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Louisiana Bond Blues Deepen as Rating Cut Seen on Budget Deficit.

With tax revenue from the oil industry falling short of projections, the deficit has swelled to \$1.6 billion for the fiscal year that starts July 1. Moody's Investors Service and Standard & Poor's say they may lower Louisiana's credit rating if officials don't come up with sustainable budget solutions.

Louisiana paid the price when it sold \$335 million of general obligations Wednesday, its first deal this year. Borrowing costs jumped compared with an issue in November, with the yield spread more than doubling on some maturities.

"They have to make significant cuts across the board — it's almost a foregone conclusion they'll be downgraded," said Tom Metzold, co-director of municipal investments in Boston at Eaton Vance Management, which oversees \$25 billion in local debt.

Lawmakers are grappling with the state's finances in part as the price of crude oil, which along with natural gas generates 13 percent of its revenue, is down about 40 percent from mid-2014. The mounting fiscal strains threaten to pinch funding for programs such as higher education, contributing to a buyers' revolt last month against a bond sale from the state's flagship university.

School Deal

Investors asked for extra compensation to own the state's debt in Wednesday's offering. Obligations maturing in May 2025 priced at a yield of 2.5 percent, or about 0.3 percentage point above benchmark munis, according to data compiled by Bloomberg. The gap swelled from 0.03 percentage point when the state issued 10-year securities in November.

Louisiana State University scrapped its \$114 million bond offering after officials warned that exigency, which would allow it to restructure and fire tenured faculty, may be a worst-case scenario for the school.

Treasurer John Neely Kennedy had warned that the canceled deal might push up the state's borrowing costs.

"When a state mismanages its money, it can't expect people to give it more until it proves it changed its ways," Kennedy said in an interview before the bond sale.

Waiting Game

Both Moody's and S&P affirmed Louisiana at the third-highest rank last month. The companies dropped their outlooks to negative in February after sinking crude prices led the state to cuts its revenue forecast.

"They're struggling to figure out how to balance their budget and we're waiting to see" what happens, Marcia Van Wagner, a Moody's analyst in New York, said in an interview.

As part of the fiscal fix, Governor Bobby Jindal, a potential Republican presidential candidate, is proposing cutting more than \$200 million from higher education and lowering corporate tax credits by over \$500 million.

"When there are budgetary challenges, we manage them in a timely way," Kristy Nichols, Louisiana's commissioner of administration, said in an interview from Baton Rouge before the bond issue. "There's confidence that we'll move through the legislative process in the next month and a half and walk away with a balanced budget that addresses some structural issues by identifying recurring savings and recurring revenue."

Proceeds from Wednesday's deal will fund hospital and sports-arena projects in New Orleans, nicknamed "The Big Easy," Nichols said.

The yield spreads in recent trading aren't enough for some investors.

Steve Hlavin, who runs a Louisiana fund for Nuveen Asset Management in Chicago, said he hasn't bought state general obligations since 2010 and probably won't dive back in Wednesday.

"For a state that's exhibited chronic structural budget imbalance, you aren't being compensated with a lot of credit spread," Hlavin said. "They're being forced to come to terms with the fact that one-shot solutions are no longer available."

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