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NYC Bondholders Pricing In Downgrades on Worst Crisis in Decades.

- **None see repeat of city's 1975 brush with bankruptcy**
- **NYC's finances were solid before pandemic, investors say**

New York City's bondholders have downgraded the city, even if rating companies haven't.

Yields on the city's bonds are rising to compensate for the risks posed by the pandemic lockdown that could destroy an estimated 475,000 jobs this year and cost the government $7.4 billion in lost tax revenue. That has left New York's general-obligation debt trading at a level akin to A- rated securities, three steps below its current grade from S&P Global Ratings, according to data compiled by Bloomberg.

The coronavirus is providing one of the biggest tests of bondholders' faith in the most-populous U.S. city, which rebounded from a 1975 brush with bankruptcy, the Sept. 11, 2001 terror attacks and the 2008 financial crisis. While investors are confident New York will pay its debts, they're uncertain how long it will take for the economy to regain its footing.

"People who live in New York tend to love it and they have a lot riding on getting it back in place," said Guy Davidson, chief investment officer of municipal investments at AllianceBernstein Holding LP. "Will it come back? Yes. It's just a matter of how quickly."

New York's Office of Management and Budget forecasts the city's economy will contract 13% in 2020, almost triple the decline during the financial crisis of 2009. Job losses of 475,000 projected by the city's Independent Budget Office would be the worst the city has faced since the early 1970s, with the leisure, hospitality and retail expected to be the hardest hit. Budget officials project employment won't fully recover until 2023.

Risk Reflected

The city's bond yields reflect the risk. New York City's 10-year general-obligation bonds yield 1.85%, in line with those on full, faith and credit bonds rated A-, according to Bloomberg BVAL indexes. The city's bonds now yield 0.55 percentage point more than AAA bonds of the same maturity.

Investors' views of the Metropolitan Transportation Authority are more dire. With ridership down 95%, its bonds maturing in 3 years trade at an average yield of 5.1%, or the equivalent of 8.6% on a taxable bond — higher than the 8.3% yield on Nigeria's 5-year bonds.

S&P and Fitch Ratings rate the city's general-obligation debt AA, the third highest level. Moody's Investors Service rates the city's debt Aa1, one step higher. Both Fitch and Moody's changed their outlook on the city's bonds to negative this month.

New York isn't facing an immediate cash crunch. It had $8 billion available at the end of March, according to Fitch. If necessary, it can borrow from the $500 billion municipal lending facility set up by the Federal Reserve last month to support the $3.9 trillion municipal-bond market by extending short-term loans.

Bondholders take comfort in safeguards imposed after the 1975 fiscal crisis. The state would take over the city's finances if it doesn't pay its debts on time. Holders of the city's $38.8 billion general-obligation bonds are paid before property taxes are released to the general-fund budget.

Stable Source

The property tax, a stable source of revenue during recessions, is projected to raise $31 billion in the fiscal year starting July 1, more than seven times the debt service on general-obligation bonds. Another $40.7 billion of revenue bonds are backed by a first claim on personal income-tax receipts and sales-tax revenue.

"We've gone through a financial crisis, so the security on most of the bonds are pretty darn strong," said Davidson, the investor with AllianceBernstein.

Before the pandemic hit, New York City's economy was growing at a solid pace.

Employment grew for a 10th consecutive year in 2019, marking the longest expansion since at least 1950, as an economy long dominated by Wall Street continued to diversify.

Rising personal income-tax collections enabled the city to build up its reserves to about $10 billion.

"We're not talking about something that was teetering before this happened," said John Flahive, head of fixed income investments for BNY Mellon Wealth Management.

In the short term, New York City is balancing its budget by cutting spending and drawing on reserves. Mayor Bill de Blasio has proposed an $89.3 billion budget for the fiscal year beginning July 1 that was $6 billion less than the one planned in January. To bridge an $8.7 billion gap over the next 14 months, the city is tapping $4 billion of its reserves and cutting $2.7 billion in spending. The city expects to receive $2.6 billion in federal aid.

More Aid

Both de Blasio and Governor Andrew Cuomo are asking the federal government for billions more to make up lost tax revenue and increased spending related to the coronavirus. Without additional aid, the state could cut aid to municipalities by more than $8 billion, with most of the cuts falling on New York City.

"I'm very, very concerned," de Blasio said Sunday at a news conference, where he announced the formation of advisory councils to guide a reopening of the city's economy. "If New York City can't provide basic services there won't be a restart of the economy in New York City or New York State."

Also on Sunday, Cuomo outlined plans to begin a phased restart, beginning with construction and manufacturing, once the region experiences a 14-day decline in the hospitalization rate. The second phase, separated by a two week gap to assess progress, would open businesses based on how essential they are and the risk levels of infection, Cuomo said.

The phased reopening could begin upstate as soon as May 15. Reopening the densely populated New York City metropolitan area will take longer because of the complexity and need to coordinate with neighboring states, Cuomo said.

Businesses will have to develop plans to protect employees and customers and minimize the risk of infection. Everything from office configurations, to cleaning to transportation will have to be reexamined, Cuomo said.

Investors don't foresee an exodus of companies from New York. In time, commuters will return to the subways, trains and buses, albeit wearing masks and gloves.

"The habits of people in New York City will just adapt as they did after Sept. 11," said Rob Amodeo, head of municipal bond investments at Western Asset Management.

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