



Breaking News Or Information? 12/6/10

Over the weekend, the press was busy elaborating on the predicament facing state and local governments. In particular, a New York Times article entitled “Mounting state debt stokes fears of a looming crisis” didn’t cover any new ground, but it organized a lot of information quite well. In fact, the author delivered much of the same content that we communicated in RSW’s third quarter 2010 commentary. As a refresher, in October we wrote:

The Recession’s Over? Go Tell It to State and Local Government Budget Officers.

- State governments have confronted budget shortfalls in fiscal years 2009, 2010, and to-date in fiscal 2011 (most fiscal years start on July 1), that have totaled \$425 billion. Gaps have been closed by combinations of: federal stimulus monies, reserve draw downs, tax and revenue increases, and expenditure cuts. At the same time, local governments continue to deal with similar issues.
- Many states and local governments are already encountering mid-year fiscal 2011 budget gaps with depleted resources, and despite various tax increases.
- Approximately 40 states already identified gaps estimated at \$110 billion to \$140 billion in planning for fiscal year 2012.
- The exhaustion of federal stimulus funds in fiscal year 2012 (only \$6 billion estimated to be available as compared to \$60 billion in the previous year), coupled with the jobless recovery to-date, will continue to strain state and local governmental resources.
- The public has little, if any, appetite for tax increases, especially in states that have raised taxes while still confronting budgetary pressures.

Furthermore, we stated: “After decades in the making, our nation’s economic underbelly is exposed, and the extent of our predicament has come to the fore. With respect to spending and debt, ‘the first step in curing an addiction is first recognizing the problem.’ Now, progress can be made since solutions to problems are rarely forthcoming until politicians stare into the abyss and the anger of the taxpayers. Topics of reform are now being discussed that were once considered the ‘third rail’, namely: Social Security and pension benefits. Now, at long last, these topics, the previous lightning rods of conversation and debate, are no longer unmentionables. While politicians are famous for kicking the can down the road, we are running out of road. As a result, real solutions may not be far behind.”

With that said, this article and most others, tend to draw conclusions from today’s predicament by assuming that future actions are not forthcoming. The same could be said for the deficits on the Federal level. Here too, the



public and policy makers are fully outraged and engaged. For better or worse, this is sometimes a necessary ingredient that must be part of the process before solid reforms can be implemented to address the fiscal imbalances. Drawing a straight line from where we are today, and connecting it to the abyss, assumes that this process does not take place. It is also important to know that while it has not received much attention from the media, state tax revenues for the third quarter of 2010, (according to preliminary data), increased by 3.9% from the same period a year earlier. This was the third consecutive quarter of same period year-over-year growth.

“Staying the course - It is with this in mind, that our commitment to our clients remains unchanged “We remain judicious with our outlook, tempered by a disciplined approach to credit, structure, and interest rate risk. This strategy has served clients well, and we believe should continue to do so at a time of uncertain economic recovery persistent credit strain.”

As always, we will keep you informed should our views change or if there is any new information that we think it is important for you to be apprised.

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