

THE INTEREST FOR THE MUNICIPAL BONDS

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Abstract: The emissions of municipal bonds are a pretty recent apparition in the evolution of the Romanian capital market. The reduced level of the local administrations available funds and the impossibility to increase the local taxes so as to get higher incomes cashed by the local budgets, impose the finding of some alternative financing sources to sustain the local investment programs.

1.The legal frame of the municipal bonds

The municipal bonds are movable values issued by the local authorities, especially cities and towns, through which are attracted funds from the capital market to finance some investment projects of local interest [1].

In the ex socialist states, the local authorities started to issue municipal bonds in 1995, Poland being the first country in the Eastern Europe in which these titles are largely used to attract financing for investments. In Romania, existed some unsuccessful attempts to launch municipal bonds, including on the international markets (Sinaia, December 1996), but the issuers did not received the necessary certificate from the Ministry of Finance.

The emissions of municipal bonds were not possible till 2001 because there had not been found the pandors to provide the security and the good development of such action, there was no legal basement to allow such operations.

According to Govern's Order(GO) 45/2003 regarding the local public finance, Art.58 (2) The instruments of the local public duty to which the local administrations have access are the value titles and the loans from banks or other credit institutions. According to the same normative act, through local public duty we understand the general debenture that must be reimbursed from the self incomes of the administrative-territorial units, according to the concluded contracts [2]. The regulation allows the municipality to create some budgets of whose execution is responsible; to plan average and long term investments based on the foreseen incomes; to establish local priorities; to finance by loans from the bank or by municipal bonds; Law 525/2002 of the capital markets regulates the emission and transaction conditions.

The emissions of municipal bonds are a pretty recent apparition in the evolution of the Romanian capital market, because they became possible only the entering in rule of Law 189/1998 regarding the local public finance, replaced in the present by Law 273/2006, completed by the Govern's Emergency Order no. 64/2007. The legal frame of the municipal bonds emissions is completed with the Capital Market Law and with Regulation CNVM no.1/2006, regarding the public offer of movable values and other financial instruments regarding the issuers and the movable values operations.

1. The advantages of the municipal bonds

The reduced level of the local administrations available funds and the impossibility to increase the local taxes so as to get higher incomes cashed by the local budgets, impose the finding of some alternative financing sources to sustain the local investment programs. From the point of view of the costs, of the reimbursement terms, of the easiness to obtain

financing, the obligatory loans are more advantageous in comparison with the bank loans. For investors, the bonds offer an intermediary output between the shares holdings directly on the stock exchange and the bank deposits. They are also called “determinate income instruments”, which refer to their coupon. Their enormous advantage to the deposits is that they are transactional on the organized markets.

In the mature markets, the volume of the transactions with bonds is bigger than the volume of transactions with shares or other derivate financial instruments. This is because the bonds market is the investment place of many investment banks and the bonds are their favorite instrument, from the corporative ones to Eurobonds, from those issued by the local administrations to the ones issued by governs or multi-national companies or national banks, etc [4].

The bonds are always an alternative to the stock investment and to the bank deposits that is why they function quite reversely: if the stock or the interests to deposits decrease, the transactional prices of the bonds increase and vice-versa.

As to the influence of the currency market, generally it is the same: when the national currency decreases in comparison with other currency, the bond market increases and vice-versa. The advantages of the bond emissions are clear both for the investors and for city halls. They both avoid the financial intermediation of the banks. The investors receive higher interests than at deposits while the city halls get cheaper loans than if they would make a bank credit [5].

3. The interest for the municipal bonds

In 2001, for the first time after the World War II, two resort-towns in Romania, Mangalia and Predeal, proclaimed their independence to the state budget for investments in the sub-structure and launched a municipal bonds emission.

For Romania, this was a premiere and this emission was also a test to see how things evolve. The interest of these bonds was counted with an arithmetic average between the active and passive interests on the interbank market - BUBID/BUBOR – at which we add 2 percentage points for the titles issued by Mangalia and 3 for those issued by Predeal. At the initial value, this represented for their first semester an interest of 36% for Mangalia and 37% for Predeal. In that moment, on the Romanian bank market, for the natural persons the interests fluctuated in the interval 26-36% for the bank deposits on three months, 27-37% at six months, and 26-38% for one year. At the state titles for the population, the interest was of 36% for six months. For the state titles for the population, the interest was of 36% for six months.

These emissions of municipal bonds were later followed by other municipalities: Zalau, Alba Iulia, Cluj-Napoca, Breaza, Bacau, Sebes, Targu Mures, and Slobozia.

Presently, the interest for the municipal bonds is much below the values registered 7 years ago. Thus, for the bonds launched by Bacău at the end of the past year, the interest is variable, counted according to the interbank rate average $[(BUBID_{6M} + BUBOR_{6M})/2] + 0,85\%$; at the beginning of April 2008, the average rate of interest at deposits on the interbank market at 6 months is around 10,37 %, while for Romanian Interbank Offer Rate (ROBOR), the average rate of interest for the loans given on the interbank market is of 11,12%, which means that for the Bacău municipal bonds the interest is around 11,595 %, while the deposit interest is between 7,25-8,5%.

2007 was the year of the credit titles at the Bucharest Stock Exchange. From the 16 transacted emissions, seven started at the stock exchange in 2007. Nevertheless, the credit titles market at the Bucharest Stock Exchange is still modest even if lately, the number of bond emissions almost doubled.

The values of the emissions are relatively small, in a total of LEI 182 million. Presently at BSE there are present a series of 16 municipal bonds issued by 12 city halls that decided to finance their projects with the help of the capital market. Some of them were attracted by the bonds reaching the second or even the third emission. We talk here about Alba Iulia, Bacău, Deva, and Timișoara, which all have at transaction two bonds emissions(Table1).

Table 1. Municipal Bonds(Bucharest Stock Exchange)

Symbol	Name	Total bonds	Principal initial (RON)	Issue value(ROn)	Issue Date	Listind Date	Maturity Date	No. coupons
BAC08	MUNICIPIUL BACAU	89.500	100,00	8.950.000,00	19.06.2004	24.02.2005	15.09.2008	8
DEV08A	MUNICIPIUL DEVA	19.160	100,00	1.916.000,00	14.10.2004	04.02.2005	30.09.2008	8
TIM11	MUNICIPIUL TIMISOARA	200.000	100,00	20.000.000,00	07.07.2005	20.07.2005	01.03.2011	11
AIU08	MUNICIPIUL AIUD	7.000	150,00	1.050.000,00	03.02.2005	29.07.2005	01.09.2008	15
MED09	MUNICIPIUL MEDGIDIA	21.000	100,00	2.100.000,00	01.04.2005	23.08.2006	20.03.2009	16
NAV09	PRIMARIA MUNICIPIULUI NAVODARI	45.000	100,00	4.500.000,00	23.06.2005	11.05.2006	19.06.2009	16
DEV08	MUNICIPIUL DEVA	58.000	100,00	5.800.000,00	15.09.2003	20.02.2004	24.04.2008	19
ORD10	MUNICIPIUL ORADEA	100.000	150,00	15.000.000,00	24.06.2004	26.11.2004	20.05.2010	24
TEU20	ORASUL TEIUS	15.000	100,00	1.500.000,00	18.08.2006	12.02.2008	25.11.2020	29
LGJ14	Primaria Lugoj	35.000	100,00	3.500.000,00	15.11.2006	27.03.2007	15.09.2014	32
ALB25A	Primaria Alba Iulia	80.000	100,00	8.000.000,00	10.01.2007	26.11.2007	15.04.2025	37
ALB25	Primaria Alba Iulia	80.000	100,00	8.000.000,00	27.09.2005	26.11.2007	15.04.2025	39
TGM27	MUNICIPIUL TARGU MURES	200.000	100,00	20.000.000,00	29.08.2007	14.12.2007	15.08.2027	75

Although from the number point of view, the credit titles emissions listed at the Stock quota should have insured a minimum cash amount, in reality, the number of transactions with such movable values was up to the present extremely low due to the reduced value of the emissions.

2. Municipal bonds perspectives

Even if at first sight the total value of the bonds emissions and of the bank credits accessed by various municipalities was low, in the past years it increased significantly. For 2006, the credit market accessed by the local municipalities reached an important amount (EUR 1,5 million), which increased in 2007 at about EUR 2 million. The market is reduced in value due to the few listings and to the small values; In the following years, the number of the municipalities to choose this solution of financing shall increase, being stimulated by the example given by those in Timisoara, Deva, or Alba Iulia, who each have at transaction two bond emissions and the money was efficiently invested in local development programs.

This year, various city halls in the country announced that they want to launch bond emissions on the local capital market. If initially neither the city halls, nor the state made loans on longer terms than seven years on the capital market, in the last years, the municipalities have tried the internal market with three times bigger maturities.

Together with the EU adhering, the municipalities shall have more and more work to do. The rehabilitation of the sub-structure shall benefit of the biggest structural funds, but to access them they will need their own money too [3]. The money may be obtained

through bank credits or bonds. More advantageous are the municipal bonds that can be run on longer periods and which are immediately “absorbed” by the market (insurers and private pension funds) considering that the non-payment risk is almost zero. Together with the apparition of the private pension funds, it is estimated a bigger and bigger volume of bonds and long term loans. Almost 30 municipal bonds offers issued by at least 10 city halls, could be run in 2001, through the agency of the Bucharest Stock Exchange (BSE), doubled to the ones run in 2007.

The municipal bonds are among the most successful titles transacted at the Stock due to the interest over the market’s average and to the investment guarantee assured by municipalities. 2008 could bring a real revivment on the bond market, in concordance with the expected increase of activity on the whole local capital market. If in the present there are run 16 bond emissions, this year we could assist at a double number, 10 new offers having already been confirmed.

Till not long ago, the seven years loans made the rule with the titles issued by city halls and by the Ministry of Finance, now, the mayors or the district boards launch bonds emissions on 18-20 de years. They need to attract money on longer terms in order to co-finance the projects for which they want to attract structural funds from the European Union.

Especially the sub-structure works but other big local projects too, brought on the financial market with such titles the authorities in Iași, Alba, Hunedoara, Timișoara, Bistrița, Bacău, Focșani, or Târgu Mureș. The Iași city hall shall even launch an emission with a record value – LEI 200 million having the term in 2028. It is one of the few municipal bonds who used the bridge credit (a pre-finance of the future bond emission that allows the payment of the interest for the amounts used on the investment period only). In its turn, the Ministry of Finance shall launch in April the first state titles on ten years. These instruments shall be a reference point for other actors of the financial market too, interested in issuing bonds with higher and higher maturity.

The offer for such titles becomes more and more consistent when the request shall also greatly increase in the following years. The most interested shall be the insurance companies, but mainly the administrators of the private pension funds. About to function from 2008, they will need to put the contributors’ money into low risk instruments and on longer terms possible.

The municipal bonds and state titles fulfill all these conditions. That is why they could attract the interest of the foreign investors who would wish to build more diversified portfolios. A benefic effect over the future outputs of the municipal bonds shall also have the cash on the market and the presence of the non-residential interested in more various investment instruments.

Moreover, the municipal bonds have the advantage of a very long running period with output over the market average, both for legal and natural persons [6]. The outputs shall be influenced by the evolution of inflation that acts for decreasing, but also by a cash price for the mobilization of the amounts on longer terms, that act for the increasing of the output.

3. Conclusions:

The signals were positive and we may expect that in some years all important cities in the country develop local investments based on the funds obtained from the bond emissions.

The positive evolutions both of the emission values and of maturities mark a positive and correct direction of development of the municipal debt market in which the bonds are basically used for the long term financing of the municipality needs.

The interest shown to the municipal bonds prove that the issuers consider these instruments as an efficient way of financing their investment projects, while the investors find them an instrument which offers interests superior to those existent on the bank market and with a lower risk degree in comparison to the shares on the stock exchange.

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