

# CITY OF HOUSTON

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To: Budget and Fiscal Affairs Committee From: Finance Working Group

**Cc:** Date: July 2, 2012

Subject: Combined Utility System First Lien Revenue Bonds Series 2012C

(Series 2010B Conversion)

#### **Finance Working Group Recommendation**

- Refinance and maintain existing index floating structure
- Establish a 4-year term
- Select RBC Capital Markets Corporation to remarket the bonds

### **Background**

The Combined Utility System's liquidity needs consist of a \$700 million commercial paper program, almost \$600 million of variable rate demand bonds, and about \$475 million of SIFMA Index Floaters (see Table 1).

In 2008, the market experienced a sharp decline in the amount of credit available and a significant increase in the fees associated with provision of variable rate debt.

The Securities Industry and Financial Markets Association (SIFMA) indexed notes, which did not require credit proved to be a viable option. The SIFMA notes trade at SIFMA plus a fixed rate spread. In the 2010 market environment, the spread for a privately placed note transaction ranged from 130-140 bps for an essential service credit with a split rating. On March 18, 2010, RBC directly purchased \$249.08 million of index floaters, Series 2010B-1, B-2, at a spread of 130 basis points (or 1.30%) for a term of 3 years. The City is required to refund the bonds by March 2013. However, spreads, or the fixed rate constants, on this product have come down considerably.

The existing agreement with RBC does not expire until March 2013. RBC has agreed to end the agreement early, at no charge to the City, provided that they are selected to remarket these bonds.

## **Recommendation Rationale**

- Maintain existing index floating structure
  - o This structure does not require bank exposure, and instead involves selling the bonds to investors for a period of time that is typically inside of 5 years. The variable rate exposure of the CUS remains below the City's maximum policy target of 20%.
  - See Attachment 1 for savings analysis
- Establish a 4-year term (staggers term from the 3-year and 5-year tranches just completed)
  - Staggered maturities reduce the remarketing risk at the end of the term.
- Select RBC Capital Markets Corporation to remarket the bonds
  - o Allowing RBC to remarket bonds will enable the City to end original agreement before March 2013 expiration and go out to market while rates are still favorable.

**Table 1: CUS Liquidity Summary** 

Liquidity Type	Series	Size (\$ millions)	Bank	Expiration	Requires Bank Letter of Credit
Commercial Paper	B-1	250	JPMorgan Chase	12/16/2013	
	B-2	75	Wells Fargo	12/14/2012	
	B-3	75	Bank of Tokyo-Mitsubishi	1/20/2015	V
	B-4	100	Barclay's	7/15/2013	Υ
	B-5	100	BBVA	5/27/2015	
	B-6	100	Citibank	7/15/2013	
	Total	700			
	•				
Variable Rate Demand Bonds	2004B-2	100	State Street	4/5/2013	
	2004B-3	75	Sumitomo	4/3/2015	
	2004B-4	75	JPMorgan Chase	4/6/2013	Y
	2004B-5	100	Lloyd's	4/6/2013	
	2004B-6	78.33	Sumitomo	4/3/2015	
	2008D-1	132.01	JPMorgan Chase	12/31/2012	
	Total	560.34			
	Subtotal	1,260.34			
SIFMA Index Floater	2010 B-1	200	RBC	3/22/2013	
	2010 B-2	49.08	RBC	3/23/2013	N
	2012A	125	Loop Capital Markets	6/1/2015	
	2012B	100	Wells Fargo Securities	6/1/2017	
	Total	474.08			
	TOTAL	1,734.42	18.5%	*	
Total Outstanding Debt		5,966.92	·	=	

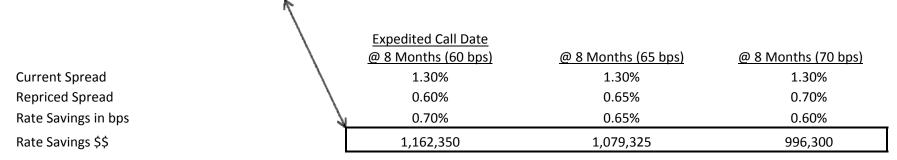
<sup>\*</sup> The percentage of variable rate exposure includes \$902 million of hedged debt and \$70.4 million of commercial paper. The calculation does not include the entire \$700 million commercial paper program.

## **Attachment 1: Cost Comparison**

SUMMARY: As shown below, a 4-year Index Floater will save the City approximately \$1.0 - 1.2 million over maintaining the current structure at the higher spread.

## **Savings from Refunding the CUS 2010B SIFMA Index Notes**

Call Date	3/22/2013
Par Amount:	249,075,000
Close Date:	7/27/2012
# of Months	8 months
Estimated Savings:	\$1.0- \$1.2 million



#### Notes:

Please note that the placement fee that we will pay the underwriters is not included in this comparison because the Combined Utility System will be required to pay this fee in FY13 regardless of the execution date (July 2012 or March 2013).