
N.Y. Bonds Keep Bargain Level as Millionaire Tax Hike Nears.

- **Risk spread on key bonds near where they were last April**
- **NYC may have highest tax rate, boosting value of tax-free debt**

New York is about to test a bedrock principle on Wall Street — that higher taxes drive up the value of municipal bonds.

Governor Andrew Cuomo and lawmakers struck a tentative deal Monday to raise taxes on some of the richest New Yorkers to the highest in the U.S., promising to make the tax-shelter provided by the securities more valuable.

But the slow moving municipal-debt market, a haven dominated by buy-and-hold investors, has yet to react. Despite the impending tax hike, the gradual reopening of New York City's economy and almost $24 billion in aid to the state and its localities from President Joe Biden's stimulus package, New York state bonds backed by income-tax revenue are trading at roughly the same risk premium as last April, when New York was the epicenter of the coronavirus pandemic.

Nine-year state personal-income-tax debt rated AA+ traded Tuesday at an average yield of 1.25%, or 29 basis points more than point more than AAA rated bonds — roughly the same level where similar maturity bonds were trading a year ago, according to data compiled by Bloomberg. When the state sold $1.9 billion of bonds last month, nine-year debt was priced at 51 basis points higher than top-rated debt, a 30 basis-points jump since before the pandemic.

"Spreads are still way too wide for what are very, very stable, if not strong credits," said Andrew Clinton, chief executive officer of Clinton Investment Management, who has made New York state and local muni debt the largest position in client portfolios. "Investors currently have not priced in any of the risk of potentially higher taxes, either at the federal level and certainly not at the state level."

New York's income-tax rates would temporarily increase to 9.65% from 8.82% for single filers earning more than $1 million, according to agreement announced Tuesday after it was worked out by Cuomo and the Democratic leaders of the Senate and the Assembly, Andrea Stewart-Cousins and Carl Heastie. Those making $5 million or more would be taxed at 10.3%, and income for those earning over $25 million would be taxed at 10.9%. The new rates would expire in 2027.

When combined with the New York City's top income-tax rate of 3.88%, city residents with income over that threshold will pay between 13.5% and 14.8%. That compares with 13.3% on income over $1 million in California, currently the highest in the nation.

California general-obligation debt maturing in 10 years yields about 11 basis points more than top-rated bonds, according to data compiled by Bloomberg. That's less than the yields on New York's income-tax bonds even though the California debt is rated one level lower by Fitch Ratings and two levels lower by S&P Global Ratings.

Clinton said technical factors — including a flood of new debt sales last month and a cautious buyer base — is keeping New York's risk premiums wider. New York state and cities issued $7.5 billion bonds in March, almost $5 billion more than March 2020, according to data compiled by Bloomberg.

Yet the fundamentals in New York are improving. New York City's economy, the engine of the state, is gradually reopening as vaccinations continue apace. The city has administered 4.2 million vaccine does as of April 2, more per capita than most other cities that publish timely data, according to city comptroller Scott Stringer.

Private employment in the city rose by 21,000 in February, led by 10,000 jobs in the leisure and hospitality sector as travel picked up and indoor dining expanded, according to Stringer's office. Broadway is reopening after Labor Day and the city's tourism promotion agency is forecasting the number of visitors will increase to 38 million this year, up from about 23 million in 2020.

And Wall Street is booming, too. Securities firms earned $38 billion in the first three quarters of 2020, the highest since 2009, according to Stringer.

Still private sector jobs have declined by more than 640,000 since February 2020, or a 16% drop, and higher taxes could push some of the rich, who pay a large share of state income taxes, to leave, said Clinton.

As of 2018, about 54,571 state residents with incomes of $1 million or more paid about 40% of total income taxes, according to E.J. McMahon, senior fellow at the Empire Center for Public Policy, a research group that advocates for less government spending and lower taxes.

"At the end of the day, there will be enough people who remain that will support the outstanding debt," said Clinton, whose firm oversees $1.26 billion of municipal debt. "You're not going to rip your kids out of school and ruin their relationships, just because you're saving eight or nine percent."

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