TIMES UNION

A $500 billion loan fund for state governments has barely been tapped, despite deficits

September 17, 2020

Emilie Munson

WASHINGTON — The Federal Reserve's $500 billion short-term borrowing program intended to give state and local government agencies and entities access to cash has barely been touched, despite mounting budget shortfalls in many states across the country.

Only the state of Illinois and New York City's Metropolitan Transportation Authority have received loans from the federal Municipal Liquidity Facility Program, for a total of $1.65 billion.

Although they're hurting for money and crying out for federal help, many states' leaders have rejected the new pandemic lending program because of what they say are overly strict terms and their own limitations on using borrowed funds.

While New York is staring down a $14.5 billion deficit, much of it attributed to pandemic-related revenue declines, the state is not looking at the program as a solution.

"New York state is not seeking to make use of the Municipal Liquidity Fund as we've been able to access the municipal bond market at low rates throughout this crisis, and what we really need is federal funding to offset the State's $62 billion, four-year revenue loss," said Freeman Klopott, a spokesman for the Department of Budget. "That said, the MLF has provided much-needed stability to the municipal bond market, and the deadline to access it should be extended beyond the end of this year, and it could prove more helpful to potential borrowers if the rates were more competitive and notes could be purchased for a period longer than three years."

According to Kent Hiteshew, a deputy director at the Division of Financial Stability for the Board of Governors of the Federal Reserve System, a stable municipal bond market means the MLF is working.

The program was intended to be a "backstop," a lender of last resort, to bring confidence and lending power back to the municipal bond market after an "unprecedented liquidity crisis" in the spring, Hiteshew said. The Federal Reserve has never before taken such a step in its 100 year history, he added.

In a hearing by the Congressional Oversight Commission Thursday, commissioners agreed that the MLF had largely achieved its goal of rescuing the market, allowing state and local governments to get private market loans if they need them. But as far as delivering actual relief for state and local government, the MLF's impact has been more muted.

Democrats argued that since the facility is getting little direct use, it should be adjusted to provide more relief to state and local governments many of whom are cutting employees to make ends meet. They blasted the program as too rigid with its terms.

"State and local governments are desperate for help but the loans offered by this administration are so punitive that even governments in deep trouble can't justify using them. Yet at the same time, the Treasury and Fed are offering much more generous, no-strings-attached support to many of America's biggest and most profitable corporations," said Commissioner Bharat Ramamurti.

Republicans argued that the program ensured that states receive loans if they need them — at historically low interest rates — from other sources and Congress should stick to that original intent. They knocked the idea that blue states were being fiscally responsible during the pandemic, noting they sent $456 billion in federal relief to states already.

Sen. Pat Toomey, R-Pa., noted that New York had delayed but not canceled a scheduled pay increase for about 80,000 state employees, while Connecticut gave unionized workers a 5.5 percent raise.

“Does that kind of behavior suggest to you dire circumstances that can only be met with additional federal money?” he asked.

The conversations mirrored a broader debate in Congress over how much support for state and local governments should be considered in another COVID-19 relief package.

Patrick McCoy, finance director of the New York City Metropolitan Transportation Authority, testified Thursday that the MLF had purchased $450 million of the MTA's debt to lower its borrowing costs. He recommended that the Federal Reserve adjust the program so more municipalities can access it directly and make the terms less restrictive.

"The MTA's consistent and overarching request from our federal legislators is for direct, unencumbered funding to ensure stability in this environment where revenues are falling drastically short due to suppressed ridership," he said. "The MTA desperately needs $12 billion in federal funding to get through 2021. This is not hyperbole. Without additional funding we will be forced to make a series of untenable choices that will further devastate our growth and recovery for years to come."

The MLF's only other user, Illinois, the lowest-rated U.S. state at a notch above junk, sold $1.2 billion of its general obligation certificates to the program.

“If Illinois had been more responsible and saved in its rainy day fund, it would not need the MLF loans,” said Chris Edwards, director of Tax Policy Studies at the Cato Institute. He said federal intervention in state borrowing undermines "healthy discipline."

Mark Zandi, chief economist at Moody's Analytics, countered that there is "no evidence" that states were profligate spenders before the pandemic. But some states have seen a greater impact of the pandemic on their budget shortfalls. New York, New Jersey, Connecticut, Maine, Louisiana, Idaho, Alaska, Hawaii and West Virginia have all suffered budget shortfalls through fiscal year 2022 of more than 2 percent of gross state product, more than all other states, according to data he produced.

Aid to state and local government is a "tried and true method" of promoting recovery during recessions, he said.