LEGISLATIVE FISCAL ESTIMATE

[First Reprint]

ASSEMBLY, No. 4175

STATE OF NEW JERSEY
219th LEGISLATURE

DATED: JULY 21, 2020

SUMMARY

Synopsis: "New Jersey COVID-19 Emergency Bond Act," authorizes issuance of State bonds totaling up to $9.9 billion.

Types of Impact: Multi-year State debt service payment and State revenue increases.

Agency Affected: Department of the Treasury.

Office of Legislative Services Estimate

Fiscal Impact	
Multi-Year State Debt Service Payment Increase	Indeterminate
Multi-Year State Revenue Increase	Indeterminate

- The Office of Legislative Services (OLS) cannot project the total debt service cost the State would incur from issuing different forms of indebtedness to address State government funding needs related to the COVID-19 pandemic. This is so because the final debt service cost would be a function of the amounts, structures, and terms of the authorized debt instruments, of which many elements remain to be determined.

- Annual State revenues would increase by an indeterminate amount over several years from interest earned on unexpended borrowed funds. Any State revenue gain, however, would be widely outpaced by the increase in State debt service payment obligations.

BILL DESCRIPTION

The bill permits the issuance of up to $9.9 billion in State indebtedness without voter approval to address State government funding needs arising from the COVID-19 pandemic. Of the total, up to $2.7 billion may be used in FY 2020 and up to $7.2 billion in FY 2021. The indebtedness may either be in the form of general obligation bonds, which may mature no later than 35 years from the date of issuance; or short-term notes sold to the federal government on such terms as the federal government stipulates. Any debt issuance may subsequently be refunded. The State would back all debt instruments with its taxing powers, pledging its full faith and credit to the required semiannual debt service payments. Any interest the State may earn on any unexpended principal amount would be deposited into the State General Fund.

FISCAL ANALYSIS

EXECUTIVE BRANCH

None received.

OFFICE OF LEGISLATIVE SERVICES

The OLS determines that the bill would produce indeterminate multi-year State expenditure and revenue increases with expenditure growth widely outpacing added revenue.

State Debt Service Payments: The OLS cannot project the total debt service cost the State would incur from issuing different forms of indebtedness to address State government funding needs related to the COVID-19 pandemic. This is so because the final debt service cost would be a function of the amounts, structures, and terms of the authorized debt instruments, of which many elements remain to be determined.

General Obligation Bonds: Although the bill allows the issuance of up to $9.9 billion in general obligation bonds, the Executive may not exercise the full authority. With the amount, structure, and terms of the general obligation bond issuance unknown, the OLS conducts a sensitivity analysis that identifies possible State debt service payment scenarios for each $1 billion in general obligation bonds issued. In performing the analysis, the OLS makes the following simplifying assumptions: a) the bonds' maturity period will be 20 years; b) two debt service payments will be made each year; c) the debt service payments will be level until maturity; and d) the bond issuance will have a basic structure without any credit enhancements or original issue premiums or discounts.

For each scenario, the table below displays annual debt service payments as well as total debt service and interest payments until the bonds are paid off. The adjustable variable is the annual interest rate, which ranges from 4.0 percent to 6.0 percent. Regarding the interest rate choice, the OLS places a one-percent band around the 5.0 percent rate the State secured in January 2020 for debt service payments for those series of a $150 million tax-exempt general obligation bond sale that have the latest maturity dates. The OLS cautions, however, that conditions actually existing in the bond market at the time of issuance may dictate interest rates outside of the OLS' band.

Debt Service Payment Scenarios for Issuance of $1 Billion in Bonds, 20-Year Maturity Period (In Millions)

	Annual Interest Rate				
	4.0%	**4.5%**	**5.0%**	**5.5%**	**6.0%**
Annual Debt Service	**$73.1**	**$76.4**	**$79.7**	**$83.1**	**$86.5**
Total Debt Service Payments	**$1,462.2**	**$1,527.1**	**$1,593.4**	**$1,661.3**	**$1,730.5**
A) Total Principal Payments	$1,000.0	$1,000.0	$1,000.0	$1,000.0	$1,000.0
B) Total Interest Payments	$462.2	$527.1	$593.4	$661.3	$730.5

Accordingly, the OLS calculates that for each $1 billion borrowed the State might incur total debt service costs ranging from $1.5 billion to $1.7 billion spread over 20 years, which includes total interest payments ranging from $462.2 million to $730.5 million (46.2 percent to 73.1 percent of the $1 billion borrowed). The lower bound represents a 4.0 percent annual interest rate and the upper bound a 6.0 percent annual interest rate. If the assumptions hold, annual debt service payments for each $1 billion borrowed could be as low as $73.1 million at a 4.0 percent interest rate and as high as $86.5 million at a 6.0 percent interest rate. The OLS further notes that total debt service would be lower if bonds were issued for a shorter term and all other assumptions remained the same, and the converse.

Federal Borrowing: The up to $9.9 billion in authorized State indebtedness may be borrowed from the federal government on such terms as the federal government stipulates. Currently, one pertinent federal program is available.

Under the Municipal Liquidity Facility, the Federal Reserve Bank of New York will purchase up to $9.25 billion of eligible short-term notes with a payback period not to exceed 36 months directly from the State of New Jersey at the time of issuance, if so requested by the State. The State may use the proceeds to manage its cash flow pressures resulting from the COVID-19 pandemic and to pay the origination fee equal to 0.1 percent of the par amount issued.

Interest rates would vary depending on the term of the short-term notes. According to the Municipal Liquidity Facility sample purchase rates published by the Federal Reserve Bank of New York on July 13, 2020, New Jersey could currently expect an interest rate of just under three percent for three-year notes. For the issuance of $1 billion in three-year notes at an interest rate of three percent with interest-only payments every six months and the $1 billion repaid in full at maturity, the State would owe $30 million in interest per year, and $90 million in total interest over the three-year term of the borrowing. Interest payment liabilities would continue to accrue if the State were to refund the notes before they mature.

State Revenue Increase: An indeterminate annual State revenue increase would occur over several years from interest earned on unexpended borrowed funds. Insufficient information precludes the OLS from quantifying the revenue gain, as its magnitude depends on future Executive determinations as to the promptness of bond fund disbursements.

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This fiscal estimate has been prepared pursuant to P.L.1980, c.67 (C.52:13B-6 et seq.).