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Incentive To Pay: How Recent Bankruptcies Inform Analysis Of Distressed Local Government Credits.

Though rating trends are overwhelmingly upward across all municipal sectors (see "U.S. Public Finance Positive Ratings Streak Reaches 14-Year High," Sept. 2, 2015) Standard & Poor's Ratings Services has also seen borrowers like Atlantic City, N.J.; Wayne County, Mich.; and, most recently, Hillview, Ky., trying to work through fiscal stress. Though comprising only a very small percent of overall local government ratings, distressed credits bring into play analytical considerations that aren't usually a factor in this overall strong sector.

Often the hallmark of extremely distressed credits is concern regarding sufficient liquidity, whereby issuers may face a decision on who to pay: Peter or Paul (or Jane or Jenny, for that matter). While the framework of our local government criteria applies to all of our local government ratings, for distressed credits, where rating caps are often invoked, we address the questions regarding management's incentives to pay under strain. This report will focus on the somewhat unique analytical considerations we believe play into this subset of issuers.

Overview

- Pockets of stress continue to arise in the local government sector, though we still anticipate municipal bankruptcies and defaults will remain extremely low.
- Prioritization of payments during distress and while in bankruptcy may not be precedent-setting, but inform our analysis of how governments may act under stress.
- We continue to apply our criteria and insights gained to our analysis and the often unique set of incentives issuers have to prioritize payments. Standard & Poor's U.S. public finance credit ratings reflect the likelihood of default and do not incorporate recovery.

Continue reading.

24-Sep-2015