RSW INVESTMENTS

How Systemic is the "Rot"? (5/11/16)

Today's front page of the *New York Times* Business Section lead story was entitled "A Harbinger of U.S. Woes – Puerto Rico's Fiscal Fiasco Is Facing Many Troubled Cities and States".

- At this time, we continue to stress to our clients that while we do not downplay the message of the article, it appears that the author is attempting to "paint" the municipal bond market with a broad brush.
- Certainly there are "pockets of rot", and we are acutely aware of the obstacles that confront many fiscally challenged municipal issuers, as cited in the article.
- Just as important, is that our analysis and portfolio selection is proactive and not reactive. RSW's outlook is forward looking, seeking to avoid issuers with structural budgetary imbalances that rely on "one shot" solutions. To date, RSW client portfolios have not felt the consequences of the previous Great Recession and the weak recovery.
- In addition, we avoid issuers with excessive unfunded pension liabilities that ultimately should prove to be beyond solution without fiscal consequence.
- RSW's long standing credit discipline does not include the investment in marginally investment grade or non-investment grade bonds.

We have always sought to share our market and issuer views with candor, clarity and consistency. For example, in the recent past we have said:

From: 1st Quarter Fixed Income Newsletter (4/6/2016):

…Storm clouds continue to gather in other states as well. For example, Pennsylvania went more than 6 months without a budget, with a stalemate finally brokered without any substantive attempt to deal with growing pension liabilities. After two recent billion dollar plus tax increases, Connecticut is trying to balance the books for this year and still confronts a billion dollar gap for the fiscal year starting July 1.

Pension issues in Chicago and Illinois (is New Jersey next?) are not to be resolved without further hardship to taxpayers and bondholders. The deterioration in these credits is well known and will only prove to get worse.

There are no magic wands in the municipal market that can cure these issues.

From 2015 Q1 Quarterly Commentary (4/17/2015):

-While state and local governments have cut billions in spending, pressures persist especially in core areas such as health and education, notwithstanding the "800 pound gorilla in the room" – pension liabilities.

From 2014 Q2 Quarterly Commentary (7/14/14):

Structural and fundamental credit weakness was always apparent even when the Commonwealth and its various public authority debt ratings were in the "A" category. With that in mind, RSW has never invested client funds in any Puerto Rico obligations. Professional municipal market participants should not be surprised by what some may consider the recent and rapid deterioration in the Commonwealth's various bonding programs for the systemic weakness was always apparent and became "as clear as day" during the past recession and the weak recovery that bypassed Puerto Rico.

As always, thank you for your trust and confidence, and we look forward to keeping you informed.