THE BOND BUYER

Fed muni program open for business

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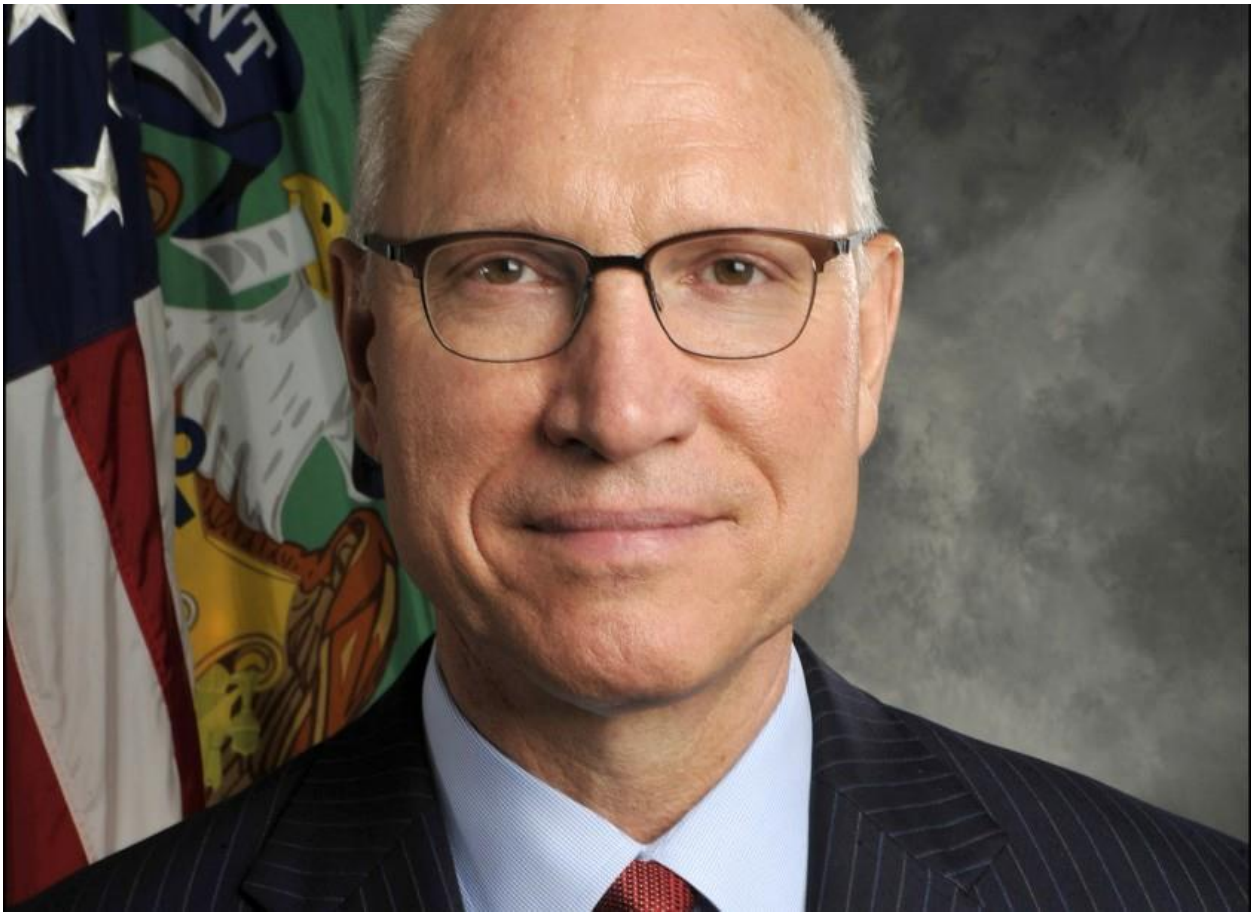
The Federal Reserve's short-term municipal note program is "open today" to states and local governments struggling with financial woes during the pandemic, though it was reiterated that the program is a last resort.

During a Government Finance Officers Association roundtable Monday, Kent Hiteshew, who was recently hired by the Fed to help with municipal markets, said the Municipal Liquidity Facility is open. Illinois already said it is exploring its options with the program.

"Once we begin getting notices of interests and approving applications then we should begin purchasing notes in the very near future, certainly within the next several weeks," Hiteshew said. Hiteshew said he expects to have very quick approvals of those applications, assuming that issuers propose straightforward credits that are consistent with released MLF frequently asked questions.

On Monday, the New York Fed released application materials for issuers interested in the program. Last week, the Fed announced it was accepting notices of interest — a form issuers must fill out to express interest in selling notes under the MLF. The Fed also released legal documents on Monday.



During a GFOA roundtable, the Fed's Kent Hiteshew was asked when its muni program would be open for business to which he responded, "really today."

Once an NOI is complete and the issuer and notes meet the MLF’s eligibility requirements, issuers will be sent an NOI approval email and an invitation to complete an application, the Fed said.

The program, announced in early April, will buy $500 billion of short-term notes from issuers. The program covers counties of 500,000 or more and cities of 250,000 or more. Last week, the Fed announced a baseline of 150 basis points for triple-A issuers to 590 points for below investment-grade-rated issuers to use the MLF — a large premium.

The MLF’s pricing table was established in the same manner as other facilities created during the pandemic, Hiteshew said.

“The MLF pricing has been established to serve as a backstop, not as a first stop,” Hiteshew said

“The penalty is designed to make sure, as we said at the outset, that state and local governments have access to liquidity, but it’s not designed to replace market sources,” Hiteshew later said.

Hiteshew was asked during GFOA’s roundtable what measures the Fed will use to gauge its success.

“Our primary objective is to ensure that state and local governments have adequate access to liquidity under reasonable credit terms during this crisis and the ensuing economic recovery,” Hiteshew said.

To the extent that liquidity is available from the MLF or through banks, Hiteshew says that the Fed will have met its objective.

Meanwhile, private placements, bank loans and direct lines of credit have been an important component in the municipal market, Hiteshew said. Mid-March, the market began to see an **uptick in bank facilities**.

“In just the last six weeks alone on EMMA, we’ve seen twice the number of such filings for bank facilities, as were reported in the entire first quarter of this year,” Hiteshew said. “Anecdotally, we are hearing that banks are stepping up to the plate.”

The Fed added Hiteshew to its staff in March to beef up its municipal market expertise. He had been working as a strategic advisor at Ernst & Young and as a senior fellow at New York University. From 2014-2017, Hiteshew was the first director of Treasury’s Office of State and Local Finance, serving as Treasury’s point person on Puerto Rico.

Sources have said because the MLF is expensive it is really meant for the lowest-rated issuers while higher-rated issuers should probably stick to the municipal market, which most market participants say was the Fed’s intention all along.

GFOA’s debt committee members were straw-polled after the pricing information was released last week to see whether they would use the MLF. There were no takers, said Emily Brock, director of GFOA’s federal liaison center, which could be because there are a fair amount of issuers who are finding capital in other ways. Brock noted that a number of the debt committee members are smaller issuers that will not benefit from the program anyway.

Earlier this month, a bipartisan letter written by Reps. Steve Stivers, R-Ohio, and Dutch Ruppersberger, D-Md., with 40 other lawmakers signing on, asked the Federal Reserve to create a facility to purchase medium and long-term municipal securities issued in the secondary market, and provide an additional $35 billion in CARES Act funds to do so.

Last week, Sen. Bob Menendez, D-N.J., led a bipartisan group in asking Treasury Secretary Steven Mnuchin and Fed Chair Jerome Powell to create a program to further help municipalities in the medium and long term.

"Just like in the aftermath of the last financial crisis, state and local spending is going to be a key determinant of whether we have a quick recovery that makes the right long-term investments," Menendez said Monday. "Or if federal stimulus is going to be offset by cuts in our local governments and plunge us into a long recession.”