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Illinois Bond Spread Hits Six-Month High Over Political Discord.

- **Political uncertainty spooks investors in run up to election**
- **Governor wants to roll back tax hike that ended impasse**

Six months after Illinois resolved a budget stalemate that pushed its bonds close to a junk rating, investors are concerned that another political fight may be on the horizon.

In a sign that bondholders are bracing for election-year dysfunction from the worst-rated U.S. state, the extra yield that investors demand to hold Illinois's 10-year general-obligation bonds instead of benchmark debt rose to about 1.9 percentage points, according to data compiled by Bloomberg. That's the most since July 20.

Illinois avoided becoming the first state to be downgraded below investment grade after it ended a record, two-year budget impasse in July, when the Democrat-led legislature approved an income-tax hike over Republican Governor Bruce Rauner's veto. But on Monday, Rauner reiterated plans to roll back that increase, telling reporters he will lay out a process to do so during his budget address next month, fueling speculation of another standoff with Democrats.

"The market doesn't know what to expect from the political perspective," said Guy Davidson, director of municipal investments at AllianceBernstein LP, which oversees about \$40 billion of municipal fixed income securities.

Another impasse could again threaten the state's rating and leave the government reckoning with unpaid bills. Last year, Illinois spent \$1 billion on fees for not paying its bills on time, according to the comptroller's office.

"This is like putting \$1 billion in the street and lighting it on fire," said Laurence Msall, president of the Civic Federation, a nonprofit that monitors the state's finances. "It's a penalty of our own creation from our own financial recklessness."

Concerns about another impasse may be "providing a degree of caution" for investors, said Neene Jenkins, vice president and municipal credit analyst at AllianceBernstein. Rauner, a Republican, is up for re-election on Nov. 6, 2018, assuming he survives a primary challenge in March.

A potentially contentious budget and election season could mean extra yield for Illinois bondholders.

"You're going to be paid by the state," said Davidson who doesn't think Illinois is a default risk. "It could be a volatile period ahead due to politics."

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