

U.S. Municipal Bond Market State of Confusion

The U.S. labor market continued its nosedive today, including another two million jobless claims filed, per morning numbers in line with the consensus estimate. That brings the total amount of jobless claims filed to over 40 million, or over a quarter of the U.S. labor force, which far exceeds the total 8.7 million jobs lost during the Great Recession. We also saw the first quarter 2020 GDP contraction revised to -5.0% from -4.8%, indicating the significant depth of the current economic contraction. Sentiment is also growing that a V-shaped recovery is unlikely.¹

Counter to this morning's dire economic information, we are seeing equity indexes such as the DOW and NASDAQ indices continue their multi-day advances. In addition, the leader of a major U.S. bank was quoted as saying, "You're starting to see the economy come out of the hole" during a morning interview.²

Record State and Local Government Budget Shortfalls

Contrasting opinions of the current financial landscape are leading some to a state of confusion. According to most state and local government and municipal finance officers, a state of confusion does not exist, as they have seen revenues plummet over the last two months. They also quickly diagnosed the fiscal backdrop and while the magnitude may differ entity to entity overall, record-breaking budget shortfalls continue to worsen. Finance officers are working to plug budget gaps in the current fiscal year while developing dire spending plans for the beginning of the next budget cycle. The Center on Budget and Policy Priorities estimates state budget shortfalls at a record \$650 billion. The National League of Cities projects total revenue loss for cities, towns, and villages to be about \$360 billion. These are unimaginable numbers.

More Cuts are Bad for Delivery of Services, Long-Term Credit, and the Economy

Public finance officers are struggling to find strategies to cope with the current fiscal landscape. Most of those coping mechanisms are likely to be grim at best and exacerbate the deepening economic contraction. Coming out of the last recession, we saw state governments mostly enact spending cuts in order to balance budgets.³ State and local governments have already been cutting spending, which is especially troubling at a time when their services are most needed and also because they are the entities on the front lines of the health crisis.⁴ They are also going to be the entities on the front lines of the current fiscal crisis. To navigate the current budget cycles, state and local governments are likely going to have to continue enacting significant expenditure reductions. Additional expenditure cuts negatively impact the delivery of services at a time when they are most needed, may result in reduced issuer credit quality, and could drag down the economy at the same time. These negatives could be minimized with additional federal relief.

Update on Additional Federal Relief for State and Local Governments

The U.S. House created and passed a \$3 trillion Health and Economic Recovery Omnibus Emergency Solutions Act (HEROES Act) in the middle of May. Almost \$1 trillion of the HEROES Act aid would be direct, unencumbered relief for state and local governments.⁵ Before this week there was almost no indication that the Senate was going to consider another round of relief. That is, until Senate Majority Leader Mitch McConnell said on Tuesday that there would "likely" be a fifth coronavirus relief bill "in the next month or so."⁶ Only time will tell what that relief finally looks like, as it is left to the policymaking process to finalize the details.

Please see disclosure starting on page 2.

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Summary

It is impossible for lawmakers to create effective and efficient policy in the absence of clarity and transparency. The current state of confusion will complicate that process. Renowned physicist, mathematician, and inventor Sir Isaac Newton is ordinarily known for common wisdom such as, "What goes up must come down" and "If I have seen farther than others, it is because I was standing on the shoulders of giants," in addition to his significant advancements in physical science, physics, astronomy, and mathematics. He is lesser known for this passage, "Truth is ever found in the simplicity, and not the multiplicity and confusion of things."⁷ However, this lesser known saying, which came from a mind of complex understanding, is fitting as we continue to monitor the current fiscal and political landscape and try to navigate this state of confusion.

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¹ Schulze, Elizabeth; [V-shaped recovery is unlikely](#); Mark Zandi says; CNBC; May 28, 2020.

² Son, Hugh; [Bank of America CEO Brian Moynihan says U.S. Economy starting to 'come out of the hole'](#); CNBC; May 28, 2020.

³ Oliff, Phil; Chris Mai and Vincent Palacios; [States Continue to Feel Recession's Impact](#); Center on Budget and Policy Priorities; June 27, 2012.

⁴ Mueller, Eleanor and Kellie Mejdrich; [State, Local governments slash services as demand rises](#); Politico; May 13, 2020.

⁵ Kozlik, Tom; the HEROES Act: [The House Democrats' Opening Proposition](#); HilltopSecurities; May 12, 2020.

⁶ Carney, Jordain; [McConnell: Talking about fifth coronavirus bill 'in the next month or so'](#); The Hill; May 26, 2020.

⁷ Bariso, Justin; [12 Brilliant Quotes From the Genius Mind of Sir Isaac Newton](#); Inc.; Dec. 29, 2016.

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