



*Presentation to:*

**State of Iowa**

*Relating to:*

➤ *Tobacco Settlement Asset-Backed Bonds, Series 2005*

December 18, 2013

# 2005 Bonds – Overview

- In November 2005, the Tobacco Settlement Authority (“TSA”) issued \$831,962,030 of Tobacco Settlement Asset-Backed Bonds, Series 2005 (the “Series 2005 Bonds”)

## Use of Proceeds

- The Series 2005 Bonds refunded the TSA’s Series 2001A and 2001B Bonds. The Pledged TSRs remained at 78%, leaving 22% of TSRs (the “Unencumbered TSRs”) which are owned by the TSA and flow to the Tobacco Settlement Trust Fund

## Amount Outstanding

Description	Amount	Call Date (6/1)	S&P Rating	Moody's Rating
<b>Current Interest Bonds (“CIBs”):</b>				
2023 (Taxable) (Series A)	\$137,705,000	2015	BB+	Ba1
2034 (Series B)	\$178,010,000 <sup>1</sup>	2017	B+	B2
2038 (Series C)	\$103,475,000	2015	B+	B2
2042 (Series C)	\$135,120,000	2015	B+	B2
2046 (Series C)	\$174,130,000	2015	B+	B2
<b>Capital Appreciation Bonds (“CABs”)</b>				
2046 (Series D)	\$15,775,344 <sup>2</sup>	2015	B-	N/R
2046 (Series E)	\$21,182,893 <sup>2</sup>	2015	N/R	N/R
<b>Total</b>	<b>\$765,398,237</b>			

1. Accreted value as of conversion date.
2. Initial Principal Amount.

## Expected Repayment

- Consumption declines have been more severe than originally forecasted (particularly in 2009: -9.15% and 2010: -6.41%) and the NPM Adjustment Dispute has reduced Pledged TSRs by approximately \$38.9 million to date
- Using the most recent IHS Global projection of future cigarette consumption (approximately -3% year-over-year decline) and TSRs adjusted for both future expected NPM Adjustments and DPA recoveries, the Series 2005 CIBs will be fully paid in 2044 but the Series 2005 CABs will default in 2046 (defaulted amount: \$463.3 million of the \$551.8 million maturity value)
  - ▶ The Series 2005 CABs are not expected to be fully paid until 2063, seventeen years after their scheduled maturity date
  - ▶ The Pledged TSRs (78%) will not be available to the State until all of the Series 2005 Bonds are fully paid, therefore the State has a very real economic interest in the default status of the Series 2005 Bonds

# Existing Series 2005 Bonds Default in 2046 Under IHS Forecast (3% Y-o-Y Decline)

Revenue Year	78% of Iowa's TSRs	Reserve Earnings	Reserve Withdrawal / (Deposit)	Reserve Balance	Total Available for DS and Redemptions	Operating Expenses at the Operating Cap	Maturing Principal	Redeemed Principal	Interest	Principal Paid after Default	Interest Paid after Default
2014	56,836,165	17,760	-	59,198,916	56,853,925	277,775	-	15,355,000	41,208,541	-	-
2015	56,498,080	147,997	-	59,198,916	56,646,077	286,108	-	16,110,000	40,185,929	-	-
2016	51,662,266	236,796	-	59,198,916	51,899,061	294,691	-	12,295,000	39,262,766	-	-
2017	54,793,883	295,995	-	59,198,916	55,089,878	303,532	-	16,430,000	38,329,204	-	-
2018	46,212,580	384,793	-	59,198,916	46,597,373	312,638	-	8,730,000	37,511,504	-	-
2019	48,707,749	443,992	-	59,198,916	49,151,740	322,017	-	11,960,000	36,839,079	-	-
2020	48,019,264	443,992	-	59,198,916	48,463,256	331,678	-	12,075,000	36,057,941	-	-
2021	47,876,935	443,992	-	59,198,916	48,320,927	341,628	-	12,725,000	35,251,941	-	-
2022	45,537,271	443,992	-	59,198,916	45,981,263	351,877	-	11,155,000	34,475,841	-	-
2023	45,506,011	443,992	(8,493,650)	50,705,266	37,456,353	362,433	20,870,000	-	33,435,029	-	-
2024	45,532,685	412,141	8,493,650	59,198,916	54,438,476	373,306	-	4,215,000	32,638,734	-	-
2025	45,621,418	443,992	-	59,198,916	46,065,410	384,505	-	13,540,000	32,141,594	-	-
2026	45,759,014	443,992	-	59,198,916	46,203,006	396,040	-	14,450,000	31,357,874	-	-
2027	45,930,117	443,992	-	59,198,916	46,374,109	407,922	-	15,445,000	30,520,814	-	-
2028	46,121,748	443,992	-	59,198,916	46,565,740	420,159	-	16,520,000	29,625,794	-	-
2029	46,317,276	443,992	-	59,198,916	46,761,268	432,764	-	17,660,000	28,668,754	-	-
2030	46,509,252	443,992	-	59,198,916	46,953,244	445,747	-	18,860,000	27,646,194	-	-
2031	46,701,267	443,992	-	59,198,916	47,145,259	459,119	-	20,130,000	26,554,474	-	-
2032	46,897,225	443,992	-	59,198,916	47,341,217	472,893	-	21,480,000	25,389,394	-	-
2033	47,096,906	443,992	-	59,198,916	47,540,898	487,080	-	22,905,000	24,146,614	-	-
2034	47,268,331	443,992	-	59,198,916	47,712,323	501,692	12,805,000	11,570,000	22,835,790	-	-
2035	47,433,818	443,992	-	59,198,916	47,877,810	516,743	-	25,890,000	21,470,513	-	-
2036	47,599,120	443,992	-	59,198,916	48,043,112	532,245	-	27,475,000	20,036,328	-	-
2037	47,756,007	443,992	-	59,198,916	48,199,999	548,213	-	29,140,000	18,514,800	-	-
2038	47,815,842	443,992	-	59,198,916	48,259,834	564,659	9,400,000	21,405,000	16,890,400	-	-
2039	47,964,004	443,992	-	59,198,916	48,407,996	581,599	-	32,675,000	15,150,575	-	-
2040	48,089,836	443,992	-	59,198,916	48,533,828	599,047	-	34,635,000	13,299,550	-	-
2041	48,208,403	443,992	-	59,198,916	48,652,395	617,018	-	36,695,000	11,337,975	-	-
2042	48,340,638	443,992	-	59,198,916	48,784,630	635,529	9,710,000	29,200,000	9,240,588	-	-
2043	48,458,880	443,992	-	59,198,916	48,902,871	654,595	-	41,255,000	6,992,016	-	-
2044	48,567,738	221,996	59,198,916	-	107,988,650	674,232	-	103,763,468	2,915,859	-	-
2045	48,670,845	-	-	-	48,670,845	694,459	-	4,219,160	43,759,941	-	-
2046	48,768,851	-	-	-	48,768,851	715,293	-	3,973,187	44,076,774	-	-
2047	48,871,068	-	-	-	48,871,068	736,752	-	-	-	3,742,924	44,395,613
2048	48,977,623	-	-	-	48,977,623	758,855	-	-	-	3,525,062	44,689,317
2049	49,088,643	-	-	-	49,088,643	781,620	-	-	-	2,296,480	46,012,545
2050	49,204,262	-	-	-	49,204,262	805,069	-	-	-	2,075,218	46,326,090
2051	49,324,616	-	-	-	49,324,616	829,221	-	-	-	1,938,494	46,552,691
2052	49,449,846	-	-	-	49,449,846	854,097	-	-	-	1,811,452	46,787,866

█ = Default

## Default of Existing Series 2005 Bonds (Cont'd)

Revenue Year	78% of Iowa's TSRs	Reserve Earnings	Reserve Withdrawal / (Deposit)	Reserve Balance	Total Available for DS and Redemptions	Operating Expenses at the Operating Cap	Maturing Principal	Redeemed Principal	Interest	Principal Paid after Default	Interest Paid after Default
2053	49,580,097	-	-	-	49,580,097	879,720	-	-	-	1,692,331	47,003,731
2054	49,715,519	-	-	-	49,715,519	906,112	-	-	-	1,581,719	47,232,121
2055	49,856,265	-	-	-	49,856,265	933,295	-	-	-	1,477,856	47,438,112
2056	50,002,495	-	-	-	50,002,495	961,294	-	-	-	1,381,621	47,665,379
2057	50,154,371	-	-	-	50,154,371	990,133	-	-	-	1,291,253	47,871,950
2058	50,312,062	-	-	-	50,312,062	1,019,837	-	-	-	1,207,048	48,082,876
2059	50,475,741	-	-	-	50,475,741	1,050,432	-	-	-	1,128,416	48,292,203
2060	50,645,587	-	-	-	50,645,587	1,081,945	-	-	-	1,055,360	48,517,548
2061	50,821,783	-	-	-	50,821,783	1,114,403	-	-	-	986,411	48,707,905
2062	51,004,518	-	-	-	51,004,518	1,147,836	-	-	-	922,743	48,935,240
2063	51,193,988	-	-	-	51,193,988	-	-	-	-	563,034	32,065,227
							52,785,000	683,935,815	907,769,121	28,677,422	786,576,414

# Default Prevention Approaches

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## Refunding

- The vast majority of Series 2005 Bonds can not be advance refunded on a tax-exempt basis until June 1, 2015 (the Series B Bonds are callable in 2017)
- A current refunding of the bonds callable in 2015 may not be feasible due to the high leverage of the 2005 Bonds (as indicated by the current credit ratings) and the relatively low coupons
  - ▶ Thin coverage on new refunding bonds will limit marketability and fail to meet rating agency criteria for investment grade ratings due to more stringent stress tests than in 2005

## Credit Enhancement

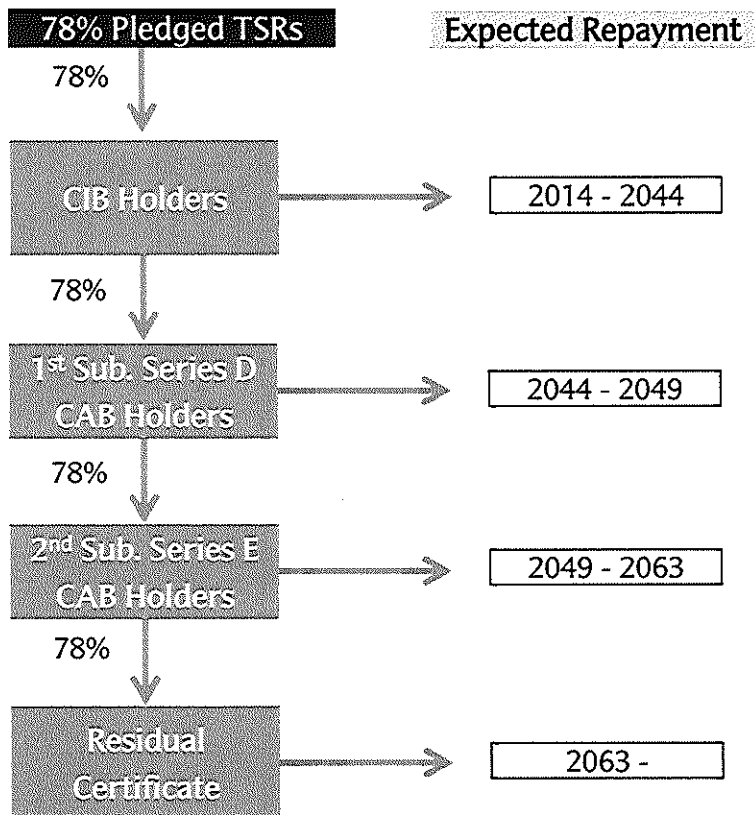
- The TSA can avoid default and generate significant fee income for the State today by having the State provide credit enhancement consisting of a pledge of its remaining 22% of TSRs for an expected short duration
  - ▶ Providing the 22% pledge to the 2005 CABs will dramatically improve their credit ratings (the “Enhanced CABs”)
  - ▶ Beginning in 2015, the 22% of TSRs would be used annually to optionally redeem the CABs at their then accreted value until all of the CABs are retired
  - ▶ Based on current estimates of TSRs<sup>1</sup>, the CABs would be fully paid in 2020 returning the 22% of TSRs to the State
  - ▶ Remarketing the Enhanced CABs today will generate sufficient proceeds to pay the State a Credit Enhancement Fee
- The TSA would maintain full optional callability of the Series 2005 Bonds in 2015 and 2017
- Access to 100% of Pledged TSRs in 2044<sup>(1)</sup> when the Series 2005 Current Interest Bonds are expected to be fully paid
- Total PV benefit of approximately \$123.2 million including the approximately \$38.1 million Credit Enhancement Fee paid to the State at closing, subject to negotiations with existing bondholders

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<sup>1</sup> Assumes IHS Global projection of cigarette consumption with 10% NPM Adjustment and annual DPA recoveries.

# Current Series 2005 Structure (“Status Quo”)<sup>1</sup>

## Bond Expected Repayment with 78% Pledged TSRs

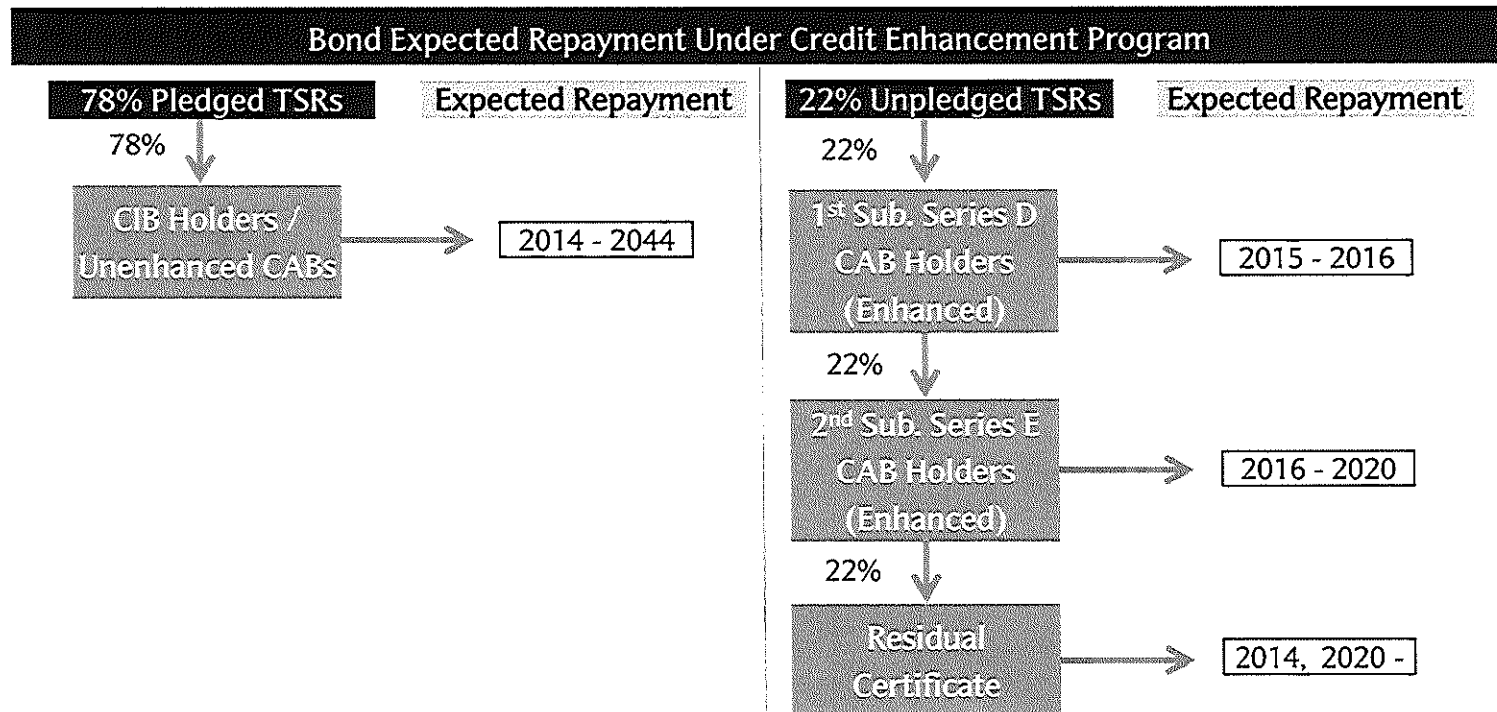


- The current Series 2005 structure will pay the CIB holders through 2044, the Series D CAB holders through 2049 and the Series E CAB holders through 2063
  - ▶ The CABs will default in 2046
  - ▶ The State receives its first residual payment in 2063

<sup>1</sup> Assuming IHS Global forecast.

# Enhanced CAB Holders - Credit Enhancement Program<sup>1</sup>

- Beginning in 2015, the State's Unpledged TSRs will be applied to redeem Enhanced 2005 CABs
  - Barclays has identified all existing CAB holders
  - The holders would pay the State a Credit Enhancement Fee of approximately \$38.1 million
  - The CIB holders are unaffected by the Credit Enhancement Program



<sup>1</sup> Assuming IHS Global forecast.



## Credit Enhancement Impact on Redemption and Market Value

- Annually, the Trustee will mandatorily apply the 22% Unpledged TSRs to the optimal redemption of the Credit Enhanced Bonds at their original accreted value beginning in 2015
- The CABs are fully redeemed by 2020 with the credit enhancement, 43 years sooner than the status quo
  - ▶ The average life is reduced to 1.95 years and 4.72 years for the Credit Enhanced 1<sup>st</sup> subordinate and 2<sup>nd</sup> subordinate CABs, respectively

Debt Service of Credit Enhanced CABs		
Date	Debt Service of 1 <sup>st</sup> Sub CAB	Debt Service of 2 <sup>nd</sup> Sub CAB
6/1/2015	\$15,935,023	\$ -
6/1/2016	13,162,375	1,408,969
6/1/2017		15,454,786
6/1/2018		13,034,160
6/1/2019		13,738,505
6/1/2020		7,812,024
<b>Total</b>	<b>\$29,097,398</b>	<b>\$51,448,444</b>

CAB Current Market Value	
Series D (8.50% / \$6.684)	\$12,753,072
Series E (11.50% / \$2.641)	9,533,746
	<b>\$22,286,818</b>

CAB Ending Market Value	
Series D (6.25% / \$13.531)	\$25,818,072
Series E (7.125% / \$10.276)	37,093,746
	<b>\$62,911,818</b>

CAB Market Gain Value	
Series D (\$6.847)	\$13,064,997
Series E (\$7.635)	27,560,000
	<b>\$40,625,000</b>

- Net of transaction expenses the Credit Enhancement Fee paid to the State is estimated to be \$38.1 million

<sup>1</sup> Assuming IHS Global forecast.



## Series 2005 PV of Residual Calculations

- The Credit Enhancement Program will provide the State with a total PV benefit of approximately \$123.2 million including the \$38.1 million Credit Enhancement Fee paid to the State at closing, subject to negotiations with existing bondholders

PV Calculations <sup>1</sup>		
Dates	Net Change in TSRs Available to the State	PV Difference (PV @ 4.5%)
6/1/2015	\$(15,935,356)	\$(14,804,756)
6/1/2016	(14,571,408)	(12,892,932)
6/1/2017	(15,454,685)	(13,023,300)
6/1/2018	(13,034,317)	(10,460,679)
6/1/2019	(13,738,083)	(10,500,462)
6/1/2020	(13,543,895)	(9,859,084)
...		
6/1/2044	945,981	213,517
6/1/2045	48,670,845	11,688,042
6/1/2046	48,768,851	11,207,252
6/1/2047	48,871,068	10,747,121
6/1/2048	48,977,623	10,306,749
6/1/2049	49,088,643	9,885,275
6/1/2050	49,204,262	9,481,873
6/1/2051	49,324,616	9,095,757
6/1/2052	49,449,846	8,726,173
6/1/2053	49,580,097	8,372,399
6/1/2054	49,715,519	8,033,749
6/1/2055	49,856,265	7,709,562
6/1/2056	50,002,495	7,399,210
6/1/2057	50,154,371	7,102,090
6/1/2058	50,312,062	6,817,627
6/1/2059	50,475,741	6,545,269
6/1/2060	50,645,587	6,284,491
6/1/2061	50,821,783	6,034,790
6/1/2062	51,004,518	5,795,683
6/1/2063	33,005,056	3,588,890
<b>Totals</b>	<b>\$842,597,483</b>	<b>\$85,046,834</b>

<sup>1</sup> Assuming IHS Global forecast.

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