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Credit Analysts Cautious Over Illinois Budget, Infrastructure Plan.

CHICAGO (Reuters) - Some results from Illinois' action-packed spring legislation session that produced a budget and a variety of revenue-raising measures won initial praise on Monday from credit rating analysts, who cautioned that fiscal challenges remain.

Lawmakers wrapped up the session on Sunday, passing a \$40.1 billion fiscal 2020 budget and a \$45 billion infrastructure plan, along with a variety of tax and fee hikes and projected new revenue from a massive gambling expansion that includes sports betting, and from legalizing recreational marijuana.

Illinois has the lowest credit ratings among U.S. states at a notch or two above the junk level due to its huge \$133.5 billion unfunded pension liability and chronic structural budget deficit.

Carol Spain, an S&P Global Ratings analyst, said the state's recently increased forecast for income tax collections along with revenue measures passed by the legislature resulted in a budget with "few one-time revenues."

"In S&P Global's view, the fiscal 2020 budget signals near-term credit stability and buys the state more time to address out-year gaps," she said in an email.

Spain added that to maintain an investment-grade rating, further progress is needed "toward sustainable structural balance, paying down its bill backlog, and addressing its pension liabilities."

Ted Hampton, a Moody's Investors Service analyst, said full payment of Illinois' fiscal 2020 pension contribution, which lawmakers said was in the budget, would be a positive move.

After an unexpected income tax revenue surge in April, Democratic Governor J.B. Pritzker dropped a proposal to extend the state's current 50-year pension payment plan and reduce the coming fiscal year's contribution.

Hampton said he will have to look at a provision in the budget that would restore a 6% cap on end-of-career teacher salary increases that had previously been lowered to 3% to cut pension costs.

Lawmakers also voted for a three-year extension of a bond-financed pension benefit buyback program also aimed at reducing costs.

A "Rebuild Illinois" capital plan passed by lawmakers is supported by higher taxes on gasoline, parking, and cigarettes, as well as money from a gambling expansion that adds casinos, including the first for Chicago.

"Generally, when we see states gathering the political courage to do things like raise gasoline taxes for an infrastructure plan that's also positive," Hampton said.

The \$20.8 billion of bonds included in the plan would “substantially” increase Illinois’ debt burden, according to Spain.

“The new revenues that will support increased debt service will relieve some state operating pressure, but Illinois’ large liabilities will continue to weigh on its credit profile,” she said.

Meanwhile, Illinois’ yield penalty in the U.S. municipal bond market, the biggest among states, has shrunk to its lowest level since 2014 for 10-year bonds, according to Municipal Market Data (MMD). The state’s bonds are yielding 139 basis points over MMD’s benchmark triple-A yield scale, down from as much as 185 basis points earlier this year.

(Reporting by Karen Pierog in Chicago; Editing by Matthew Lewis)

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