Bond Case Briefs

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Municipal Bonds: When Full Faith And Credit Falls Flat.

Summary

- **With the proportion of retired pensioners and lifespans increasing across the globe, many governments face a challenging dilemma: how to raise enough tax revenues from the young to pay for the pensions promised to the retired?**
- **Pension liabilities didn't rattle US municipal bond markets much before the financial crisis a decade ago.**
- **Illinois bond ratings are already skating just one notch above "junk" status. If Illinois gets downgraded, the pain could be sharp.**

Once upon a time, US municipal bonds were generally considered less risky than corporate bonds. Backed by the full faith and credit of state governments, investors had confidence they would receive their principal plus interest without fail. Times have changed. For some states and local governments, decades of financial mismanagement and massive pension liabilities are threatening to upend the full faith and credit pledge. In this article, Franklin Templeton Fixed Income takes a look at the situation, with Illinois being an example of a particularly dire case.

As municipal bond analysts, assessing pension risks hinges partly on the willingness of elected officials to implement tangible pension reforms. Absent that, large pension obligations can significantly degrade budgets, credit quality, and eventually impair bondholders.

Continue reading.

Franklin Templeton Fixed Income Group

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