BOND MARKET UPDATE

Official Conference Title

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GEORGIA PUBLIC FINANCE

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SECTION 1

Bond Market Basics

LEGAL MECHANISMS FOR LONG-TERM BORROWING

General Obligation
Requires voter approval
Unlimited full, faith and credit tax-backing
Not subject to annual appropriation

Revenue Bonds
Security is dependent upon the strength of pledged payments from a particular enterprise

Intergovernmental Contract
Contract between local government and an Authority with the legal ability to construct a particular project
Limited to statutory M&O taxing limits (i.e. 20-mill, limit for school districts)
Not subject to annual appropriation

Lease
Subject to annual appropriation
Limited to statutory M&O taxing limits
Total amounts limited to 7.5% of prior years local tax receipts (Sales tax issues)

BOND PRICING

Every bond has three characteristics: coupon, yield and price.

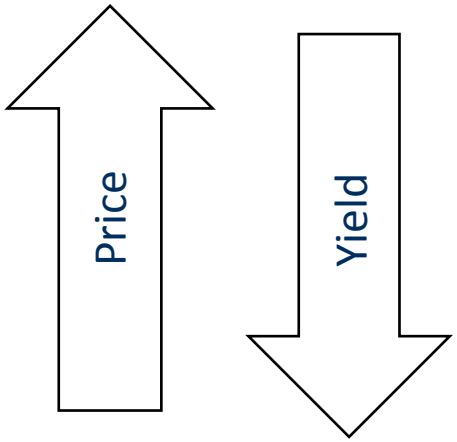
Coupon – The stated rate on the bond
A $100,000 maturity with a 5% coupon will pay $5,000 a year in interest.

Yield – Indicates the total cost to the issuer of the bonds.
The key for investors and issuers.

Price – The amount paid by the investors for the bonds.

Price and Yield have an inverse relationship.

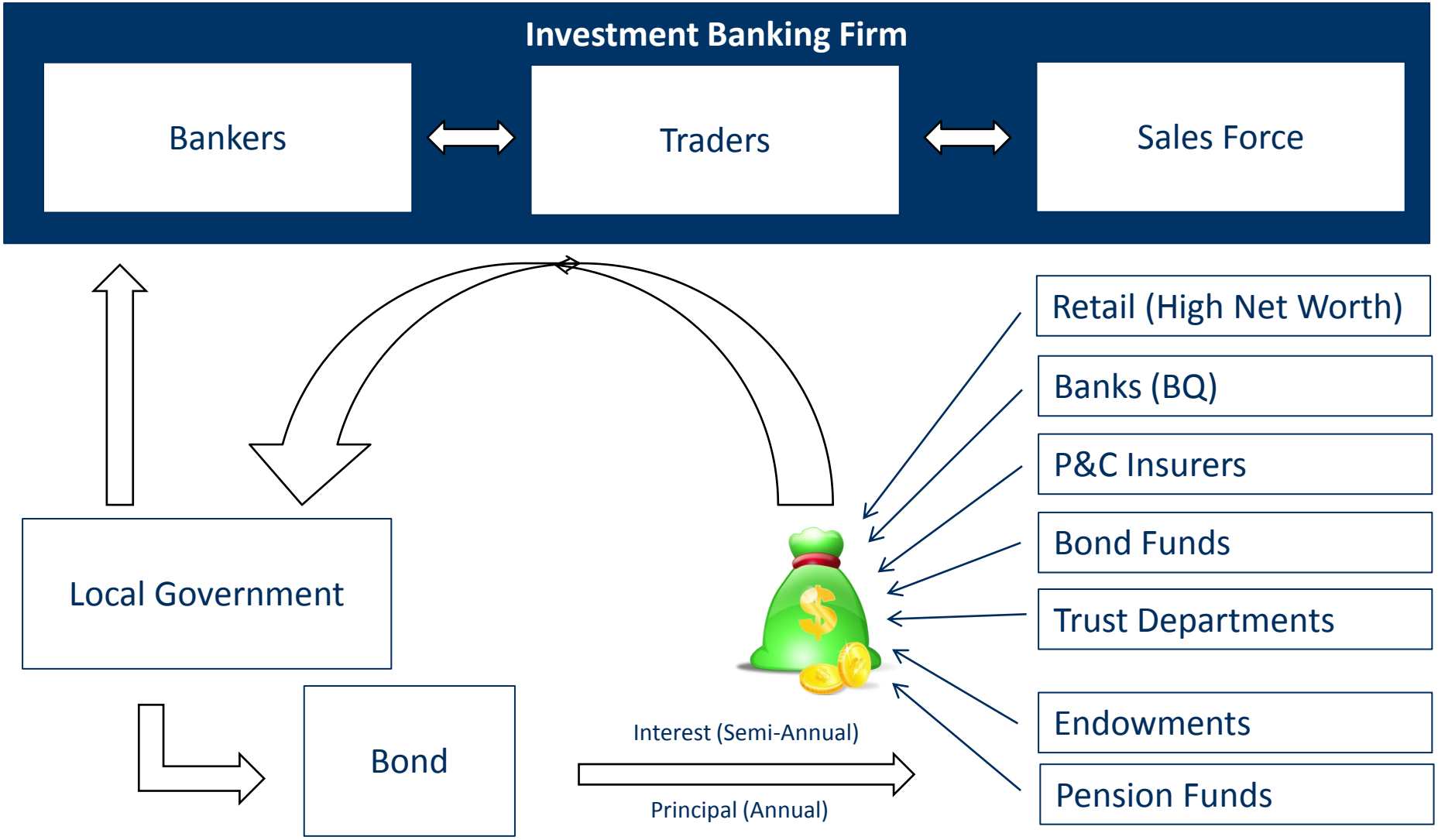
If an investor pays a higher price for a set stream of cash flows the yield (return on investment) will be less.



BOND PRICING

	Par		Premium		Discount	
Total Par	100,000		98,106		101,968	
Coupon	5.00%		5.25%		4.75%	
Yield	5.00%		5.00%		5.00%	
Price	$100.00		$101.93		$98.07	
Proceeds	$100,000		$100,000		$100,000	
Year	**Payments**	**PV Payments**	**Payments**	**PV Payments**	**Payments**	**PV Payments**
1	5,000	4,762	5,151	4,905	4,843	4,613
2	5,000	4,535	5,151	4,672	4,843	4,393
3	5,000	4,319	5,151	4,449	4,843	4,184
4	5,000	4,114	5,151	4,237	4,843	3,985
5	5,000	3,918	5,151	4,036	4,843	3,795
6	5,000	3,731	5,151	3,843	4,843	3,614
7	5,000	3,553	5,151	3,660	4,843	3,442
8	5,000	3,384	5,151	3,486	4,843	3,278
9	5,000	3,223	5,151	3,320	4,843	3,122
10	105,000	64,461	103,257	63,391	106,811	65,573
	150,000	**100,000**	**149,612**	**100,000**	**150,403**	**100,000**

WHERE DO INVESTMENT BANKS SELL BONDS?



MARKETING OF BONDS

Premium or Discount

Ratings

Liquidity

Call Features

Municipal Bond Insurance

Debt Service Reserve

Serial Bonds and/or Term Bonds

SECTION 2

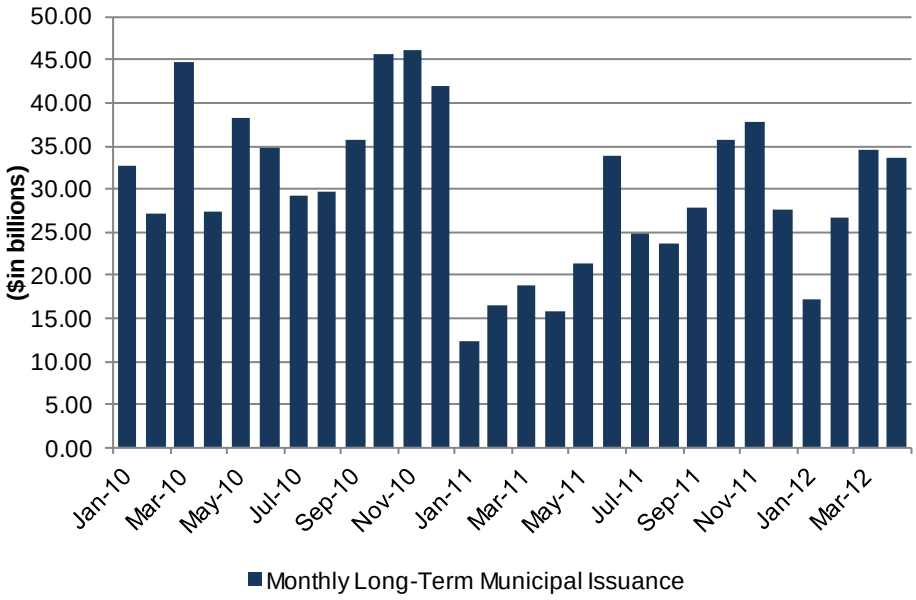
Current Market Update

MUNICIPAL LONG-TERM ISSUANCE

Long-term municipal new issue volume was down 31.5% in 2011 compared to 2010, and is up 63.5% year-to-date versus 2011.

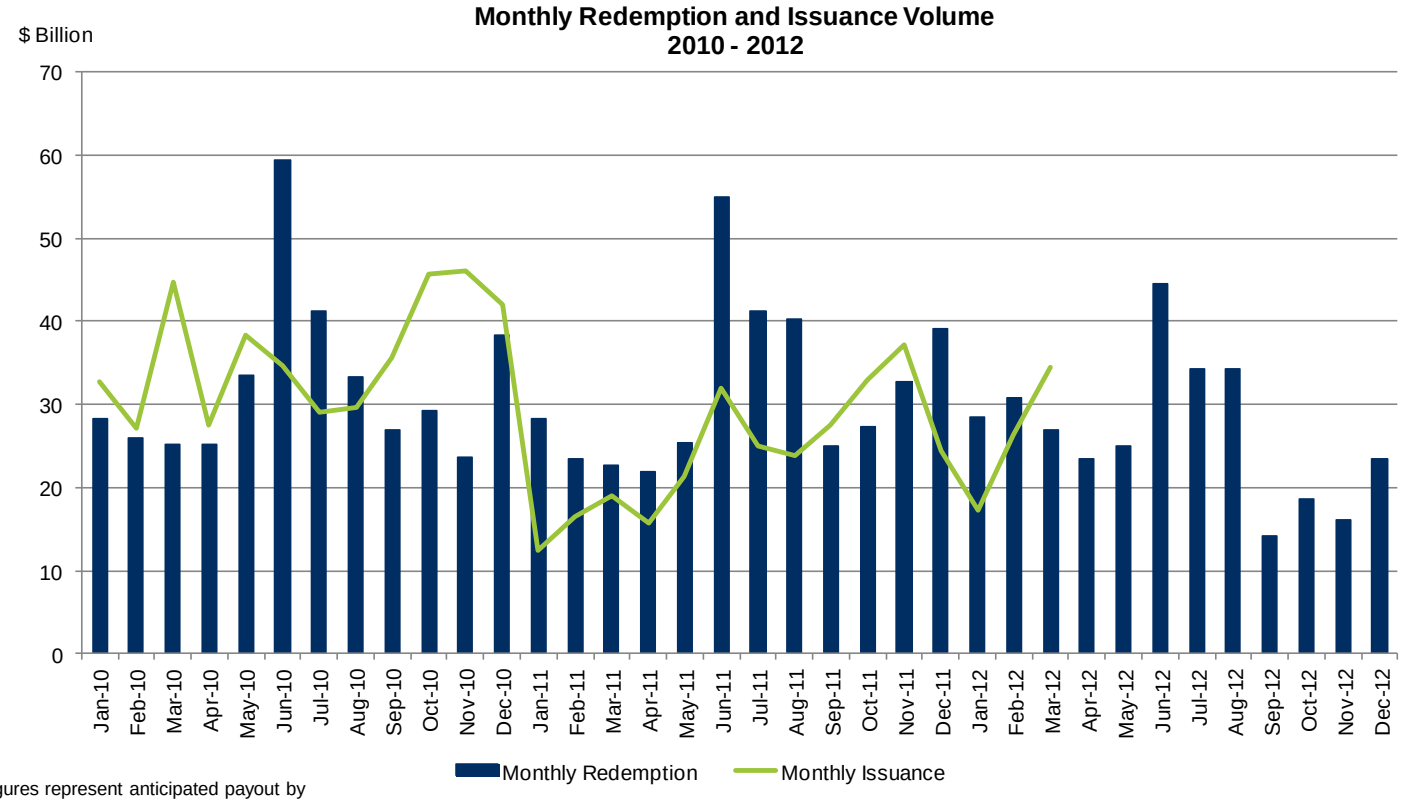
Municipal Long-Term Issuance				
$ in billions	2010	2011	2012	YoY %
January	$32.660	$12.445	$17.200	38%
February	27.055	16.535	26.723	62%
March	44.693	18.911	34.645	83%
April	27.498	15.756	33.639	113%
May	38.324	21.377		-44%
June	34.682	33.978		-2%
July	29.152	24.930		-14%
August	29.708	23.799		-20%
September	35.645	27.906		-22%
October	45.730	35.745		-22%
November	46.070	37.734		-18%
December	42.051	27.579		-34%
Total	$433.269	$296.694	$112.208	

Source: The Bond Buyer



MONTHLY MUNICIPAL BOND REDEMPTIONS

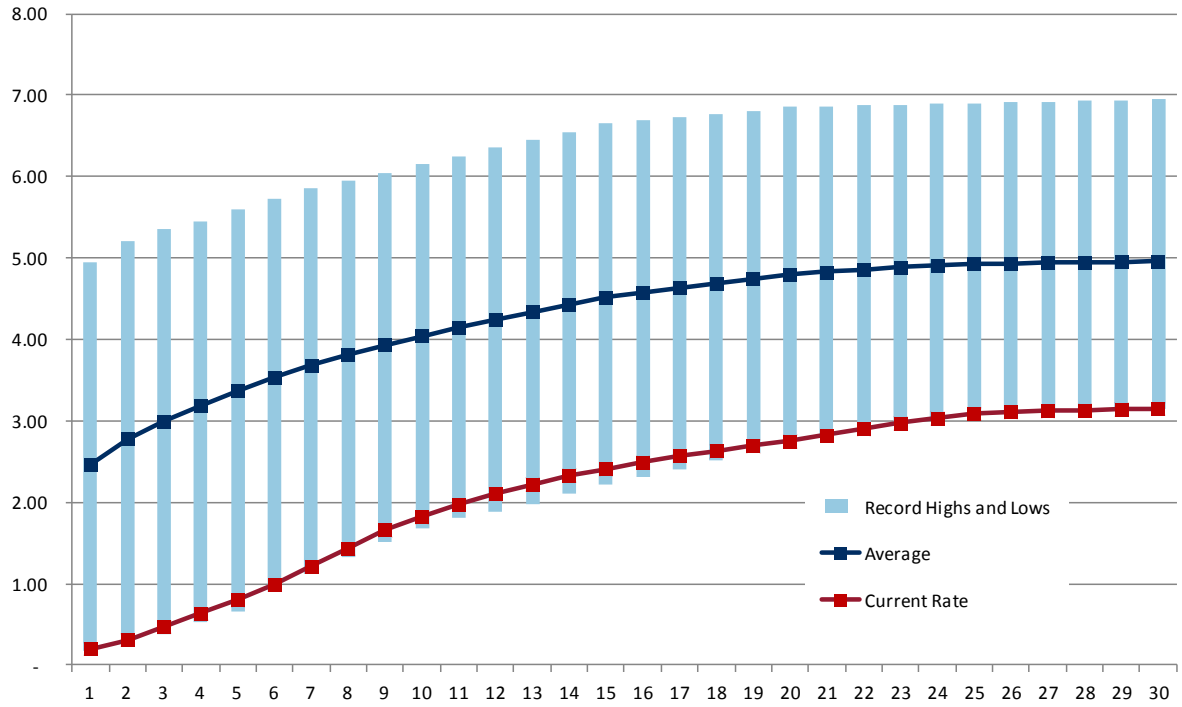
- Monthly redemption indicates June has the highest redemption volume in the last three years, and the trend will continue in 2012.
- Redemptions in January 2012 totaled $28 billion, unchanged from the monthly volume in the last two years.
- The large amount of redemption dollars (a source of market demand), together with low monthly issuance ($17 billion), pushed MMD yields to all-time lows in January.



Source: MuniView; Figures represent anticipated payout by municipal issuers

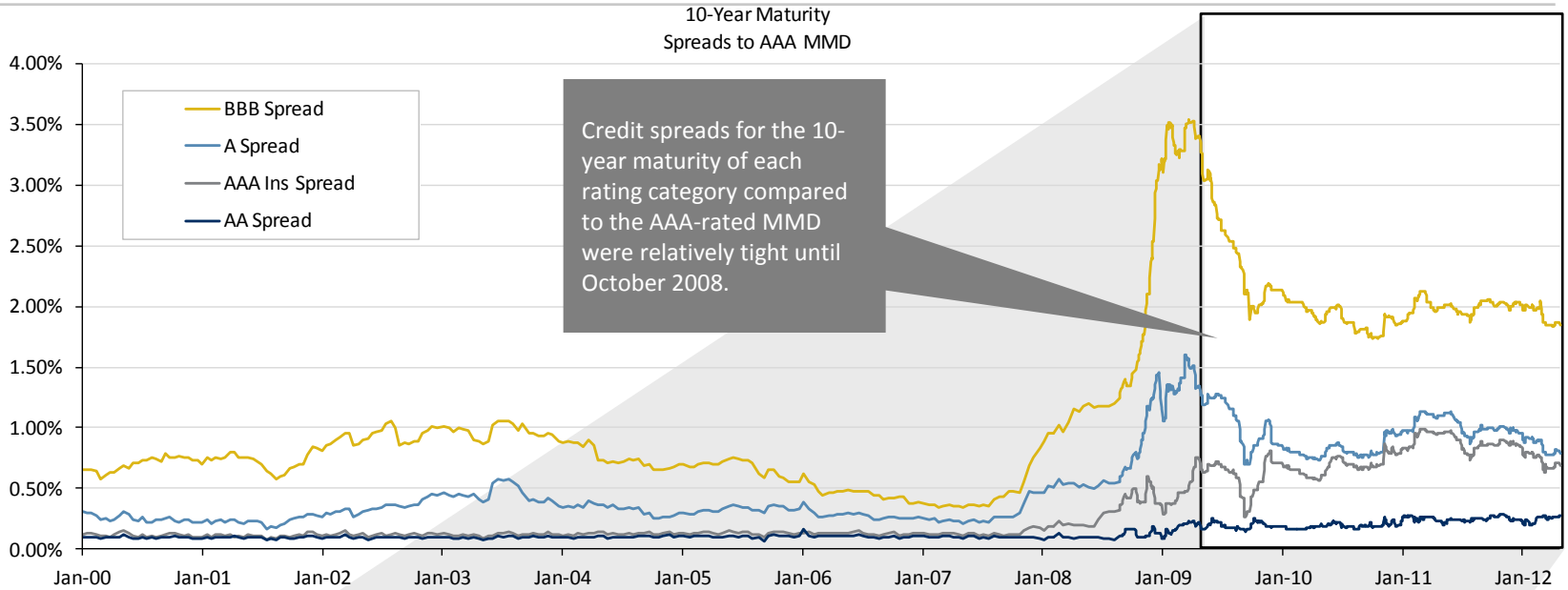
HISTORICAL AAA MMD RATES

- The graph below shows the range between the record highs and lows of AAA MMD at each maturity since 1993, along with the average rate over this time frame and the current rate.
- AAA MMD rates are currently near the lowest they have been since 1993.



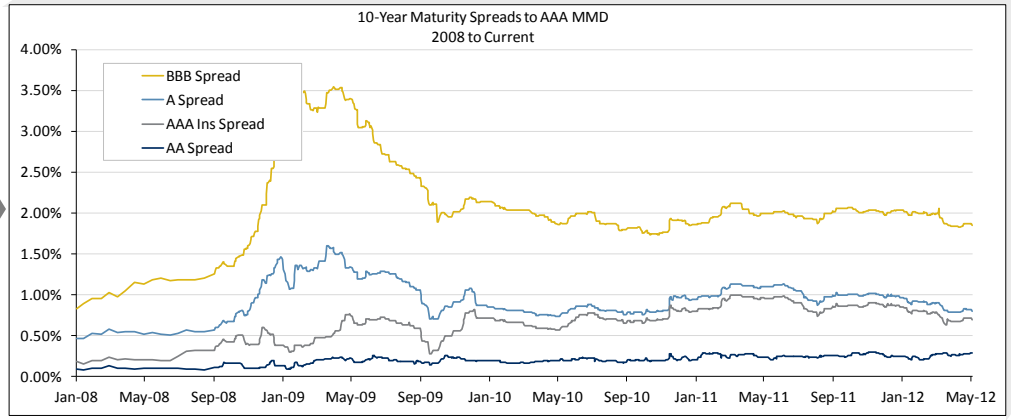
	1	5	10	15	20	25	30
Record Low	0.18	0.65	1.67	2.21	2.70	3.08	3.14
Record High	4.95	5.60	6.15	6.65	6.85	6.90	6.95
Average	2.46	3.36	4.04	4.52	4.80	4.93	4.96
Current	0.20	0.80	1.82	2.41	2.75	3.09	3.15

HISTORICAL CREDIT SPREADS TO AAA MMD

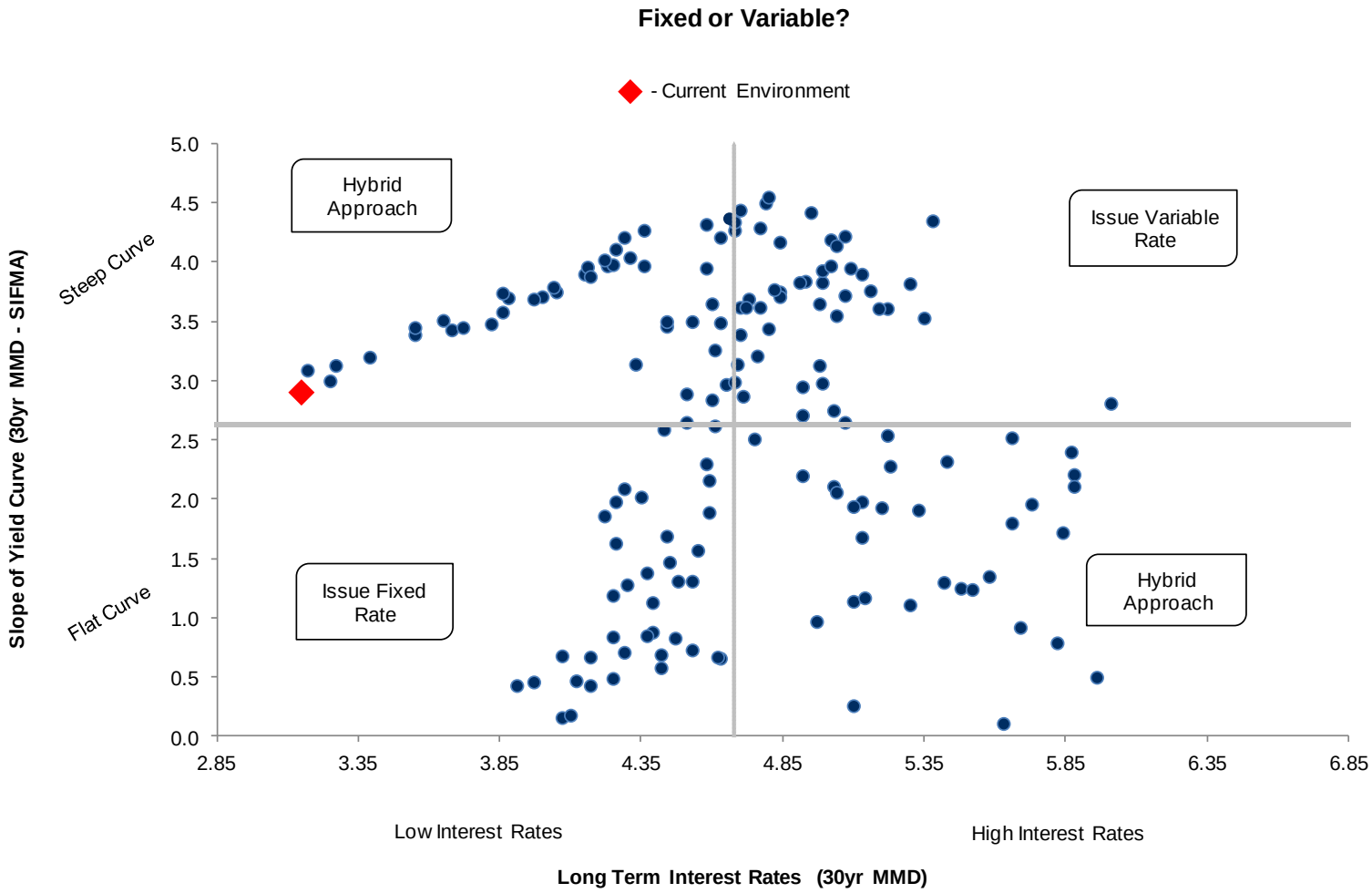


Credit spreads for the 10-year maturity of each rating category compared to the AAA-rated MMD were relatively tight until October 2008.

At the start of the credit crisis in October 2008, spreads began to rise well above the AAA MMD, reflecting concerns with underlying credit quality.



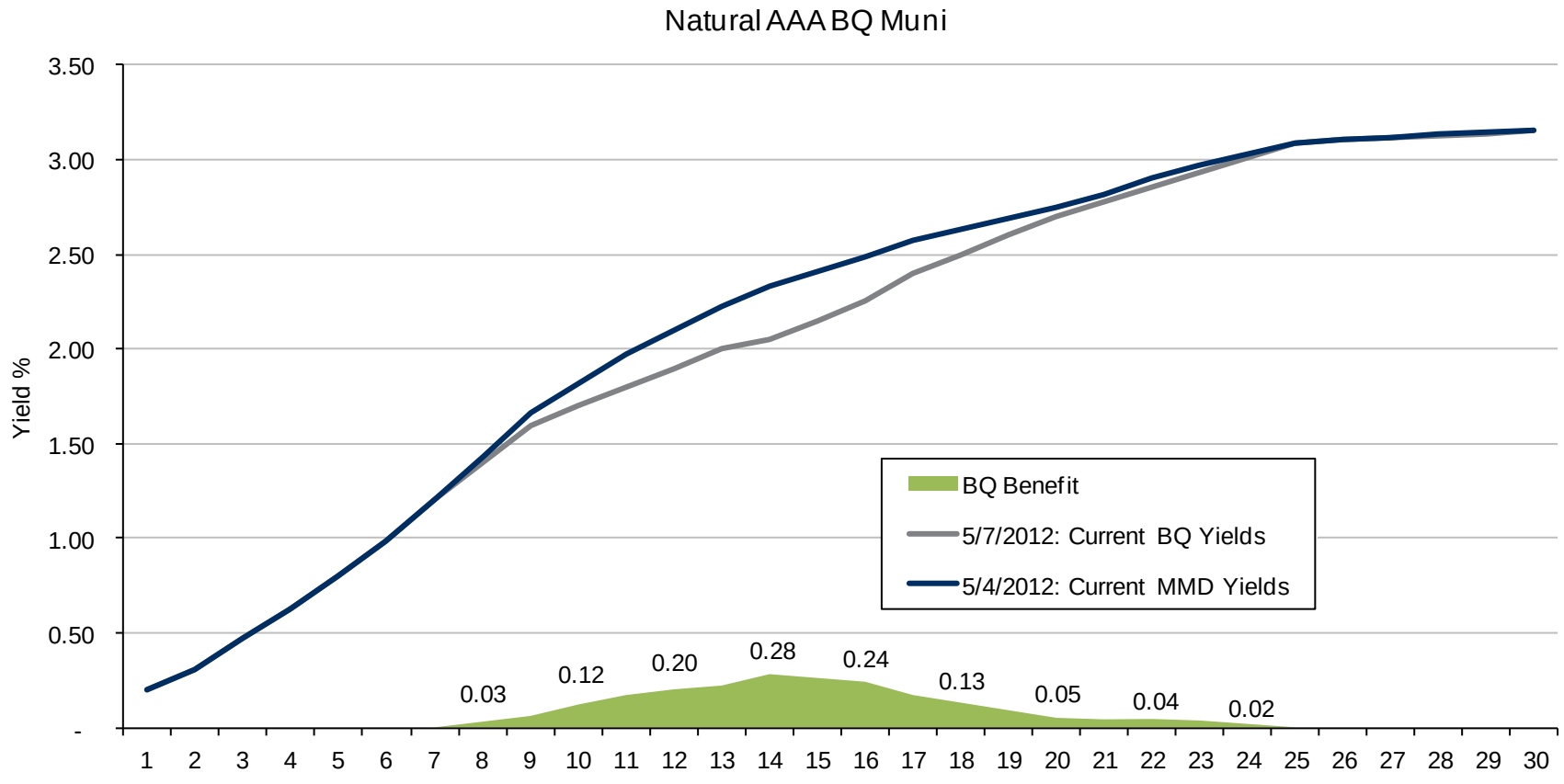
INTEREST RATE ENVIRONMENT SINCE 1/1/1999



*Data points represent monthly rates since 1/1/1999.

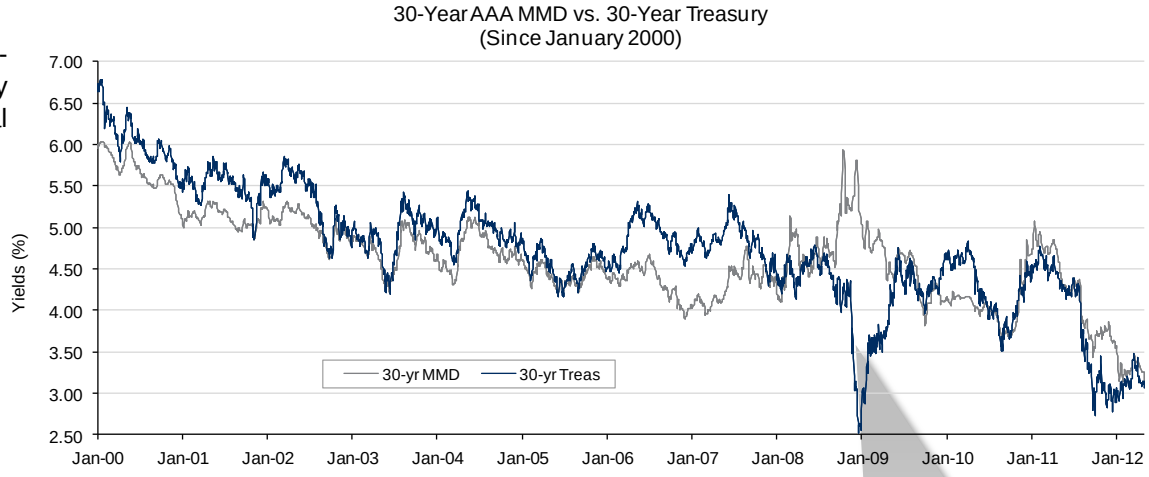
CURRENT AAA BANK QUALIFIED CURVE VS. MMD

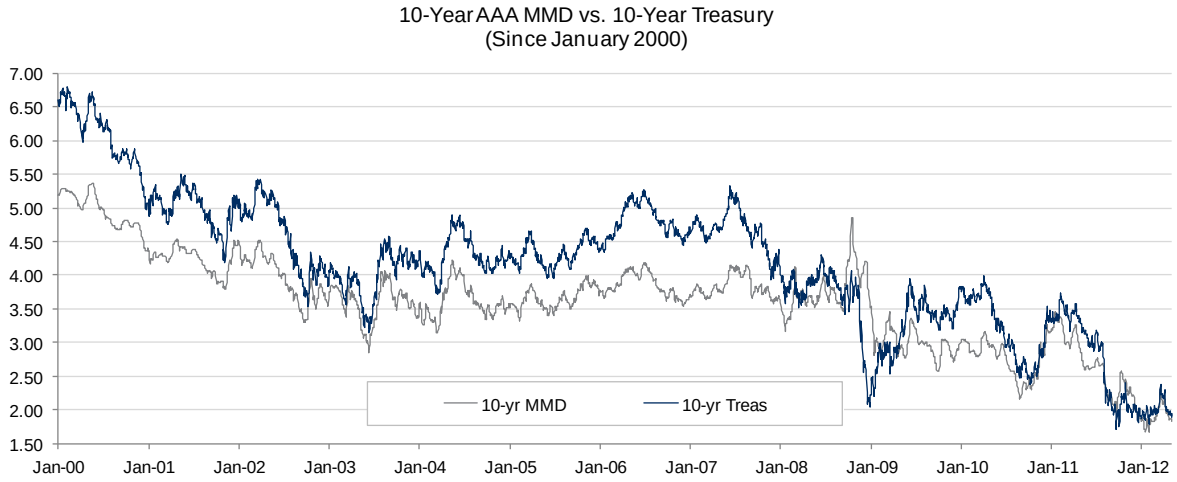
The current AAA BQ Yield Curve is shown below in comparison to today's AAA MMD curve. The greatest benefit for BQ deals is usually seen in the 10-year to 20-year range of the curve.



RELATIONSHIP OF AAA MMD TO TREASURIES

The spread relationship between the 10-Year and 30-Year taxable and tax-exempt curves has been relatively consistent until the recent turmoil in the financial markets.

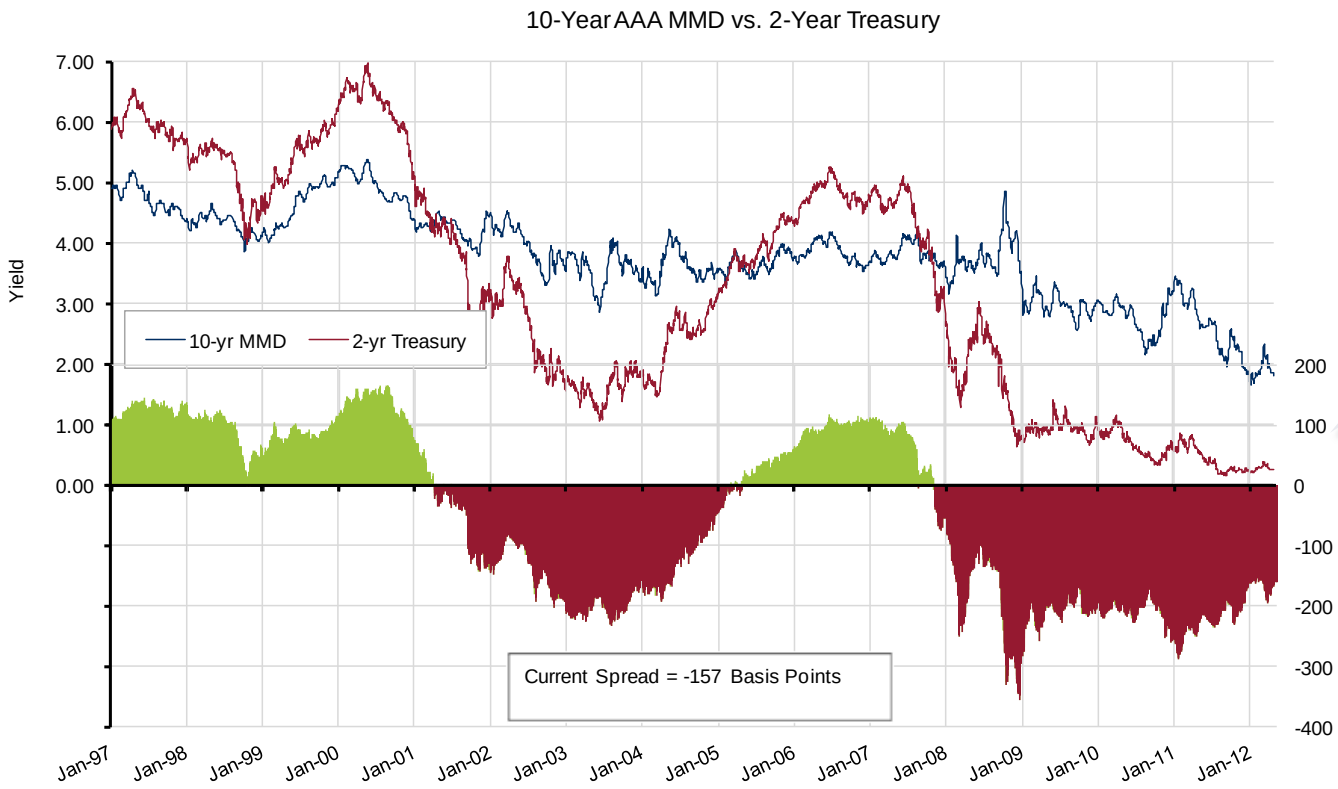




In late 2008, ratios inverted as investors preferred to purchase U.S. Treasuries. The ratios are trending back to historical levels indicating that investors are seeking investments with higher yields than Treasuries.

NEGATIVE ARBITRAGE: RECENT CHANGES BEWTEEN AAA MMD AND TREASURIES

- State and Local Government Securities, or SLGS, are special Treasury securities sold by the United States Treasury Department to states, municipalities, and other local government bodies. SLGS are most commonly used as investments in an escrow account in connection with the issuance of refunding bonds. SLGS yields are derived from Treasuries.
- Negative arbitrage is the difference between the actual investment earnings in the escrow (the yield on the SLGS) and the investment earnings that can legally be earned in the escrow (the arbitrage yield on the refunding bonds).



- The 10-yr MMD is used as a proxy for refunding bonds and the 2-yr Treasury is used as a proxy for escrow accounts.

Negative arbitrage continues to be a problem as spreads between short-term treasury yields and AAA MMD yields remain relatively wide.

Red represents periods of negative arbitrage while green represents times of favorable arbitrage.

RATE FORECAST

- Both the Morgan Keegan economist (Dr. Donald Ratajczak) and the Bloomberg consensus of economists predict that rates will rise over the next year and a half.

Morgan Keegan Economist

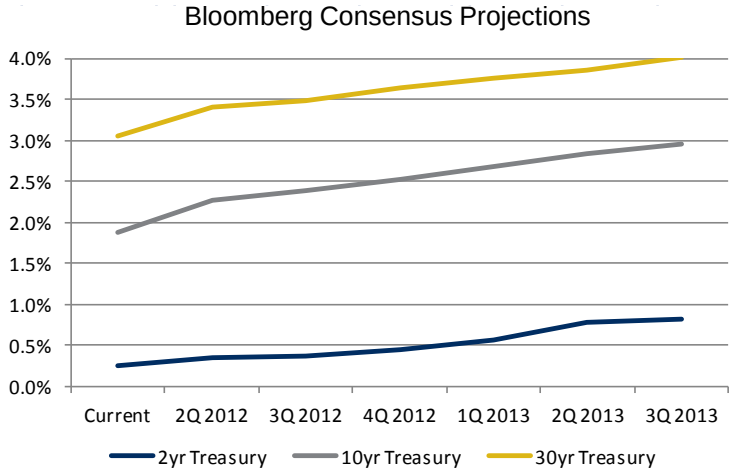
US Treasury	Current Rate	2012			2013			Increase from
		2Q	3Q	4Q	Q1	Q2	Q3	current to 2013 Q3
2 Year	0.26%	0.26%	0.27%	0.33%	0.40%	0.51%	0.63%	0.37%
10 Year	1.88%	1.97%	1.98%	2.06%	2.24%	2.43%	2.62%	0.74%
30 Year	3.06%	3.12%	3.13%	3.18%	3.32%	3.53%	3.72%	0.66%

*As of May 7, 2012.

Bloomberg Consensus

US Treasury	Current Rate	2012			2013			Increase from
		2Q	3Q	4Q	Q1	Q2	Q3	current to 2013 Q2
2 Year	0.26%	0.35%	0.38%	0.45%	0.57%	0.79%	0.83%	0.53%
Economists Surveyed	-	64	64	64	59	53	49	
10 Year	1.88%	2.28%	2.38%	2.53%	2.69%	2.84%	2.96%	0.96%
Economists Surveyed	-	79	78	79	74	68	62	
30 Year	3.06%	3.41%	3.49%	3.64%	3.77%	3.85%	4.01%	0.79%
Economists Surveyed	-	61	61	61	57	52	49	

*Source: Bloomberg as of May 7, 2012.



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