



**HOW TO HANG ON AND CLOSE A DEAL:**  
Update on the Bond Market and Important Considerations  
for South Carolina Issuers

**NEXSEN PRUET**

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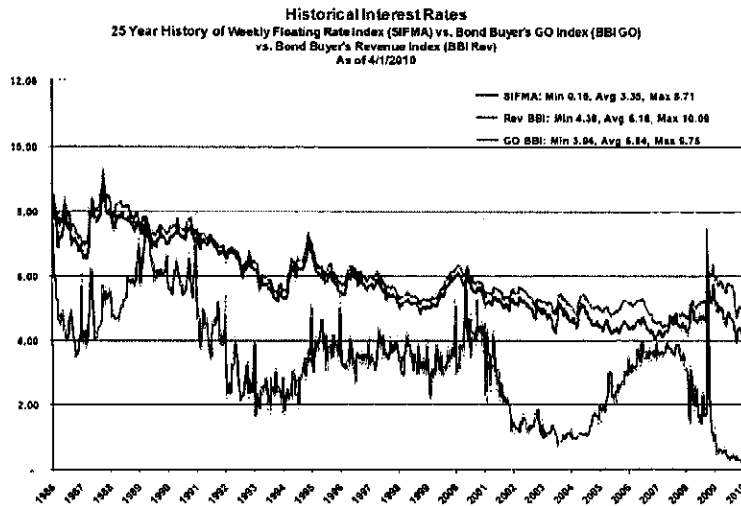
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**Topics for Discussion**

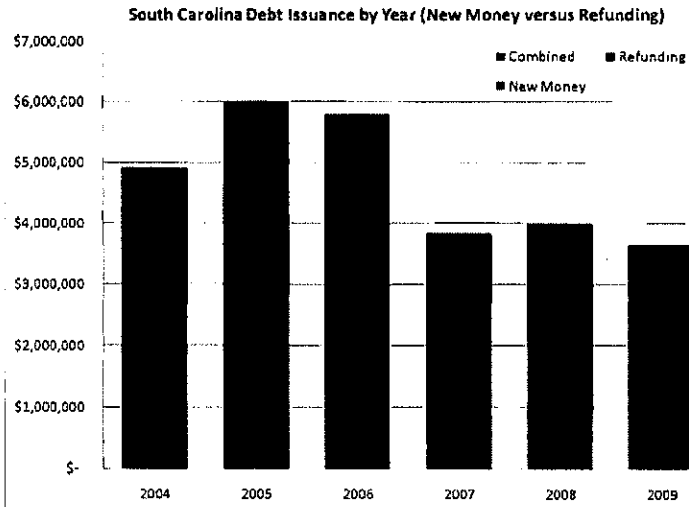
- **Current Market Update**
  - Interest Rate Environment
  - Debt issuance volume in South Carolina
  - Financial institutions .. purchasing for their portfolios
  - Bond Insurers. ..changing landscape
  - Credit ratings...importance of having a rating and how it impacts your borrowing cost
- **American Recovery and Reinvestment Act**
  - What it is not
  - Major municipal initiatives
  - Build America Bonds Overview
  - Recovery Zone Economic Development Bonds Overview
- **Conclusions**
- **Questions/Answers**

## Section 1 – Current Market Update

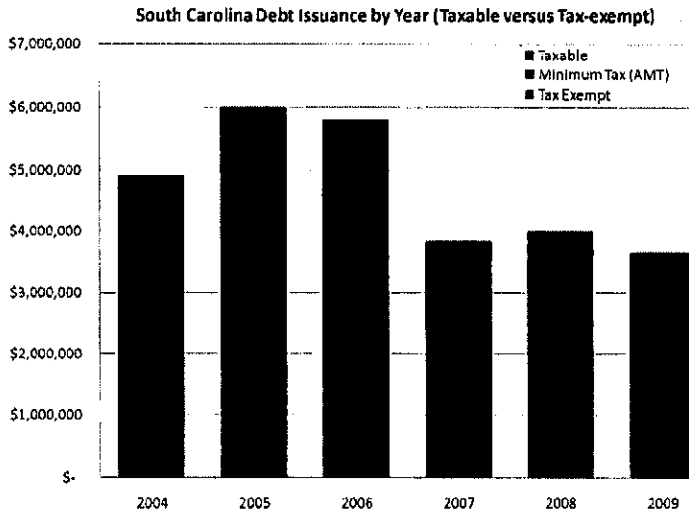
Despite market turmoil, interest rates remain at very attractive levels



**South Carolina Debt Issuance in 2009 was the lowest in six years**



**South Carolina Historical Debt Issuance**



## Appetite of Banks for South Carolina Debt:

- Banks have shown continued willingness to purchase debt.
- Rates remain at attractive levels.
- Most banks prefer amortizations of 15 years or less. However, there are a few banks willing to purchase bonds with a 20 year amortization.
- Issuers should allow extra time in the bidding schedule for banks to complete their credit approval process (recommend two weeks).

## Overview of Municipal Bond Insurers

### Municipal Bond Insurers Ratings Summary

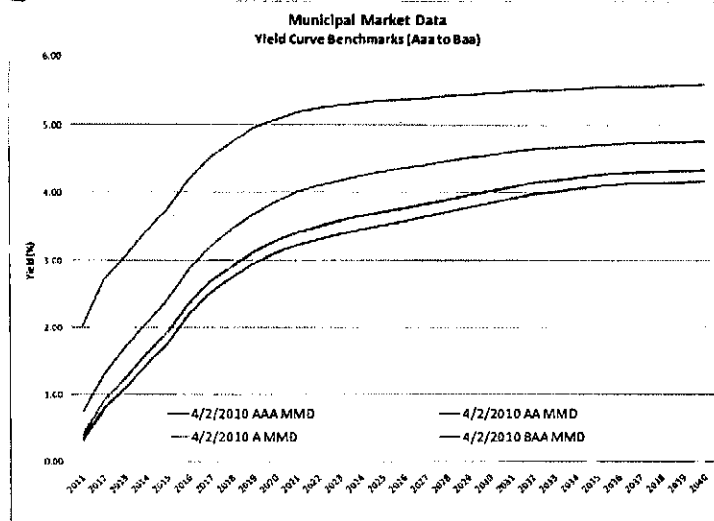
As of Monday, March 29, 2010 6:00 P.M. ET

Insurer	Legend		
	Stable	Negative Outlook	Positive Outlook
	Developing Watch / Review With Monitor Intention	Watch Positive / On Track for Possible Upgrade	
<b>Berkshire Hathaway</b> (Columbia and National Insurance Co. "NICO")	A-1 / Stable (as of 4/18/09)	AAA / Stable (as of 2/24/10)	No Rating
<b>Assured Guaranty</b>	AA- / Negative Outlook (as of 2/18/09)	AAA / Negative Outlook (as of 7/1/09)	Rating Withdrawn (as of 2/24/10)
<b>Assured Guaranty Municipal</b> (formerly FIA, pending approval)	AA- / Negative Outlook (as of 3/18/09)	AAA / Negative Outlook (as of 7/1/09)	Rating Withdrawn (as of 2/24/10)
<b>National Public Finance</b> (formerly MBIA Bond)	Baa- / Developing (as of 6/25/08)	A- / Developing (as of 9/28/07)	Rating Withdrawn (as of 6/26/08)
<b>Radian</b>	B-1 / Stable (as of 3/11/09)	BB- / Negative Outlook (as of 2/22/09)	Rating Withdrawn (as of 5/22/08)
<b>MBIA</b>	B-1 / Negative Outlook (as of 6/25/09)	B-1 / Negative Outlook (as of 9/22/08)	Rating Withdrawn (as of 6/26/08)
<b>Ambac</b>	Check / Review for Possible Upgrade (as of 7/26/10)	BB- / Negative Outlook (as of 2/22/09)	Rating Withdrawn (as of 6/26/08)
<b>Syncora</b>	C- / Developing (as of 3/09/08)	B- / Negative Outlook (as of 7/7/07)	Rating Withdrawn (as of 9/25/08)
<b>CIFG</b>	Rating Withdrawn (as of 1/11/09)	Rating Withdrawn (as of 2/26/10)	Rating Withdrawn (as of 10/21/08)
<b>FGIC</b> (Certain Policies Covered by National)	Rating Withdrawn (as of 7/21/09)	Rating Withdrawn (as of 4/22/09)	Rating Withdrawn (as of 11/24/08)
<b>ACA</b>	No Rating	Rating Withdrawn (as of 12/15/08)	No Rating

### Importance of Credit Ratings:

- With the downgrades of bond insurers, investors are increasing relying on the underlying credit rating of issuers.
- For issuer's who already have credit ratings, now is the time to review your rating with your finance team (bond counsel, financial advisor, underwriter) and develop a long term rating strategy.
- Ongoing and frequent communications with rating analysts are important.
- For issuers who do not currently have credit ratings, it may be appropriate to pursue obtaining a rating.
- Allow ample time in the financing calendar to obtain ratings (3-4 weeks for rating confirmations, 6-8 weeks for first time ratings)

### Interest Rates are dependent on the Borrower's Credit



### Recalibration of U.S. Municipal Bond Ratings

- Historically, municipal bond ratings have been on the same scale as corporate bond ratings (AAA, AA, A, BBB...), however it was widely acknowledged by investors that municipal issuers were less likely to default compared with similarly rated corporate borrowers.
- "*U.S. Municipal Bond Defaults and Recoveries, 1970-2009*" released by Moody's last week. Only 54 rated issues have defaulted since 1970 (51 have been non-GO debt).
- 5-year cumulative default rate for investment-grade municipal debt is 0.03% vs. 0.97% for corporate issuers

### Recalibration of U.S. Municipal Bond Ratings

- July 2008 – Fitch releases report discussing a recalibration of their municipal ratings to a comparable credit risk scale for corporate, sovereign, and other entities.
- July 2008 -- Standard & Poor's releases a report confirming their use of the same rating scale across the structured finance, corporate, and government sectors. Report noted on-going review of U.S. Public Finance criteria
- April 5, 2010 – Fitch began the recalibration of US Public Finance Ratings
- May 7, 2010 – Moody's will begin the recalibrations of the US Public Finance Ratings

**Recalibration of U.S. Municipal Bond Ratings – What does it mean?**

- According to a report released by Moody's Investor Service in March 2010, the majority of General Obligation and Water/Sewer credits will receive at least a 1-notch upgrade.

Moody's Upward Shift in Ratings in the Global Rating Scale (# of notches)

Municipal Scale Rating	GO; Water & Sewer	Special Tax (Non-GO)	Public Universities and University Foundations	Public Health Care; Housing; Private Education Institutions
Aaa	0	0	0	0
Aa1	0-1	1	0-1	0
Aa2	1	1	1	0
Aa3	1	1	1	0
A1	2	1	1	0
A2	2	1	1	0
A3	2	1	1	0
Baa1	3	1	1	0
Baa2	3	0	1	0
Baa3	2-3	0	1	0

**Section 2 – American Recovery and Reinvestment Act of 2009**

### **American Recovery and Reinvestment Act of 2009 (ARRA)**

- **What it is not:**
  - Not pot of federal money to buy or provide credit enhancement or liquidity for bonds
  - Not a guarantee by the United States Government . . . Build America Bond subsidy is just a “subsidy”
  - Not a new authorization to issue bonds . . . Issuer must comply with state law requirements (purposes, debt limits) and provisions of applicable bond documents (additional bonds test, rate covenants)

### **American Recovery and Reinvestment Act of 2009 (ARRA)**

- Major municipal initiatives
  - Build America Bonds (BABs)
  - Recovery Zone Economic Development Bonds
  - Qualified School Construction Bonds
  - Bank Qualified Bonds (through 2010)
    - Increased limit from \$10 million to \$30 million annually
    - Allows favorable interest deduction to the extent percentage of Bank’s tax-exempt assets do not exceed 2% of total assets
  - Alternate Minimum Tax (through 2010)
    - No adjustment to adjusted current earnings

### **American Recovery and Reinvestment Act of 2009 (ARRA)**

- Hiring Incentives to Restore Employment Act (HIRE) expanded BAB-style direct payments to the following "tax credit" bond programs:
  - Qualified school construction bonds
  - Qualified zone academy bonds
  - New clean renewal energy bonds
  - Qualified energy conservation bonds

### **Build America Bonds Overview**

- BABs broaden the market for state and local governmental bonds by allowing a taxable alternative to tax-exempt bonds while providing a tax credit to holders or refundable tax credit to issuers
  - Allows investors who do not benefit from tax-exempt income to participate...much larger potential market
  - Issuers that continue to sell tax-exempt bonds should benefit because of the reduction in volume, as many large deals are sold to taxable investors
- To generalize Build America Bonds, two types have been issued
  - Deals structured to tax-exempt investors typically are smaller in size, have a 10-year call feature, and amortize principal over time
  - Deals with more of a corporate structure are non-callable and typically have bullet maturities
  - Build America Bonds are more sensitive to proceeds generated (i.e. very limited premium on the Bonds)

### **Build America Bonds Overview (Continued)**

- Finance Governmentally-owned facilities only
- BABs must be issued before the end of 2010
- Small Business and Infrastructure Jobs Tax Act pending
  - If passed, will extend BABs through April 1, 2013 at rates gradually reducing to 28%
- Since inception, there have been over \$70.7 billion of Build America Bond Issuance \*
- BABs now constitute about 20% of municipal bond issuance \*
- \$479 million (16 issues) has been issued by South Carolina issuers \*
- The majority of the issuance has been direct pay option

\* Source: U.S. Department of the Treasury, data as of 1/6/2010

### **Practical Considerations for Issuers of Build America Bonds**

- Treatment of refundable tax credit received from Treasury-BABs (Direct Pay)
  - Constitutional debt limits
  - Additional bonds test
  - Coverage calculation
  - Timing of receipt of credit
  - Reduction in subsidy rate
  - IRS intercept of BABs refundable tax credit
  - Additional reporting and audit requirement
- Difference in call features, couponing and maturity structure
  - Taxable market historically non-callable or make whole versus traditional 10-year call
  - Limitation on premium may force different couponing

## The Benefit of Build America Bonds - Interest Rate Comparison

### Build America Bond vs. Tax-Exempt Bond Interest Rate Comparison

#### Build America Bond vs. Tax-Exempt Bond Interest Rate Comparison

	Taxable	Subsidy	Net BAB Rate	Tax-Exempt	BAB Cost (Benefit)
1 Year	1.35%	0.47%	0.88%	0.34%	+0.54%
5 Year	<b>3.36%</b>	1.18%	2.18%	1.76%	+0.42%
10 Year	4.68%	1.64%	3.04%	3.20%	(0.16%)
15 Year	<b>5.33%</b>	1.67%	3.46%	3.67%	(0.21%)
20 Year	5.98%	2.09%	3.87%	4.06%	(0.19%)
25 Year	6.40%	2.24%	4.16%	4.40%	(0.24%)

- Note: Actual rates may differ based upon the underlying credit rating.

## The Benefit of Build America Bonds – Difference to the Buyer of the Bonds

### Municipal Build America Bond:

- St. Charles Park IL 3.15% 12/15/2015
  - AA rated
  - General Obligation Bond
  - Priced @ 3.00% yield to maturity
  - ~+65 bps spread vs. 5-year treasury bond

### Corporate Bond:

- Wal Mart 4.50% 7/1/2015
  - Aa2/AA rated
  - Priced at 2.85% yield to maturity
  - ~+50 bps spread vs. 5-year treasury bond

### **Recovery Zone Economic Development Bonds Overview**

- Facilities must be governmentally owned
- Taxable, Direct Payment BABs, which increase the refundable tax credit payable to the issuer from 35% to 45%
- Bond proceeds must be used to promote economic development in a recovery zone
  - Public infrastructure and public facilities
  - Job training and educational programs
- Issue must be closed before the end of 2010

### **Designation of Recovery Zones**

- Issuer designates zones within its jurisdiction
- Zones must have significant poverty, unemployment, rate of home foreclosures or general distress; or
- Zone must be economically distressed due to closure or realignment of military installation per Defense Base Closure and Realignment Act of 1990; or
- Zone is an Empowerment Zone or Renewal Community as in effect on date of Act

### **Volume Cap for Recovery Zone Economic Development Bonds**

- Volume Cap - volume caps allocated on the basis of relative decline in employment in 2008
- Nationwide Cap of \$10 Billion
- South Carolina Cap of \$115,041,000
- See handout for volume cap allocation within South Carolina
- Small Business and Infrastructure Jobs Tax Act, pending - If passed, will increase allocation by \$25 Billion and ensure that each locality receives allocation

### **Section 3 – Conclusions**

### Conclusions / Checklist for Issuers

- Outstanding debt:
  - **Check for savings opportunities** With interest rates at such low levels, refundings are producing significant savings. Call your bond counsel or financial advisor and ask for a refunding summary report of all of your outstanding debt.
  - **Continuing Disclosure**: For issuers who have publicly offered debt outstanding, contact your bond counsel or financial advisor to ask if you are in compliance with your continuing disclosure filing. Because of the downgrades of insurers, there has been a flood of required disclosure filings and its important to make sure you are current.

### Conclusions / Checklist for Issuers

- Upcoming Bond Issues:
  - **Alternative Structures**: Evaluate borrowing options under American Recovery and Reinvestment Act to consider alternative structures which may lower debt service costs. Consider giving bidders multiple bidding options.
  - **Credit Ratings**: Because of the downgraded insurers, investors are now focusing more heavily on the underlying credit rating of issuers. Work with your financial advisor or underwriter to evaluate your current credit rating, benchmark your rating against peer issuers and identify areas which need to be improved. Communicate often and early with the rating agencies.

Area	Recovery Zone Economic Development Fund	
	Residual	Residual
South Carolina		115,841,000
Charleston city, SC		720,000
Columbia city, SC		848,000
Albemarle County, NC		1,833,000
Albemarle County, SC		0
Albemarle County, SC		780,000
Anderson County, SC		8,820,000
Bamberg County, SC		814,000
Beaufort County, SC		250,000
Beaufort County, SC		0
Beaufort County, SC	Residual	940,000
Calhoun County, SC		81,000
Charleston County, SC	Residual	1,640,000
Charleston County, SC		6,587,000
Cherokee County, SC		1,759,000
Cherokee County, SC		1,814,000
Clarendon County, SC		1,873,000
Columbia County, SC		1,194,000
Darlington County, SC		17,130,000
Dillon County, SC		810,000
Dorchester County, SC		797,000
Dorchester County, SC		0
Durham County, SC		724,000
Fairfax County, SC		3,515,000
Florence County, SC		0
Georgetown County, SC		4,878,000
Greenville County, SC		3,048,000
Greenville County, SC		1,346,000
Horry County, SC		19,042,000
Jasper County, SC		0
Kershaw County, SC		300,000
Lancaster County, SC		4,515,000
Laurens County, SC		733,000
Lee County, SC		801,000
Lee County, SC	Residual	1,883,000
Lee County, SC		487,000
Madison County, SC		1,730,000
Madison County, SC		1,988,000
Newberry County, SC		1,274,000
Orangeburg County, SC		3,301,000
Orangeburg County, SC		4,900,000
Pickens County, SC		7,504,000
Pickens County, SC	Residual	1,668,000
Saluda County, SC		105,000
South Carolina		3,081,000
Sumter County, SC		4,048,000
Union County, SC		827,000
Williamsburg County, SC		874,000
York County, SC		2,881,000

## Questions

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