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Financial crisis leads counties to rethink strategies

Local governments, including many that borrowed to offset declining tax revenues, now must pay higher interest to service their debts.

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Posted: Friday, Sep. 19, 2008

The upheaval on Wall Street is affecting local governments, with some officials rethinking how they'll borrow or invest money in coming weeks.

In Cabarrus County, officials are keeping an eye on the stock market to see if it'll impact next week's planned sale of about \$57 million in debt for a jail project. Union County just bought certificates-of-deposits from banks because the yield for federal treasuries, traditionally seen as one of the safest types of investment, has dropped.

And governments also are seeing a spike this week in interest rates on money that has already been borrowed.

In Mecklenburg County, the average interest on variable rate bonds rose to 6.1 percent from 1.8 percent last week, said Finance Director Dena Diorio. That affects about one-third of the county's outstanding debt – or about \$718 million. The variable rate is reset weekly and now exceeds that of longer-term bonds, which traditionally are higher.

Said State Deputy Treasurer Vance Holloman: “We are optimistic that (the rate increase) will be a temporary reaction to the financial market uncertainty.”

Falling markets have prompted investors to shun all but the safest federal government assets. And local government debt is not seen as safe as federal treasuries or gold, said Jack Vogt, who specializes in local government finances at the School of Government at UNC Chapel Hill.

The changes come at a critical time for governments, many of which are borrowing more debt to make up for falling tax revenues, said Tony Plath, a finance professor at UNC Charlotte.

Still, many finance experts say North Carolina's strong regulation of local government finances means its communities – and the public's money – are likely to fare better than other parts of the country will.

“Local governments have very conservative and prudent stat sheets that protect us in these times,” said Melinda Canady, finance director for Wake County.

Wake was scheduled to sell \$354 million in fixed-rate bonds next week to pay for a variety of projects, including schools, open space and libraries. Canady said at this time, she doesn't

expect Wake will sell the bonds until a later date, though an official decision won't be made until Monday. She said a temporary delay won't affect the start of construction.

The N.C. Higher Education Assistance Authority also has pushed back, for now, a bid to refinance about \$1.3 billion in student loan-backed debt until market conditions calm.

Back in the Charlotte area, Union County Finance Director Kai Nelson said that on Wednesday, his department had about \$15 million to invest. They looked at treasuries, but found the yield was only 0.23 percent.

"You could probably make more money by taking your cash and sticking it in a mattress," Nelson said.

So the county bought certificates of deposit at BB&T and Wachovia – for a yield of 2.7 percent.

The bank CDs are a safe move, Vogt said, because many are protected by securities owned by the bank.

While some local officials are hopeful that the current woes on their bond rates and investments will be temporary, experts said more troubles could loom down the road. For example, Vogt said, declining housing values could lead to a drop in property tax revenues.

Add the rising cost of public works projects and financing, and Plath predicts local governments are on a path to crisis.

"We're headed for a perfect storm in municipal government finance in the next year or two," Plath said. "It is going to get worse before it gets better."

Staff writer Julia Oliver and Bloomberg News contributed



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