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Wildfires Could Hurt Some Municipal Bonds.

The West Coast wildfires are posing rising risks to some municipal bonds, analysts say.

Even as heavy rainfall and thunderstorms this past week in Oregon provided relief to one of the states hardest hit by wildfires, risks of flash floods and mudslides arose. There are reportedly 79 active large fires burning in the U.S., with the largest numbers in California, Idaho and Oregon. Already, fires have burned more than 7 million acres across the west.

According to rating agency AM Best, “the current wildfire season in California has been setting new records in terms of the number of fires and the acreage burned.”

“There seems to be an elevated risk to credit quality this year compared to years past, and we are still in the beginning part of the fire season,” says Tom Kozlik, head of municipal strategy and credit at Hilltop Securities.

For example, Standard & Poor’s placed on Credit Watch with negative implications the ratings for Phoenix, Ore., currently at AA-minus, and Jackson County School District No. 4 in Phoenix-Talent, currently A-plus.

There are 9,024 local governments in California, Oregon, Washington, and Idaho, according to the website Governing.com. Not all have issued bonds of course. California is the biggest issuer, with \$65.2 billion issued in 2019, according to the Municipal Securities Rulemaking Board. Washington issued \$9.2 billion; Oregon, \$6.8 billion; and Idaho, \$1.2 billion. Idaho was ranked the most creditworthy state in a recent review of all 50 states by Eaton Vance for Barron’s. Washington was No. 11, Oregon was No. 17, and California was No. 30.

“There’s a good amount of nuance when it comes to the way wildfires are affecting the muni space,” says Chris Hartshorn of risQ, a research firm that is analyzing the financial risks posed by climate change for Municipal Market Analytics. In particular, smaller cities and other types of muni issuers “could be looking at some impairment.”

One issuer at risk of impairment, Hartshorn says, is Oregon’s Asante Health System, which has three hospitals in Ashland, Medford and Grants Pass, all towns around one of the most destructive fires. That could affect its 5% refunding bonds due in 2025, or any related issues.

“It’s not that any of the hospitals themselves were impacted, but their catchment area—the population that represents their patients and revenues—certainly was,” says Hartshorn. In the past, revenues for hospitals are greatly affected if the population declines or is forced to spend discretionary income on rebuilding rather than on elective procedures.

Pioneer Union Elementary School District in California, which issued bonds in February, is also at some risk because of the fires, says Hartshorn. The district includes Berry Creek Elementary School, which burned down. Others at risk include the entities related to Butte County, Calif., which contains many of the most damaged areas from this year’s fires, as well as the town of Paradise,

which was destroyed in 2018. “I’m not sure how many more it can take before property value and population starts to take a downward trajectory, along with the county’ balance sheet,” says Hartshorn.

Officials at Butte County, Pioneer Union, and Asante weren’t immediately available to comment.

Property insurers, meanwhile, are facing a bill of \$3 billion and counting,

Typically the places most hurt by fires are remote and sparsely populated. “A lot of the towns destroyed have been very small communities, (where) the whole tax base gets wiped out,” says Bill Glasgall, director of state and local initiatives at the Volcker Alliance. They’re unrated, and have limited amounts of debt.

And historically, municipalities receive significant support from FEMA, “which can cover 75% of losses and private insurance as well,” explains Bill Delahunty, director of municipal credit research for Eaton Vance. After the 2018 fire that burned the town of Paradise, the state of California announced measures to replace property tax losses to a number of entities. Paradise was eligible.

There has been only one muni default directly related to wildfires: The PG&E (ticker: PCG) bankruptcy in 2018. Still, the risks may be rising this year. “Even though we are still closer to the beginning rather than the end of the fire season, it seems the threat to larger populations centers exist,” says Kozlik of Hilltop Securities. The LNU Lightning Complex fire now burning through California’s wine country is reportedly 98% contained, but if it heads south, it could threaten the area near Travis Air Force Base, with a population of about 200,000, Kozlik says.

Barron’s

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