

U.S. Municipal Bond Market

President Cannot Cut Public School Funding; Schools, State and Local Governments Likely to See Aid in July/August; Jobless Claims Remain Elevated, At Risk; National MEI Index Falling Again

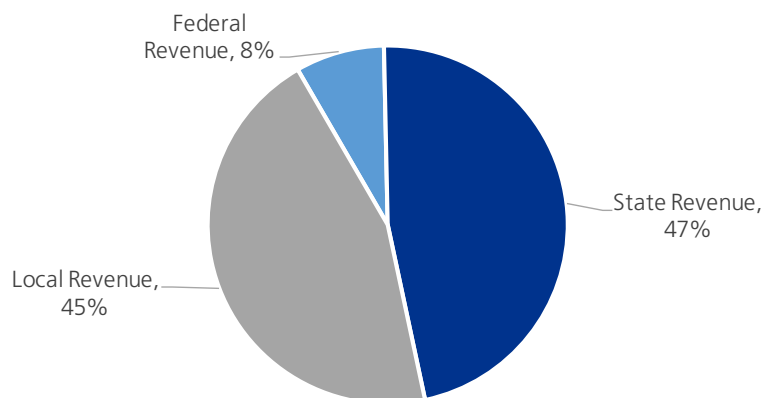
Summary

- Policymakers in California, Florida, New Jersey, Texas, and others showed us in recent weeks that the numbers and concern for public safety are the priorities helping to dictate policy.
- Initial jobless claims declined to 1.314 million from last week's 1.413 million. This was the 14th consecutive week they declined. Today's single number is still higher than any single week of claims we saw during the Great Recession. We believe next week's initial jobless claims data is at risk because of the reopening rollback. Those claiming unemployment insurance rose to a record 32.922 million, an important data point for investors and policymakers.
- The reopening rollbacks have already started to dampen mobility and engagement data. Data for the week ending July 4 was released on July 8, and the Dallas Federal Reserve's national Mobility and Engagement Index (MEI) turned negative. The Dallas Fed's weekly economic index also started to fall.
- As a result of the likely negative impact from the reopening rollback, we expect state and local government aid to be prioritized by the House, Senate, and White House. We believe pressure is building, and federal relief is likely to take shape when both chambers are in session July 21-31, and then the Senate remains in session from August 3-7.
- The President has no ability to cut federal funding to public schools unilaterally. Only Congress has the ability to adjust funding. The federal government provides about 8% of public school funding, according to a Center on Budget and Policy Priorities report, citing Census Bureau data.

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President Cannot Cut Public Schools' 8% of Federal Government Funding



Source: Center on Budget and Policy Priorities, Census Bureau, and HilltopSecurities.

Please see disclosure starting on page 5.

Numbers Dictating Policy, States Prioritizing Safety, Rolled Back Reopenings

Almost everyone is operating, or trying to operate, within the limitations of the current COVID-19 pandemic. This reality came slower to some, but it is finally sinking in across the country. Concerns about health and safety are beginning to be driving forces behind decision-making during the COVID-19 pandemic. This priority minimizes the spread of the virus, prevents hospitals from being overrun, keeps at-risk populations separated, allows for immunity to spread at a reasonable pace, and helps buy time until a vaccine is available.

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The numbers and public safety, not politics, are supposed to inform and help dictate actions. Policymakers in California, Florida, New Jersey, Texas, and others showed us in recent weeks that the numbers and concern for public safety are the priorities that are helping to dictate policy. Recent increases in confirmed cases are also likely to bring the importance of cooperation and financial relief to the front and center in some situations and reinforce those themes in others.

Weekly Jobless Claims Still High, But Under Economists' Expectations this Week

Initial jobless claims declined to 1.314 million from last week's 1.413 million. This was the 14th consecutive week they declined. Today's number is also better than the 1.375 million consensus estimate. Continuing claims also came in at 18.062 million which is better than the survey expectation of 18.800 million. Those claiming unemployment insurance rose to a record 32.922 million, an important data point for investors and policymakers.

It is also important to note that this is the 16th consecutive week jobless claims have exceeded 1 million. This is still a substantial continued reduction, even if the overall trend is slightly better. Today's single number is still higher than any single week of claims we saw during the Great Recession.

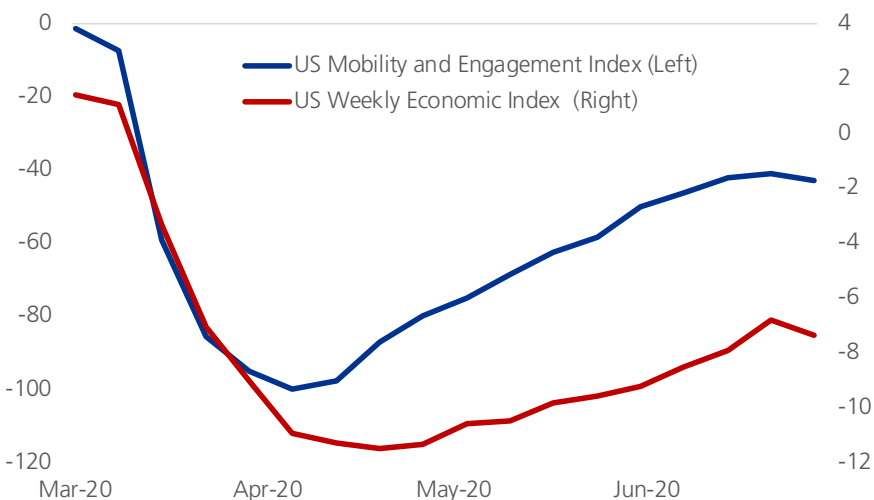
Initial jobless claims declined to 1.314 million from last week's 1.413 million, which was the 14th consecutive week they declined.

We believe next week's initial jobless claims data is at risk because of the reopening rollback. The Dallas Federal Reserve's Mobility and Engagement Index (MEI) started to drop again, as of data ending July 4. Therefore, there is an elevated potential for next week's jobless claims data to worsen. The reopening rollback is dampening this mobility and engagement activity, which could mean economic activity could fall too. Employers may pick up the pace of layoffs as a result.

National Mobility and Engagement Index Falling Again

The reopening rollbacks have already started to dampen mobility and engagement data. Data for the week ending July 4 was released on July 8, and the Dallas Federal Reserve's MEI, which is a national indicator of activity, is falling again. The Dallas Fed's weekly economic index, which is also a national index, started to drop, too.

Mobility and Engagement, Economic Indices Worsened, as We Expected



Data for the week ending July 4 was released on July 8, and the Dallas Federal Reserve's MEI, which is a national indicator of activity, is falling again. The Dallas Fed's weekly economic index, which is also a national index, started to drop, too.

Source: SafeGraph, Homebase, Federal Reserve Bank of Dallas data for week ending July 4th, and

HilltopSecurities.

It is possible that other important economic data, including future jobs data, is likely to worsen in the coming weeks as a result of the reopening rollbacks.¹ The falling MEI data is just a preview of what is likely to come. Our expectation of weakening data is in contrast to the recently released strong May and June jobs numbers, because those numbers are stale, and should not be indicators of the employment picture at this time. Even the stronger trend in this week's initial jobless claims data is at risk. Hits to other data points from the reopening rollback may not be felt in jobs and economic numbers for several weeks. Though the ultimate effect will be delayed, the impact is going to be undesirable.

Even without the reopening rollback, we expect state and local government relief in the next round of federal aid, which should be sometime in either July or September.

Another Round of Federal Relief Almost Ensured by End of July/Beginning of August

Even without the reopening rollback, we expect state and local government relief in the next round of federal aid, which should be sometime in either July or September. As a result of the likely negative impact from the reopening rollback, we expect state and local government aid to be prioritized by the House, Senate, and White House. We believe pressure is building, and federal relief is likely to take shape when both chambers are in session July 21-31, and then the Senate remains in session August 3-7.

White House Threatened School District Budgets

The details of what will be included another round of relief are not yet known.

However, we still firmly believe Congress will focus on:

- Individual unemployment
- Aid for state and local governments and other municipal entities
- Liability protection for businesses
- Expanded small business relief

In total, the relief package will likely need to amount to \$1-2 trillion. We think that \$500 billion - \$1 trillion of that could be allocated to aid for state and local governments and the other municipal entities category. This would be a boost for most municipal bond market-related credits, but we need to see the details to assess the full effect. We also expect this will not be the last relief package if the infection experience falls then rises and lawmakers must continue to re-open and then re-close—especially if this occurs multiple times in the coming months.

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Although President Donald Trump threatened to cut funding to schools yesterday,² it is still very likely that Congress, who has a better read on state and local matters than the White House, will prioritize aid to state and local governments, including school districts. State and local government aid has been a priority for the Democrats since the CARES Act was agreed upon.

House Democrats passed a \$3 trillion HEROES Act that included almost \$1 trillion of direct aid for state and local governments back at the beginning of the summer. The Republicans called it a "wish-list," which in some cases it was. The White House and Republicans are looking for something smaller, but a consensus has been building for more state and local aid. One reason is because the \$150 billion included in the CARES Act was nowhere near enough. Another reason is the economic environment is slowing deteriorating again. Senate Majority Leader Mitch McConnell just this week said he is open to more state and local relief and individual and family relief for those making less than \$40,000.³

To Be Clear, the President Cannot Withhold or Cut Local School Funding

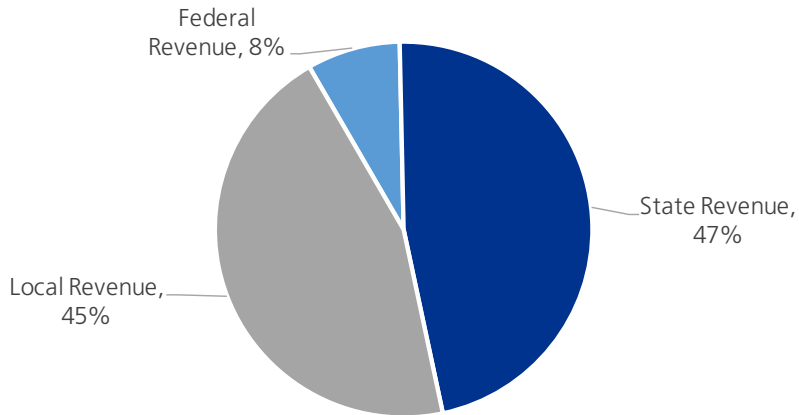
In an interview Wednesday afternoon, Maryland Governor Larry Hogan said, "I don't believe it was a serious statement, and I don't think the governors are taking it seriously,"⁴ regarding President Trump's threat to cut school funding.

The federal government provides about 8% of public school funding according to a Center on Budget and Policy Priorities report, citing Census Bureau data.⁵ This is the

A consensus has been building for more state and local aid, with one of the reasons being the \$150 billion included in the CARES Act was nowhere near enough.

smallest piece of the public school funding pie. The largest piece (47%) is provided by the states, and the remaining 45% is from local government sources mostly in the form of property taxes.

President Cannot Cut Public Schools' 8% of Federal Government Funding



Source: Center on Budget and Policy Priorities, Census Bureau, and HilltopSecurities.

The President has no ability to cut federal funding to public schools unilaterally. Only Congress has the ability to adjust funding.⁶ Now, the President could weigh in and threaten to withhold or not sign near-term aid for state and local governments because it flows down to schools. But, we are not hearing of that as a possibility. In fact, just this week one of Vice President Mike Pence's top aides stressed the importance of passing another round of relief before the first week in August.⁷

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¹ Please see: Kozlik, Tom; [Mobility Index Falling in Select States, Warns Recent Improvements Could be at Risk](#); HilltopSecurities; July 7, 2020.

² Baker, Peter and Erica Green; [Trump Threatens to Cut Funding if Schools Do Not Fully Reopen](#); New York Times; July 8, 2020.

³ Shutt, Jennifer; [Senate GOP aid package may tailor payments to low-income households](#); Rollcall; July 6, 2020.

⁴ CNN Politics. Twitter Post. July 8, 2020, 4:44 PM. <https://twitter.com/CNNPolitics/status/1280981076580593665>

⁵ Leachman, Michael and Eric Figueroa; [K-12 School Funding Up in Most 2018 Teacher-Protest States, but Still Well Below Decade Ago](#); Center on Budget and Policy Priorities; March 6, 2019.

⁶ Lybrand, Holmes; Daniel Dale; Tara Subramaniam; Manu Raju and Lauren Fox; [Fact-checking Trump's threat to cut off education funding if schools don't reopen](#); CNN; July 8, 2020.

⁷ Fabian, Jordan and Kevin Cirilli; [White House Wants Stimulus by August Recess With \\$1 trillion Cap](#); Bloomberg Politics; July 7, 2020.

Recent HilltopSecurities Municipal Commentary

- [Mobility Index Falling in Select States, Warns Recent Improvements Could Be At Risk](#), July 7, 2020
- [Jobs Up Again, Too Much Uncertainty from Reopening Rollback, Spread of the Virus Still What Matters](#), July 2, 2020
- [No Municipal Debt Binge, and There Won't Be One](#), July 1, 2020
- [The New Surge Renders Thursday's June Jobs Numbers Meaningless, Almost Ensures Federal Relief in July](#), June 29, 2020
- [COVID-19 is a National Stress Test; Surprise Record Infections, Policy Shifts Occurring](#), June 26, 2020

Readers may view all of the HilltopSecurities Municipal Commentary [here](#).

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