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City And State Budget Squeeze Could Drag Down Muni Market, Putting New Pressure On The Fed.

The failure to pass another Covid stimulus package because of Senate Republican resistance is increasing the budget squeeze on cities and states and raising cautions in the municipal bond market. Although Joe Biden and the Democrats want significant new spending aid, post-election gridlock could hurt cities, states, and the public finance market and also damage the economic recovery. That in turn will increase calls for aggressive new Federal Reserve powers and actions that could dramatically affect the muni market.

State and city revenues remain under water, and the sputtering economic recovery isn't likely to bail them out. According the Center on Budget and Policy Priorities, "state tax collections for March through July 2020 were 7.5% less than in the same months of 2019." And in September, Moody's MCO 0.0% said its improved baseline economic forecast would still mean that "the fiscal consequences…for states and local governments would be the worst since the Great Depression."

Chicago illustrates the problem. With revenues pummeled by the ongoing recession and no relief from a troubled state or a gridlocked federal government, the city plans to refinance existing debt at lower interest rates to generate short-term savings, and also stretching out the period for repayment.

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Forbes

by Richard McGahey

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