-
Connecticut	Aa3	Stable	1/20/2012	AA	Stable	9/26/2003	AA	Negative	7/2/2013
Delaware	Aaa	Stable	4/30/2010	AAA	Stable	2/22/2000	AAA	Stable	4/13/2006
Dist. of Columbia	Aa2	Stable	8/2/2013	AA-	Stable	3/21/2013	AA-	Stable	4/5/2010
Florida	Aa1	Stable	4/16/2010	AAA	Stable	7/12/2011	AAA	Stable	8/23/2013
Georgia	Aaa	Stable	4/16/2010	AAA	Stable	7/29/1997	AAA	Stable	4/13/2006
Hawaii	Aa2	Stable	5/17/2011	AA	Positive	10/10/2013	AA	Stable	6/15/2011
Idaho (*)	Aa1	Stable	4/16/2010	AA+	Stable	3/30/2011	AA	Stable	4/5/2010
Illinois	A3	Negative	6/6/2013	A-	Negative	6/23/2014	A-	Negative	6/3/2013
Indiana (*)	Aaa	Stable	4/16/2010	AAA	Stable	7/18/2008	AA+	Stable	4/5/2010
Iowa (*)	Aaa	Stable	4/16/2010	AAA	Stable	9/11/2008	AAA	Stable	4/5/2010
Kansas (*)	Aa2	Stable	4/30/2014	AA	Negative	8/6/2014	None	None	None
Kentucky (*)	Aa2	Stable	6/2/2014	AA-	Negative	1/31/2013	A+	Stable	11/8/2012
Louisiana	Aa2	Stable	4/16/2010	AA	Stable	5/4/2011	AA	Stable	4/5/2010
Maine	Aa2	Stable	6/4/2014	AA	Stable	5/24/2012	AA	Stable	1/23/2013
Maryland	Aaa	Stable	7/19/2013	AAA	Stable	5/7/1992	AAA	Stable	4/13/2006
Massachusetts	Aa1	Stable	4/16/2010	AA+	Stable	9/16/2011	AA+	Stable	4/5/2010
Michigan	Aa2	Positive	3/28/2013	AA-	Stable	6/17/2014	AA	Stable	4/2/2013
Minnesota	Aa1	Stable	7/30/2013	AA+	Stable	9/29/2011	AA+	Stable	7/7/2011
Mississippi	Aa2	Stable	4/16/2010	AA	Stable	11/30/2005	AA+	Negative	11/15/2013
Missouri	Aaa	Stable	7/19/2013	AAA	Stable	2/16/1994	AAA	Stable	4/13/2006
Montana	Aa1	Stable	4/16/2010	AA	Stable	5/5/2008	AA+	Stable	4/5/2010
Nebraska (*)	Aa2	Stable	4/16/2010	AAA	Stable	5/5/2011	NR	-	-
Nevada	Aa2	Stable	3/24/2011	AA	Stable	3/10/2011	AA+	Stable	4/5/2010
New Hampshire	Aa1	Stable	4/16/2010	AA	Negative	4/21/2014	AA+	Stable	4/5/2010
New Jersey	A1	Negative	5/13/2014	A	Stable	9/10/2014	A	Negative	9/5/2014
New Mexico	Aaa	Stable	7/19/2013	AA+	Stable	2/5/1999	NR	-	-
New York	Aa1	Stable	6/16/2014	AA+	Stable	7/23/2014	AA+	Stable	6/25/2014
North Carolina	Aaa	Stable	1/12/2007	AAA	Stable	6/25/1992	AAA	Stable	4/13/2006
North Dakota (*)	Aa1	Stable	4/16/2010	AAA	Stable	12/13/2013	NR	-	-
Ohio	Aa1	Stable	3/16/2012	AA+	Stable	7/19/2011	AA+	Stable	4/11/2011
Oklahoma	Aa2	Stable	4/16/2010	AA+	Stable	9/5/2008	AA+	Stable	4/5/2010
Oregon	Aa1	Stable	4/16/2010	AA+	Stable	3/10/2011	AA+	Stable	4/5/2010
Pennsylvania	Aa3	Stable	7/21/2014	AA	Negative	7/19/2012	AA	Negative	7/16/2013
Puerto Rico	B2	Negative	7/1/2014	BB+	Watch Neg	7/1/2014	BB-	Negative	7/9/2014
Rhode Island	Aa2	Negative	7/1/2013	AA	Watch Dwn	5/12/2014	AA	Stable	7/18/2011
South Carolina	Aaa	Stable	12/7/2011	AA+	Stable	7/11/2005	AAA	Stable	4/13/2006
South Dakota (*)	Aa2	Stable	5/27/2010	AA+	Stable	3/25/2011	AA	Positive	8/1/2014
Tennessee	Aaa	Stable	12/7/2011	AA+	Stable	11/5/2013	AAA	Stable	4/5/2010
Texas	Aaa	Stable	4/16/2010	AAA	Stable	9/27/2013	AAA	Stable	4/5/2010
Utah	Aaa	Stable	4/16/2010	AAA	Stable	6/7/1991	AAA	Stable	4/13/2006
Vermont	Aaa	Stable	4/16/2010	AA+	Positive	9/17/2012	AAA	Stable	4/5/2010
Virginia	Aaa	Stable	7/19/2013	AAA	Stable	11/11/1992	AAA	Stable	4/13/2006
Washington	Aa1	Stable	7/19/2013	AA+	Stable	11/12/2007	AA+	Stable	7/19/2013
West Virginia	Aa1	Stable	7/9/2010	AA	Stable	8/21/2009	AA+	Stable	7/8/2011
Wisconsin	Aa2	Stable	4/16/2010	AA	Stable	8/15/2008	AA	Stable	4/5/2010
Wyoming (*)	NR	-	-	AAA	Stable	5/3/2011	NR	-	-

Source: Moody's; S&P; Fitch and Janney FIS. (\*) Denotes a Lease or Issuer Credit Rating.

# MUNICIPAL BOND MARKET MONTHLY

September 16, 2014



## Municipal Credit Rating Scale and Definitions

	Rating Agency			Definition
	Moody's	S&P	Fitch	
Investment Grade	Aaa	AAA	AAA	Exceptionally strong credit quality and minimal default risk.
	Aa1	AA+	AA+	Upper medium grade and subject to low credit risk.
	Aa2	AA	AA	Upper medium grade and subject to low credit risk.
	Aa3	AA-	AA-	Upper medium grade and subject to low credit risk.
	A1	A+	A+	Strong credit quality and subject to low default risk.
	A2	A	A	Strong credit quality and subject to low default risk.
	A3	A-	A-	Strong credit quality and subject to low default risk.
	Baa1	BBB+	BBB+	Subject to moderate risk and possess some speculative characteristics.
	Baa2	BBB	BBB	Subject to moderate risk and possess some speculative characteristics.
Baa3	BBB-	BBB-	Subject to moderate risk and possess some speculative characteristics.	
Sub-Investment Grade	Ba1	BB+	BB+	Weak credit quality with speculative elements and substantial credit risk.
	Ba2	BB	BB	Weak credit quality with speculative elements and substantial credit risk.
	Ba3	BB-	BB-	Weak credit quality with speculative elements and substantial credit risk.
	B1	B+	B+	Very weak credit quality, very speculative with high credit risk.
	B2	B	B	Very weak credit quality, very speculative with high credit risk.
	B3	B-	B-	Very weak credit quality, very speculative with high credit risk.
	Caa1	CCC+		Extremely weak credit quality and subject to very high credit risk.
	Caa2	CCC	CCC	Extremely weak credit quality and subject to very high credit risk.
	Caa3	CCC-		Extremely weak credit quality and subject to very high credit risk.
	Ca	CC		Highly speculative and are in or near default with some prospect for recovery.
		C	CC	Lowest class of rated bonds and may be in default with little prospect for recovery.
			C	Lowest class of rated bonds and may be in default with little prospect for recovery.
	D	D	RD/D	Issuer is in default and/or has failed to make a payment.

Source: Moody's; S&P; Fitch and Janney FIS.

# MUNICIPAL BOND MARKET MONTHLY

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## Janney Municipal Bond Market Publications

Title	Date	Pub	Notes
Your Municipal Bond Portfolio	September 5, 2014	Note	Credit quality and duration are important for portfolios
Mid-Year Municipal Market Review/Outlook	August 27, 2014	Monthly	Municipal credit quality is high, but falling
Detroit Water and Sewer Update	August 25, 2014	Weekly	30% of bonds tendered, but an important step
Parsing the PREPA News	August 18, 2014	Weekly	PREPA reached agreement with stakeholders
U.S. State Fiscal Health Update	August 12, 2014	Note	March of next year
Steady as She Goes	August 11, 2014	Weekly	Municipals continue to show stability, credit is improving
This Summer is Different	August 4, 2014	Weekly	Volume indicators are lower this year
Are S&P's Local Govt. Ratings Too High?	July 14, 2014	Monthly	We have become increasingly skeptical of S&P
Puerto Rico: It All Goes Back to Economy	June 30, 2014	Weekly	Puerto Rico's economy continues to contract
OPEBS v Pension Primer	June 23, 2014	Weekly	OPEB is funded on a pay as you go basis
A Brief Pension Primer	June 16, 2014	Weekly	Update on pension funding
Inertia - Not Best Response to Rate Concerns	June 12, 2014	Note	Investors are concerned about potential for rising rates
What a Difference a Year Makes	June 9, 2014	Weekly	M/T Ratios have stabilized since last summer
Puerto Rico - Post Visit Update	June 5, 2014	Note	April revenue miss increases budget balance
Supply Constraints	June 2, 2014	Weekly	Summer supply and demand collision
The Rime of Municipal Bond Issuance	May 22, 2014	Monthly	Municipal Issuance will drop in 2014 & in coming years
Tobacco Bond Update	May 19, 2014	Weekly	Trends in the tobacco sector remain negative
Municipal Default Update	May 12, 2014	Weekly	Municipal defaults remain low compared to other sectors
Atlanta Hartsfield Jackson Int Airport	May 12, 2014	Note	Key takeaways from our closer look at ATL
Municipal Airport Sector	May 9, 2014	Note	Headwinds have receded in Airport sector
New Jersey Downgraded	May 5, 2014	Weekly	NJ spreads have remained steady since the downgrade
Municipal Market Technical Review	April 28, 2014	Weekly	M/T Ratios have been declining
Tax Day Reminder of Muni Value	April 15, 2014	Note	Let municipal help alleviate the pain of higher taxes
U.S. State Fiscal Health Update	April 11, 2014	Note	A new spending paradigm for state governments
The Bond Insurers- Now There are Three	April 9, 2014	Note	Upgrades for Assured and National
Chp 9 Bankruptcies Remain Low	March 28, 2014	Monthly	Review Chp 9 bankruptcies, RI willingness
Heavy New Issue Week Comes and Goes	March 17, 2014	Weekly	Heavy calendar and Puerto Rico issuance
Size of Municipal Market Shrinks Again	March 10, 2014	Weekly	Fed data indicates amt. bonds is gradually diminishing
Our Annual Municipal Sector Credit Reviews	February 28, 2014	Monthly	Still have "Cautious" outlooks on 6 (of 11) sectors
Municipals: Positive but Tepid Demand	February 24, 2014	Weekly	Modest mutual fund inflows
Moody's and Fitch Downgrade - Puerto Rico	February 11, 2014	Note	Moody's & Fitch downgraded GO below investment grade
Municipals: Puerto Rico Downgrades	February 10, 2014	Weekly	A Review of recent downgrades related to Puerto Rico
S&P Downgrade - Puerto Rico	February 6, 2014	Note	S&P downgraded GO below investment grade
Municipals: Low January New Issue Volume	February 3, 2014	Weekly	Volume is lower but new money issuance is rising
Lower Yields Breeds Duration Adjustment	January 27, 2014	Weekly	Opportunity to manage duration by realigning portfolios
PA Intercept Program for School Districts	January 22, 2014	Note	In-depth Look at the mechanisms and Moody's changes
Municipals: A Good Start to 2014	January 13, 2014	Weekly	Munis enjoyed a strong start for the year amid light supply
Janney Outlook for Local Governments	January 7, 2014	Note	Outlook still "Cautious"
U.S. State Fiscal Health Update	January 6, 2014	Note	"Stable" Outlook for U.S. States- full steam ahead
Municipals: Fewer New Munis	January 6, 2014	Weekly	Borrowing for projects remains below pre-recession pace
A Unique Local Govt Refunding Strategy	December 19, 2013	Note	IL school districts funding escrows with IL GOs
The Municipal Market in 2014	November 22, 2013	Monthly	We highlight 5 events/issues we expect to be big
Municipals: Jefferson Cty, AL and Puerto Rico	November 25, 2013	Weekly	Questionable debt structure and PR econ indicators
Municipals: Rating Action Divergence	November 18, 2013	Weekly	Difficult to rationalize upgrades by S&P
Connecticut: A Review of State Issuers	November 8, 2013	Note	CT faced significant economic challenges
Municipals: Puerto Rico Update	November 4, 2013	Weekly	Disclosure has improved and yields narrowed
Municipals: Old Normal Returns	October 28, 2013	Weekly	Market stabilizing, S&P's optimistic view
Municipals: Back to Normal?	October 21, 2013	Weekly	Growing primary market calendar post-shutdown
Municipals: Regional Economic Shutdown	October 7, 2013	Weekly	State & regions just around DC to be most affected
Puerto Rico: Island Visit and COFINA	October 4, 2013	Note	Sales & use tax revs growing despite weak economy
U.S. State Fiscal Health Update	October 3, 2013	Note	Status of U.S. States largely secure, laggards remain
Municipals: Washington Crunch	September 30, 2013	Weekly	Commentary on outflows and DC interference
Debt Ceiling Debate Part II: Treat Uncertainty	September 27, 2013	Monthly	More uncertainty, but will be less impactful than in 2011
M/T Ratios Continue to Retreat	September 23, 2013	Weekly	Sparse supply helps municipals stabilize

Source: Janney Fixed Income Strategy.

## Analyst Certification

We, Tom Kozlik and Alan Schankel, the Primarily Responsible Analysts for this report, hereby certify that all of the views expressed in this report accurately reflect our personal views about any and all of the subject sectors, industries, securities, and issuers. No part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

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**Positive:** Janney FIS believes there are apparent factors which point towards improving issuer or sector credit quality which may result in potential credit ratings upgrades

**Stable:** Janney FIS believes there are factors which point towards stable issuer or sector credit quality which are unlikely to result in either potential credit ratings upgrades or downgrades.

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**Negative:** Janney FIS believes there are factors which point towards weakening in issuer credit quality that will likely result in credit ratings downgrades.

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**Overweight:** Janney FIS expects the target asset class or sector to outperform the comparable benchmark (below) in its asset class in terms of total return

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**Agencies:** Janney FIS ratings employ the "Barclay's U.S. Agency Index" as a benchmark.

**Mortgages:** Janney FIS ratings employ the "Barclay's U.S. MBS Index" as a benchmark.

**Investment Grade Credit:** Janney FIS ratings employ the "Barclay's U.S. Credit Index" as a benchmark.

**High Yield Credit:** Janney FIS ratings for employ "Barclay's U.S. Corporate High Yield Index" as a benchmark.

**Municipals:** Janney FIS ratings employ the "Barclay's Municipal Bond Index" as a benchmark.

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