Municipal Bond Market Monthly

JANNEY FIXED INCOME STRATEGY

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A Mid-Year Municipal Market Review and Outlook

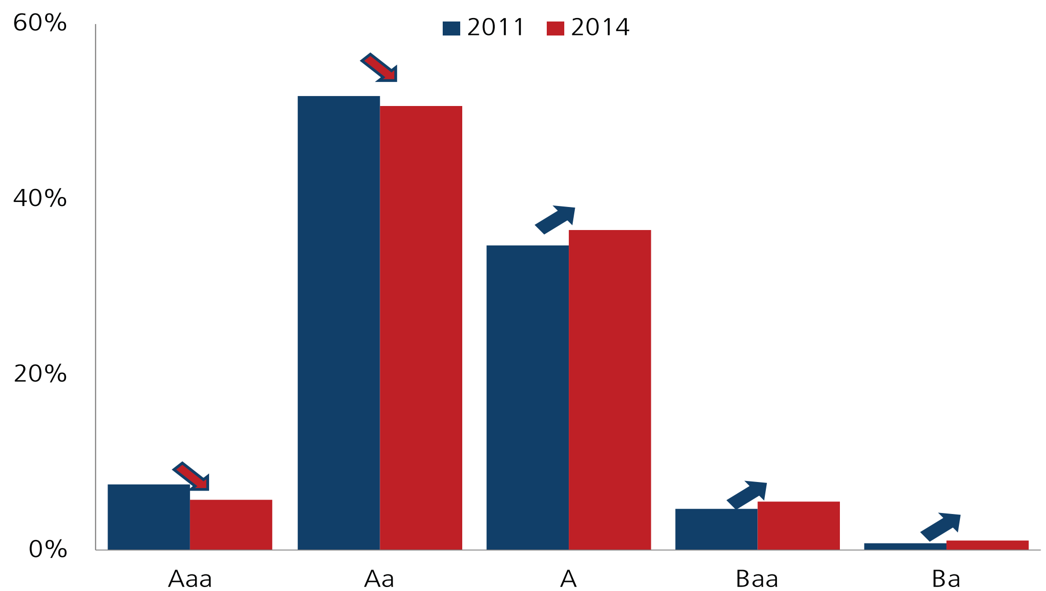
- In a relatively short period of time, the fixed income community went from not paying close attention to municipal credit- to vehemently defending municipals and now, despite its still generally high rating level, may be missing some important trends showing some credit deterioration.
- We recommend investors consider only high quality municipal bonds, especially in the local government sector. Municipals are still an important fixed income option, but credit selection remains increasingly important.
- Although less than 30% of Detroit Water and Sewer bonds were recently tendered, the city accepted. Detroit's challenge to the Chp. 9 bankruptcy code protection of "special revenue" bond treatment was replaced by a more consensual process, which is a positive development for the municipal market.
- Municipal bond performance was strikingly positive for most municipal related indices. This defied most analysts' expectations.
- D.C. interference has not materialized in 2014. A March 2015 deadline, the underfunding of the Social Security Disability Trust Fund, and federal deficit projections could ignite tax reform conversations in coming years. But, nothing is imminent
- Pennsylvania downgraded by Moody's; New York upgraded by S&P; Illinois' outlook lowered by S&P; Kansas' downgraded by S&P; Pittsburgh, PA outlook raised by Moody's; Pennsylvania Housing Finance Agency's outlook raised by S&P; and NJ Housing and Mortgage Finance Agency downgraded by Moody's.

Municipal Credit

A Review & Update on the Status of Municipal Credit Conditions

The closing weeks of the summer season are upon us. The baseball season is winding down (it finished a few weeks ago where the Phillies are concerned), the English Premier League season just began, and Janney's summer interns recently left to begin a new school year. Most will soon graduate.

Municipal Credit Quality Remains High, but has Fallen Slightly Recently



Source: Moody's rating distribution of about 15,000 rated public finance entities and Janney FIS.

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Our interns presence gave us ideas and also offered perspective.

Perspective because most of them started their undergraduate studies, mostly in finance and economics related majors, the year after Meredith Whitney's municipal market forecast.

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This was one of the best classes of interns we have had the pleasure to work with. They were eager, intelligent and full of ideas. It is much easier to deliver high quality work when surrounded by sharp and challenging minds. Their presence energized our efforts. Their presence and ideas also offered perspective. Perspective because most of them started their undergraduate studies, mostly in finance and economics related majors, the year after Meredith Whitney's municipal market forecast. And, this summer was really the first year we found that we had to explain in detail who Whitney was, what she said, what the effects on the market were afterward, and then as their eyes glazed over we then found ourselves explaining some of the details about the events that led up to the Great Recession. Because, after all, much of our intern class was just starting high school around the time Bear, Stearns "merged" with J.P. Morgan and Lehman Brothers filed for Chapter 11 bankruptcy.

Janney Municipal Sector Credit Outlook and Review

Sector	Janney Credit Outlook	Last Month Change	Barclay's 12 Month Return	Key Sector Trends	Recent Janney Sector Review
Municipal Bond Index	-	-	7.27%	Barclay's Muni Index, 46k issues	-
State Government	Stable	Same	6.20%	1Q14 tax revs were lower, 2Q14 prob lower too	Aug 2014 Note
Local Government	Cautious	Same	7.33%	Budgets squeezed, downgrades outpace upgrades	Feb 2014 MBMM
School Districts	Cautious	Same	-	Credit deterioration will continue, but remain limited	Feb 2014 MBMM
Airports	Stable	Same	8.80%	Sector stabilizing, consolidations largely finished	May 2014 Note
Health Care	Cautious	Same	9.87%	Reimbursement uncertainty, margins pressured	Feb 2014 MBMM
Higher Education	Cautious	Same	7.91%	Enrollment declines equal financial stress	Feb 2014 MBMM
Housing	Stable	Same	7.31%	Some benefits for HFAs from higher interest rates	Feb 2014 MBMM
Public Power (Elec.)	Stable	Same	5.90%	Essential purpose nature enhances stability	Feb 2014 MBMM
Tobacco	Cautious	Same	N/A	More downgrades, consumption dropping	May 2014 MBMM
Toll Facilities	Cautious	Same	8.80%	Activity is leveling off, but still near 2004 levels	Feb 2014 MBMM
Water and Sewer	Stable	Same	8.32%	Essentiality factor, system upgrades looming	Feb 2014 MBMM

Source: Barclay's Capital as of August 4th and Janney FIS.

During many discussions we found that we had to start from scratch. This was not necessarily a bad exercise, actually. In fact, the municipal market investing landscape has changed so much that it is helpful even for experienced investors to rethink or reaffirm municipals' place in portfolios. Benjamin Graham was quoted as saying, "You can get in way more trouble with a good idea than a bad idea, because you forget the good idea has limits." We find that is the case often in the municipal market, especially currently and for those who have not recognized the limits created by many of the credit-related changes that have occurred. In a relatively short period of time, the fixed income community went from not paying close attention to municipal credit- to vehemently defending municipals and now, despite its still generally high rating level, may be missing some important trends showing some credit deterioration.

Brief History: Perception and Reality of Municipal Credit Before 2008

Prior to 2008 municipal issuance was booming. There were years where issuance was over $400 billion. Products like variable rate demand bonds and interest rate swaps were used quite a bit. The use of monoline municipal insurance helped the investor community become lazy. Some years over 50% of issuance was wrapped with insurance. Underlying credit was often not considered and credit spreads reflected this fact. There was a distinct commoditization of municipal bonds during this time.

Just After the Great Recession, 2009 and 2010

The Great Recession officially ended in June of 2009, according to the National Bureau of Economic Research. We remember at the end of 2009 and into 2010 many investors started to get nervous about municipal credit quality. This was agitated by the popular financial press who published a great deal of inexpert advice concerning municipal credit. Several reporters were dead set on the idea that the municipal market was the next sub-prime market and the municipal market would melt-down. Some were comparing California to Greece for example. And in the beginning to the middle of 2010, the negative press accounts were constant. Sentiment became so negative back in 2010 that we published on June 15, 2010 a report titled, "The Reality of the Factors Stressing the

Municipal Bond Market." This was a fitting title in retrospect because there were in fact stresses to consider, but nothing catastrophic for the near term.

...and now, despite its still generally high rating level, may be missing some important trends showing some credit deterioration

Examples of Municipal Headline Risk from the Middle Part of 2010

Date	Title	Periodical	Note
June 14, 2010	Investors Looking Past Red Flags	Wall Street Journal	Investors are ignoring signs
May 24, 2010	Municipal Bonds: The Next Financial Land Mine?	Time Online	The looming municipal crisis
March 29, 2010	State Debt Woes Grow Too Big to Camouflage	New York Times	Same fate as Greece
March 15, 2010	The $2 Trillion Hole	Barron's	More Defaults and Chp 9

Source: Moody's, S&P and Janney FIS.

The Meredith Whitney Bomb

Then one Sunday night late in December 2010 during a 60 Minutes segment titled "Day of Reckoning," Steve Kroft interviewed Meredith Whitney, a former banking sector analyst, who predicted a "spate" of municipal bond defaults. She then went on to define a "spate" as 50-100 (or more) sizeable defaults. The most troubling part to investors was the dollar amount she gave- she said that those defaults could amount to hundreds of billions of dollars. She went on to say that this would be something to worry about in the next 12 months. We, along with many other analysts immediately disputed her charge. And it turns out that default and/or Chapter 9 bankruptcy filings did not increase all that much above their historical averages. In other words, they remained low sector-wide and state and local government sector defaults and Chp. 9 filings were minimal, outside of Detroit's in 2013. This did not matter though. Many investors, because they were spooked as a result of the financial crisis, over-reacted and sold municipal bonds and municipal funds indiscriminately. And we spent a good portion of 2011 talking investors down off the ledge.

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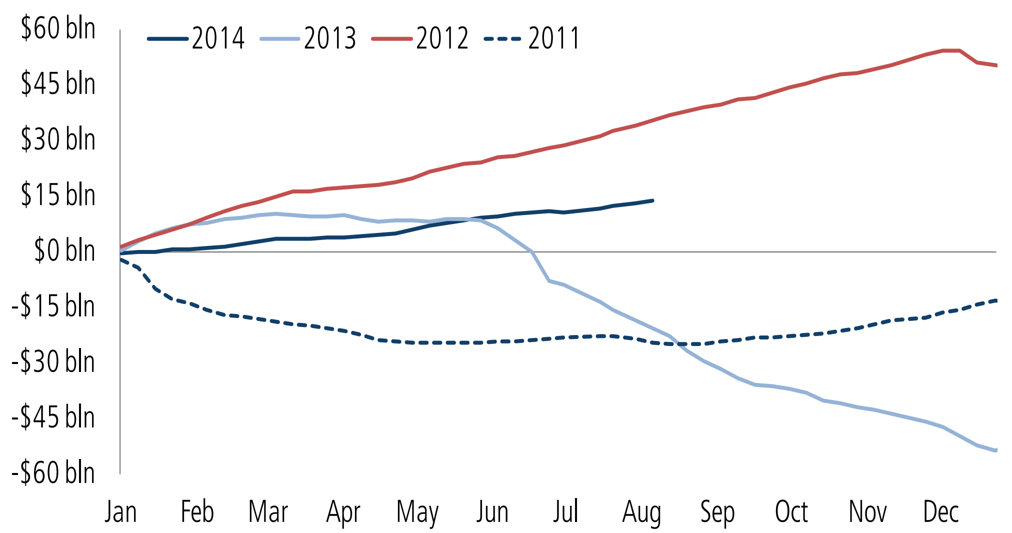
Fund Flows from Municipal Mutual Funds Were Grossly Negative in 2011



Source: Investment Company Institute and Janney FIS. Data is cumulative for the year.

It was the positive aspects of municipal credit and the data showing that the sector was recovering that the market and municipal analysts' focused on most regularly.

Municipal Credit Cited as Resilient

During the time immediately after the Meredith Whitney bomb, municipal analysts (including us) spent a great deal of time explaining to investors that while there were credit issues to watch, a "municipal melt-down" or levels of defaults or bankruptcy filings well above the historical average were not going to occur. There were some moments when investors were spooked. During the summer of 2012 a small number of CA municipalities filed/or tried to file for municipal bankruptcy. Then, Detroit filed in the summer of 2013. But the root causes of these events were largely the result of extenuating circumstances. It was the positive aspects of municipal credit and the data showing that the sector was recovering that the market and municipal analysts' focused on most regularly.

Now, there seems to be some uncertainty as to the status of municipal credit.

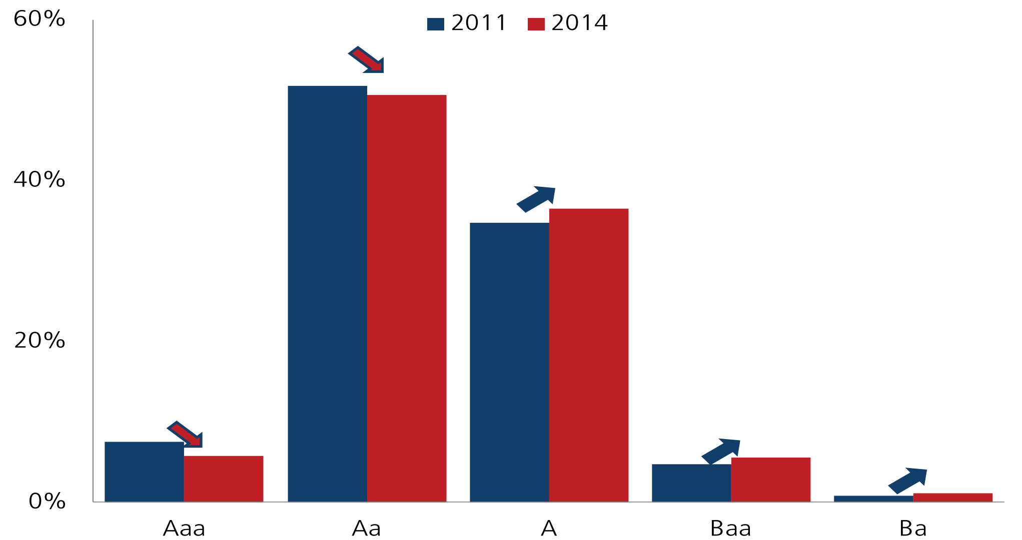
It is a misconception for investors to think municipal credit quality will get to a point where investors can just put their municipal investments into a drawer and forget about them.

We think municipal bond credit quality is still generally high, but we still see several factors that are slowly eating away at a small portion of the market.

Current Status of Municipal Credit

Now, there seems to be some uncertainty as to the status of municipal credit. On the one hand, municipal credit quality is still generally pretty high. The majority are rated in the Aaa and Aa range by Moody's. There are also indications that some important positive credit-related indicators have stabilized. However, it is a misconception for investors to think municipal credit quality will get to a point where investors can just put their municipal investments into a drawer and forget about them. That is not going to happen. There have been too many credit-related factors that have surfaced in recent years and too many that are likely to compound in the future. Knowing this, we want all municipal investors to understand that credit quality is still high, and will likely remain in the elevated ranges, but that there are negative factors to watch out for throughout the municipal bond market.

Municipal Credit Quality Remains High, but has Fallen Slightly Recently

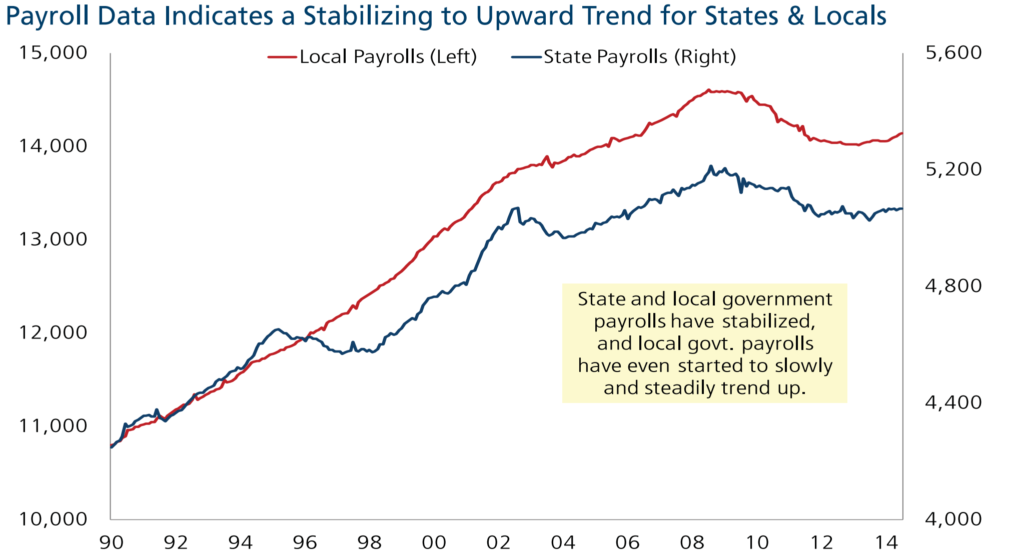


Source: Moody's rating distribution of about 15,000 rated public finance entities and Janney FIS.

Municipal Credit Quality Generally Still High, Some Downgrades to Continue

Our key theme regarding credit quality now, with a little over half of the year past, is that municipal bond credit quality is still generally high, but we still see several factors that are slowly eating away at a small portion of the market. Moody's data shows that credit quality is slightly lower. Overall most municipal issuers have proven to be very resilient considering the financial depths reached by many during the last few years. Municipal holdings need to be monitored for potential credit deter-

Payroll Data Indicates a Stabilizing to Upward Trend for States & Locals



Source: Bureau of Labor Statistics and Janney. #s in thousands

For almost six years- an unprecedented run- public finance downgrades have outpaced upgrades.

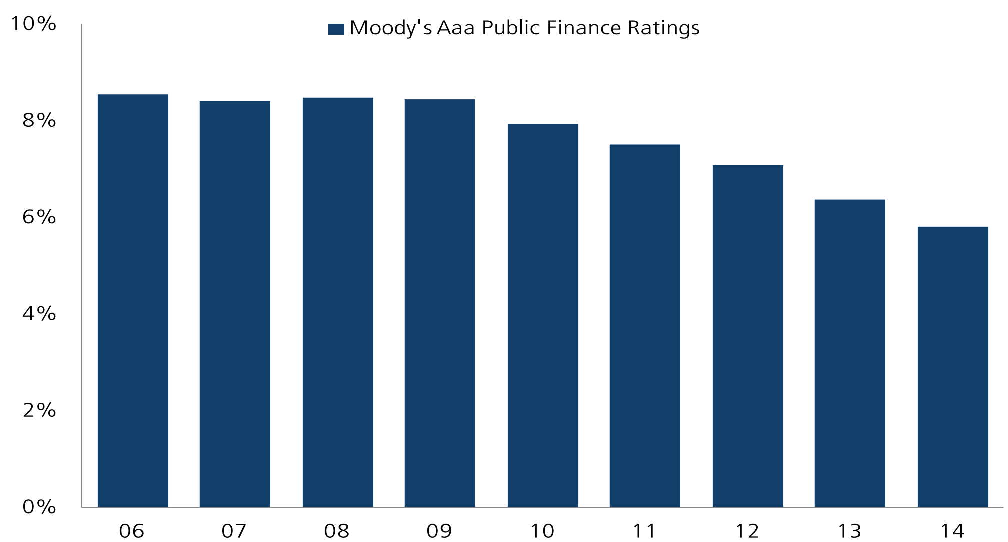
There has been an overall rating migration from the Aaa/Aa levels into the A/Baa range.

The percentage of A and Baa rated municipal issuers has increased.

ioration, even those secured by general obligation pledges. It is the threat of more downgrades, not widespread defaults or bankruptcies, we are most concerned about currently. We think defaults and bankruptcies will remain rare.

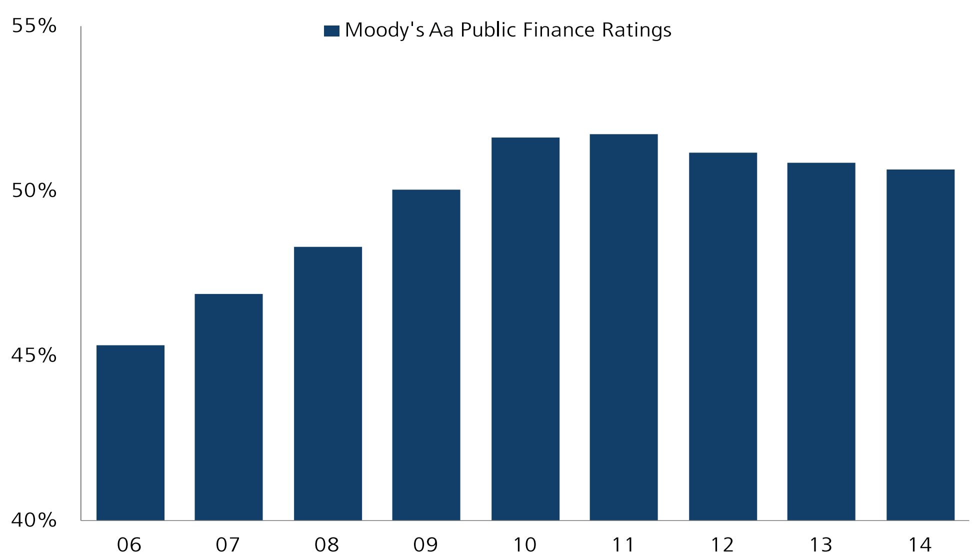
But, some have not been quite as successful in the post-Great Recession balancing act. The credits experiencing negative credit-related trends are a relatively small portion of the municipal market, but enough to make it not only noticeable in the data but also in investors' portfolios. This does not mean we think investors should stay away from the municipal market. The opposite is true, in fact. We think that credit quality in the municipal market is still and will remain fairly high. This is illustrated by the fact that 56% of Moody's rated public finance credits are still currently in the Aaa and Aa categories. Although ratings have generally been migrating lower, and we think this will continue to a degree, the downward trend should stay rather contained. It is also important to note that while downgrades continue to outpace upgrades, the pace is lessening. For almost six years- an unprecedented run- public finance downgrades have outpaced upgrades. The consequences are that there has been an overall rating migration from the Aaa/Aa levels into the A/Baa range. In other words, the percentage of A and Baa rated municipal issuers has increased.

The % of "Aaa" Ratings Dropped Since the Recession



Source: Moody's and Janney. Data as of Jan. 1, 2014.

The % of "Aa" Rated Municipals Also Fell Recently, Even After Recalibration



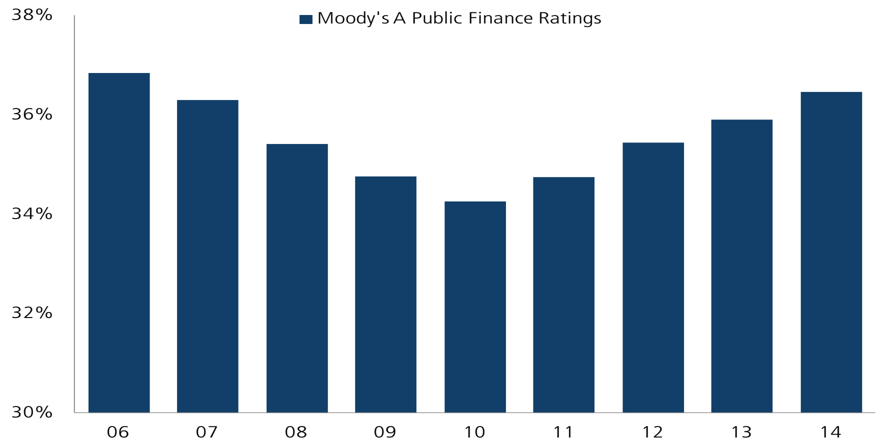
Source: Moody's and Janney. Data as of Jan. 1, 2014.

We still believe the municipal bond market is an important fixed income option for most investors, but we want to again stress that credit selection is increasingly important.

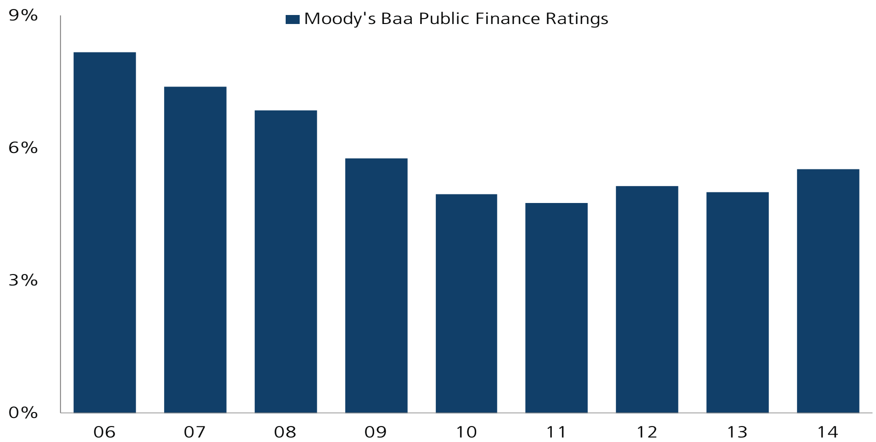
Investors need to use care when holding and reviewing potential purchases and investors should stay away from credits with weakening credit profiles.

There are many [municipal credits] that have and are weathering the post-Great Recession period with their credit quality intact, but there are some worsening too.

The % of "A" Rated Public Finance Entities has Been on the Rise



And the % of "Baa" Rated Public Finance Entities has Also Risen



Source: Moody's and Janney. Data as of Jan. 1, 2014.

Investor Recommendation

We still believe the municipal bond market is an important fixed income option for most investors, but we want to again stress that credit selection is increasingly important. Sector by sector there are definitely stronger performing credits, and it is important for investors to differentiate among the stronger and the deteriorating credits. Investors need to use care when holding and reviewing potential purchases and investors should stay away from credits with weakening credit profiles. There are many that have and are weathering the post-Great Recession period with their credit quality intact, but there are some worsening too. **Tom Kozlik**

Only 30% of Detroit Water and Sewer Bonds Tendered

A Positive Development for the Municipal Market

Last week's Detroit Water and Sewer tender offer represents another important step in the relatively fast pace of Detroit's bankruptcy process. Although only 30% of bonds were tendered, the city chose to go ahead with acceptance. The city's challenge to the Chapter 9 bankruptcy code protection of "special revenue" bond treatment was replaced by a more consensual process, which is a positive development for the municipal market.

Detroit's bankruptcy process continues at what we consider to be a brisk pace. In early August, the city announced it would accept tender offers at pre-determined prices for up to $5.2 billion of Detroit Water and Sewer bonds. The tender offer covered about 333 CUSIPs with tender prices ranging from a high of 119.10 to as low as 84.60 (not including zero coupon bonds and adjustable rate issues). Many of the prices were simply too low for investors to accept. We found multiple instances where recent trading levels for bonds were well above tender prices. The majority of Water and Sewer bonds are insured by Assured Guaranty (A2/AA) or National Public Finance Guaranty Corp (A3/AA-), which typically enhances the trading value compared to uninsured bonds.

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Detroit's "Plan of Adjustment"

Under the city's initial Plan of Adjustment, filed in February of this year, with an antecedent dating back to the Emergency Manager's pre-bankruptcy filing Proposal to Creditors of June, 2013, the city designated about 47% of outstanding water and sewer debt as impaired, with plans to unilaterally lower coupon rates and/or redeem bonds prior to the date of stated call protection. Plans also proposed replacing much of outstanding water and sewer debt with new bonds issued by a to-be-established "regional" authority, with an off-the-top slice of water and sewer revenue going to the city, effectively subordinating bondholders. Bondholders were not the only stakeholders protesting this proposal. More than half of water and sewer revenue received by the city authority is derived from suburban communities outside of Detroit, which are understandably reluctant to have a portion of their utility payments redirected to city coffers.

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Detroit's Bankruptcy Process Timeline

Date	Event
March 14, 2013	Michigan governor appoints Kevyn Orr as Emergency Manager of Detroit
June 14, 2013	EM releases Proposal for Creditors
July 18, 2013	City files for bankruptcy protection under Chapter 9 of federal code
December 5, 2013	After hearing arguments from 110 different stakeholders, bankruptcy judge rules that city is eligable for bankruptcy
March 21, 2014	City releases first Plan of Adjustment
April 2014	City reaches agreement to settle with unlimited tax GO holders at 74 cent per dollar
June 2014	City reaches agreement to settle with limited tax GO holders at 34 cent per dollar
August 2014	Detroit Water and Sewer tender offer is accepted by the city. No bonds impaired

Source: Janney FIS.

As it turned out, only about $1.7 billion (32%) of the bonds were tendered, but this was enough for the city to proceed with buying the bonds back. A key provision of the plan is that since the city decided to accept tenders, no bonds will be impaired, including bonds not tendered. The buyback will be financed by new issuance, partially insured by Assured Guaranty and subject to bankruptcy court approval. The Bond Buyer says the city will save about $240 million in interest costs. The city's initial plan to cram down a settlement on water and sewer bondholders flies in the face of Chapter 9 of the federal code, under which the revenue streams supporting "special revenue" bonds such as water and sewer municipal utility bonds would continue to support bonds. Resistance to the city plan was staunch enough to force reconsideration which led to the tender offer. This is an important, if not surprising, development for bondholders in general. The special revenue protection of Chapter 9 seems likely to survive the Detroit situation, which should be reassuring to municipal market investors. **Alan Schankel**

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Technical Market Update

Municipal Market Performance and Levels Defy Expectations

As in any relationship, it is refreshing to have expectations exceeded. That is what happened with many municipal bond market related relationships over the first half of 2014. Municipal bond performance was strikingly positive for most municipal related indices. Year to date performance for Barclay's 46,000 issuer Municipal Bond Index returned 6.18% in 2014 through July 31, 2014. Both the General Obligation and the Revenue Bond Indices were positive as they returned to investors 5.55% and 6.78% respectively. This defied most analysts' (us included) expectations and begs the question of what to anticipate for the rest of 2014.

Janney CAPITAL MARKETS

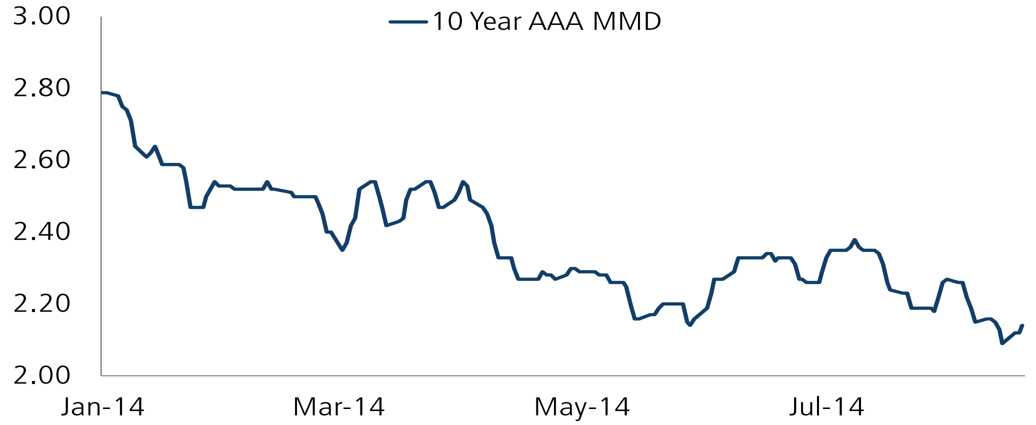
The AAA MMD benchmark began 2014 at almost 2.80% and most recently closed out trading at a 2.14%.

the possibility for higher rates is building, especially as the Federal Reserve prepares to move its target rate higher.

Janney's Guy LeBas now expects the Fed to make a move sometime between the 2nd and 3rd quarters of 2015.

The key reason for the positive returns was because municipal market yields (and Treasuries) surprised investors and fell through the first seven months of the year. The AAA MMD benchmark began 2014 at almost 2.80% and most recently closed out trading at a 2.14% on Monday August 25th. That is still not as low as 2012 bottom point of 1.58% or 2013's 1.75%, but 2.14% is much lower than we anticipated for August 2014, when we and most analysts expected interest rates (and municipals specifically too) to move higher. That just did not happen. But, the possibility for higher rates is building, especially as the Federal Reserve prepares to move its target rate higher.

The Municipal AAA Benchmark Fell 65 Basis Points in 2014, So Far



Source: Thomson Reuters and Janney FIS.

U.S. Interest Rate Forecasts

Guy LeBas, Janney's Chief Fixed Income Strategist, published the firm's most recent U.S. Interest Rate Forecasts back on August 7, 2014. He now expects the Fed to make a move sometime between the 2nd and 3rd quarters of 2015. Slightly more hawkish than expected comments from FOMC chair Janet Yellen on August 22nd were closely watched as will be the August 28th Jobless claims data. LeBas will publish revised forecasts in the beginning of the month of September. Please also see LeBas' August 7th Interest Rate Forecast report and August 22nd report about Janet Yellen's comments for more details.

Janney U.S. Interest Rate Forecasts

Central Bank Rates	Current	3Q 2014	4Q 2014	1Q 2015	2Q 2015	3Q 2015	4Q 2015	4Q 2016
Fed Funds O/N	0.13%	0.13%	0.13%	0.13%	0.13%	0.25%	0.50%	1.50%
Treasury Curve	Current	3Q 2014	4Q 2014	1Q 2015	2Q 2015	3Q 2015	4Q 2015	4Q 2016
3m Bill	0.02%	0.06%	0.09%	0.10%	0.28%	0.35%	0.65%	1.69%
2yr Note	0.46%	0.58%	0.77%	0.99%	1.08%	1.32%	1.46%	1.92%
5yr Note	1.65%	1.77%	1.81%	1.76%	1.87%	1.92%	2.01%	2.26%
10yr Note	2.46%	2.61%	2.89%	2.92%	3.01%	3.04%	3.06%	3.21%
30yr Bond	3.27%	3.33%	3.43%	3.49%	3.52%	3.55%	3.58%	3.66%

Source: Janney's August 7, 2014 forecasts, see Janney FIS report for more detail.

Supply and Demand Trends for the First Half (Seven Months) of the Year

Supply and demand trends are always important indicators to consider when investing the municipal bond sector. On the supply side, we have seen issuance much lower through the first seven months of the year when compared to the first seven months of 2013 and also lower to almost every year for the last ten (except 2011 due to the expiration of BABs). This trend of lower issuance we expected. Overall, municipal market issuers sold $179 billion of debt through the end of July; this is $30 billion less than the market saw last year through this same time period when issuers sold $209 billion of debt. However, issuance to date has been higher than we expected despite its lower overall trend.

Investor demand (for municipal bonds) has continued to be strong through most of 2014.

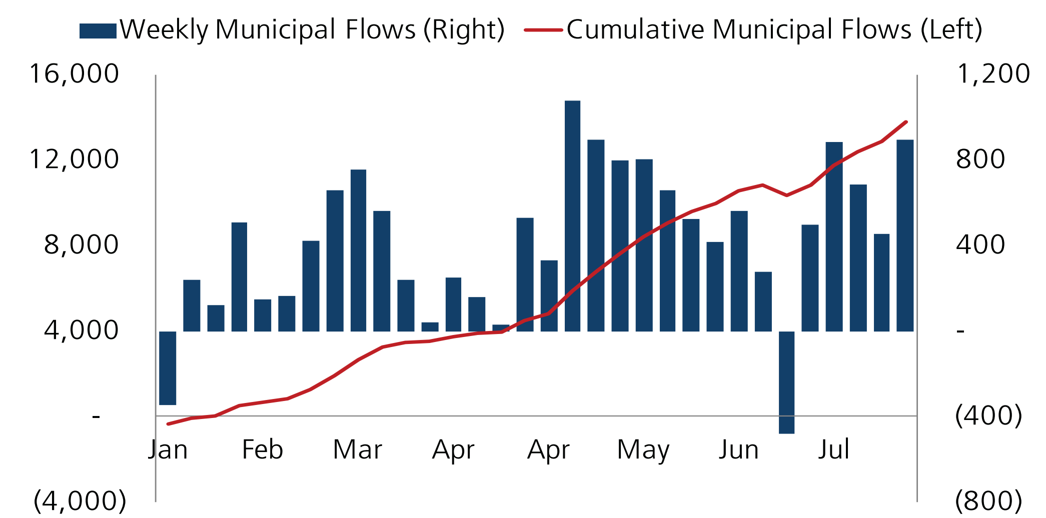
The 16 day government shutdown in October 2013 was enough to convince political leaders on the right that a fight over the debt ceiling was a bad way to begin 2014.

The Republicans might have retreated in 2014 with the expectation that they will come out with guns blazing in 2015.

The reason is that interest rates surprised us, allowing issuers to utilize refunding transactions more this year than we anticipated. Of the $179 billion, $85 billion was for new money, $60 million was refunding and $32 million was designated as "combined." Our convention is to split the "combined" number in half into new money and refunding, so there was about $76 billion of refunding issuance this year. That is much more than we expected. In all, issuance has still been down- a trend that we not only expect for the remaining part of 2014 but for years going forward.

Demand has continued to be strong through most of 2014. This was not necessarily the case in previous years. The only weeks of net negative flows were during the first and twenty-seventh weeks. Aside from those times we did see flows fall slightly just before tax season, but this is a very common occurrence as portfolio adjustments are usually made during this time. Otherwise demand in the form of flows into municipal mutual funds has been strong and mostly steady through the year. This is in contrast to fund flows in recent years. Cumulative flows were significantly negative through most of 2011; this was right after Meredith Whitney gave her December 2010 prediction about municipal market defaults on 60 Minutes. Flows were mostly positive in 2012, recovering from the year before it seems. Then flows into funds continued at a decent pace until the summer of 2013, when they again turned negative. (Please also see our cumulative flow chart for the last several years on the Technical Market Indicators page.) **Tom Kozlik**

Weekly Flows In/Out of Municipal Mutual Funds



Source: Investment Company Institute and Janney FIS. ($ in millions)

Not Much D.C. Interference This Year, Maybe Some in 2015

A Surprise Deal to Start the Year

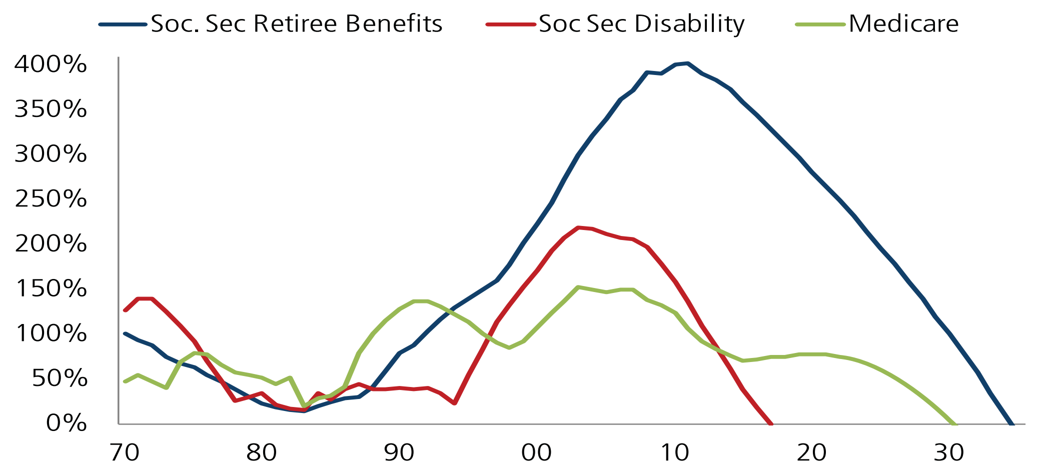
We noted in our 2014 preview that the potential for additional D.C. interference could be a hot topic for the coming year turns out we were dead wrong. The sixteen day government shutdown in October 2013 was enough to convince political leaders on the right that a fight over the debt ceiling was a bad way to begin 2014. This was especially true with a mid-term election coming up. In a surprise move at the beginning of this year, compared to circumstances in November when we wrote our 2014 outlook, lawmakers voted to suspend the debt limit until March 15, 2015. With the 2014 mid-term elections right around the corner, Republicans did not want to shift focus away from attacks on President Obama's "ObamaCare" health plan. Another debt ceiling showdown very well could have done that. It is also very likely that voters were already fatigued as a result of the October government shutdown. As a result there has not been much D.C. interference this year to date.

Observers should not count on Republican lawmakers to use such a restrained strategy at the beginning of 2015. If anything, debate could heat up politically as the March15th deadline approaches. After the mid-terms it is very likely that the Republican Party will retain control of the U.S. House of Representatives and possible that they pick up some seats in the Senate. The Republicans might have retreated in 2014 with the expectation that they will come out with guns blazing in 2015.

It is very unlikely comprehensive tax reform makes any meaning progress in the near term.

Observers should not count on Republican lawmakers to use such a restrained strategy at the beginning of 2015. If anything, debate could heat up politically as the March15th deadline approaches. After the mid-terms it is very likely that the Republican Party will retain control of the U.S. House of Representatives and possible that they pick up some seats in the Senate. In other words, the Republicans might have retreated in 2014 with the expectation that they will come out with guns blazing in 2015. So, what does that mean for the municipal bond market, and especially what does it mean for the threat to the municipal bond tax-exemption? We think that just before that deadline we can expect more rhetoric. However, it is very unlikely that comprehensive tax reform makes any meaning progress in the near term and thus the threat to the tax-exemption will remain rather low, despite what we might be reading and hearing in the press. Soon after, there are two other items municipal observers should be aware of that could cause conversations about tax-reform to simmer. The first is a deadline that has some real numbers behind it and requires attention by lawmakers. According to a 2014 Social Security and Medicare Boards of Trustee report it looks like the Social Security disability insurance program will be exhausted by the end of 2016, unless action is taken by Congress. More rhetoric about tax reform could re-surface surrounding debate on this topic.

Social Security Disability Trust Fund Will Run Dry Without Intervention



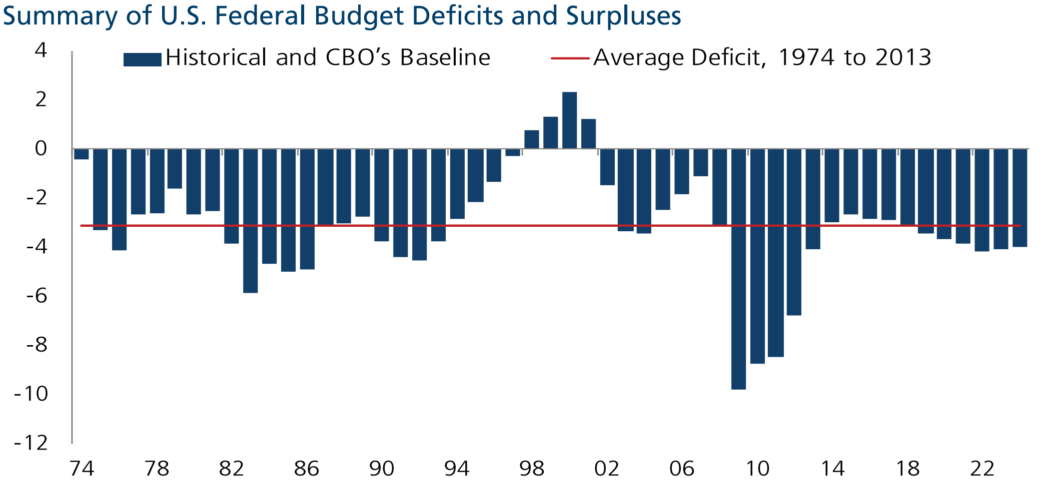
Source: Status of the Social Security and Medicare Programs, Board of Trustees & Janney FIS.

Congressional leaders still have some very tough choices to make considering federal spending (mostly surrounding entitlements).

Overall, Congressional leaders still have some very tough choices to make considering federal spending (mostly surrounding entitlements). They have received a bit of a pass in recent years because deficits are coming in at slightly lower levels. But in coming years deficits are expected to increase again, which may start off another round of calls for spending cuts or additional revenue (higher taxes). It is during this time that the threat to the municipal bond tax-exemption could grow stronger, but much could also change between now and then. Congressional Budget Office projections have the rise in the federal deficit starting in 2017. So it is very likely that much attention will be paid to the budget until we get closer to that time period. **Tom Kozlik**

So it is very likely that much attention will be paid to the budget until we get closer to that time period.

Summary of U.S. Federal Budget Deficits and Surpluses

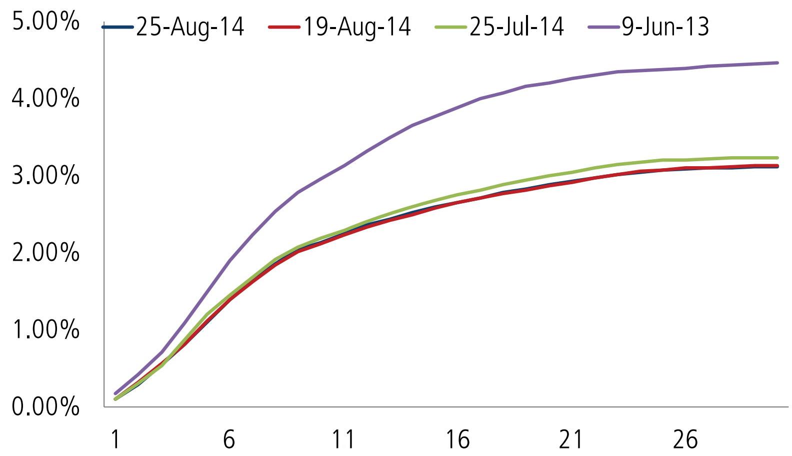


Source: CBO & Janney FIS. In % of U.S. Gross Domestic Product.

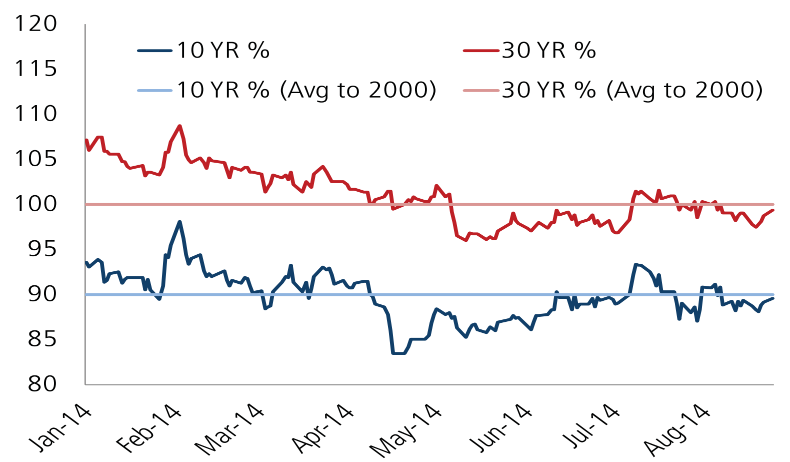
Aaa Municipal Benchmark Yields

Maturity	Aug 25th (as of)	W-O-W Change	M-O-M Change	Y-O-Y Change
1	0.11%	0.00%	0.00%	-0.07%
2	0.30%	-0.02%	-0.01%	-0.13%
3	0.55%	-0.02%	0.01%	-0.17%
4	0.81%	0.00%	-0.06%	-0.28%
5	1.11%	-0.01%	-0.10%	-0.39%
6	1.40%	0.01%	-0.05%	-0.50%
7	1.64%	0.02%	-0.05%	-0.59%
8	1.86%	0.02%	-0.05%	-0.68%
9	2.04%	0.02%	-0.03%	-0.74%
10	2.14%	0.02%	-0.05%	-0.82%
11	2.25%	0.02%	-0.05%	-0.89%
12	2.36%	0.02%	-0.05%	-0.96%
13	2.44%	0.02%	-0.07%	-1.05%
14	2.52%	0.02%	-0.08%	-1.13%
15	2.60%	0.02%	-0.08%	-1.17%
16	2.66%	0.01%	-0.09%	-1.23%
17	2.72%	0.01%	-0.10%	-1.28%
18	2.78%	0.01%	-0.11%	-1.30%
19	2.83%	0.01%	-0.12%	-1.33%
20	2.88%	0.01%	-0.12%	-1.33%
21	2.93%	0.01%	-0.12%	-1.33%
22	2.98%	0.01%	-0.12%	-1.33%
23	3.02%	0.00%	-0.13%	-1.33%
24	3.05%	-0.01%	-0.13%	-1.31%
25	3.07%	-0.01%	-0.13%	-1.31%
26	3.09%	-0.01%	-0.12%	-1.31%
27	3.10%	-0.01%	-0.12%	-1.32%
28	3.11%	-0.01%	-0.12%	-1.33%
29	3.12%	-0.01%	-0.12%	-1.33%
30	3.12%	-0.01%	-0.12%	-1.34%

Aaa Municipal Benchmark Yield Curve

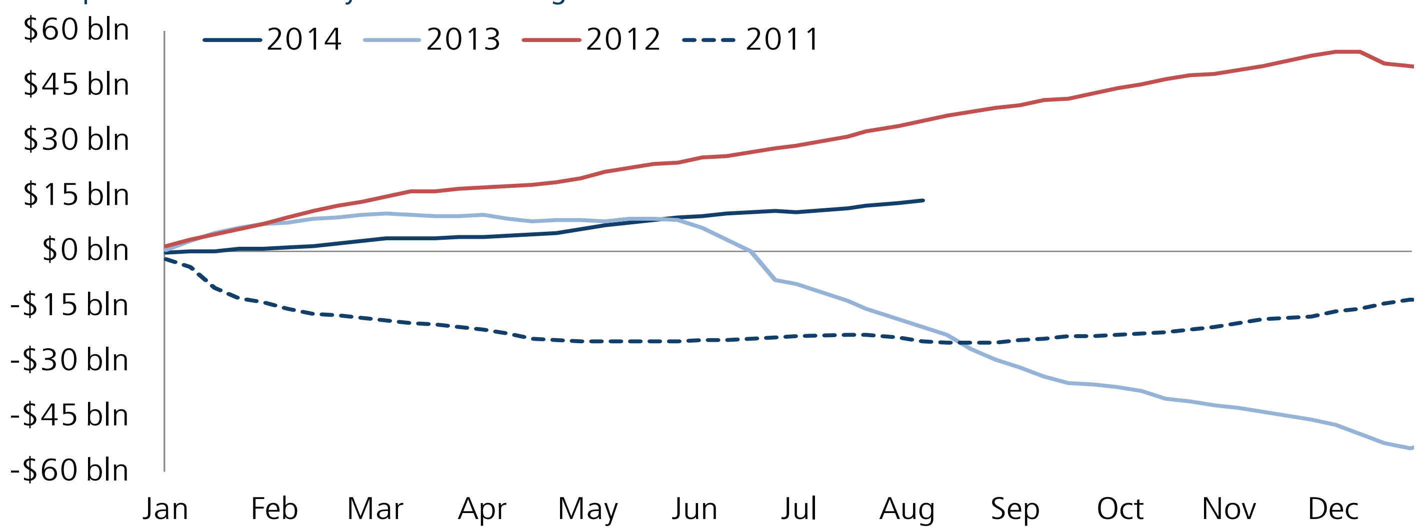


10 Year and 30 Year M/T Ratios



Source: Thomson Reuters and Janney FIS. Average goes back to 2000.

Municipal Fund Flow Activity has Been Strong in 2014



Source: Thomson Reuters, ICI Data and Janney FIS.

Select Recent Changes to Ratings & Outlooks (as of Aug 25, 2014)

Issuer	State	Recent Rating Action	Date	Underlying Rating(s)	Notes
Chicago O'Hare Airport	IL	Raised outlook to Stable from Negative by Fitch	21-Aug-2014	A-	Steadying airport traffic trends
Cooper Health System	NJ	Upgraded to Baa2 from Baa3 by Moody's	11-Aug-2014	Baa2	Improving financial performance
Drew University	NJ	Downgraded to Baa3 from Baa1 by Moody's	7-Aug-2014	Baa3	Falling enrollment
Pittsburgh (City of)	PA	Raised outlook to Positive from Stable by Moody's	7-Aug-2014	A1/A/A	Steps taken to reduce liabilities
Kansas (State of) ICR	KS	Lowered outlook to Neg from Stable	6-Aug-2014	Aa2/AA/NR	Structural imbalance, tax cuts
Kansas (State of) ICR	KS	Downgraded to AA from AA+ by S&P	6-Aug-2014	Aa2/AA/NR	Structural imbalance, tax cuts
Mt. Lebanon (Township)	PA	Downgraded to Aa2 from Aa1 by Moody's	5-Aug-2014	Aa2	A falling general fund balance
South Dakota (State of) ICR	SD	Raised outlook to Positive from Stable	2-Aug-2014	Aa2/AA+/AA	Improved budget planning and results
New Jersey Housing MFA	NJ	Downgraded to Aa2 from Aa1 by Moody's	31-Jul-2014	Aa2	Weakening financial position
PA Hsg Finance Agency	PA	Raised outlook to Stable from Negative by S&P	28-Jul-2014	Aa2/AA+	High level of assets, lower # VRDOs
Atlantic City (City of)	NJ	Downgraded to Ba1 from Baa2 by Moody's	23-Jul-2014	Ba1/A-	Weakened tax base, casino closings
Illinois (State of)	IL	Lowered outlook to Neg from Stable by S&P	23-Jul-2014	A3/A-/A-	Structurally imbalanced FY15 budget
New York (State of)	NY	Upgraded to AA+ from AA by S&P	23-Jul-2014	Aa1/AA/AA	Improved budgetary management
Pennsylvania (Comm of)	PS	Downgraded to Aa3 from Aa2 by Moody's	21-Jul-2014	Aa3/AA/AA	Structural budget imbalance & pensions
Alabama State University	AL	Downgraded to Ba1 from Baa1	3-Jul-2014	Ba1/A-	Continued weakening financial position

Source: Moody's; S&P; Fitch and Janney FIS.

State and Other Select Issuer Ratings (Aug 25, 2014)

	Moody's			S&P			Fitch		
State	Rating	Outlook	Last	Rating	Outlook	Last	Rating	Outlook	Last
Alabama	Aa1	Stable	4/16/2010	AA	Positive	11/27/2013	AA+	Stable	5/3/2010
Alaska	Aaa	Stable	11/22/2010	AAA	Stable	1/5/2012	AAA	Stable	1/7/2013
Arizona (*)	Aa3	Positive	11/26/2013	AA-	Stable	12/23/2011	NR	-	-
Arkansas	Aa1	Stable	4/16/2010	AA	Stable	1/10/2003	NR	-	-
California	Aa3	Stable	6/25/2014	A	Positive	1/14/2014	A	Stable	8/5/2013
Colorado (*)	Aa1	Stable	4/16/2010	AA	Stable	7/10/2007	NR	-	-
Connecticut	Aa3	Stable	1/20/2012	AA	Stable	9/26/2003	AA	Negative	7/2/2013
Delaware	Aaa	Stable	4/30/2010	AAA	Stable	2/22/2000	AAA	Stable	4/13/2006
Dist. of Columbia	Aa2	Stable	8/2/2013	AA-	Stable	3/21/2013	AA-	Stable	4/5/2010
Florida	Aa1	Stable	4/16/2010	AAA	Stable	7/12/2011	AAA	Stable	8/23/2013
Georgia	Aaa	Stable	4/16/2010	AAA	Stable	7/29/1997	AAA	Stable	4/13/2006
Hawaii	Aa2	Stable	5/17/2011	AA	Positive	10/10/2013	AA	Stable	6/15/2011
Idaho (*)	Aa1	Stable	4/16/2010	AA+	Stable	3/30/2011	AA	Stable	4/5/2010
Illinois	A3	Negative	6/6/2013	A-	Negative	6/23/2014	A-	Negative	6/3/2013
Indiana (*)	Aaa	Stable	4/16/2010	AAA	Stable	7/18/2008	AA+	Stable	4/5/2010
Iowa (*)	Aaa	Stable	4/16/2010	AAA	Stable	9/11/2008	AAA	Stable	4/5/2010
Kansas (*)	Aa2	Stable	4/30/2014	AA	Negative	8/6/2014	None	None	None
Kentucky (*)	Aa2	Stable	6/2/2014	AA-	Negative	1/31/2013	A+	Stable	11/8/2012
Louisiana	Aa2	Stable	4/16/2010	AA	Stable	5/4/2011	AA	Stable	4/5/2010
Maine	Aa2	Stable	6/4/2014	AA	Stable	5/24/2012	AA	Stable	1/23/2013
Maryland	Aaa	Stable	7/19/2013	AAA	Stable	5/7/1992	AAA	Stable	4/13/2006
Massachusetts	Aa1	Stable	4/16/2010	AA+	Stable	9/16/2011	AA+	Stable	4/5/2010
Michigan	Aa2	Positive	3/28/2013	AA-	Stable	6/17/2014	AA	Stable	4/2/2013
Minnesota	Aa1	Stable	7/30/2013	AA+	Stable	9/29/2011	AA+	Stable	7/7/2011
Mississippi	Aa2	Stable	4/16/2010	AA	Stable	11/30/2005	AA+	Negative	11/15/2013
Missouri	Aaa	Stable	7/19/2013	AAA	Stable	2/16/1994	AAA	Stable	4/13/2006
Montana	Aa1	Stable	4/16/2010	AA	Stable	5/5/2008	AA+	Stable	4/5/2010
Nebraska (*)	Aa2	Stable	4/16/2010	AAA	Stable	5/5/2011	NR	-	-
Nevada	Aa2	Stable	3/24/2011	AA	Stable	3/10/2011	AA+	Stable	4/5/2010
New Hampshire	Aa1	Stable	4/16/2010	AA	Negative	4/21/2014	AA+	Stable	4/5/2010
New Jersey	A1	Negative	5/13/2014	A+	Neg Watch	6/2/2014	A+	Negative	5/1/2014
New Mexico	Aaa	Stable	7/19/2013	AA+	Stable	2/5/1999	NR	-	-
New York	Aa1	Stable	6/16/2014	AA+	Stable	7/23/2014	AA+	Stable	6/25/2014
North Carolina	Aaa	Stable	1/12/2007	AAA	Stable	6/25/1992	AAA	Stable	4/13/2006
North Dakota (*)	Aa1	Stable	4/16/2010	AAA	Stable	12/13/2013	NR	-	-
Ohio	Aa1	Stable	3/16/2012	AA+	Stable	7/19/2011	AA+	Stable	4/11/2011
Oklahoma	Aa2	Stable	4/16/2010	AA+	Stable	9/5/2008	AA+	Stable	4/5/2010
Oregon	Aa1	Stable	4/16/2010	AA+	Stable	3/10/2011	AA+	Stable	4/5/2010
Pennsylvania	Aa3	Stable	7/21/2014	AA	Negative	7/19/2012	AA	Negative	7/16/2013
Puerto Rico	B2	Negative	7/1/2014	BB+	Watch Neg	7/1/2014	BB-	Negative	7/9/2014
Rhode Island	Aa2	Negative	7/1/2013	AA	Watch Dwn	5/12/2014	AA	Stable	7/18/2011
South Carolina	Aaa	Stable	12/7/2011	AA+	Stable	7/11/2005	AAA	Stable	4/13/2006
South Dakota (*)	Aa2	Stable	5/27/2010	AA+	Stable	3/25/2011	AA	Positive	8/1/2014
Tennessee	Aaa	Stable	12/7/2011	AA+	Stable	11/5/2013	AAA	Stable	4/5/2010
Texas	Aaa	Stable	4/16/2010	AAA	Stable	9/27/2013	AAA	Stable	4/5/2010
Utah	Aaa	Stable	4/16/2010	AAA	Stable	6/7/1991	AAA	Stable	4/13/2006
Vermont	Aaa	Stable	4/16/2010	AA+	Positive	9/17/2012	AAA	Stable	4/5/2010
Virginia	Aaa	Stable	7/19/2013	AAA	Stable	11/11/1992	AAA	Stable	4/13/2006
Washington	Aa1	Stable	7/19/2013	AA+	Stable	11/12/2007	AA+	Stable	7/19/2013
West Virginia	Aa1	Stable	7/9/2010	AA	Stable	8/21/2009	AA+	Stable	7/8/2011
Wisconsin	Aa2	Stable	4/16/2010	AA	Stable	8/15/2008	AA	Stable	4/5/2010
Wyoming (*)	NR	-	-	AAA	Stable	5/3/2011	NR	-	-

Source: Moody's; S&P; Fitch and Janney FIS. (*) Denotes a Lease or Issuer Credit Rating.

Municipal Credit Rating Scale and Definitions

	Rating Agency			
	Moody's	S&P	Fitch	Definition
Investment Grade	Aaa	AAA	AAA	Exceptionally strong credit quality and minimal default risk.
	Aa1	AA+	AA+	Upper medium grade and subject to low credit risk.
	Aa2	AA	AA	Upper medium grade and subject to low credit risk.
	Aa3	AA-	AA-	Upper medium grade and subject to low credit risk.
	A1	A+	A+	Strong credit quality and subject to low default risk.
	A2	A	A	Strong credit quality and subject to low default risk.
	A3	A-	A-	Strong credit quality and subject to low default risk.
	Baa1	BBB+	BBB+	Subject to moderate risk and possess some speculative characteristics.
	Baa2	BBB	BBB	Subject to moderate risk and possess some speculative characteristics.
	Baa3	BBB-	BBB-	Subject to moderate risk and possess some speculative characteristics.
Sub-Investment Grade	Ba1	BB+	BB+	Weak credit quality with speculative elements and substantial credit risk.
	Ba2	BB	BB	Weak credit quality with speculative elements and substantial credit risk.
	Ba3	BB-	BB-	Weak credit quality with speculative elements and substantial credit risk.
	B1	B+	B+	Very weak credit quality, very speculative with high credit risk.
	B2	B	B	Very weak credit quality, very speculative with high credit risk.
	B3	B-	B-	Very weak credit quality, very speculative with high credit risk.
	Caa1	CCC+		Extremely weak credit quality and subject to very high credit risk.
	Caa2	CCC	CCC	Extremely weak credit quality and subject to very high credit risk.
	Caa3	CCC-		Extremely weak credit quality and subject to very high credit risk.
	Ca	CC		Highly speculative and are in or near default with some prospect for recovery.
		C	CC	Lowest class of rated bonds and may be in default with little prospect for recovery.
			C	Lowest class of rated bonds and may be in default with little prospect for recovery.
	D	D	RD/D	Issuer is in default and/or has failed to make a payment.

Source: Moody's; S&P; Fitch and Janney FIS.

Janney Capital Markets

Janney Municipal Bond Market Publications

Title	Date	Pub	Notes
Detroit Water and Sewer Update	August 25, 2014	Weekly	30% of bonds tendered, but an important step
Parsing the PREPA News	August 18, 2014	Weekly	PREPA reached agreement with stakeholders
U.S. State Fiscal Health Update	August 12, 2014	Note	March of next year
Steady as She Goes	August 11, 2014	Weekly	Municipals continue to show stability, credit is improving
This Summer is Different	August 4, 2014	Weekly	Volume indicators are lower this year
Are S&P's Local Govt. Ratings Too High?	July 14, 2014	Monthly	We have become increasingly skeptical of S&P
Puerto Rico: It All Goes Back to Economy	June 30, 2014	Weekly	Puerto Rico's economy continues to contract
OPEBS v Pension Primer	June 23, 2014	Weekly	OPEB is funded on a pay as you go basis
A Brief Pension Primer	June 16, 2014	Weekly	Update on pension funding
Inertia - Not Best Response to Rate Concerns	June 12, 2014	Note	Investors are concerned about potential for rising rates
What a Difference a Year Makes	June 9, 2014	Weekly	M/T Ratios have stabilized since last summer
Puerto Rico - Post Visit Update	June 5, 2014	Note	April revenue miss increases budget balance
Supply Constraints	June 2, 2014	Weekly	Summer supply and demand collision
The Rime of Municipal Bond Issuance	May 22, 2014	Monthly	Municipal Issuance will drop in 2014 & in coming years
Tobacco Bond Update	May 19, 2014	Weekly	Trends in the tobacco sector remain negative
Municipal Default Update	May 12, 2014	Weekly	Municipal defaults remain low compared to other sectors
Atlanta Hartsfield Jackson Int Airport	May 12, 2014	Note	Key takeaways from our closer look at ATL
Municipal Airport Sector	May 9, 2014	Note	Headwinds have receded in Airport sector
New Jersey Downgraded	May 5, 2014	Weekly	NJ spreads have remained steady since the downgrade
Municipal Market Technical Review	April 28, 2014	Weekly	M/T Ratios have been declining
Tax Day Reminder of Muni Value	April 15, 2014	Note	Let municipal help alleviate the pain of higher taxes
U.S. State Fiscal Health Update	April 11, 2014	Note	A new spending paradigm for state governments
The Bond Insurers- Now There are Three	April 9, 2014	Note	Upgrades for Assured and National
Chp 9 Bankruptcies Remain Low	March 28, 2014	Monthly	Review Chp 9 bankruptcies, RI willingness
Heavy New Issue Week Comes and Goes	March 17, 2014	Weekly	Heavy calendar and Puerto Rico issuance
Size of Municipal Market Shrinks Again	March 10, 2014	Weekly	Fed data indicates amt. bonds is gradually diminishing
Our Annual Municipal Sector Credit Reviews	February 28, 2014	Monthly	Still have "Cautious" outlooks on 6 (of 11) sectors
Municipals: Positive but Tepid Demand	February 24, 2014	Weekly	Modest mutual find inflows
Moody's and Fitch Downgrade - Puerto Rico	February 11, 2014	Note	Moody's & Fitch downgraded GO below investment grade
Municipals: Puerto Rico Downgrades	February 10, 2014	Weekly	A Review of recent downgrades related to Puerto Rico
S&P Downgrade - Puerto Rico	February 6, 2014	Note	S&P downgraded GO below investment grade
Municipals: Low January New Issue Volume	February 3, 2014	Weekly	Volume is lower but new money issuance is rising
Lower Yields Breeds Duration Adjustment	January 27, 2014	Weekly	Opportunity to manage duration by realigning portfolios
PA Intercept Program for School Districts	January 22, 2014	Note	In-depth Look at the mechanisms and Moody's changes
Municipals: A Good Start to 2014	January 13, 2014	Weekly	Munis enjoyed a strong start for the year amid light supply
Janney Outlook for Local Governments	January 7, 2014	Note	Outlook still "Cautious"
U.S. State Fiscal Health Update	January 6, 2014	Note	"Stable" Outlook for U.S. States- full steam ahead
Municipals: Fewer New Munis	January 6, 2014	Weekly	Borrowing for projects remains below pre-recession pace
A Unique Local Govt Refunding Strategy	December 19, 2013	Note	IL school districts funding escrows with IL GOs
The Municipal Market in 2014	November 22, 2013	Monthly	We highlight 5 events/issues we expect to be big
Municipals: Jefferson Cty, AL and Puerto Rico	November 25, 2013	Weekly	Questionable debt structure and PR econ indicators
Municipals: Rating Action Divergence	November 18, 2013	Weekly	Difficult to rationalize upgrades by S&P
Connecticut: A Review of State Issuers	November 8, 2013	Note	CT faced significant economic challenges
Municipals: Puerto Rico Update	November 4, 2013	Weekly	Disclosure has improved and yields narrowed
Municipals: Old Normal Returns	October 28, 2013	Weekly	Market stabilizing, S&P's optimistic view
Municipals: Back to Normal?	October 21, 2013	Weekly	Growing primary market calendar post-shutdown
Municipals: Regional Economic Shutdown	October 7, 2013	Weekly	State & regions just around DC to be most affected
Puerto Rico: Island Visit and COFINA	October 4, 2013	Note	Sales & use tax revs growing despite weak economy
U.S. State Fiscal Health Update	October 3, 2013	Note	Status of U.S. States largely secure, laggards remain
Municipals: Washington Crunch	September 30, 2013	Weekly	Commentary on outflows and DC interference
Debt Ceiling Debate Part II: Treat Uncertainty	September 27, 2013	Monthly	More uncertainty, but will be less impactful than in 2011
M/T Ratios Continue to Retreat	September 23, 2013	Weekly	Sparse supply helps municipals stabilize
New Issuance & Outstanding Debt Declining	September 16, 2013	Weekly	Municipal issuers have reduced new money borrowing
Puerto Rico Accomplishments and Challenges	September 13, 2013	Note	Fiscally better but headwinds remain
Taper, a New Fed Chief and War- Oh My!	September 11, 2013	Monthly	Advice: municipal investors stay composed

Source: Janney Fixed Income Strategy.

Analyst Certification

We, Tom Kozlik and Alan Schankel, the Primarily Responsible Analysts for this report, hereby certify that all of the views expressed in this report accurately reflect our personal views about any and all of the subject sectors, industries, securities, and issuers. No part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

Definition of Outlooks

Positive: Janney FIS believes there are apparent factors which point towards improving issuer or sector credit quality which may result in potential credit ratings upgrades

Stable: Janney FIS believes there are factors which point towards stable issuer or sector credit quality which are unlikely to result in either potential credit ratings upgrades or downgrades.

Cautious: Janney FIS believes there are factors which introduce the potential for declines in issuer or sector credit quality that may result in potential credit ratings downgrades.

Negative: Janney FIS believes there are factors which point towards weakening in issuer credit quality that will likely result in credit ratings downgrades.

Definition of Ratings

Overweight: Janney FIS expects the target asset class or sector to outperform the comparable benchmark (below) in its asset class in terms of total return

Marketweight: Janney FIS expects the target asset class or sector to perform in line with the comparable benchmark (below) in its asset class in terms of total return

Underweight: Janney FIS expects the target asset class or sector to underperform the comparable benchmark (below) in its asset class in terms of total return

Benchmarks

Asset Classes: Janney FIS ratings for domestic fixed income asset classes including Treasuries, Agencies, Mortgages, Investment Grade Credit, High Yield Credit, and Municipals employ the "Barclay's U.S. Aggregate Bond Market Index" as a benchmark.

Treasuries: Janney FIS ratings employ the "Barclay's U.S. Treasury Index" as a benchmark.

Agencies: Janney FIS ratings employ the "Barclay's U.S. Agency Index" as a benchmark.

Mortgages: Janney FIS ratings employ the "Barclay's U.S. MBS Index" as a benchmark.

Investment Grade Credit: Janney FIS ratings employ the "Barclay's U.S. Credit Index" as a benchmark.

High Yield Credit: Janney FIS ratings for employ "Barclay's U.S. Corporate High Yield Index" as a benchmark.

Municipals: Janney FIS ratings employ the "Barclay's Municipal Bond Index" as a benchmark.

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