

# MUNICIPAL BOND MARKET NOTE

## JANNEY FIXED INCOME STRATEGY

January 10, 2011



The key strength of U.S. state governments is that they are the masters of their own destinies.

States have the sovereign ability to cut spending and increase revenues.

## States' Ability and Willingness to Pay Debt Service Remains Strong

- States have the ability and willingness to pay tax backed debt service.
- Fiscal health has improved over first three quarters in 2010.
- Key strength of states is their sovereign ability to cut spending and increase revenues (taxes).
- See Janney's State Fiscal Health Scorecard for important indicators.

### What is the Condition of States' Fiscal Health?

The fiscal health of most U.S. states has strengthened since the beginning of 2010 and there should be little question in investors' minds about states' ability of willingness to pay tax backed debt obligations. Three quarters of higher overall state tax revenue through 3Q2010 is a positive trend, although receipts are still not back to pre-2007 levels. Now, at the forefront of most investors' minds is what the FY2012 budget negotiations might have in store. Negotiations will undoubtedly be harsh. Most scheduled federal aid has expired and many political actors have still not fully grasped the current economic reality. This could make party politics all too common resulting in political gridlock. An increased amount of headline risk is anticipated. Over the next six months we will have a seat front and center as news of budget negotiations will likely take center stage.

### States Possess Sovereign Power to Modify Budgets

The key strength of state governments, especially where their budgets are concerned, is that they and only they are the masters of their own destinies. This is despite what some lawmakers want observers to believe. In most cases states will be able to balance budgets by making spending cuts. Agreeing on where that pain will take place will be the difficult part. A few states will likely need to

### Top Five Projected Budget Shortfalls

State	Shortfall as a % of Budget	Projected FY2012 Deficit	Spread 10 Year- 1/4/10 (bps)	Spread 10 Year- 1/4/11 (bps)
Illinois	51%	\$17 billion	95	210
New Jersey	37%	\$10 billion	28	54
Nevada	37%	\$1.3 billion	78	80
South Carolina	27%	\$1.3 billion	5	2
Minnesota	25%	\$3.9 billion	3	3

Source: Center on Budget and Policy Priorities, Thomson and Janney FIS.

hike taxes and or fees in order to balance their budgets. The budget situations are dire as a % of FY2011 spending plans in IL and NJ, and NV. While the news of Illinois' tentative budget agreement, which included higher personal income, corporate and cigarette taxes, is encouraging it was not unexpected. Its announcement is an example of states' sovereign authority in action.

### State Fiscal Health Scorecard

On the following page we have listed a collection of relevant data that should give investors an idea of where each state is relative to one another. The data includes where state credit spreads to AAA MMD yields were a year ago and are currently. See the AAA MMD scale for comparison purposes.

### AAA GO Municipal Market Data Yields

Date	1 Year	3 Year	5 Year	7 Year	10 Year	15 Year	20 Year	25 Year	30 Year
January 4, 2011	0.37%	1.05%	1.72%	2.36%	3.18%	3.97%	4.47%	4.66%	4.68%
January 4, 2010	0.30%	0.91%	1.67%	2.43%	3.04%	3.42%	3.77%	4.10%	4.16%
One Year Change	0.07%	0.14%	0.05%	-0.07%	0.14%	0.55%	0.70%	0.56%	0.52%

Source: Thomson Reuters and Janney FIS.

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## Janney State Fiscal Health Scorecard

State	Bond Ratings	Spreads to 10Y MMD Year Ago	Spreads to 10Y MMD- Jan 4, 2011	Projected Budget Shortfalls- (\$MM)	Total % Change in Tax Collections	Net Tax-Supported Debt as % of GDP	State Pension Funding %	Mortgage Foreclosures (All Loans)	Unemploy. Rate
United States	Aaa/AAA/AAA				3.9%			9.40%	9.80%
Alabama	Aa1AA/NR	40	30	\$0	-0.5%	2.20%	77%	10.44%	9.00%
Alaska	Aaa/AA+/AA+	28	25	\$0	-15.0%	1.96%	76%	4.76%	8.00%
Arizona	Aa2/A+/NR	45	38	\$1,400	4.3%	2.24%	80%	10.89%	9.40%
Arkansas	Aa1/AA/NR	30	30	\$0	6.1%	0.92%	87%	8.43%	7.90%
California	A1/A-/A-	146	125	\$19,200	0.6%	4.73%	87%	10.39%	12.40%
Colorado	NR/AA/NR	28	30	\$1,100	5.3%	0.81%	70%	6.36%	8.60%
Connecticut	Aa2/AA/AA	28	21	\$3,700	12.6%	7.91%	62%	8.16%	9.00%
Delaware	Aaa/AAA/AAA	0	0	\$0	11.7%	3.56%	98%	8.32%	8.40%
Florida	Aa1/AAA/AAA	38	38	\$2,500	5.9%	2.80%	101%	10.97%	12.00%
Georgia	Aaa/AAA/AAA	2	2	\$1,700	7.9%	2.77%	92%	12.39%	10.01%
Hawaii	Aa1/AA/AA+	28	27	Yes- unknown	-13.6%	8.11%	69%	6.84%	6.40%
Idaho	Aa1/AA/AA-	32	30	\$300	1.8%	1.58%	93%	7.19%	9.40%
Illinois	A1/A+/A	95	210	\$17,000	2.7%	3.78%	54%	9.97%	9.60%
Indiana	Aaa/AAA/AA+	30	30	\$0	6.9%	1.24%	72%	10.35%	9.80%
Iowa	Aaa/AAA/AAA	27	23	\$294	7.6%	0.16%	89%	6.30%	6.60%
Kansas	Aa1/AA+/NR	70	35	\$492	11.6%	2.62%	59%	7.16%	6.80%
Kentucky	Aa1/AA-/AA	40	28	\$780	5.8%	4.65%	64%	8.85%	10.02%
Louisiana	Aa2/AA-/AA	40	33	\$1,700	-7.5%	2.57%	70%	10.61%	8.20%
Maine	Aa2/AA/AA+	28	25	\$436	7.6%	2.02%	80%	8.52%	7.30%
Maryland	Aaa/AAA/AAA	0	0	\$1,600	5.8%	3.35%	78%	9.78%	7.40%
Massachusetts	Aa1/AA/AA+	24	28	\$2,000	10.2%	8.32%	63%	8.80%	8.20%
Michigan	Aa2/AA-/AA-	110	80	\$1,400	1.4%	1.95%	84%	11.41%	12.40%
Minnesota	Aa1/AAA/AAA	3	3	\$3,900	11.4%	2.08%	81%	6.45%	7.10%
Mississippi	Aa2/AA/AA+	37	32	\$634	4.0%	4.75%	73%	13.66%	9.90%
Missouri	Aaa/AAA/AAA	3	0	\$1,100	2.6%	1.96%	83%	8.81%	9.40%
Montana	Aa1/AA/AA+	30	25	\$154	11.3%	0.97%	84%	5.11%	7.20%
Nebraska	Aa2/AA+/NR	30	40	\$314	2.8%	0.03%	92%	5.85%	4.60%
Nevada	Aa1/AA+/AA+	78	80	\$1,300	ND	1.86%	76%	13.23%	14.30%
New Hampshire	Aa1/AA/AA+	20	16	\$0	0.2%	1.47%	68%	8.20%	5.40%
New Jersey	Aa2/AA/AA	28	54	\$10,500	1.7%	6.73%	73%	8.78%	9.20%
New Mexico	Aaa/AA+/NR	30	24	\$410	ND	3.52%	83%	7.42%	8.50%
New York	Aa2/AA/AA	30	31	\$9,000	4.5%	5.35%	107%	8.80%	8.30%
North Carolina	Aaa/AAA/AAA	0	1	\$3,800	6.8%	1.79%	99%	9.39%	9.70%
North Dakota	Aa1/AA+/NR	30	30	\$0	29.5%	0.68%	87%	3.54%	3.80%
Ohio	Aa1/AA+/AA-	35	32	\$3,000	6.6%	2.28%	87%	10.03%	9.80%
Oklahoma	Aa2/AA+/AA+	35	28	Yes- unknown	9.0%	1.43%	61%	7.93%	6.90%
Oregon	Aa1/AA/AA+	30	24	\$1,800	6.7%	4.40%	80%	6.30%	10.60%
Pennsylvania	Aa1/AA/AA+	19	17	\$2,400	5.9%	2.14%	87%	8.77%	8.60%
Rhode Island	Aa2/AA/AA	40	50	\$290	10.7%	4.73%	61%	10.44%	11.60%
South Carolina	Aaa/AA+/AAA	5	2	\$1,300	2.8%	2.68%	70%	9.63%	10.60%
South Dakota	A1/AA/AA	30	40	\$0	-3.1%	0.30%	97%	4.57%	4.50%
Tennessee	Aaa/AA+/AAA	6	4	Yes- unknown	4.0%	0.79%	95%	10.47%	9.40%
Texas	Aaa/AA+/AAA	22	26	\$10,000	4.8%	1.05%	91%	9.28%	8.20%
Utah	Aaa/AAA/AAA	4	2	\$0	19.9%	2.43%	84%	8.11%	7.50%
Vermont	Aaa/AA+/AAA	20	18	\$112	5.8%	1.73%	88%	5.59%	5.70%
Virginia	Aaa/AAA/AAA	0	0	\$2,300	-1.5%	1.78%	84%	7.31%	6.80%
Washington	Aa1/AA+/AA+	34	24	\$2,900	3.1%	4.60%	100%	7.27%	9.20%
West Virginia	Aa1/AA/AA	32	35	\$155	17.8%	3.18%	64%	9.83%	9.30%
Wisconsin	Aa2/AA/AA	42	30	\$1,800	5.5%	4.05%	100%	6.65%	7.60%
Wyoming	NR/AA+/NR	33	30	\$0	0.7%	0.12%	79%	5.23%	6.60%

Sources: Janney Fixed Income Strategy; spreads are per Thomson Reuters; projected budget shortfalls from Center on Budget and Policy Priorities Dec 16, 2010; % change in tax revenue is 3Q2010 to 3Q2009 and per the Rockefeller Institute. Alaska's change actual change was -48.1%; NTSD to state GDP is per Moody's May 2010 State Debt Medians Report; State pension data from Pew 2010 report (most data is actually from 2008). A plan 80% funded is considered healthy by the GAO; Mortgage foreclosure data from the Mortgage Bankers Association 2Q 2010; and Unemployment rate per the Bureau of Labor Statistics as of Nov 2010.

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