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## Illinois's Bond-Market Penalty Hits Lowest Since Pandemic Crash.

- **10-year yields hover around 2.8%, down from over 6% in March**
- **Lowest-rated state benefits from hunt for higher yield debt**

No state is reaping the bond-market benefits from the promised end of the pandemic more than Illinois.

The state, whose bonds tumbled early this year on speculation it would become the first stripped of its investment-grade credit rating, has since seen its bonds rally back as investors plow into higher-yielding debt on speculation the financial blows of the shutdowns won't be as bad as once feared. That's driven down the yield on Illinois's 10-year bonds from more than 6% in March to about 2.8%, reducing the yield penalty investors are demanding to the smallest in nine months, according to Bloomberg's BVAL indexes.

The drop reflects the broader optimism among investors and shows how the Federal Reserve's promise to keep interest rates low has cut the financing costs for governments. Connecticut's and California's yields have drawn closer to the benchmark, too, as their tax collections stand to gain from this year's stock market surge. Even the water utility of the still bankrupt territory of Puerto Rico borrowed \$1.4 billion this week for yields of 3.2% on those due in five years.

"During the spring when the pandemic hit, Illinois got hurt worse than other states because they have less margin for error with their budget," said Daniel Solender, director of the municipal bond group at Lord, Abbett & Co. LLC, which holds Illinois debt as part of \$31 billion in municipal assets. "Of the states, Illinois is benefiting the most from the recovery of the lower quality part of the municipal bond market."

The expected rollout soon of vaccines in the U.S. has helped buoy optimism that an economic recovery is on the way even as an impasse in Congress over another stimulus measure threatens to withdraw support that has helped states to weather the slump.

In Illinois, the state increased its revenue estimates for the current fiscal year by about \$2.3 billion as sales- and income-tax collections outstrip previous expectations, according to a November report by the Commission on Government Forecasting and Accountability.

But Illinois still has a bond rating just one step above junk, partly due to its persistent budget deficits. It has a \$141 billion unfunded pension liability, a \$7.9 billion bill backlog, and is the only state that has turned to the Fed's emergency lending program for governments that are facing high interest rates in the public market.

Gabe Diederich, a portfolio manager at Robert W. Baird & Co., said the drop in Illinois's bond yields shouldn't be interpreted as a sign that investors think the state has addressed its financial challenges.

Investors searching for yields “are forced to cast a wider net” to issuers such as Illinois and New Jersey, said he said.

Recent deals by the Puerto Rico Aqueduct and Sewer Authority and Fortress Investment Group-backed passenger railroad Brightline Holdings LLC bonds also show “demand for spread,” he said. It “feels like there is a recovery trade taking place.”

## **Bloomberg Markets**

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