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Muni Market Faces Test With Cut to Fed Lifeline That Ended Crash.

- **Treasury Secretary doesn't intend to extend credit programs**
- **Backstop improved investor confidence, though few loans made**

In March and April, the Federal Reserve's interventions in the municipal-bond market helped reverse a record-setting crash that erupted when panicked investors fled over concern about the financial impact of the coronavirus pandemic.

The central bank's commitment to lend to states and local governments if needed helped the price of their bonds to rally and has left yields hovering around the lowest levels in decades, even though only two borrowers tapped the \$500 billion program.

Now, even with the coronavirus raging anew and states and cities still struggling to gauge the scale of the financial hits they're facing, that support is poised to end. Treasury Secretary Steven Mnuchin late Thursday announced a decision to allow some of the Fed's novel lending programs to lapse at the end of the year as scheduled, raising the risk that if the market seizes up again there won't be anywhere for governments to turn as a lender of last resort.

"It doesn't make sense to pull away this kind of support at this stage," Thomas Graff, head of fixed income and portfolio manager at Brown Advisory. "This is like taking off your seatbelt as you pull into your neighborhood. It is probably fine. But it is all risk, no reward."

The nation's \$3.9 trillion municipal-bond market currently seems at little risk and prices edged up slightly Friday. Even as governments unleashed a record flood of debt sales last month, yields held not far from the record lows hit in August. New Jersey and Suffolk County, New York, which considered borrowing from the Fed, were able to borrow easily in the public markets at a lower interest rate this week. New Jersey paid yields of about 1% for three-year debt. Those securities have rallied and traded at a 0.5% yield Friday.

"That was a resounding affirmation that the market feels healthy enough," said Christopher Brigati, head of municipal trading for Advisors Asset Management Inc.

The market has also benefited from optimism about the initial results of two coronavirus vaccines. That's eased worries about the financial outlooks for a broad swath of borrowers, including airports and colleges, that have been heavily affected as the pandemic upended daily life.

Yet a turnaround is far from completely assured for states and cities whose tax collections tend to remain depressed long after the end of recessions, and the individual investors who dominate the market have frequently fled en masse in the face of bad news — a phenomenon that analysts call headline risk.

Agencies such as New York's Metropolitan Transportation Authority, the operator of the city's subway and bus system, are also pleading for help from Washington, where talks about a stimulus

bill have made little headway since President Donald Trump's electoral defeat this month. It's not clear how much opposition Joe Biden may face once he takes office in January, since the political control of the Senate hinges on runoff elections in Georgia.

The MTA and Illinois were the only two to borrow from the Fed because they faced such large penalties in the public market, though other governments eyed it as a potential backstop that they didn't want to see withdrawn.

Before the Fed program lapses, the MTA has said it could sell \$2.9 billion in debt to the Fed. Illinois has also raised the possibility of borrowing from the Fed again.

Barclays Plc strategist Mikhail Foux said cash-strapped borrowers who are the target audience for the Fed's loans could be negatively affected by the end of the program, though he noted there may be little impact for the broader market. Bank of America Corp. analysts said in a report the end of the Fed program could be a "small negative."

"This is very disappointing, especially for weaker credits which are still facing the financial impact from the pandemic," said Gary Pollack, head of fixed income for private wealth management at Deutsche Bank. "On the other hand, the muni lending facility was not utilized that much because its interest rate was too onerous. But still it is a back-stop for those who need it."

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