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Why Harvey's Not Rattling a Bond-Market Haven: QuickTake Q&A

The record-setting flooding that's devastating Houston has caused thousands to flee their homes, submerged much of the city and left tens of billions of dollars in damage. It has also cast some uncertainty over the finances of governments in the devastated region that routinely raise money in the U.S. municipal-bond market. In just Texas's Harris County, the home of Houston, there are about \$67 billion of outstanding government bonds, some issued for hospitals, sewer lines, schools and other projects potentially affected by the deluge. So far, however, investors appear relatively confident that an influx of aid will keep those borrowers from going under.

1. Will Harvey cause municipal-bond defaults?

That's extremely unlikely. Natural disasters haven't caused a single default by a municipal borrower that was rated by Moody's Investors Service, according to David Jacobson, the company's spokesman. Even Hurricane Katrina, which flooded much of New Orleans and triggered a lasting exodus from the city, didn't force it to renege on bond payments as the state and federal government extended aid to help the region rebuild.

2. How has the bond market reacted?

There's been very little trading of bonds issued by affected government agencies since Harvey hit, with no significant changes in the prices of those that have changed hands. Such a muted reaction also followed Katrina and Sandy, the superstorm that hammered New York and New Jersey in 2012. The small lots of securities that have traded indicate that it's individual bondholders who are reacting, not mutual funds and other big investors. Matt Fabian, a managing director at Municipal Market Analytics, said in a note to clients that if there is a significant drop in the price of Houston's bonds it may be a good time to buy.

3. How strong are the public finances of the region?

Texas for years had one of the fastest growing state economies in the U.S., thanks to an oil boom, a population influx and companies relocating there. While the pace of growth slowed in 2016 after oil prices slipped, Texas expanded at a rate of 3.9 percent during the first quarter of 2017, faster than any other state and more than triple the pace of the overall U.S. Texas's government has a AAA grade from the two major credit rating companies. Houston has also been gaining ground before the storm. Houston will have the funds needed to handle the aftermath of the storm, Mayor Sylvester Turner said in a post on Twitter, citing the city's controller.

4. How will this impact public finances in the region?

With the area still gripped by the flooding, it's still too early to say. S&P Global Ratings, which grades 25 of the 54 counties included in Texas's declaration of emergency, said that while the disaster could have a negative impact on the ratings of various governments, federal and state aid

and insurance payments tend to offset the impacts of natural disasters. “There’s no question the hurricane’s devastation of the fourth-largest city in the U.S. could have a negative effect on the credit quality of various local government issuers, but it’s too soon to tell,” the company said. Much depends on the response of the federal government. President Donald Trump has said he’ll work with Congress to extend emergency funds to Texas, as was done for the areas battered by Katrina and Sandy.

5. Are there any types of bonds worth watching?

One niche that may be affected are so-called Municipal Utility Districts, which issue bonds to finance infrastructure for new housing developments. The debt is repaid through a portion of homeowners’ property taxes. S&P said it rates 564 such districts in the Houston area. If too many people leave after the storm, it could hinder their ability to make debt payments, according to S&P.

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