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Premium Municipal Bonds and Issuer Fiscal Distress

Federal Reserve Bank of Cleveland, Working Paper No. 15/34

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Abstract


Economic theory suggests that bond issuers of lower credit quality or higher opacity should be more likely to issue bonds with premium coupons (higher coupon rates relative to yields at issuance). Using a comprehensive data set of municipal bonds issued between 1992 and 2012 by more than 21,000 issuers, we show that this has not been the case until the early 2000s. We examine what changed in this market to bring it into greater alignment with economic principles. We argue that the Government Accounting Standards Board's Statement 34 that required the use of accrual accounting rules in government financial reports deserves the credit.

Keywords: Premium Bonds, Public Financial Management, Municipal Bonds, Fiscal Stress, GASB Statement 34

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