MARYLAND STATE TREASURER
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Testimony of the Maryland State Treasurer's Office

X00A00 – Public Debt Budget | Fiscal Year 2025

Senate Budget & Taxation Committee
February 6, 2024

House Appropriations Committee
February 9, 2024

The State Treasurer's Office (STO) respectfully requests that the committees concur with the Department of Legislative Services' (DLS) recommendation to concur with the Governor's allowance for the proposed public debt budget for fiscal year 2025.

The DLS analysis raises two issues, one relating to a funding shortfall for capital projects and the other relating to the State's bond ratings.

First, the analysis notes that less actual bond premium is available for capital project expenditures relative to the amount that was budgeted in the fiscal year 2024 capital budget. STO is aware of the issue and working with the Administration and DLS to explore potential resolutions. Regardless of how the issue is resolved, the State is positioned to pay its debt service on time and in full.

Second, the analysis acknowledges the decision the State has made to increase the annual debt limit for the foreseeable future, despite already being viewed as a high debt state. Maryland is now one of 15 states with AAA ratings from all three rating agencies. The State's credit strengths are well-known and unwavering, including the 15-year maturity requirement for debt, which is shorter than other states' maturity standards, and the respected institutional frameworks, such as the Capital Debt Affordability Committee (CDAC) process, which lend stability to Maryland's fiscal planning.

The State's strong standing should not, however, be taken for granted. More recently, the U.S. Government's rating was downgraded from a stable outlook to a negative outlook. In turn, in November 2023, Moody's initiated a review of the State's rating and ability to withstand fiscal stress from the federal government. The review was initiated due to Maryland's comparatively high dependency on federally derived gross domestic product

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(GDP) and employment. After review, Moody's reaffirmed the State's AAA-stable outlook, indicating that the rating is supported by proactive fiscal management that enables Maryland to make midcourse corrections and weather economic cycles. Along with the State's strong governance framework, financial reserves and high-wealth levels make the State more resilient to withstand economic shocks, including those affecting connections to the federal government.

The report did caution, however, that certain factors could contribute to a future downgrade. These include:

- economic and financial deterioration that results in deficits, fund transfers, and reserve draws without a plan for near-term replenishment and structural balance;
- failure to adhere to policies in place to address large unfunded pension liabilities; and
- substantial reductions in federal employment and the role in the State's economy that directly undermine the State's relative performance.

In addition, STO is monitoring developments with the rating criteria utilized by S&P, as the rating agency is currently in a review and comment period for a proposal to modify its criteria in a way that would place more emphasis on economic outputs, highlight the role of reserves and liquidity, and adjust the analysis of long-term liabilities to account for funding discipline and pension liability risk.

Although STO provides the rating agencies regular updates on the financial condition of the State and responds to any specific inquiries made throughout the year, maintaining the State's AAA rating is a responsibility that extends well beyond the Office. STO will continue to ensure that the State fulfills its obligations to pay debt service. The myriad of factors that the State's credit is evaluated on, however, are heavily influenced by fiscal, economic, and policy decisions made by the Administration and the General Assembly. While the State's current budget challenges are significant, Maryland has been rated AAA by S&P since 1949, by Moody's since 1970, and by Fitch since 1993. During that time, Maryland has maintained its ratings through the 1970s oil shocks, the savings and loan crisis, the dotcom crash, the 2007-2008 financial crisis, the resulting Great Recession, and, most recently, the global COVID-19 pandemic. Although the circumstances have changed, the State's message remains the same: Maryland is a state that identifies and acknowledges problems, evaluates the causes, and makes plans to address them. Maintaining the AAA rating will require State leaders to rely on historical experience and work together to develop solutions to these new challenges. It has been done before and will be done again.

Looking ahead, the next General Obligation Bond sale is scheduled for June 5, 2024, at the Board of Public Works meeting. STO anticipates that this will be the only GO bond sale for calendar 2024, unless future circumstances were to dictate otherwise. STO regularly monitors interest rates and the bond markets, in addition to seeking advice and guidance of financial advisors and underwriters regarding the potential timing and structure of sales. STO is also monitoring the monthly expenditure of bond proceeds to determine whether additional funds are needed to support the capital program. With the unprecedented amount of resources put into the State's capital program in recent years, particularly through the use of PAYGO, STO has observed a slowdown in the expenditure of GO bond proceeds. Although projects continue to be authorized, the State does not issue debt unless it is needed. In evaluating the timing for the next bond sale, there is not a need for additional funds to support the capital program until late spring.

As part of the June bond sale, STO anticipates hosting the analysts from the rating agencies in early May for in-person site visits. This will be the first time the State has hosted rating agency visits in over a decade, and STO looks forward to collaborating with the Administration and the General Assembly for the opportunity to highlight Maryland's finest assets and resources. Following the sale, STO will submit copies of the ratings and accompanying reports to the legislature.

After careful review of the analysis, STO respectfully requests that the committees concur with the DLS recommendation to concur with the Governor's allowance, pending the Administration's resolution of the bond premium shortfall. Please contact Jonathan Martin, Chief Deputy Treasurer (jmartin@treasurer.state.md.us), with any questions.