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Wave of Deficit Borrowing Coming From States Hit by Downturn.

- **New Jersey, New York, Illinois selling debt to plug shortfalls**
- **'It's pretty simple math,' Citigroup muni executive says**

A wave of deficit borrowing is headed for the municipal-bond market to close gaping budget holes caused by the coronavirus shutdowns.

New Jersey lawmakers agreed last week to borrow $10 billion to finance half of the state's estimated budget gap. Illinois plans to sell as much as $5 billion in notes to a municipal facility set up by the Federal Reserve. New York state authorized $11 billion in short-term borrowing that may be refinanced on a long-term basis, if necessary, and New York City is seeking the legislature's approval to borrow $5 billion.

"It's pretty simple math," said Patrick Brett, the head of Citigroup Inc.'s municipal debt capital markets business. "Hundreds of billions of dollars of deficits opened up really quickly. They're all not going to get plugged with cuts, they're all not going to get plugged with tax increases."

Unlike the federal Government, U.S. states are required to balance their budgets, though they frequently rely on short-term loans to cover temporary shortfalls.

Those deficits are poised to swell. With the coronavirus lock-downs decimating sales- and income-tax revenue and costs rising for healthcare, unemployment assistance and social services, municipalities will need at least $500 billion in additional federal aid over the next two years to avoid inflicting a major blow to the economy, according to Moody's Analytics.

When the economy slows, states typically terminate or furlough employees, put off public-works projects or borrow before raising taxes. Since the coronavirus pandemic hit the U.S., states and local governments have cut nearly 1.5 million jobs, far more than were eliminated after the last recession.

The size of the borrowing wave will depend on how much aid comes from Washington. Republicans and Democrats are negotiating to pass another round of economic relief during the last week of July.

Democrats in the House approved a $3 trillion measure that included about $1 trillion for state and local governments. Republicans have set a $1 trillion ceiling on another stimulus. Barclays Plc municipal strategists estimate states and local governments will get $200 billion to $500 billion.

While most states began the fiscal year on July 1 with full-year budgets in place, coronavirus infections have accelerated in Florida, Texas, California and Arizona since mid-June, prompting renewed lockdowns and weighing on an economic recovery. Uncertainty over tax collections and spending on government services means states will likely need to meet in special sessions to revise their budgets, according to Municipal Market Analytics.

"The interesting stuff and the non-recurring stuff tends to happen in the mid-year sessions," said

Matt Fabian, a managing director at Municipal Market Analytics on a Thursday webinar.

While borrowing to fund operations is a negative sign to bond-rating analysts and investors, they may be more forgiving with states and local governments facing the biggest fiscal crisis since the Great Depression.

“People are viewing this as a one-in-a-century kind of event,” Citigroup’s Brett said. “Even many of those who would generally oppose deficit borrowing are saying this is an act of God, and we should borrow.”

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By Martin Z Braun

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