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Fed Expands Muni-Debt Program to Cover Smaller Cities, Counties.

- **Program adds multi-state issuers, 'fallen angel' provision**
- **Federal Reserve's new term sheet offers no new pricing details**

The Federal Reserve expanded the scope and duration of the Municipal Liquidity Facility, a $500 billion emergency lending program for state and local governments enduring the economic fallout from the coronavirus pandemic.

The U.S. central bank lowered the population thresholds under which counties and cities would be eligible to sell short-term debt to the facility. The new levels were at least 500,000 for counties and 250,000 for cities, down from 2 million and 1 million.

"That's fantastic," said Aaron Klein, a fellow at the Brookings Institution who was among critics of the program's original guidelines. The effort would now cover many of the nation's large cities that were previously excluded, he said, including Atlanta, Miami, Baltimore, Boston and New Orleans.

Klein and others had criticized the program's design for disproportionately excluding cities with large minority populations.

Record Sell-Off

The facility, which is not yet operational, is among nine programs announced by the Fed to limit the economic harm from the virus as businesses shutter to limit contagion. Its mere announcement on April 9 has helped municipal bonds recover from a record sell-off in March.

The rout caused borrowing costs for state and local governments to soar and billions of dollars in bond deals to be scuttled, raising concerns that municipalities would be unable able to raise money just as they shoulder the cost of fighting the pandemic.

Most recently, state and local debt has continued to struggle, with 30-year benchmark yields rising about 0.2 percentage points since April 20, according to Bloomberg BVAL.

"The broadening of the scope here might benefit market stability given the fragmented nature of munis," said Doug Benton, a senior municipal credit manager at Cavanal Hill Funds in Texas.

Wider Access

Lobbying groups like Government Finance Officers Association had asked the Fed to expand the scope of its short-term lending facility and offer access to a wider range of issuers, saying that some states may be reluctant to take on debt on behalf of smaller cities.

There are 87 cities that have populations above 250,000 as of 2018 and 140 counties that have populations above 500,000 as of 2019, according to Census Bureau statistics.

Guy LeBas, chief fixed income strategist at Janney Montgomery Scott LLC, said the expansion doesn't change the economics of the program. Smaller cities and counties could benefit from the funding under the original structure, but had to go hat in hand to their state governments. Under the new terms, they can sell debt directly to the facility.

Fallen Angels

The program was expanded to include certain multi-state entities. A new term sheet for the program also adds a so-called fallen angel provision, allowing some issuers whose credit ratings were downgraded after April 8 to qualify, provided they had been rated investment grade by two agencies as of that date.

The Fed said it was considering expanding the MLF to allow a limited number of governmental entities that issue bonds backed by their own revenue to participate directly in the facility.

The termination date for the program was also extended, to Dec. 31 from Sept. 30.

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The statement offered no new information on how the Fed intended to price the securities it purchases under the program, repeating this would be based on the issuer's rating at the time of purchase "with details to be provided later."

Separately, the New York Fed said PFM Financial Advisors LLC was acting as the administrative agent for the MLF.

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By Christopher Condon and Amanda Albright

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— With assistance by Steve Matthews, Danielle Moran, and Alexandre Tanzi