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Illinois Becomes First to Tap Fed Loans After Yields Surge.

- **State is poised to borrow \$1.2 billion from central bank**
- **Illinois is at risk of being first U.S. state cut to junk**

Illinois, which has faced escalating penalties in the bond market as the coronavirus batters its finances, is poised to become the first state to borrow from the Federal Reserve's \$500 billion lifeline for local governments.

The state is planning to borrow \$1.2 billion from the central bank for one-year to cope with revenue losses brought on by the economic shutdowns caused by the pandemic and the delay of its annual tax-filing deadline.

The step comes after Illinois last month put off a planned auction of such short-term debt as the interest rates demanded by investors soared amid concern it could be the first state to have its bonds cut to junk. The deal was put on day-to-day status, and now the state is instead turning to the Fed. The central bank will charge an interest rate of 3.82%, more than a full percentage point less than it paid during a bond sale last month.

"The Federal Reserve Bank worked closely with our team to make this transaction possible through the Municipal Liquidity Facility, which is an important tool the state is using to answer the unprecedented economic challenges posed by the COVID-19 pandemic," Alexis Sturm, director of the Governor's Office of Management and Budget, said in the statement.

The closing is planned for June 5, and the borrowing will be repaid on or before June 5, 2021, according to the statement.

Illinois will be the first to tap the Federal Reserve's lending program, which was rolled out after the municipal-bond market was hammered by a liquidity crisis in March that raised the risk that some governments would be unable to borrow to close temporary budget shortfalls.

Since the announcement of the program, the market has rallied, driving yields on some of the safest securities to nearly zero.

But Illinois continues to face a steep penalty to borrow. That has left it among those that could benefit from the Fed's loans, since the penalty the central bank is charging is less than it would face in a public debt sale.

Illinois in April lowered its fiscal 2020 revenue projections by \$2.7 billion and its estimates for 2021 by \$4.6 billion after the stay-at-home order brought a near halt to economic activity. Illinois's \$138 billion of unfunded pension liabilities, lack of savings, and \$7 billion in unpaid bills has left it with a bond rating one step above junk.

On Monday, S&P Global Ratings, which has a negative outlook on the state, said Illinois's fiscal 2021 budget "continues to be precariously balanced, and does not include measures to meaningfully address structural instability."

Illinois's General Assembly during its short spring session in May amended the state's borrowing statutes to allow it to sell short-term debt to the Fed facility. Until now, the state's short-term borrowing required competitive bids.

The new provision also authorizes longer-term borrowing of up to \$5 billion, if merited, from the Fed.

Governor J.B. Pritzker, a Democrat, has been advocating for more aid from the federal government. Pritzker has said he's seeking more than \$7 billion in federal aid to make up for revenue lost amid the virus outbreak.

Bloomberg Economics

By Shruti Singh and Amanda Albright

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