

# Research

## U.S. Market Outlook



### Municipal, Mortgage, and ABS Issuance Expected to Decrease in 2003

Bond dealers predict a drop in issuance in 2003 for municipal, mortgage-backed and asset-backed securities relative to record issuance levels in 2002.<sup>1</sup> Lower issuance levels will come about as rising interest rates and

continued moderate economic growth limit demand for new capital. These projections reflect the results of a survey of Bond Market Association members on their outlooks for 2003 market activity.

### Municipal Outlook

MUNICIPAL ISSUANCE			
\$ Billions	2002*	Projected 2003	% Change
Short-Term	72	67	-7.8%
Long-Term	358	294	-17.9%
Total	430	361	-16.2%

\* Source: Thomson Financial Securities Data

Municipal issuance is expected to fall in 2003 to \$361 billion, down 16.2 percent from the record of \$430 billion set in 2002. Despite the lower volumes projected for 2003, issuance will likely be above the previous record set in 2001. Long-term issuance is anticipated to decrease to \$294 billion in 2003, down from the \$358 billion issued in 2002. The decrease in short-term note issuance will be less pronounced and is projected to total \$67 billion, down 7.8 percent from the \$72 billion

issued in 2002. Survey respondents expect 2003 to be very challenging year for local and state governments, who will continue to face significant fiscal pressures. Modest economic growth and a sluggish stock market will result in slower growth in tax receipts, particularly for capital gains taxes. Weak state and local budget conditions will result in a likely increase in new money issuance as governments have less cash on hand to fund capital expenditures. Overall issuance in the first quarter of 2003 is expected to be strong, before declining for the remainder of the year. Interest rates are expected to increase, especially in the second half of 2003, which will contribute to lower refunding bond issuance. Also, an expected dearth of massive financing deals such as those completed in New York and California in 2002 will contribute to lower overall issuance volume.

### Mortgage-Related Outlook

Issuance volumes in the mortgage-related securities market, which includes agency and private-label pass-throughs and CMOs, set a record in 2002 of \$2.27 trillion. The weak

economy in 2002 contributed to a decline in the mortgage interest rates to 40-plus-year lows, which led to higher refinancing and origination activity. Mortgage originations

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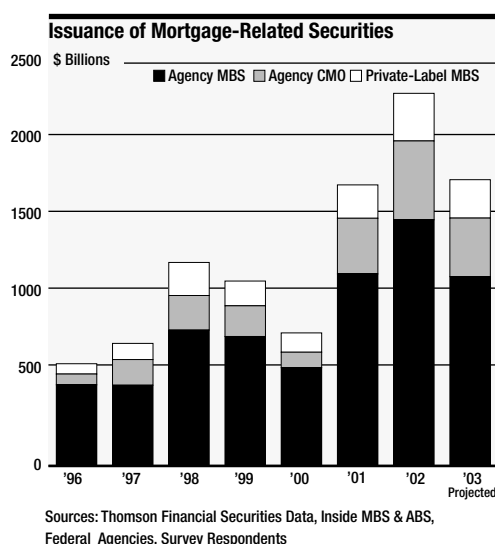
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<sup>1</sup> Estimates were derived by surveying Association member firms. The projections represent the median of the individual member's submissions. Data for 2002 is preliminary and may be subject to revision.

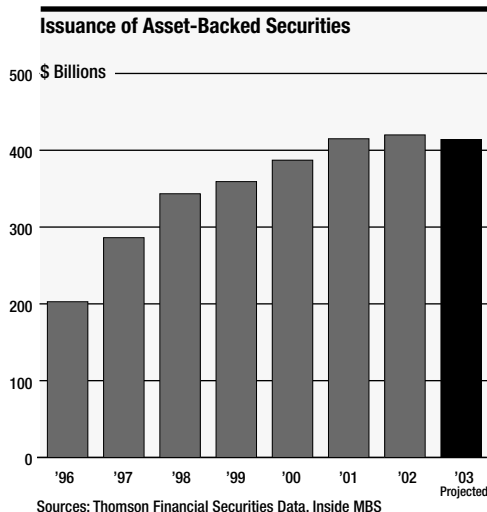
## Mortgage-Related Outlook



reached a record of \$2.46 trillion in 2002, according to the Mortgage Bankers Association of America. In 2003, new issue activity of mortgage-related securities are projected to decrease 24.8 percent, to \$1.78 trillion, down from the \$2.27 trillion issued in 2002. Market participants expect mortgage rates to remain stable and near the current low in the upcoming year. Loan originations and MBS issuance will drop as a result, given that many homeowners who could refinance at current rates have already done so. Housing starts and new and existing home sales are expected to decrease slightly in 2003, again contributing to lower MBS

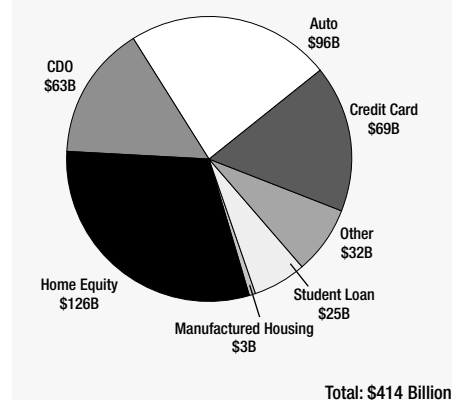
volume. Issuance of agency pass-throughs is projected to decline 25.6 percent, to \$1.08 trillion in 2003, down from the \$1.45 trillion issued in 2002. Agency CMO issuance is expected to decline 25.7 percent, to \$381 billion in the upcoming year, down from the \$513 billion issued in 2002. Private-label MBS is projected to decrease 19.4 percent, to \$250 billion in 2003, down from the \$310 billion issued in 2002. Market participants anticipate CMBS new issue volume to remain flat due to continuing downgrades and credit deterioration in certain sectors as well as rising interest rates and modest economic growth.

## ABS Outlook



New issue volume in the ABS market, including public and private issues, is expected to decrease slightly to \$414 billion in 2003, down 1.5 percent from the \$420 billion issued in 2002. The ABS market set a record in 2002, partly due to the weak economy and

**2003 ABS Projected Issuance by Major Type of Credit**



Estimates were derived by surveying Association member firms

the credit and liquidity difficulties observed in the corporate sector. Issuers utilized the ABS market in 2002 to lower funding costs while investors looked for safer investments. Market participants expect interest rates to begin rising in the second half

of 2003, and the home equity sector is likely to experience a decrease in issuance due to these higher interest rates. The auto sector had a very strong year in 2002 and is expected to remain relatively flat in 2003. Market participants anticipate a slight growth in the credit card market issuance volumes, but chargeoffs and delinquencies will continue to concern investors. Issuance in the student loan sector was strong in 2002, and it is expected to increase moderately in 2003 partly due to the fact that most transactions are backed by federally guaranteed collateral. Collateralized debt obligation (CDO) issuance is predicted to increase in 2003, reflecting an easing of credit concerns as the economy recovers. Market participants anticipate the manufactured housing sector will continue to decrease due to persisting delinquencies and high repossession of inventories in 2003.