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California, Once Compared to Greece, Is Now Trading Better Than AAA.

- State benefits from booming real estate, stock markets
- 5-year G.O. index trading at yields below AAA counterparts

Seven years ago, California was “the next Greece.” Today, the state’s bonds are trading better than AAA.

As the Golden State benefits from record-breaking stock prices, Silicon Valley’s boom and a resurgent real estate market, demand for tax-exempt debt in the state with the highest top income tax rate in the U.S. is “insatiable,” said Nicholas Venditti, a portfolio manager for Thornburg Investment Management. Spreads are so tight that Venditti has stopped buying California bonds for his national fund.

“They’ve gone to a level that just seems ridiculous,” Venditti said. “It just seems unsustainable for any long period of time.”

If demand for California bonds is insatiable, supply is meager. Over the next 30 days, almost \$4 billion more bonds are set to mature or be paid off earlier than planned issuance, leaving investors with more cash to invest.

An investor Tuesday bought about \$1.1 million of state general obligation bonds maturing in six years at a yield of 1.33 percent, or 4.3 basis points below AAA rated bonds with the same maturity. California bonds are rated AA- by S&P Global Ratings and Fitch Ratings and Aa3 by Moody’s Investors Service.

If the market turns and spreads widen, investors holding California bonds may be “hit disproportionately hard,” Venditti said.

“It’s got to widen out quite a bit to get to a reasonable level relative to Kansas or Texas,” he said.

After the Great Recession, California was so strapped it took to issuing IOUs and drew comparisons with Greece. Now, flush with cash from the tech economy and record-breaking stock prices, California has boosted budget reserves to \$8.5 billion and made an extra \$6 billion payment to the state employee pension. At the local level, assessed values have recovered, bolstering property tax revenue.

“You have a whole swath of tech employees, tech investors, who are now trying to protect that substantial wealth from Uncle Sam,” Venditti said. “So they’ve gone out and they have bought up every municipal bond.”

Comparing California to Greece was obviously hyperbole, Venditti said. California’s gross domestic product rivals that of the U.K., the world’s fifth biggest economy. Greek sovereign bonds of 2027 maturity, meanwhile, have rallied from less than 12 cents on the dollar in June 2012 to about 88

cents today.

Bloomberg Markets

By Martin Z Braun

August 8, 2017, 11:01 AM PDT August 8, 2017, 2:03 PM PDT

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