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Christie's Recovery Elusive as Bond Market Penalizes New Jersey.

As New Jersey prepared for its biggest bond sale in more than two years, Governor Chris Christie's office said a break in rating cuts for the Garden State showed that its finances are on the mend. Bond prices suggest otherwise.

The extra yield investors demand to buy New Jersey bonds instead of top-rated debt is holding close to the highest since at least January 2013. When New Jersey began marketing the $2.2 billion of securities last week, 20-year bonds were offered for a yield of 5.07 percent, more than 2 percentage points above the benchmark, according to three people familiar with the sale who requested anonymity because pricing wasn't final.

"The state is going to continue to have issues," said Scott McGough, who helps manage about $3 billion of municipal debt as director of fixed income for Glenmede Trust Co. in Philadelphia and isn't buying New Jersey bonds. He said officials aren't "making the adjustments you would want them to do."

New Jersey has a lower rating than any state except Illinois after nine downgrades since Christie took office in January 2010 and vowed to repair a government battered by the recession and squeezed by swelling shortfalls in its pension funds. That deficit, now $83 billion, has continued to grow despite a cut to benefits, as the slow recovery left Christie without money needed to make up for years of shortchanging the retirement system.

Ratings Respite

While New Jersey's bond yields have climbed relative to other securities, they're still less than they were in 2013 as municipal borrowing costs hover at a five-decade low.

New Jersey Assistant Treasurer Steven Petrecca said yield penalties have risen because of heightened investor scrutiny brought on by the fiscal struggles of Puerto Rico and Chicago.

"The bottom line here is that we believe that our bonds will be received because we always pay our debt," he said.

The state won a respite from the cuts to its rating ahead of the sale Tuesday by its Economic Development Authority, which is raising money to refinance debt and fund school construction. It's New Jersey's biggest securities offering since January 2013, Petrecca said.

Fitch Ratings on Aug. 18 changed the outlook on New Jersey to stable from negative, signaling that the state won't be downgraded again soon. The New York-based company said conservative revenue forecasts reduce the risk of another late-year budget deficit like those that have "plagued the state in recent years."

'Continued Progress'

Christie, who is campaigning for the Republican presidential nomination as a politician who cleaned up a fiscal mess he inherited, seized on the assessment.

The report from Fitch recognizes Christie's "continued progress in responsibly managing the state's finances by cutting discretionary spending, increasing reserves, and conservatively forecasting revenue," his office said in a statement.

The administration also drew on a less sanguine assessment from Moody's Investors Service, which said New Jersey's rating could be reduced again if the pension strains worsen, to make the case for further benefit cuts. "The problem is the unwillingness of Democrats in the legislature to come to the table and fix a broken system," his office said.

Assemblyman Gary Schaer, a Democrat who chairs the house's budget committee, said Christie has continued to shortchange the retirement system and failed to put needed money into schools and infrastructure.

Festering Wounds

"All of these problems remain and they are, at best, festering wounds with little or no triage going on," Schaer said. "There's no long-term plan to confront any of the fiscal issues facing the state."

The pension-system deficit may widen because Christie's administration is contributing $1.3 billion to it this year, less than half the $3.1 billion set by a 2011 law he signed that sought to make up for years of underfunding. He used the money to cover the government's bills when tax collections fell short of forecasts.

Fitch and Standard & Poor's grade New Jersey debt A, the sixth-highest level, while Moody's places it in the same rank at A2.

"There's been no success really in terms of dealing with the liability side of the equation," said Paul Brennan, a money manager in Chicago at Nuveen Asset Management, which oversees about $100 billion of munis. "We're now at the point where it's becoming critical."

Market's View

His view is reflected in the bond market. Ten-year New Jersey debt yields 3.2 percent, or 0.96 percentage point more than benchmark tax-exempt munis. That's close to the record high touched in July, according to data compiled by Bloomberg. The data begin in January 2013.

Investors have also demanded a higher premium to buy bonds sold by the economic development authority, which are rated one step below the state's general obligations. Securities due December 2016 traded Monday for a yield of 1.5 percent, about 1.16 percentage points over benchmark munis. That's higher than the average of 1.1 percentage point since March.

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