

U.S. Municipal Bond Market

Fifth Phase of Fiscal COVID-19 Relief is No State and Local Government Windfall

Summary

- This week's federal fiscal relief should not be considered a windfall for state (or local) governments.
- Although Congress has spent \$4.5 trillion on COVID-19 relief to date, there has not been any direct unencumbered funds allocated to state and local governments that could be used to offset budget shortfalls.
- After assuming that \$64 billion of this week's relief offsets some state and local spending we are still expecting state and local government budget shortfalls of at least \$107.5 billion.

State and Local Budget Shortfalls Will Remain Significant After Fiscal Support

The U.S. Congress passed a \$2.3 trillion fiscal relief and budget bill this week. About \$910 billion of those funds are considered a fifth phase of COVID-19 relief. Since March, D.C. has spent a total of about \$4.5 trillion on COVID-19 related aid. This is a significant number in aggregate to be sure. However, the latest round of COVID-19 relief should not be considered a windfall for state (and local) governments as indicated in today's opinion piece, The State Covid Windfall published by the Wall Street Journal Editorial Board.

There has not been any relief approved by Congress since March (including the money voted on this week) that could be considered direct, unencumbered state and local government assistance. In other words, there is nothing state and local governments will be able to use to offset budget shortfalls. This is a result of the political calculus lawmakers had to scratch together in order to finalize fiscal aid before the end of the year. It was a massive oversight some lawmakers are still trying to remedy.

State and Local Government Shortfall Update, Net of Federal Support, Reserves, and \$910B Relief (July 2020 - June 2022, \$ billions)

	Base Case	Severe Case
Gross combined shortfall:	331.5	468.2
Enhanced FMAP (FFCRA)	71.0	71.0
Education Grants (CARES)	17.0	17.0
Shortfall net of existing fed help	243.5	380.2
State Reserve Funds (FY19) End	72.0	72.0
Total Net Shortfall (prior to \$910B)	171.5	308.2
Education, from \$910B relief (\$82)	64.0	64.0
Adjusted Shortfall (after \$910B)	107.5	244.2

Source: Moody's Analytics (Dec. 17, 2020) and HilltopSecurities.

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Since March, D.C. has spent a total of about \$4.5 trillion on COVID-19 related aid.

This week's aid package includes money for education (\$82 billion), healthcare (\$63 billion), and transportation (\$45 billion). State and local governments are still facing budget shortfalls of at least \$107.5 billion even if we consider that \$64 billion (\$54 billion for k-12 schools and \$10 billion for higher-ed) of this week's relief indirectly helps offset budget shortfalls.

This week's fiscal relief helps state and locals mostly indirectly, but this is not going to directly help manage the fiscal year 2021, 2022, and 2023 budget shortfalls that are inevitably going to occur. Shortfalls are going to be especially severe in the states, regions, and cities hardest hit by the virus and resulting shutdowns and decreases in activity. We have written that we expect [Public Finance Downgrades to Outpace Upgrades, Probably for Years](#). This week's relief does not change that expectation.

State and local governments are very resilient. One of the levers they can use to balance budgets is to manage expenditures. We have also been regularly writing about the [cuts to government jobs in recent months](#). We expect government job cuts to continue because budget shortfalls will need to be dealt with. Although, this trend could be less severe than we expected going into 2021 as schools are going to benefit from the education targeted relief. This relief also could lessen the magnitude or number of property tax increases we expected to see in order to offset school budgets.

Recent HilltopSecurities Municipal Commentary

- [Late and Limited is Better Than Nothing](#), December 21, 2020
- [D.C. Nears an Almost \\$1 Trillion Fifth Phase COVID-19 Relief Compromise](#), December 16, 2020
- [Leadership Working on Support for \\$908 Billion Bipartisan COVID-19 Relief Proposals](#), December 15, 2020
- [Gone to Texas, Land of Opportunity](#), December 14, 2020
- [Final Municipal Liquidity Facility Transactions, Most Likely](#), December 11, 2020
- [Optimistic Scenarios Related to Vaccines and COVID-19 Relief](#), December 10, 2020
- [Funding Deadline Pushed, Hope for COVID-19 Relief Remains](#), December 7, 2020
- [November Sees Third Straight Month of State and Local Government Job Losses](#), December 4, 2020
- [D.C. Deadlines: Government Funding and the "Benefits Cliff," MLF's Expiration, Transit Cuts Announced](#), December 2, 2020
- [Infrastructure Gap Barely Dented by Record 2020 Bond Sales, Expect Lower 2021 Issuance](#), November 19, 2020

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