

MUNICIPAL BOND MARKET NOTE

JANNEY FIXED INCOME STRATEGY

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ALAN SCHANKEL
Managing Director
215.665.6088
aschankel@janney.com

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Receiver Unveils the "Harrisburg Strong Plan"

This Plan Will Stand as a Strong Example of a Collaborative Approach to Dealing with Extreme Municipal Fiscal Stress, Assuming Approval

- The state appointed receiver submitted the "Harrisburg Strong Plan" to Pennsylvania's Commonwealth Court, on August 26, 2013;
- "Harrisburg Strong" offers the city an opportunity to regain fiscal stability and perhaps even thrive in coming years'
- Keystone elements of the Strong Plan are the sale of the incinerator and long term lease of parking facilities;
- The initial haircut to the major creditors, Assured Guaranty and Dauphin County, at about 30% is significant, but it is notable that agreement was achieved without the expensive and time-consuming process of bankruptcy;
- Also notable in Harrisburg Strong is the state's positive presence at key intersections, increasing the chances of the Strong Plan's successful implementation.

HARRISBURG STRONG PLAN

A Plan to Regain Fiscal Stability and Thrive in Coming Years

On August 26, 2013, the state appointed receiver submitted the "Harrisburg Strong Plan" to Pennsylvania's Commonwealth Court, seeking confirmation of a complex set of initiatives. If the plan is approved and successful, Harrisburg will be relieved of its guarantee obligations related to more than \$300 million of debt issued to finance the retrofitting of its troubled resource recovery plant, which prior city administrations believed would generate incremental income to the city, but which in fact was barely able to cover operating expenses, let alone service the bloated debt load.

The first notable element of the plan is its unusual name, which in contrast to legislative characterization as a recovery plan, seeks to title the plan in "a more positive, forward-looking manner." More important to the substance of the plan is the apparent success of Receiver General William Lynch's approach, avoiding the adversarial bankruptcy process and achieving significant concessions from creditors, the city and other stakeholders, including unions representing city employees. The plan offers the city an opportunity to regain fiscal stability and perhaps even thrive in coming years, although as with any such plan uncertainty clouds achievement of optimal long term outcomes. Also notable in the plan is the state's positive presence at key intersections, increasing the chances of the Strong Plan's successful implementation.

Asset Sales

It is no surprise that the keystone elements of the Strong Plan are sale of the incinerator and long term lease of parking facilities. As expected, the Lancaster County Solid Waste Management Authority (LCSWMA) will purchase the resource recovery plant for a price between \$126 million and \$132 million, with acquisition to be funded with long term debt issued by LCSWMA. Underlying the sale are agreements with the City and Dauphin County to provide LCSWMA with a flow of waste to be processed by the facility. Also key to the transaction is a long term agreement on the sale of electricity to the state. These agreements assure a base revenue stream for the facility, which generates about 76% of revenue from tipping fees paid to the plant by waste haulers and about 21% from sale of electricity generated by the plant. The second piece of the asset monetization is the 40 year lease of the city's parking facilities (9 of 10 garages, and 4 of 5 lots, and 1,250 on street-metered parking spaces) to Harrisburg First, a group including Guggenheim Securities, Piper Jaffray & Co., AEW Capital Management and Standard Parking Corp. Facilities will be owned (via 40 year lease) by the Pennsylvania Economic Development Financing (PEDFA), which will enable financing with tax exempt debt. A key underpinning of the transaction is the state lease of more than half of parking

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The plan also sets aside money to begin funding retiree health benefits as well as infrastructure improvement and economic development.

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spaces, providing a dependable stream of income for Harrisburg First. The transaction will be financed with issuance of tax bonds by PEDFA. About \$99 million of the proceeds, along with certain reserve fund balances, will be used to retire or defease about \$106 million of existing parking debt.

Creditors

Along with most proceeds of the incinerator sale, Assured Guaranty (AGM) Dauphin County, which separately and together guarantee about \$300 million of debt used to finance the incinerator, will receive about \$210 million, leaving a gap of \$90 million. (Note: Dauphin County and AGM are essentially treated as a single entity in the Strong Report with the supposition that the two entities have or will develop a separate agreement for deciding their individual liabilities.) Additionally, the county and insurer have agreed to insure some of the new bonds to be issued by LCSWMA and PEDFA. The structure of the parking transaction is complex. AGM and Dauphin County will potentially receive further payment from future parking operations as well as certain other sources.

Ambac has been making payments on general obligation zero coupon debt since the city defaulted on the March 2012 payment. Under the Strong Plan, Ambac will continue to make payments, with the city making repayment to Ambac over a time frame extending 10 years beyond final maturity. Settlements have been reached with other creditors, including Covanta which operates the incinerator, for varying amounts at less than 100 cents per dollar, with a few smaller claims yet to be resolved.

The City

The Strong Plan anticipates a balanced budget for the city in years 2014 through 2016. Increased revenue sources include additional annual revenue from the parking transaction and potentially a piece of state fuel tax revenues (legislation pending). Expense reductions have been ongoing and will include renegotiated union contracts and other reductions. The plan also sets aside money to begin funding retiree health benefits as well as infrastructure improvement and economic development.

Conclusion

Evident throughout the Strong Plan is the receiver's intent to assure Harrisburg an opportunity to revive its financial fortunes. The initial haircut to the major creditors, AGM and Dauphin County at about 30% is significant, but it is notable that agreement was achieved without the expensive and time consuming process of bankruptcy. Because of coverage by bond insurance, bondholders will emerge intact, with \$400 million of existing parking debt as well as resource recovery debt retired or defeased. The plan still needs court approval, and there remain a few unresolved issues, including an unresolved union agreement with firefighters, but the plan as communicated is substantive. At several intersections, state support was key to reasonable agreements. Assuming approval, this plan will stand as a strong example of a collaborative approach to dealing with extreme municipal fiscal stress.

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