



Written by [Bob Adelman](#) on June 2, 2017

Credit Rating of Illinois Cut Again to One Notch Above Junk

The day after Illinois failed to reach a budget agreement (for the third year in a row), Moody's Investors Service [followed](#) S&P Global Ratings by downgrading the state's credit rating to just one notch above junk status. The legislature has 30 days to come up with a budget or else the state's rating will be downgraded further to junk status.



Moody's was blunt in its assessment of the rolling catastrophe: "Legislative gridlock has sidetracked efforts not only to address pension needs [\$129 billion in unfunded liabilities] but also to achieve fiscal balance [the state has \$14.5 billion in unpaid bills with \$800 million in late fees and penalties adding to the total]. Moody's analyst Ted Hampton added:

During the past year of fruitless negotiations and partisan wrangling, fundamental credit challenges have intensified enough to warrant [our] downgrade, regardless of whether a fiscal compromise is reached [by July 1].

S&P's analyst Gabriel Petek spelled out the core problem: inability for the state house, virtually controlled by Democrat leader Michael Madigan, and the state's Republican Governor Bruce Rauner to agree on nearly anything. They each want more taxes, but Rauner doesn't want as much of an increase as does Madigan. Wrote Petek:

The rating actions largely reflect the severe deterioration of Illinois' fiscal condition, a byproduct of its stalemated budget negotiations, now approaching the start of a third fiscal year. We placed the ratings on CreditWatch with negative implications because, in our view, the unrelenting political brinkmanship now poses a threat to the timely payment of the state's core priority payments.

It gets worse:

We also believe that Illinois is now at risk of entering a negative credit spiral, where downgraded credit ratings would trigger contingent demands on state liquidity, further exacerbating its fiscal distress.

And, if there's no agreement by the end of June, the rating agency would apply the *coup de grâce*:

If lawmakers fail to reach agreement on a budget with provisions designed to reduce the state's structural deficit, it's likely we will again lower the ratings.

That would make Illinois the first state with junk credit ratings from all three credit rating agencies, resulting in default triggers, demands for immediate payment on various bond issues, and the



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withdrawal of bond buyers such as hedge fund managers and bond mutual funds. In other words, the sources that have allowed Illinois to continue to spend so wildly beyond its means for so long would dry up.

Would Illinois turn into Puerto Rico? No. According to John Miller, a Nuveen asset manager, Illinois has a substantially better economic base, a larger population, a more diverse array of small businesses, lower debt per capita and a more stable economy than does the island. But one advantage Puerto Rico has over Illinois is this: On June 11 the island's voters decide whether to stay independent, or to apply for statehood. With half of the island's voters living below the poverty level, and the promise of federal aid in the billions just waiting for a statehood decision, that vote for all intents and purposes is already in.

But Illinois is already a state, and by law it cannot declare bankruptcy. So as the downward death/debt spiral accelerates, those who will be hurt the most are the very ones who can least afford it. Bond holders will get hosed, small businesses which have been waiting patiently for months to get paid for services already rendered will get stiffed, pensioners counting on full benefits upon retirement will be forced to make other plans, and taxpayers will see their sales, income, and property taxes raised.

In fact, according to one observer, John Humphrey, head of credit research for Gurtin Municipal Bond Manager (which doesn't own any Illinois debt), the state is quickly nearing the point of no return:

We are probably approaching that point of impaired ability to function at [a] basic level. We've already probably passed that point. We haven't seen this in a modern state before.

It's like a game of chicken between two testosterone-laden teenagers with the players caught in the middle. They refuse to give up the game, and the end result will be a crash for the record books.

An Ivy League graduate and former investment advisor, Bob is a regular contributor to The New American magazine and blogs frequently at [LightFromTheRight.com](#), primarily on economics and politics. He can be reached at badelman@thenewamerican.com.

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