

READING RISK: CREDIT RATING AND THE POLITICS OF MUNICIPAL DEBT

by

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Abstract

Since the Great Recession, the dynamics of municipal debt have moved to the center of American urban politics. In this context, the once obscure credit rating agencies have become key institutions in the processes of financialization and austerity unfolding across the municipal landscape. The following thesis seeks to interrogate this new urban “regime of financial control,” unpacking the credit rating process and exploring how local actors relate to its imperatives. Drawing on interviews with credit rating analysts in New York and local financial professionals in New Jersey, it follows the ratings from the headquarters of the agencies to the city finance departments which mediates their impact on urban everyday life. Chapter 1 introduces the thesis by discussing the “return” of the urban fiscal crisis since the breakdown of the subprime mortgage market in 2007-2008, arguing that the dynamics of the municipal bond market are crucial to comprehend at this historical moment. Thereafter, Chapter 2 provides an overview of that market and its shifting character since the 1970s. Building on these foundations, Chapter 3 opens the “black box” of the rating process. Drawing on renewed interest in value theory under conditions of financialization, it argues that the rating process pivots around a key contradiction between on the one hand understanding the concrete uncertainties of investing in place and on the hand inevitably having to abstract from these to compare investment risk across space. Stepping outside the agencies, Chapter 4 examines the nature of credit rating power. Drawing on a case study of New Jersey it argues that, rather than descending from above, the urban politics of “creditworthiness” is co-constructed in the interactions between rating analysts, local financial professionals and the state’s regulation of municipal finance. Lastly, Chapter 5 concludes the thesis by highlighting the violent effects of municipal indebtedness.

Lay Summary

Credit rating agencies are private corporations assessing the creditworthiness of municipal, sovereign and corporate debtors. These debtors, in turn, often seek to fulfil the financial management criteria of the agencies as failure to do so might make borrowing difficult and more expensive. In this sense, the rating agencies present a striking illustration of the power finance in contemporary capitalism. The following thesis seeks to interrogate how this power is expressed in American urban politics. Drawing on interviews with credit rating analysts in New York City and local financial professionals in New Jersey, it follows the ratings from the headquarters of the agencies to the city finance departments which mediates their impact on urban everyday life. As such, it unpacks a particularly opaque area of local politics.

Preface

This thesis is the original, unpublished and independent work of the author, Tuve Mikael Omstedt. It is in part based on interviews undertaken in New Jersey and New York City in the summer of 2016. This research was approved by the University of British Columbia's Behavioral Research Ethics Board, certificate number H16-00545.

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List of Abbreviations

BAN	Bond Anticipation Note
CFO	Chief Financial Officer
CDO	Collateral Debt Obligation
CDS	Credit Default Swap
DLGS	Department of Local Government Services
FIRA	Financial Industry Regulatory Authority
GAAP	General Accepted Accounting Principles
GO	General Obligation
GFOA	Government Finance Officers Association
LFB	Local Finance Board
MRERA	Municipal Rehabilitation and Economic Recovery Act
MSRB	Municipal Securities Rulemaking Board
MQB	Municipal Qualified Bond
NFMA	National Federation of Municipal Analysts
NRSRO	Nationally Recognized Statistical Rating Organization
OS	Official Statement
PILOT	Payment in Lieu of Taxes
RMBS	Residential Mortgage-Backed Securities
SEC	Securities and Exchange Commission
SIFMA	Securities Industry and Financial Markets Association
TAN	Tax Anticipation Note

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Chapter 1: Introduction

In 1968 Roy M. Goodman, then Finance Administrator of New York City, appeared before the Joint Economic Committee of the U.S. Congress to give testimony on behalf of “all the cities and towns around the country that are being dreadfully buffeted as they try to float their bonds on the increasingly stormy seas of fast rising interest rates” (Goodman, 1968: 59). The topic under consideration was the economic effects of municipal bond rating, performed by agencies that had, by this time, “assumed almost Biblical authority throughout the American investing economy” (ibid: 60). Criticizing their “inadequate fact gathering,” he lamented a recent “rating fiasco” from one of the rating agencies: Moody’s downgrade of New York City’s General Obligation bonds from A to Baa (ibid: 60, 61). This downgrade would increase the city’s annual interest payments from 5.20% to 5.70%, equivalent to an additional cost of \$20 million over each of the city’s bonds’ maturities, money that instead could have gone to constructing seven elementary schools, to provide 500 hospital beds or to “put 2,000 policemen on the beat” (ibid: 62). As Poon (2012: 12, emphasis in original) points out, this testimony illustrates how with credit rating “the government has been confronted by an ambitious *financial logic* ... which was being propagated by the very instrument it elevated into an handmaiden of domestic *legal administration*.” That is, while the power and influence of credit rating agencies is crucially predicated on their use in financial regulation by government agencies such as the Securities and Exchange Commission (SEC), they have assumed increasing powers over governments themselves when “[t]o survive in a financescape ... ruled by ratings, capital dependent organizations must concede to accounting and managerial practices that implement a set of values characterizing a growing regime of financial control” (ibid: 25).

The following thesis is an investigation into this “regime of financial control” and throughout its pages I will unpack the workings of the rating agencies, arguably some of the opaqueness of American urban political economy. The rating agencies are, simply put, private companies that rate the creditworthiness of sovereign, municipal and corporate debt. Analyzing financial statements, macro-economic trends and political dynamics, they judge the likelihood that borrowers will default on their debt, assigning them a rating on a scale ranging from AAA (least likely) to D (already in default). The agencies were originally established in the early 20th century to overcome spatial barriers to knowledge in the westward expansion of American capitalism (Sylla, 2002), developing as infrastructures of “time-space compression” (Harvey, 1989b: 240) to allow eastern capital to flow into, in particular, the railway sector. This role has only been strengthened in later rounds of financial globalization, where the rating agencies as “embedded knowledge networks” help facilitate investment decisions by distant lenders in an increasingly disintermediated financial system (Sinclair, 2005: 15).

They are therefore crucial institutions enabling capital markets to be sustained across vast geographies. As such, the rating agencies have been central to the roll-out of financial markets in moments of capitalist expansion, but they also make themselves present in moments of economic contraction. This because, by enabling investors to steer capital to the least risky investments, the rating agencies are “part of a system that keeps an eye on who is violating the prevailing norms of financial and commercial practice” (ibid: 53). In this role, they help facilitate the flight of investors from localized crises, providing a key disciplinary function since debtors are eager to please their standards. The consequences for not doing so can be dire, ranging from higher interest rate payments eating up larger and larger portions of the budget to absolute denial of access to finance. The latter, which might not only impair long-term borrowing, but can also

pose a more immediate danger by cutting off the short-term accesses to capital markets that can be so important for debt management in financially stressed organizations (Ferri, Liu, & Stiglitz, 1999; Sbragia, 1983). Indeed, as Thomas Friedman famously put it in 1995, “[w]e live again in a two-superpower world. There is the U.S. and there is Moody’s. The U.S. can destroy a country by levelling it with bombs: Moody’s can destroy a country by downgrading its bonds” (quoted in Sinclair, 2005: 1).

Ever since Roy Goodman (1968: 60) testified against the “Biblical authority” of ratings, this power has made itself felt across America cities. Local governments in places like New York City, Detroit and Philadelphia have all had their room of policy maneuver circumscribed as the agencies have “app[lied] to the public realm forms of knowledge developed in the private world” (Sinclair, 2005: 117). That is, forms of knowledge that put “bondholder value” at the center of municipal administrative “best practice” and privilege the repayment of debt at the expense of public service commitments or collective bargaining agreements. As “entrepreneurial” cities since the 1970s have sought to fill the vacuum left by the roll-back of federal funding (cf. Harvey, 1989; Leitner, 1990) by tapping into a municipal bond market that has become larger and ever more speculative (cf. Davidson & Ward, 2014; Kirkpatrick, 2016), the rating agencies have come under scrutiny from urban scholars.

In particular, Hackworth (2002, 2007) early identified them as key institutional mechanisms constraining local autonomy and facilitating the neoliberalization of urban governance. Rating pressures catalyze the rolling back of social welfare commitments and their subsequent replacement by more marketized forms of administration (cf. Peck & Tickell, 2002). As such, Hackworth (2007: 17) contends that “the shift to entrepreneurial or neoliberal urban governance is less a result of an organic shift to the right made in the face of capital flight than it is the result

of an institutionally regulated (and policed) disciplining of localities.” In this context, what were once relatively obscure institutions have become central for understanding the present urban condition (see also Biles, 2015; Peck & Whiteside, 2016; Sinclair, 2005). But despite frequent invocations of their importance, the actual workings of municipal bond rating have largely been understudied. That is to say, although their spectacular points of engagement with big city mayors have been chronicled, we know relatively little about how rating analysts make their judgements, what kind of sources of information they rely on, what events they react to or how they make sure that their criteria are applied consistently. Urban political economy has largely treated the rating process itself as a “black box” (cf. MacKenzie, 2005). Similarly, the actual power mechanisms of credit rating are often vaguely defined, mostly referred to as the abstract steering of capital investment but without much specification of how this influence manifests at the urban scale beyond the regular invocation of bond market constraints by municipal leaders. The purpose of my thesis is therefore to examine this underspecified area of urban political economy, but first I will explore the contemporary context in which it operates.

1.1 The return of the urban fiscal crisis

The urban “regime of financial control” (cf. Poon, 2012: 12) becomes particularly visible in moments of public finance crisis. Such was the subordination of Roy Goodman’s own city to the overriding authority of the New York State’s Financial Control Board in 1975, when its inability to roll-over its short-term debt made it the very symbol of the 1970s “urban fiscal crisis” (Harvey, 2005; Peck, 2010; Phillips-Fein, 2017; Tabb, 1982). In the wake of the 2007-2008 subprime mortgage crisis, the attendant pressures and imperatives have once again moved to the forefront of politics. With the global financial meltdown being predicated on speculative

financial innovations that facilitated overinvestment in housing (Harvey, 2012), it is at the urban scale this new political economy of public financial restraint and discipline has been most pronounced (Miller & Hokenstad, 2014; Peck, 2012). Local governments in the United States are particularly reliant on property tax revenue, and as a crisis emanating from that very sector the Great Recession would have particularly severe consequences. Sharply declining property values would cascade throughout the municipal finance system (Martin, Levey, & Cawley, 2012). While not an immediate effect (property tax assessments tend to lag at least 18 months behind macroeconomic cycles (NCL, 2016: 20), the subprime crisis would therefore deeply impact cities not just because of the depth of the downturn, but also due to its particular character. As explained by the Pew Charitable Trust (2012: 9): “[i]n previous economic downturns, the property tax was steadier than other major revenue sources, including sales and income taxes, primarily because home prices remained stable in those periods. This time, the housing market collapsed and was the key driver of the Great Recession.”

The impact of this crisis on local fiscal conditions would be deeper and last longer than previous recessions, with municipal general revenue falling to depths not seen since the 1970s-1980s tax revolts (Langley, 2015). Real per capita general revenue would shrink 5.5% from fiscal year 2007 until it reached the bottom in 2012, three years after the recession had officially come to an end (ibid: 180). The recovery has also been slower. Indeed, as the latest *City Fiscal Condition*-report from the National League of Cities’ (2016: 8) makes clear, General Fund revenues of American cities had in 2016, nine years after the breakout of the crisis, only recovered to a 96.3% of their pre-crisis levels. It was not only declining property values that would impact local governments, however. Rather, they were “hit with a one-two punch” as urban aid from states declined alongside property tax revenue, being reduced by 2.6% in 2010

and delivering a serious blow to municipal governments (which on average are reliant on state aid to fund a third of their budgets) (Pew Charitable Trusts, 2012:1). Despite the major tax source of local governments (property taxes) actually being less volatile than the those of state level governments (sales and income taxes) (cf. CBO, 2010), the effects of this would be that the fiscal pressures felt by all levels of the American state would “roll downhill” (cf. Miller & Hokenstad, 2014). While many places sought to avoid lay-offs and instead focused on raising taxes and/or service fees (Ren, 2015), half a million local government employees would lose their job between 2008 and 2011 (Pew Charitable Trusts, 2012: 13). That was 3.4% of the sector (ibid).

The municipal effects of the crisis, however, extend beyond simply the reduction of personnel and services as cities seek to adapt to a “new normal” of fiscal downsizing (Martin et al., 2012). Rather, the crisis has provided a moment in which the stakes of urban politics has been redefined. As Weaver (2017) shows in his genealogy of the “urban crisis,” the concept has, through its evolution from a liberal response to urban poverty and dissent to a (neo)conservative concern with the pathologies of welfare dependency, always been used as a justification for intervention. In the 1950s this intervention would take the form of government programs to alleviate structural urban poverty, but as the “urban crisis” was re-narrated as an “urban fiscal crisis” in the 1970s it would instead come to justify the roll-back of these forms of “overspending.” New Deal-style interventions, rather than the solution to urban problems, were now promoted as their cause. Combined with moralizing narratives of welfare dependency, fiscally crippled cities like New York and Cleveland would become influential first-movers in a repertoire of policy experiments that later would be recognized as neoliberalism (cf. Glasberg, 1988; Harvey, 2005; Swanstrom, 1988; Tabb, 1982). Indeed, as Weaver (2017: 2040) points out,

“over time Richard Nixon’s ‘silent majority’ and its Reaganite progeny and the financial class were able to coalesce around the ‘urban crisis’ leitmotif to advance a simultaneously conservative and neoliberal agenda which compounded over time.”

Explored in terms of “austerity urbanism,” the latest return of these fiscal conditions has been described as a doubling down of neoliberalization. In this sense, the Great Recession, in its political re-narration from a financial market crisis into a state budget crisis, opened “up a strategic opportunity for new rounds of fiscal discipline, local government downsizing and privatization” (Peck, 2014: 18). Cities are here “where austerity bites” since they contain disproportionately service reliant populations and have been particularly hard hit in the crisis (Peck, 2012: 629). In the process, the budgetary pressures of the post-crisis state are downloaded onto the local scale and off-loaded onto its most vulnerable populations (Peck, 2014, 2014), resulting in a retrenchment of long established socio-spatial inequalities (Donald, Glasmeier, Gray, & Lobao, 2014; Kitson, Martin, & Tyler, 2011). Weaver (2017: 2051) is, however, cautious of too strong claims to a new crisis, arguing that “while [post-subprime crisis] austerity has resulted [in] deep cuts to urban services, privatization and the empowerment of capital interests ... the recession accelerated but did not create these developments.” In this sense, the fiscal crisis does not so much “return” in a cyclical fashion, but has become a structural feature of the entire urban system. This is inarguably true. Indeed, since the 1970s the urban fiscal crisis has been invoked with such regularity that it almost has become the normal state of cities (for a sample, see Burchell & Listokin, 1981; Gottdiener, 1986). We cannot, however, simply understand the present moment as the continuation of what went before. That would be to overlook the changes to municipal finance that has occurred since New York City’s inability to

roll-over its debt, changes that have dramatically redefined the stakes of local fiscal crises. In this sense, the today's urban fiscal crisis is rather simultaneously path-dependent *and* particular.

One way of understanding 1970s urban fiscal crises is to position it in the context of a generalized state fiscal crisis, one that according O'Connor's (2002[1973]) influential account stemmed from how the capitalist state, torn between the competing imperatives of accumulation and legitimation, was inherently unable to control its growing expenditures on the one hand and falling revenues on the other. First published in 1973, O'Connor's (2002: xxi) *Fiscal Crisis of the State* sought to "explain macroeconomic changes in the economy in terms of the state budget ..., not vice versa," approaching budgets as arenas for the unfolding of a key contradiction of its time: that between monopoly capital and the working class. Monopoly capital cried for social capital investments while the working class demanded spending on social services, and both sought to off-load the cost of this onto the other. On the urban scale, such crisis of competing imperatives was represented by, for example, federal policies which eroded the urban tax base by promoting suburbanization and investment shifts to the "sun belt" simultaneously as they implemented compensatory social programs to advert the state's looming legitimation crisis among the urban poor (Piven, 1984). Structurally unable to disregard either one of these constituencies in favor of the other, the compromising Keynesian state was crucially undercut and its accelerating budget deficits provided the catalyst for state downsizing and early waves of austerity (O'Connor, 2002). It was in this context liberal cities like New York would come to represent the excesses of Keynesianism, as Piven (1984) points out, not simply out of structural economic necessity but as a result of the contradictory policies of the state. Urban politics would therefore provide a crucial site for that state's neoliberal restructuring (cf. Brenner & Theodore, 2002).

While the latest crisis has indeed intensified such processes, contemporary austerity urbanism is not simply the harsher repetition of its predecessor. Rather, as Kirkpatrick (2016) has pointed out, it is playing out in a context where municipal budgets have been thoroughly *financialized* as local governments have engaged ever more speculative financial instruments, making their fiscal operations increasingly unstable. Kirkpatrick (ibid: 26) therefore argues that “conventional explanations of urban fiscal crisis only go so far in explaining contemporary cases, a limitation traced to the changing role of financial markets in urban affairs.” This requires a rethinking of the urban fiscal crisis not simply as a continuation of the crisis of the Keynesian local state, but as a crisis of the modes of speculative and entrepreneurial urban governance that sought to fill the vacuum left by its retrenchment (Davidson & Ward, 2014; Lobao & Adua, 2011; Peck & Whiteside, 2016). Indeed, while Roy Goodman might recognize the politics of localized austerity and financial control, the linages of the present crisis cannot simply be traced to liberal New York or radical-populist Cleveland. Its most immediate forerunners can instead be found in arch-conservative places like Orange County and San Diego. These are cities where California’s infamous tax-curbing “Proposition 13” has since 1978 pushed municipal managers to seek fiscal relief in financial market speculation, the raiding of pension funds and “entrepreneurial” forms of urban redevelopment (Erie, Kogan, & MacKenzie, 2011; Norris, 1994). As such, they represent a precursor to the financialized urban fiscal crisis of today.

This “speculative urbanism” (Davidson & Ward, 2014: 82) sought to balance between accumulation and legitimation by tapping into financial markets in a form of “privatized Keynesianism” (Crouch, 2009: 382). As these markets contracted, however, this new regime would run into its own contradictions. This produced a fiscal crisis which aftermath combines familiar conservative politics with new financial market logics. Tabb (2014: 93), for example,

argues that “[w]e need to understand urban fiscal crises as part of the wider buildup of debt, a central feature of the contemporary mode of social regulation” while Hinkley (2017: 2134) points out that the search for solutions has added a particular financialized twist to long established neoliberalization, emphasizing “financial expertise, external discipline and restructuring contractual obligations, along with the longstanding practices of tax cuts, privatization and retrenchment.” This is a process that redefines urban politics since the interest of local actors are increasingly contradicting those of extra-local bondholders, leading to the breakdown of long established local governing alliances (Kirkpatrick & Smith, 2011; Peck & Whiteside, 2016). Further, since “[f]inancialization involves the use of state power to enforce collection of debt” (Tabb, 2014: 92), cities have been put under increasingly punitive forms of state control. This is most significantly illustrated by the dissolution of local democracy in the roll-out of “emergency management” regimes in states like Michigan (Anderson, 2011; Peck, 2012). In this process, the lives of, in particular, racialized urban residents have become so devalued that the search for municipal fiscal solvency has come to justify the most destructive of cost cutting: including the Flint, MI lead poisoning scandal brought about by a decision to shift the city’s water supply to the cheaper, but contaminated local river (Fasenfest, 2017; Kirkpatrick & Breznau, 2016; Pulido, 2016).

Following this, the present is a moment in where the politics of debt and the institutions of the municipal bond market have become ever more central for urban politics. An adequate account of the “new” urban fiscal crisis must therefore necessarily take these dynamics as point of departure. It is in this context that the following thesis should be located, interrogating a particular financial institution (the credit rating agency) to explore what a “bond market optic” can reveal about the wider state of contemporary urban political economy.

1.2 Research questions and methods

A study of the [municipal bond] market may not give us the details of what is normally considered the ‘stuff’ of city politics, but it does indicate where and how that stuff fits into the larger picture. Although it is obvious that municipal government does not exist in isolation, it is nonetheless difficult to get a grip on the *multiple* relations in which city (as well as other local) officials are involved. Studies of intergovernmental relations, for example, necessarily focus on one set of relationships. Similarly, scholars examining the impact of capitalism on the city focus on the development of corporate capital, capital accumulation and/or conflict and legitimacy. In contrast, by focusing on the bond market, we are compelled to think about numerous intersecting relationships: those between the city government and the public authorities that operate within its boundaries, as well as those between city government and the larger economic world within which city government exists.

Alberta Sbragia
(1983: 95-96, emphasis in original)

These words by Alberta Sbragia, arguably the foremost chronicler of the history of the U.S municipal bond market, make a compelling case for how attention to the operations of this market can contribute to urban political economy by positioning the city within the vertical and horizontal relations through which finance capital, higher tier governments as well as local actors co-create the urban condition. This thesis is an attempt to follow one such market relation, that of credit rating. Rather than traditional attempts to “control for difference,” it focuses on the phenomenon of credit rating as “distributed across numerous urban contexts and produced within shared and interconnected processes” (Robinson, 2016: 188). As such, it roams rather

extensively across the variegated geographies of the urban fiscal crisis, primarily exploring reoccurring patterns, constitutive relations and common outcomes rather than singular cases.

Further, while the asymmetric interactions between globalized rating agencies and localized municipal actors are explored, the thesis aims to complement these well-rehearsed global-local dynamics of urban change by examining how local politics is positioned in relation to not only structural economic forces, but also to the organizational-internal dynamics of the rating process and its mediation through federal regulatory change and the states' oversight of local fiscal practice. The bond market becomes the medium that ties these local and extra-local processes together and, by attending to "upwards, downwards, and sideways links" the ambition of the thesis is to unearth municipal finance's "*embeddedness* and *positionality* within a broader scalar hierarchy" (Brenner, 2001: 605, 600, emphasis in original).

Substantively, this investigation set out to examine two interconnected research questions.

These were:

- 1) *How do credit rating agencies enhance/constrain the local state's ability to manage fiscal stress, and what are the implications of this variegated capacity for the financialization of urban governance?*

- 2) *How do credit rating agencies 'read', understand and respond to this moving landscape of local state capacity/potential, and how does this in turn structure their assessments of localized risk and investment opportunity?*

The original aims of my research were therefore to understand the two sides of the credit rating process in relational terms, complementing previous accounts that primarily has focused its urban repercussions. While the austerity outcomes indeed provided the original spark of interest and kept the critical flame burning during moments of near-resignation in face of the dull labyrinths of public finance, I wanted to figure out how the process leading up to, for example, a spectacular downgrade looked like. I wanted to open up one of many “black boxes” of global finance (cf. MacKenzie, 2005) to more fully position austerity urbanism within the system of public finance. Similarly, I soon realized that while the internal organization of the rating agencies had indeed been overlooked, so had the municipal finance departments through which their influence on urban everyday life is mediated. This was just as much a black box and it left open important questions about the actual mechanisms of bond rating power. My research therefore took quite a different turn from the attention to urban political leadership evident in Hackworth (2002, 2007) and Biles (2015). It became almost exclusively concerned with mid-level municipal bureaucrats. These are the people whose work in the background of urban politics is not so much concerned with the “roll-back” and “roll-out” moments of neoliberalization (cf. Peck & Tickell, 2002), but rather seek to “roll-with” normalized processes of fiscal restraint and financial prudence (cf. Keil, 2009).

The work of these professionals seldom make the headlines and to study them required more than an analysis of spectacular moments of rating change based on secondary sources. Empirically, the following text is therefore based on semi-structured interviews undertaken between May and July 2016 in New York City and the State of New Jersey. With my base in Newark’s Lower Roseville-neighborhood and with an interest in the multiple market relations connecting rating analysts, local financial professionals and state fiscal oversight bodies, I

traveled back and forth between the Wall Street offices of the financial sector, fiscally strained (post-)industrial localities in New Jersey and the state's capital, Trenton. Across these sites, I undertook 22 interviews, ranging from 30 minutes to two hours. Ten of these were with market representatives (including current and former rating analysts, bank market researchers, bond insurers and independent buy-side consultants). The other 12 interview were with municipal and state representatives (mostly local Chief Financial Officers (CFOs), but also a Business Administrator, two former directors of the state's local fiscal oversight body and a representative of the New Jersey League of Municipalities).

In recruiting these latter respondents, I would primarily rely on emails and follow up phone calls, often having to source phone numbers from unexpected places like state aid applications and make repeated calls to get past the gatekeepers of the local bureaucracy. While New Jersey's notorious machine politics at moments would make access difficult (Camden's finance staff, for example, virtually hang up the phone on me after a quick, dismissive "no, we don't do that"), at large local financial officers would be remarkably welcoming. I quickly got the sense of an under-researched group of urban actors who were more than willing to share their insights into the world of municipal finance, especially those that had taken their cities out of crises or achieved credit rating upgrades proudly displayed their achievements. The credit rating world was more closed, but the referrals of a couple of lucky early encounters allowed me to use a "snowball sampling" method. That is, relying on gaining the trust of my interviewees so that they would vouch for me to their colleagues. Indeed, it was a single early interview with a buy-side market analyst that eventually would lead to all but two of my ten "market-side" interviews. Among these, former rating analysts, some of which had more than 20 years of experience before they left their agencies, would be particularly open, reflexive and, indeed, critical

(although their concerns with the failures of the agencies largely circulated around the *lack of* financial discipline).

These interviews were complemented by the close reading of a wide range of secondary sources. In particular, Chapter 3 seeks to weave together the accounts of interviewees with a critical analysis of rating methodologies. As I will discuss, financial regulation since the 2007-2008 subprime mortgage crisis demands that the rating agencies make their methodologies publically available and that they justify every single rating in relation to these methodologies. Once interpreted, the methodologies therefore provide an accessible window not only into the kind of indicators and procedures the rating process relies upon, but also with regards to its difficulties, paradoxes and contradictions. Rating reports, buy-side market research, federal regulatory documents and textbooks about investing in the municipal market supplied additional insights. Rather than taking them at face value, I approached these market outputs as political documents in their own right. That is, they were sources allowing me to interrogate the self-understanding of the market, not neutral “facts.” Local news coverage, auditor reports and the industry magazine *Bond Buyer* were also crucial as I tried to get my head around how changes to ratings and their methodologies translated into concrete places. New Jersey’s statute was further drawn upon to understand the embeddedness of these places within the broader regulation of municipal finance. Stated simply, I tried to use everything I could get my hands on and to follow every lead that would help me understand the object of my research.

My case selection proved to have substantial, but largely unexpected, consequences for the unfolding of the research. Seeking to get inside the rating agencies, their New York City headquarters were obvious (indeed necessary) research sites. But I wanted to do more than that. I wanted to put those organizational-internal processes in relation to the localized politics of

austerity urbanism. The logistical challenge of such research was daunting at first, until I realized that New Jersey was experiencing an illustrative multi-scalar rating crisis (see Chapter 4). New Jersey suddenly seemed to be the ideal place to locate my research, providing an opportunity to travel back and forth between rating analysis and urban outcomes within the scope of a Master's thesis. To my surprise, however, this would not be as self-evident for many of my respondents. Most of them would be puzzled to why I had chosen to come all the way from Sweden, via British Columbia, to study urban fiscal stress in a state that within the world of municipal finance is considered a particularly outstanding case of financial prudence. Why had I not chosen to go to California? Why not Michigan? To them, New Jersey did not make any sense. The traditional financial prudence of municipalities in the state, however, transformed New Jersey into something more than a convenient location. It proved to be a great case for theoretical "extension" (cf. Burawoy, 1998) as it provided an understanding of the *normalized* practices of financial governance, one with stark contrasts to the stories of highly politicized confrontations that previously have dominated urban analysis of credit rating. It further illustrated how, even in the state that ought to be less crisis prone due to its close oversight of municipal finance, the new urban fiscal crisis and the pressures of credit rating were inevitably trickling down, often because of the very programs that had been developed to mitigate these crises. Rather than highlighting spectacular crisis, it came to illustrate the slow-moving failure of also the most robust corners of American municipal finance.

1.3 Outline of the thesis

Concerned with the different actors of the credit rating relation, this thesis is organized into three substantial chapters and a concluding discussion. Following this introduction, Chapter 2

discusses the changes that the municipal bond market has undergone in the last 40 years. Here, I introduce the basic characteristics of the market, including an outline of the different kinds of municipal bonds and their security structures, the bond issuing process as well as their ownership patterns. Thereafter, I provide an overview of the emerging literature that seeks to put the bond market in the center of a new financialized kind of urban governance. This literature makes claims to financialization with regards to two specific processes: (i) the increasingly speculative nature of municipal borrowing which since the roll-back of the Keynesian state has seen a proliferation of more sophisticated financial instruments to fund local infrastructure, and (ii) how this process is increasingly exposing cities to the discipline of the bond market and its actors (including rating agencies). After reviewing this literature, I examine how the more speculative nature of the market has led to important changes in market regulations as well as a different mindset among investors and credit rating agencies. This is a process that has put municipal bond issuers under intensified analytical scrutiny and has led to a more differentiated market between well-to-do cities and their struggling peers.

It is in this context the rating agencies have become central institutions for the understating of urban political economy and in Chapter 3 I dig deeper into the rating process. Here, I discuss established accounts of the prominence of credit rating. These have either emphasized the role of the agencies as knowledge producers, enabling market participants to overcome informational asymmetries, or have focused on how federal regulation has given a handful of private companies near monopoly status in the market. Drawing on recent engagements with *value theory* under conditions of financialization, I thereafter argue that the agencies play yet another crucial role: they provide the means of commensuration that enable heterogeneous local fiscal uncertainties to be price and traded as risk-bearing commodities.

Unpacking how this is achieved, I argue that the municipal bond rating process pivots around a key tension between on the one hand understanding localized credit risk in all its complexity while on the other hand having to transform that complexity into a measure of “abstract risk,” where the default risk of a AAA-rated credit always must be the same. Effectively tasked with comparing the incommensurable, the rating analysts are well aware of how fraught this process is. In the last section of the chapter I therefore examine two crucial limits to commensuration: the increasing standardization in the post-Dodd-Frank era and the so-called “global recalibration” of municipal ratings to the corporate rating scale, a process that aims to make investment risk commensurable across sectors as well as across space. In the chapter’s conclusion, I reflect on the alienation stemming from this commodity abstraction.

Shifting focus to the cities at the receiving end of the rating process, Chapter 4 interrogates the urban politics of “creditworthiness.” Asking what the mechanisms of credit rating power are, I argue that rather than simply descending from above their influence is co-constructed in a “politics of limits” arising out of the interactions between the rating agencies, local financial professionals and state municipal finance regulation. This takes the form of “accountancy urban governance,” where political questions of fiscal prioritization appear as technical questions of creditworthiness. Drawing on interviews with municipal financial professionals in New Jersey, I explore how notions of “budgetary flexibility” help steer local politics by setting the “rules of the fiscal game” while an aversion to political involvement creates a shared discourse of technocratic public finance common-sense. This is further reinforced by the state’s close oversight of local finance, which is not, however, absolute. The last section of chapter therefore seeks to unpack two moments of accountancy urban governance failure: the self-reinforcing nature of ratings and the trickle down of credit rating crises

throughout the scalar hierarchy of the state. These points towards serious limits to an urban politics of creditworthiness and reveals how, in stagnating local economies, the tools and techniques of financial prudence are increasingly exhausting themselves.

Summarizing the arguments of the thesis, the last chapter concludes by stepping outside the professional realm of municipal finance to reflect on why we should take the trouble to unpack this arena of urban politics. Asking what the political significance of the bond market is, I focus on the violence municipal debt has brought to cities. This is a violence that is both “slow” (Nixon, 2011) and “abstract” (LiPuma & Lee, 2004), it is the everyday “stuff” of urban politics (cf. Sbragia, 1983) that only a bond market optic enables us to fully comprehend.

Chapter 2: From financial backwater to urban financialization: The evolution of the municipal bond market

2.1. Introduction

In his account of the politics of local finance, Monkkonen (1995: 1) writes that “[p]ut simply, American cities do not have enough money.” This requires them to regularly seek funds beyond their normal revenue streams, whether those are locally collected taxes and fees, state municipal aid or federal grants. Seeking relief in capital markets becomes one way to stem this short fall, where the borrowing can be both short-term to fill a temporary deficit in the operating budget or be invested for long-term infrastructure provision and economic development. It is this latter long-term debt which, in Monkkonen’s (ibid: 1) words, “funds the building of cities ... pays for the big stage on which the city’s social, economic, and cultural life [sic] are all played out... [and] literally [provides] the foundation of modern urban life.” Further, while the short-term needs are often bridged by local banks, the sheer amount of money necessary for laying the “foundation” to urban life requires more specialized funding options. In North America this has taken the form of a uniquely large, robust and disintermediated capital market: the municipal bond market (Kaganova & Kopany, 2014). While seemingly opaque, the centrality of this market for everyday urban life is undisputable. Indeed, as the legendary and ever up-beat municipal bond broker Jim Lebenthal argues in his 2006 autobiography *Confessions of a Municipal Bond Salesman*, “[y]ou can’t get up in the morning, flick on a switch, take a shower, a subway, a bus, go over a bridge or under the river without a Municipal Bond touching your life” (Lebenthal & Kanner, 2006: 78). Despite this, Lebenthal notes, municipal bonds have long been “the most understood investment in America” (ibid: 10).

Shedding light on this misunderstood investment class is the purpose of this chapter, where I will also engage with the emerging claim that the after-Keynesian restructuring of the municipal bond market has entailed the *financialization* of urban governance. As Aalbers (2017: 3) defines the term, financialization entails “the increasing dominance of financial sectors, markets, practices, measurements and narratives, at various scales, resulting in structural transformation of economies, firms (including financial firms), states and households.” As such, it has moved the bond market to the center of American urban political economy. Most significantly, scholars have interrogated the proliferation financial innovations across the nation’s cities (Davidson & Ward, 2014; Kirkpatrick, 2016; Kirkpatrick & Smith, 2011; Pacewicz, 2013, 2013, Weber, 2002, 2010) and emphasized the increasing prominence of debt dynamics as the driver of local politics (Kirkpatrick & Smith, 2011; Peck & Whiteside, 2016; Tabb, 2014). Building on this literature, I will here argue that while the market has become increasingly speculative and opaque, the positionality of cities within that market has changed from safe havens of capital to self-policing debtors put under increasing investor scrutiny. To make this argument, I will first give an overview of the basics of municipal bonds, thereafter I will discuss the literature on urban governance financialization before interrogating processes of urban financialization through an historical reading of market restructuring and regulation. A concluding discussion will summarize the chapter.

2.2. Municipal bond basics

A municipal bond is a financial instrument issued by state or local governments to fund their long-term capital needs and sold on a decentralized market to investors seeking a secure, often tax-exempt, capital income. As such it can seem straightforward, primarily a “buy-and-hold”

asset for investors that rather than outwitting the market are confidently putting their feet up waiting to collect a yearly coupon. Compared to corporate equities, currencies or derivatives markets, municipal bonds have then long been perceived as a relative financial backwater. As safe, stable, and a little boring. Indeed, as Lebenthal (2009: 4) explains: “[w]hen uncertainty reigns, and the flight to safety is on, ... munis are ports in the storm.” As the value of outstanding municipal bonds has exploded in the 1980s (see Figure 2.1), however, this assumption appears greatly simplified. Rather, municipal securities have emerged as an increasingly complex market of over one million individual issues (SEC, 2012: 5) together worth \$3.8 trillion (SIFMA, 2017) on behalf of around 50,000 issuers in 40 different sub-sectors of public finance (Comes, Kotok, & Mousseau, 2015: 41). Indeed, buy-side municipal analysts have argued that it “is a large, diverse, complex market place comprising an extremely large number of issues with relatively low market value” (De Groot, Chan, & Vallecillo, 2010: 3) so that “in fact it is not really a single market at all, but a combination of different regional markets with thousands of issuers” (Wolfe & Chief Investment Officer Team, 2013: 1). Further, since each municipal bond issue is distinct in terms of its structure, underlying security and trading patterns, experienced analysts point to the difficulties, and even dangers, of generalizing about the market as a whole (Lebenthal, 2015). I will here, however, sketch some basic features.

Value of Outstanding Municipal Bonds (Billlion \$USD)

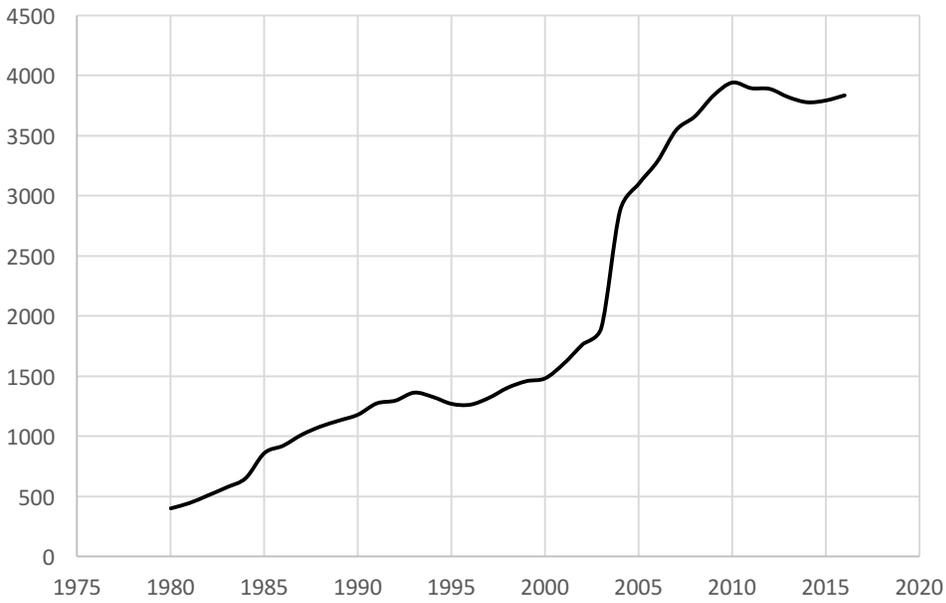


Figure 2.1. Growth of the municipal bond market, 1980-2016 (SIFMA, 2017).

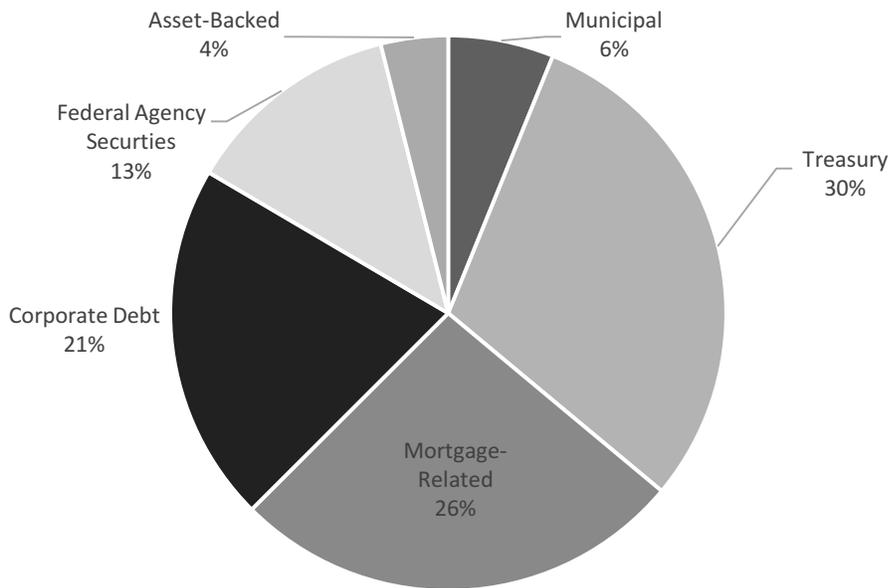


Figure 2.2. Issuance in the U.S. bond market, 2016 (SIFMA, 2017).

What traditionally makes the municipal market different from other financial securities markets is a federal (and sometimes also state and local) tax-exemption on interest income on bonds. This has been in place ever since the Sixteenth Amendment to the U.S. Constitution, passed in 1913 to allow for the levying national tax. Here municipal securities were excluded on the basis of a 1885 Supreme Court decision (*Pollock v. Farmers' Loan and Trust Co*) that deemed the taxing of state and local government bonds an unconstitutional infringement on the ability of states to operate freely, a compromising of American federalism (Sbragia, 1996). This tax-exemption allows issuing governments to borrow more affordably than would otherwise be possible because investors in municipal bonds can extend their funds for relatively low interest rates as they do not need to compensate for net-income shortfall due to taxation. Since the federal government loses out on potential revenue, however, this tax-exemption constitutes a de-facto indirect subsidy of lower tiers of government. Its status is then continually questioned, making changes to the Internal Revenue Code an important, but “much neglected force in urban political economy” (Sbragia, 1986: 200).

This became evident with the Tax Reform Act of 1986, when long standing concerns over loss of tax revenue and the growth of municipal borrowing to support local private industries provoked a definitional narrowing of which bonds were to be exempt from taxation (Sbragia, 1996). For Hildreth & Zorn (2005: 128), this constituted a “watershed event” transforming “the once placid environment for municipal securities into a frantic and arcane market.” This because while before the 1986 Act all interest from municipal debt was exempted from federal tax, afterwards only some kinds of securities and some kinds of investors would

enjoy the privilege.¹ Since the 1986 then, the municipal bond market is made up of two principal categories of bonds: traditional tax-exempt bond and taxable private activity bond.

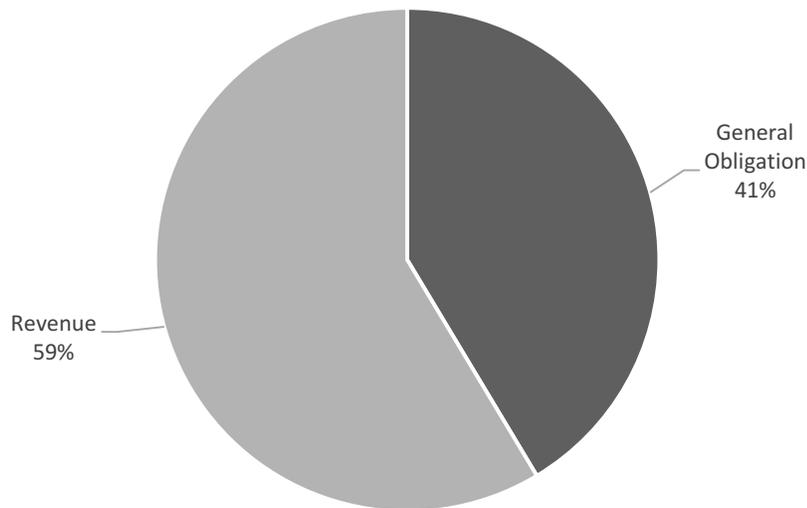


Figure 2.3. Municipal bond issues by security structure, 2016 (SIFMA, 2017).

Individual municipal bonds are classified in accordance to the sources of governmental revenue that are pledge as security for borrowing, primarily as either *General Obligation Bonds* (GOs) that pledge the municipality’s “full faith and credit” or *Revenue Bonds* that pledge a particular revenue stream. More specifically, GOs draw their security from the municipality’s general fund and they are usually “unlimited tax”-pledges obligating the issuer to use its entire taxing power to repay the bonds if so needed. This effectively gives the bondholder “a blank check ... with the promise to commit all its resources into repayment” (Comes et al., 2015: 59). The GO-pledge is considered a particularly strong one and was long treated as senior to other

¹ Principally, the Act redefined the market into two categories, bonds for ‘essential function government activities’ and ‘private activity bonds’. The latter were defined as those for which more than 10% of the proceeds would go to private businesses and/or of which more than 10% of debt service would be paid by private businesses (Hildreth & Zorn, 2005: 129).

debt obligations in Chapter 9 municipal bankruptcies (ibid). All bonds that are not GOs, on the other hand, are classified as revenue bonds. These are repaid with designated revenue streams stemming from the capital projects they are issued to pay for. Unlike GOs that are issued by general-purpose governments principally for the financing of non-exclusionary projects like streets, sewers and other publically accessible infrastructures, revenue bonds are issued, often by “special authorities,” for self-sufficient and revenue-generating infrastructures like water and utility networks or toll roads. The repayment of principal and interest is therefore narrowly reliant on the viability of the project itself rather than the local political economy at large. These revenue bonds are considered self-sufficient debt that is not technically an obligation on the balance sheet of the “root entity” (that is the general-purpose government). They are therefore not subject to the same debt limitations, mandatory voter approval or other restrictions as GOs. Revenue bonds have then been central to the “politics of circumvention” that, according to Sbragia (1996: 5, 104), has characterized municipal finance throughout the 20th century: where financial and institutional innovations to circumvent debt limits and other state-local regulations have “changed the very meaning of the term municipal government, changed its structure and helped change the kinds of public service that entered the public domain.” As such, today they amount for the great majority of funds raised on the municipal bond market (see Figure 2.3). In addition to GOs and revenue bonds, there are forms of security pledges that sit at the border of these two categories. Some of the most common are summarized in Table 2.1.

The individual bonds, which can be acquired by investors in increments of \$1,000 or \$5,000, are sold as an aggregate ‘bond issue’ with three kinds of maturity structures.² After

² Either, it is structured as a *term issue* where all bonds mature at the same date and the issuer makes a lump-sum payment (‘bullet payment’) at the bonds’ last payment date, as a *serial issue* where the bonds mature successively over several years and are paid down incrementally, or as a *series issue* when only a certain percentage of the full

deciding on the security pledge of the bonds and the issue's maturity structure,³ a credit rating is often obtained⁴ and local governments approach the market to sell their bonds to investors. These bonds are traded "over-the-counter." That is, in a decentralized market that is more opaque to the public than the registered stock exchanges on which corporate stocks trade (Fischer, 2013).⁵ The underwriters, often in groups known as syndicates, purchase the entire bond issue and resell the individual bonds to investors. Traditionally, municipal bonds are primarily purchased by individual households for their own benefit, so-called "retail investors." These investors tend to "buy-and-hold" the bonds until their maturity, favoring municipal bonds as a secure income stream. There is, however, also a secondary market. As a tax-exempt asset, municipal bonds attract investors that can take advantage of this unique feature. This primarily means wealthy individuals in the higher tax-brackets, while lenders that already pay low taxes, such as pension funds, are less interested (Sbragia, 1986). The latest yearly data from the Securities Industry and Financial Markets Association (see Figure 2.4.), show that individuals held 44% of outstanding municipal bonds in 2016, followed by mutual funds (24%), banking institutions (15%), insurance companies (13%) and other investors (4%).

bond issue comes to market at once with anticipation of further issuing until the required capital has been raised (De Groot, Chan, & Vallecillo, 2010).

³ Tailoring it to the type of capital project it is issued to pay for as well as taking account of other considerations such as municipal debt limits.

⁴ Note that the credit rating process will be discussed in detail in chapter 3. I will therefore principally dispense with this process for now, only touching upon it when necessary for an understanding of more general market dynamics.

⁵ Most municipal bonds (in 2010 over 80%) are sold through a *negotiated* offering where the issuer and underwriters negotiate the terms of the sale, including interest rates, while a minority is sold either through a *competitive bid* (18%) where the organization that offers the best bid on the bonds get to underwrite them or as *private placements* (less than 2%) where the bond is sold to a private investor rather than going through a public offering process (De Groot et al., 2010: 6). Generally, GO-bonds tend to be sold competitively while revenue bond offerings are negotiated (ibid).

Type of Bond	Type of Security Pledge
General Obligation - Unlimited Tax (GOULT)	The issuing entity pledges its “full faith and credit” and promises to devote its entire taxing ability towards the repayment of the bond; prioritizing debt repayment over any competing claims to revenue.
General Obligation - Limited Tax (GOLT)	The issuing entity pledges its “full faith and credit” towards the repayment of the bond, but does not have unlimited taxing powers.
Revenue	The issuing entity pledges that a designated revenue stream (such as the tolls from a toll road, the fees from a water and utilities network, or the lease payment from a building) will be used towards the repayment of the bond.
Special Tax	The issuing entity pledges a designated tax sources other than property tax (e.g. business license or sales taxes) towards the repayment of the bond.
Special Assessment	The issuing entity pledges to repay the bond by charging an earmarked tax upon those property owners benefiting from the improvements the bond is issued to finance.
Moral Obligation	A non-binding obligation that the issuing entity will make up potential deficits in debt service with the help of revenue sources in addition to those originally pledged.

Table 2.1. Common municipal bond security pledges (MSRB, 2013).

According to Sbragia (1986, 203), this means that “[s]o many participants are involved [in the municipal bond market] ... that no one institution or individual can control or even shape it, much less set interest rates.” As the Municipal Securities Rulemaking Board (MSRB, 2017) points out in a recent market commentary, however, these ownership patterns are changing. In 2006-2010 the market saw a decline in household investors and municipal securities dealers while the share of bonds held by mutual funds, banks and exchange traded funds increased. In addition to this, the number of households owning bonds *via* mutual funds declined while fewer American households were even involved in the market in the first place: only 1% reporting that they owned municipal bonds in the 2013 Survey of Consumer Finance compared to 3.5% in 1988 (ibid:1). Thus, MSRB (ibid: 2) concludes that “municipal bond ownership is becoming concentrated in a smaller number of hands,” although it is yet unclear what the effects this will

be on the previously more decentralized market or for the municipalities that must rely on it to finance their infrastructural needs.

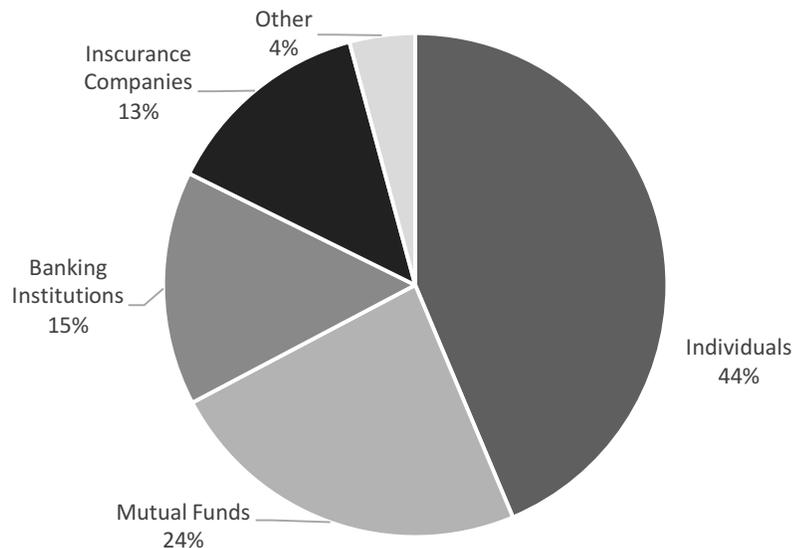


Figure 2.4. Holders of U.S. municipal securities, 2016 (SIFMA, 2017).

2.3. Financializing urban governance: politics of speculation, politics of debt

The 2007-2008 financial crisis provoked a stream of commentaries arguing for the re-centering of finance in economic geographical research, a sub-discipline long privileging the study of the supposedly “real economy” of manufacturing above the workings of financial capital (Lee, Clark, Pollard, & Leyshon, 2009; for a review of recent work on the intersections of the "real" and the financial economy see Hall, 2013). In the aftermath of the subprime mortgage crisis, however, it has been argued that such distinctions no longer hold and geographers need to give finance central status in their understandings of how circuits of value (re)produce socio-spatial inequalities (Sokol, 2013). Indeed, Engelen & Faulconbridge (2009) have implied that failure to do so will seriously compromise the discipline’s academic and political relevance in the post-

crisis era. One attempt to rise to this challenge has been the proliferation of work on *financialization*, where “the growing influence of capital markets, their intermediaries, and processes in contemporary economic and political life” has been argued to provide an opportunity to more firmly embedded finance in (economic) geographical research (Pike & Pollard, 2010: 30). The meaning of financialization has, however, been rather elusive, with Lee et al (2009) identifying at least 17 different conceptualizations.

To make sense of this diversity, commentators like French et al (2011) and van der Zwan (2014) have argued that the financialization literature is made up of three sub-fields, largely according to the scale on which the process is conceptualized. Firstly, there are macro-conceptualizations of financialization as a particular regime of accumulation in which finance dominate both as a sector in relation to GDP as a whole and, more importantly, for the profit-making activities also of non-financial firms (cf. Krippner, 2005, 2011). Secondly, finance is argued to increasingly be reaching into the micro-scale of the everyday life, where individuals and households compensate for the withdrawal of the redistributive Keynesian state by mobilizing a more “democratized” credit market to pay for housing, pensions and other crucial goods (cf. Langley, 2008; Martin, 2002). Finance is thus forming new subjectivities, as it “presents itself as a merger of business and life cycles, as a means for the acquisition of self” (Martin, 2002: 3). Finally, literature on the growth of “shareholder value” as a guiding corporate principle has focused on the scale of the firm, where it is argued that corporate management culture has been transformed by a greater emphasis on maximizing shareholder’s returns as opposed to catering for a wider constituency of stakeholders (cf. Froud, Haslam, Johal, & Williams, 2000). Aalbers (2015: 216) has, however argued that such compartmentalization is unhelpful as scholars are increasingly making connections between these realms, so that the

conceptual value of financialization “is not only that it connects different disciplines but also different levels of analysis, from the very micro to the very macro - and demonstrating how these are related.”

Like the surge of financial scholarship in economic geography in general, the 2007-2008 crisis brought an increased focus on municipal finance and the bond market to American urban political economy. This literature principally makes two interrelated claims concerning financialization: (i) that speculative financial innovations have made municipal finance more risk exposed, complex and unaccountable, and (ii) that local politics have become subsumed under the discipline of financial markets. Most significantly, the first claim is illustrated by the attention that has been given to one municipal bond market innovation in particular: that of Tax Increment Financing (TIFs). Similarly to how Sbragia (1996) argues that revenue bonds, through the “politics of circumvention,” have successively replaced GO-bonds as the preferred financing vehicle for capital-hungry municipalities, Hildreth & Zorn (2005) argue that (in the context of the 1970s and early 1980s high interest rates and inflation, economic slow-down and reductions in federal aid) municipal finance has seen increasing innovation. This includes a further turn away from GO-bonds towards revenue bonds and the development of more novel forms of infrastructure financing such as Certificates of Participation (COPs) and Tax Increment Financing (TIFs). The former is bought by investors for a share of lease revenue while the latter funds infrastructural improvements by designating “blighted” redevelopment districts and using projected increase of property tax revenue in this district (the “tax increment”) as debt security (ibid). The proliferation of these instruments was preconditioned on the rise a particular form of “speculative urbanism” responding to the rollback of federal funding and state-level tax caps, with cities pushed to “speculate on future economic growth by borrowing against predicted

future revenue streams to make this growth likely” (Davidson & Ward, 2014: 84; see also Harvey, 1989; Leitner, 1990; Sagalyn, 1990). Their use has, however, in turn had far-reaching implications for urban governance.

This because TIFs, like infrastructure leases, public-private partnerships and other innovative forms of infrastructure finance, represent “not just the disembedding of urban assets but also a complex process of governing urban problems *through* finance” (Ashton, Doussard, & Weber, 2016: 1396, emphasis in original). Weber (2002: 531; 2010), who pioneered the critical study of TIFs, argues that their spread represents a deepening of the influence of financial markets in urban governance (albeit crucially preconditioned on local state agency), exposing cities to the risks of financial and property speculation while making them “dependent on the short-term horizons of ... those institutional investors who purchase municipal bonds.” The deeply transformative powers of such local financial innovations are further identified by Pacewicz (2013: 415) who emphasizes the “recursive relationship” between local governments and finance, arguing that “[p]ublic policies can transform financial markets ... but reliance of financial markets can also transform the institutions that supply financial commodities in ways that create political and professional incentives for further financialization.” In particular, Pacewicz (2016) finds that TIFs are used by American municipal leaders to increase their fiscal capacity in the context of roll back and increased earmarking of intergovernmental fiscal transfers. Since this instrument “creates revenue streams that are discretionary by legal convention in many states: regarded by city leaders and regulators as appropriate for virtually any expenditure anywhere in the city,” the maximization of these revenues through TIFs becomes a goal in itself (ibid: 269). This despite their actual development outcomes often proving dysfunctional for local publics and economic elites alike (ibid). This process increases

the complexity of municipal finance while it has a de-democratizing effect on urban politics as the economic development professionals designating and managing TIFs achieve greater influence in fiscal matters and push for ever more use of TIFs (Pacewicz, 2013). The riskiness and de-democratizing effects of this financialized urban politics is further emphasized by Kirkpatrick (2016: 57) who argues that with the spread of TIFs American urban governance has fragmented as cities “have seen the rampant proliferation of ... an array of quasi-public institutions that are empowered to issue tax-exempt securities in the municipal market, but which are not accountable to the electorate” (see also Adams, 2007), effectively insulating municipal finances from popular control.

The second, overlapping line of argument takes the form of the centering of the politics of debt in urban governance. Prominently, Smith & Kirkpatrick (2011) and Peck & Whiteside (2016) have argued that the increasing reliance on the municipal bond market by cash-strapped local actors is remaking the fundamental dynamics of American urban politics: subsuming the traditional growth politics of real estate-dominated governing coalitions under extra-local bondholder value and the discipline of debt (see also Tabb, 2014). While building on the work on municipal market speculation, this provides an approach to urban financialization that rather than highlighting these innovations per se seeks to examine the shifting positionality of cities within the bond market and the effects this has on local politics, positioning cities in relation to the market’s “disciplinary apparatus (bond-rating agencies) and its participants (bondholders)” (Kirkpatrick & Smith, 2011: 482). In this way, it allows us to more thoroughly interrogate financialization as a socio-political transformation in the relation between creditors and debtors, an emphasis advocated by Lazzarato (2012) who contends that the “debt economy” is a more suitable term than the “financialized economy” since the former more fully gets to the heart of

the power relation that dominates contemporary capitalism.

These new debt dynamics have provoked a rethinking of established understandings of American local politics, long being understood with reference to the paradigm of the “urban growth machine.” This concept, first proposed by Molotch (1976) and further elaborated by Logan & Molotch (1987), conceptualizes American urban politics as being dominated by “growth coalitions” of localized fractions of capital, led by real estate developers and supported by local boosters in the media, municipal employees and fractions of unionized labor. These social forces are particularly dependent on localized economic growth, such that their primary interest becomes to “defend or enhance the flow of value through a particular locality,” working through business coalitions to increase the value of the built environment (Cox & Mair, 1988: 310). Local governments play a central role in these coalitions, but they “are by no means neutral instruments simply and instrumentally controlled by business coalitions” (ibid: 311). Rather, they have similarly been dependent on the local property tax-base, a “system of finance [that] compels every local state at least to maintain its revenue base by attracting investments which contribute to the market value of real property” (Fainstein & Fainstein, 1983: 251).

With increasing reliance on speculative debt-financing to provide the infrastructure that is such a crucial precondition for property development, however, these dynamics are steadily shifting because while “[o]riginally employed to reclaim local autonomy, financialization acts as an unforgiving straightjacket in times of stagnation ... [since] with every new bond issued ... the power of the local growth-machine participants is diminished, while the power of extra-local investors is expanding” (Kirkpatrick & Smith, 2011: 492, 496). This puts the debt relation at the heart of local politics as municipal governments are increasingly taking on the role of mediating between bondholders and the growth coalition dependent on debt-financed infrastructure. Under

conditions of increasing municipal debt levels, the urban growth machine is then, according to Peck and Whiteside (2016) being transformed into a machine whose immediate priority is no longer simply to achieve growth, but to manage its debt: a “debt machine.” Thus:

Conventional (critical) wisdom has it that the political economy of urban governance is animated by the pursuit of growth and, internally, by growth-elite dynamics. Increasingly, though, it is debt as much as growth that shapes and drives the system, while the locus of power and control has been shifting from growth coalitions to debt machines and from local business leaders to more distant finance-market interests.

(ibid: 239)

Further, while the “politics of speculation” highlights the entrepreneurial nature of contemporary urban governance (cf. Harvey, 1989; Leitner, 1990) the “politics of debt” speaks to the possible exhaustion of this policy regime in the context of macro-economic stagnation, so that “financialization may be thought of ... as the autumn of the post-Keynesian mode of [entrepreneurial] urban governance.” (Peck & Whiteside, 2016: 239).

Lately, the concept of financialization has, however, come under critique. In particular, Christophers (2015a: 192) has argued that much financialization theory depend on the premise that finance’s increased importance is a historically unique phenomenon, contending that by “[d]eploying a restricted historical optic, and thus overlooking historic parallels and (dis)continuities, ... the financialization thesis generally projects a false sense of newness.” Contemporary processes of financial expansion are thus easily rendered as diversions from the “normal” historical course of capitalist development, despite, in fact, having a wide range of predecessors. Following this argument, overlooking historical parallels in the bond market would

mean that claims to urban financialization are at risk of overstating the relative novelty of the process while it can also easily mistake quantitative change, such as growing indebtedness or the proliferation of increasingly sophisticated financial instruments throughout municipal finance, as structural transformation. This is particularly important considering Sbragia's (1996: 4) argument that cities long have "mobilized private money for public purposes" in a politics of circumvention with deep historical roots. Indeed, as Ward (2017: 2) argues, "in the rush to embrace what is new in the current relationship between cities and finance, we risk forgetting what we already know, which is that there is a much longer history to the repurposing of land and property as a financial asset, over which there is a local ... politics." While not a clean break with the past (cf. Peck & Whiteside, 2016), at a closer look, however, it is clear that the present historical conjuncture has fundamentally restructured the relation between financial markets and American cities.

With regards to municipal market speculation, this is most effectively shown by Kirkpatrick (2016) who draws on Hyman Minsky's "financial instability hypothesis" to analyze the changing character of municipal finance under neoliberalization. This allows him to distinguish between *hedge* cities which, by primarily issuing safe GO-bonds, "enjoy a liability structure in which tax recipients and other reliable revenue streams can comfortably cover debt repayment obligations" from *speculative* cities where "normal operating receipts do not cover their debt obligations" (ibid: 54). The latter are reliant on short-term lending and other financial tricks to manage their debt and are always in danger of turning into failing *Ponzi* units at the slightest souring of market conditions (ibid). As Weber (2010: 260) puts it, "[w]hen cities accept the risks associated with financialized policy instruments, their ability to stay solvent and fund basic government operations ... are potentially compromised." Exploring the spread of ever

more speculative financial instruments (such as Tender Option Bonds and other derivative products for active debt management) throughout American municipal finance, Kirkpatrick (2016: 53) identifies the subprime mortgage crisis as a “Muni Minsky Moment,” where increasing reliance on exotic financing brought back the urban fiscal crisis as “a cyclical crisis born out of the endogenous instability of finance markets.” As such, Kirkpatrick’s (ibid) analysis importantly points towards the need to go beyond the simple expansion of the municipal bond market to establish the financialization of urban politics as a structural transformation (cf. Aalbers, 2015). In Rutland’s (2010: 1167–1168, emphasis in original) words, we have to understand the role of “not only financial capital but *changes* in finance and changes in its relation with non-financial activities.”

While this account renders financialization as a cyclical (rather than secular) trend (cf. Arrighi, 2010), Kirkpatrick’s “speculative cities” are not simply a change in degree from the “hedge cities,” but rather different in kind. It is not just the increasing size of the municipal bond market that has financialized urban governance, it is rather the shifting character of that market from relatively safe investments to more speculative ones. As such, it points towards the need to also examine the moments of market restructuring and regulatory change that have facilitated the process by which Smith & Kirkpatrick (2011: 496) argue that the power of extra-local creditors is strengthened “with every new bond issued.” As a complement to Kirkpatrick’s (2016) account of the increasingly speculative nature of municipal finance I will then in the rest of this chapter examine the repercussions of this throughout the bond market. Throughout this discussion we will see that while Christophers’ (2015a) call for conceptual caution is well taken, American urban politics has indeed been thoroughly restructured along financialized lines as the increasingly speculative nature of the bond market has changed the mindset of investors, the

behavior of issuers and fundamentally shifted “the rules of the fiscal game” (Peck & Whiteside, 2016: 251).

2.4. From “ports in the storm” to Chapter 9 bankruptcy

One of the long defining features of the municipal bond market has been its relative safety and resilience to crises (Fischer, 2013). This goes back the 1870s when the Supreme Court (which had to deal with 100 defaults on municipal railway bonds in 1875-1876 alone) ruled that municipalities generally were not allowed to default on “public purpose” bonds (Sbragia, 1996: 91). With this, the Court established the unique safety of municipal bonds and, paradoxically expanded the market it wished to regulate as investors were assured that “[m]unicipal bonds were special. Local borrowers had unlimited obligation to their lenders, whereas private lenders could limit their own obligation by going into bankruptcy and selling their assets. So municipal bonds began to be viewed as carrying less risk than securities issued by private borrowers” (ibid: 98). The Court effectively (re)made the municipal market into a “financial backwater” and cities as safe havens for risk-averse investors by laying down exceptional rules. While it did not make defaults impossible, rated municipal bonds have historically proven to be much less likely to default than similarly rated corporate bonds. For example, Moody’s (2014: 19) latest “default study” showed that only 80 Moody’s rated municipal bonds (mostly non-GO-bonds) had defaulted between 1970 and 2013, with an annual default rate of merely 0.013%. For municipal bond issuers, this safety meant that they were long exempt from the intensity of investor scrutiny that corporate bond issuers would have to endure to access capital markets (Sbragia, 1986). As safe havens, as “ports in the storm” (cf. Lebenthal, 2009: 4), they were assumed to be low risk without the pressures to have to prove this to their potential bondholders (Sbragia, 1986).

This is, however, no longer the case. As 30 of the 80 defaults identified by Moody's (2014: 1) occurred between 2008 and 2013, market participants have started to question old truths. This is maybe most vividly illustrated by Alexandra Lebenthal (2015: 16–17), the daughter and heir of Jim Lebenthal, who describes the crisis not only as a “game changer” but goes so far as to argue that “[j]ust as the Vietnam War catalyzed a generation to question authority and expose government corruption, the financial crisis prompted this generation to re-examine the structure and function of every corner of the financial markets.” This latest crisis is, however, not unique in this regard. Rather, ever since the 1970s cities have been exposed to intensified scrutiny by ever more skeptical investors. The impact of this on municipal bond issuers has been profound, transforming their operations as they more actively have to demonstrate their creditworthiness.

2.4.1. The urban fiscal crisis of the 1970s

Parallel to the increasingly speculative nature of urban financial innovations, municipal bond investors would throughout the 1970s become more and more concerned with the underlying credit quality of local governments, leading to important changes in market regulation. Before 1975, the municipal market had been largely ignored by federal financial regulators, being exempt from most of the provisos of the Securities Act of 1933 as well as the Securities Exchange Act of 1934 (Fahim, 2012). The Securities and Exchange Commission (SEC) had no authority over municipal bond actors, although it would investigate and enforce cases of fraud (ibid). In the 1970s, however, with the mounting fiscal crises of cities like New York City and Cleveland, buy-side market actors would increasingly come to doubt the previously assumed safety of municipal bonds (ibid). This was despite the fact that neither of the crises actually were

catalyzed by *long-term* debt per se, but rather the immediate products of these cities' inability to roll-over *short-term* debt (Sbragia, 1983). Vulnerability in the short-term market can, however, easily trickle down into the long-term bond market (see Chapter 4 for a discussion of this with regards to the case of Harrison, NJ) and Sbragia (1983: 83) points out that "New York City's inability to meet its debt on short-term loans in 1975 changed profoundly and permanently the psychology of the municipal bond market." This would entail a questioning of the safety of the municipal debt pledge and demands for more transparent disclosure of financial information; culminating in the establishment of the Municipal Securities Rule Making Board (MSRB) by the Securities Exchange Act Amendments of 1975 (Sbragia, 1986).

The MSRB is the market's self-regulatory body whose rules are enforced by the SEC and the Financial Industry Regulatory Authority (FINRA). Significantly, however, neither the MSRB nor the SEC ever received authority to regulate borrowers or issuers of municipal bonds. Indeed with the so-called Tower Amendment of 1975 (which like the tax-exemption was pushed to ensure state sovereignty) the agencies are explicitly forbidden to regulate state and local governments (Doty, 2012). Therefore, according to Mochizuki (2012: 229), the MSRB "has traditionally functioned as a toothless rulemaking body without the powers of either market surveillance or enforcement authority." In the wake of the 1989 default of the Washington Public Power Supply System, however, the MSRB sought to overcome these limitations by devising Rule 15c-12, prohibiting the underwriting of municipal securities without properly prepared "Official Statements" (ibid). As Fischer (2013: 49-50) explains "[a]n official statement is a slice-in-time picture showing the essential elements of the [bond] agreement and the status of the issuer," and by requiring underwriters to obtain these the MSRB would effectively indirectly regulate bond issuers. This authority was further strengthened by rule changes in 1994-1995 that

required the continual disclosure of “material events” that may impair the credit quality of the issuer (Fahim, 2012). Crucially, however, federal regulation of the municipal bond market has primarily been aimed at protecting *investors*, rather than *issuers* (ibid).

The effects of these demands for municipal financial disclosure would be that investors started to shy away from cities which internal financial organization was deemed to not meet their standards (Sbragia, 1986). Together with the federal government’s State and Local Financial Assistance Amendments of 1976, which extended local auditing practices, this profoundly changed the relationship municipal officials had to the bond market. They “had to learn to deal more extensively with the investment community than before... [and] ‘sell’ their cities to a variety of credit analysts at numerous Wall Street breakfasts, lunches and dinners” (ibid: 208). In effect, it exposed cities to increasing bondholder discipline as investors started to think “of cities as ‘financial enterprises’ rather than simply as service providers” and local governments had to restructure their operations accordingly: strengthening the powers of local financial officers and introducing more “managerial” styles of administration (ibid: 209). As the perception of municipal bonds changed from safe havens of capital to more risky investments, this further differentiated what was once considered a rather homogenous market. Now, well-to-do cities would receive preferential treatment while already struggling places would be penalized (Sbragia, 1983). The parallel rise of bond insurance would partly alleviate this trend, but this was only until the outbreak of the 2007-2008 subprime mortgage crisis.

2.4.2. The subprime mortgage crisis

The subprime mortgage crisis had adverse effects on the fiscal health of many American cities. As Martell & Kracchuck (2012: 673) describe it, “through no fault of their own, many municipal

issuers faced increased borrowing costs, less access to capital and a changing landscape that could fundamentally alter the way in which public projects are financed.” Although Alexandra Lebenthal’s (2015) “Vietnam moment” is an exaggeration, of course, market actors have become much more cautious and questioning of old truths, putting governments under increasing analytical scrutiny. Most significantly, this has been caused by the dramatic increase of municipal Chapter 9 bankruptcies, largely unheard of before the crisis, as well as the decline of bond insurance. The post-crisis market restructuring has, however, not only been gloomy for issuers. Rather, both the American Recovery and Reinvestment Act of 2009 (ARR) and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) would somewhat strengthen their position. To start with the latter, Dodd-Frank has changed the make-up and powers of the MSRB, regulated municipal advisors and created a new Office of Municipal Securities within the SEC (Mochizuki, 2012).⁶ The Board has also received greater authority of enforcement so that “[w]hile the previous role of the MSRB was regulating broker-dealers to protect investors, now MSRB also protects state and local issuers, public pension plans and others whose credit stand behind municipal bonds” (ibid: 229). Central to this shifting focus is the regulation of municipal advisors who are now required to register with the SEC and have an explicit fiduciary duty to represent the interests of their municipal clients (ibid).

While these regulatory changes have strengthened the protection of state and local governments in a more socially embedded municipal bond market, Kirkpatrick (2016) argues that this is characterized by a “thin” veil of regulation threatened by continued market speculation. Bond issuers would, however, further benefit from the brief Keynesian-style crisis

⁶ While before the crisis most members of MSRB were representatives of broker-dealers, Dodd-Frank has shifted the balance towards representatives of the public; increasing the board to at least 15 members (in practice 21) with at least 8 who are neither representatives of municipal advisors nor of broker-dealers and at least one representative each from retail-investors, municipal entities, and the public (Mochizuki, 2012: 230).

management of the Obama administration's ARR. Concerned with diminishing liquidity in financial markets in general and the 2008-2009 panic selling of municipal bonds in favor of treasuries in particular, a two-year fiscal stimulus program for the municipal market known as the Build America Bonds (BABs) was initiated in 2009 (Comes et al., 2015). This program allowed state and local governments to issue taxable private activity bonds with a 35% subsidy that could either be used by the issuers themselves or transferred to the borrower, thus allowing issuer to circumvent the liquidity problems in the regular municipal market by attracting investors that previously had been unable or unwilling to take advantage of the tax-exemption (ibid: 173). A shift from traditional reliance on tax-free bonds to a more direct form of federal subsidy, BABs temporarily expanded the taxable municipal market and proved a popular stimulus program with issuers and investors alike (Fischer, 2013). It was not renewed beyond 2010, however. If the BABs helped alleviate some of the market pressures on cities, other post-crisis trends would further intensify these. In particular, the increase in municipal bankruptcy filings and the decline of bond insurance.

Firstly, hard hit by declining property values, the return of the urban fiscal crisis in the wake of the subprime mortgage crisis (see Chapter 1 for an extended discussion) has most significantly been manifested in the increasing filing of Chapter 9 municipal bankruptcies. To avoid the "strategic" use of the bankruptcy code (as opposed to as last resort solution), municipalities need to prove to a judge that they have negotiated in "good faith" with creditors, pensioners and unions in order to be allowed to restructure their obligations (Comes et al., 2015, see also Davidson & Kutz (2015: 1445–1446) for a brief legal primer). The creditors, however, have much less influence on the actual terms of the bankruptcy than they have when it comes to corporations. This because the basic sovereignty and service provision ability of the municipality

is protected. As Justice Felix Frankfurter argued with respect to Asbury Park, NJ in a 1942 Supreme Court ruling, “a city cannot be taken over and operated for the benefit of its creditors” (quoted in Lebenthal, 2009: 3). Local governments are generally, however, reluctant to file for bankruptcy out of fear for the long-term costs. As the Congressional Budget Office (2010: 10) explains:

Because a restructuring plan requires the consent of two-thirds of each class of creditors whose interests would be impaired by the plan, a municipality may emerge from bankruptcy in an only slightly better fiscal position than it had when it entered bankruptcy. If new debt is part of the plan to alleviate a municipal government’s cash flow problems, the government’s obligations may be stretched out over time rather than eliminated. Consequently, the restructuring may constrain government operations for years after the restructuring plan is approved by the court.

Municipal bankruptcy used to be a rare occurrence and the market has seen only 645 municipal bankruptcies filings since 1937 compared to 10-11,000 corporate bankruptcy filings (Comes et al., 2015: 157). The majority of these bankruptcies have been filed by special-purpose governmental units on speculative revenue bonds, while general-purpose governments and their GO-bonds have tended to be more stable as they have more predictable finances (Davidson & Kutz, 2015). Between 2008 and 2015, however, 15 general-purpose local governments petitioned judges to allow them to restructure their obligations (Governing, 2015; Maciag, 2013), causing significant concern among market actors.

It is not simply the increased frequency of municipal bankruptcy filings that has spread concern, however. Rather, the reasons why municipalities seek bankruptcy protection are just as worrisome. This because while bankruptcy primarily used to be sought for protection against

non-debt liabilities like pension and healthcare costs or unfavorable legal judgements, in the aftermath of the crisis large entities like Jefferson County and Detroit have filed to ease their indebtedness as well (Comes et al., 2015). Many post-bankruptcy plans of fiscal adjustment have involved not only service cuts, raised taxes, impaired pensions and revoked collective bargaining agreements, but also bondholder haircuts (see Table 2.2 for a sample of high profile bankruptcies).

This effectively “changed the rules of the game” (ibid: 146) as “[w]hat were once sacred cows are now fair game, enabling cities to threaten creditors with unilateral changes that would, a short time ago, have been unthinkable” (Davidson & Ward, 2014: 95). While still a relatively rare occurrence in the context of the larger market, the effect of these bankruptcies is an increasing skepticism regarding municipal credit quality and (after Detroit’s emergency manager Kevyn Orr’s classification of the city’s GO-bonds as unsecured debt) the safety of the GO-pledge in particular (Wolfe & Chief Investment Officer Team, 2013). While a bankruptcy may represent a temporary break of creditor control over individual municipalities, the effects of these localized cases resonated throughout the national market, paradoxically, exposing other cities to ever greater degrees of bondholder scrutiny. Just as Alexandra Lebenthal (2015: 17) argued, the bankruptcies in the wake of the crisis has pushed investors to “re-examine the structure and function of every corner” of the municipal bond market, becoming skeptical of unsecured credits and those not supported by statutory liens.⁷ Investment advisors consequently recommend their clients to diversify their portfolios and strengthen analysis of the fundamentals underlying credit quality (Wolfe & Chief Investment Officer Team, 2013). This puts increasing pressure on issuers to make sure that they fulfill the criterion of creditworthiness. The spread of municipal

⁷ Interview 13, major bond insurance firm, 23-06-2016.

bankruptcy throughout the market has therefore reinforced the role of financialized rationalities and logics in urban governance at large, despite temporarily relieving some cities of their immediate pressures. This increased scrutiny of issuers, like the reactions to the urban fiscal crisis of the 1970s, would further be intensified by another post-crisis development: the decline of bond insurance.

Bond insurance had been one of the principal innovations arising from the urban fiscal crisis of the 1970s. First introduced in 1971, this insurance is provided by specialized bond insurance firms which for a fee will guarantee repayment of principal and interest if an issuer would be unable to do so (Cirillo, 2008). Effectively taking on the credit rating of the insurer, insured bonds trade at interest rates far below what the underlying credit quality of the issuer would allow them to, lowering borrowing costs by assuring investors of the safety of the bonds (ibid). Overcoming the informational asymmetries present in the fragmented municipal market, bond insurance would become more and more popular up to the 2007-2008 crisis. The share of bonds carrying AAA insured ratings grew from 3% of all bonds issued in 1981 to almost 60% in 2007, giving “rise to commodization and homogenization in the market that drove acceptance by issuers and investors and increase[ed] the ease by which they could access the market as both buyers and sellers” (Comes et al., 2015: 117). Like so many other financial institutions, however, the bond insurers would feel the lure of the structured securities market. From the 1990s they

Local government	Date of bankruptcy filing	Causes and responses
Vallejo, CA	May 2008	Long reliant on speculative redevelopment backed by the city's General Fund, Vallejo was hard hit by declining property values and tax revenues in the wake of the 2007-2008 crisis. Still locked into collective bargaining agreements that automatically increased its employee costs as its budget contracted, however, Vallejo sought bankruptcy protection in May, 2008. This allowed the city to significantly reduce its future pension and retiree health benefit contributions. Initially, the restructuring plan also involved bondholder haircuts, but these were later renegotiated when creditors agreed to lower interests rates as long as they received full repayment of principal (see Davidson & Kutz, 2015)
Central Falls, RI	August 2011	Central Falls' state appointed receiver filed for bankruptcy in August, 2011 to allow the city to restructure a 1972 public pension plan that had left it with outstanding pension liabilities of \$80m. The final restructuring plan spared bondholders, but reduced pensions by 55%. This would set an important legal precedent as it made clear that pensioners were creditors who could be impaired in a Chapter 9 bankruptcy (see Farmer, 2013; Rushe, 2011; Russ, 2012).
Jefferson County, AL	November 2011	After the Environmental Protection Agency (EPA) in 1996 charged Jefferson County for dumping sewage into local rivers, it embarked on large-scale debt-financed improvements to its sewage systems. This was a process riddled with corruption that eventually would lead to 22 bribery and fraud convictions (including a former mayor in prison). As the debt soared, JPMorgan Chase convinced the County to take out interest rate swaps, but with the outbreak of the subprime mortgage crisis these went sour and left the County with ever more debt. For these, the bank would be charged with bribery by the SEC, settling the suit in November 2009 for \$25m in penalties, \$50m to the County and \$647m in foregone termination fees. The underlying debt would, however, remain. To get out under these obligations, County leaders filed for bankruptcy protection in November 2011: securing significant concessions from its bondholders who in October 2013 agreed to reduce their claims by \$1.55 billion matched with increasing sewage fees of 7% over 4 years (see Dickinson, 2011; SEC, 2009; Walsh, 2012; Wirz & Corkery, 2013).
Stockton, CA	June 2012	A combination of speculative redevelopment and rising employee costs left Stockton severely exposed to declining property values in the subprime mortgage crisis, forcing it to reduce its workforce by 25% in 2009 while debt service costs ballooned. Presenting a restructuring plan including sales tax hikes, budget cuts, elimination of retiree's health benefits and bondholder haircuts (but crucially no impairment of pensions), the city filed for bankruptcy protection in July 2012. Despite creditor protests, this plan was approved by a federal bankruptcy judge in October 2014 (see Christie, 2012; Davidson & Ward, 2014; Walsh, 2014; Wollan, 2012).

Local government	Date of bankruptcy filing	Causes and responses
San Bernardino, CA	July 2012	<p>With a General Fund dependent on income from the local Redevelopment Agency (RDA), San Bernardino's finances were hit hard in February 2012 when Californian Governor Jerry Brown closed-down 425 RDAs to balance the state's own budget. Left with a \$22-32 million budget deficit, the city sought bankruptcy protection in July 2012. After five years of intense negotiations, a federal bankruptcy judge finally approved the city's restructuring plan in January 2017: including staff downsizing, the slashing of retiree health benefits and increased employer contributions (although protecting the pensions themselves) and bondholder haircuts. Crucially, the city would save \$45 million by reducing its payments to Pension Obligation bondholders (see Christie, 2017; Davidson & Ward, 2014; Esquivel, 2017).</p>
Detroit, MI	July 2013	<p>Long the very symbol of urban decline, Detroit's structural fiscal stress made it the biggest American city to file for bankruptcy in July 2013, seeking to default on \$18 billion in debt (including portions of the city's Water and Sewage Department's debt, GO debt and unfunded pension and retiree health care obligations). This after failed attempts by the state appointed emergency manager to negotiate with bondholders, unions and pensioners. After more than a year of negotiations (during which several creditors settled, but not after aggressively pursuing the monetization of city assets), the bankruptcy judge approved the city's restructuring plan. This eliminated \$7 billion in long-term obligations with 80% of the reductions stemming from cut backs on retiree health benefits (see Holeywell, 2013; Peck & Whiteside, 2016).</p>

Table 2.2. High profile Chapter 9 municipal bankruptcies, 2008-2013

would increasingly diversify their insurance and investment operations, aggressively exposing themselves to the risks of more sophisticated financial products such as Residential Mortgage-Backed Securities (Martell & Kravchuk, 2012). This would cost them dearly when the credit rating of the AAA-tranches of their insured structured securities started to drop in 2007, forcing them to pay out insurance claims and depleting their reserves (Comes et al., 2015).

This would lead to their own swift downgrades which filtered down to the bonds they had insured, making their entire business model of enhancing municipal ratings defunct. The bond insurers quickly went out of business. By 2009 only 2 of the 7 insurance firms that had operated before the crisis were still standing, insuring a mere 8.7% of new bonds (Martell & Kravchuk, 2012: 671). Like with the bankruptcies, Martel & Kravchuk (2012: 672) point out that the decline of bond insurance would increase investor scrutiny of underlying credit quality, arguing that “[w]idespread use of bond insurance had effectively created a homogenous class of bonds, but the near collapse of the insurance industry has again underscored the heterogeneous nature of issues.” One municipal bond market analyst would describe the fall of bond insurance as:

A huge difference... [because] investors have to do a lot more work to figure out 'what am I buying here? I used to just buy the AAA insured bond, now I'm buying something I have to think about to figure out'... I would get phone calls from people saying 'I can't manage, we have 60 or 1000 or 200, 300 names in the portfolios and it's impossible to look at everyone'. So, to some extent *they shrank down and are only looking at the biggest, most liquid names* in the business.⁸

⁸ Interview 2, municipal bond market analyst working for a major bank, 16-05-2016.

While municipalities briefly benefitted from the federal government's fiscal stimulus policies, receiving greater protection from MSRB, two of the most significant post-crisis changes in the municipal market have that cities operate in a more differentiated credit market where they are put under greater scrutiny from investors and credit rating agencies alike. The long-term effects of these changes are still unfolding, but they have made it clear that municipal bonds are no longer the safe and boring "financial backwater" it used to be. Rather, the market has become an tumultuous place where investors are more exposed to the risks, but also the rewards, of financial speculation (cf. Nguyen, 2012) and where bond issuers need to police themselves so as to ensure that they are accepted as worthy debtors in an increasingly differentiated market. Urban governance has become financialized, not simply by the growth of the municipal bond market, but by its changing character.

2.5. Conclusion

In this chapter I have provided an overview of the municipal bond market and its historical evolution. Scholars invoking the financialization of urban governance with reference to municipal bonds principally refer to two interrelated processes: (i) the spread of speculative financial innovations in local governments making municipal finance an increasingly unaccountable and risky business and (ii) the centrality of debtor discipline as the driver of urban governance. In this overview of the municipal bond market I have primarily engaged with the latter of these claims by examining the historical evolution of creditor scrutiny of cities and their administrations. In light of this development, Christophers' (2015a) call for conceptual caution is well taken, but by no means nullify the claim that American urban governance has become financialized. Yes, the municipal bond market has been around since the 1800s, but the character

of that market and the positionality of cities within it has indeed transformed. The explosive growth of the value of outstanding municipal bonds since the 1980s (see Figure 2.1) is just an initial indicator of this. More importantly, while cities used to fund basic infrastructure by issuing straight forward GO-bonds, the successive neoliberalization of inter-governmental relations has pushed them into more and more speculative bets on their ability to spur future economic growth by taking out loans that are not covered by current revenue streams (Kirkpatrick, 2016; see the case study of Harrison, NJ in Chapter 4 for an illustrative example of this). Thus, the notion that municipal bonds provide “ports in the storm” for risk-adverse investors (Lebenthal, 2009: 4) has increasingly become defunct.

This has fundamentally changed the behaviors of the actors in the market, both that of investors who have become more skeptical as to the safety of bonds and that of urban administrators who more actively have to demonstrate that they are worthy debtors. From being a minor concern in the strategies of the “growth machine,” the politics of debt now occupy the center of urban politics. In a pioneering paper, Leyshon & Thrift (2007) argued that in contrast with the more established “social studies of finance” with its internal focus on financial markets and their complexities, the financialization literature crucially deals with the penetration of finance into more and more societal realms. Similarly, we can see how a politics of “creditworthiness” has developed not simply from the growth of the municipal bond market nor from internal innovations in markets, but from key investor responses to market and extra-market crises that have repositioned cities in relation to that market. This puts cities under increasing analytical scrutiny and required them to more actively prove that they are worthy debtors. The logics of finance have infiltrated local government. The case of the municipal bond market then shows that while we indeed might want to be cautious about claims to novelty, Christophers’

(2015a) call for abandoning the concept of financialization completely appears somewhat premature. Rather, financialization becomes a largely empirical question, one which relative novelty needs to be shown rather than simply being assumed.

The financialization of urban governance is not a straightforward process, however. Rather, just like the imposition of debt limits after the late 1800s sparked the “politics of circumvention” (Sbragia, 1996), the politics of creditworthiness has been characterized by attempts by cities to circumvent investors’ scrutiny of their “underlying” credit quality. That is, the bond market as well as state and local financial administrators have developed various accounting techniques and programs for improving the credit of struggling cities without necessarily changing the basic socio-economic conditions of the locality. One such example was the rise of bond insurance from the 1970s, where investors and issuers together ensured that the debt of fiscally strained cities could trade independently of underlying budgetary conditions. Another was the development of state credit enhancement programs, as discussed in Chapter 4. Both these examples, however, show how such financial tricks of circumvention are increasingly exhausting themselves: bond insurance becoming marginalized as the subprime mortgage crisis brought down the firms supplying the service and credit enhancement seeing diminishing returns as the fiscal crisis of the states trickle down through the programs. As such, financial pressures are further trickling down into urban governance.

This process is one that requires careful analysis of the institutional mechanisms that produce and sustain municipal debtor discipline. Rather than the spread of TIFs or other market innovations highlighting the urban politics of speculation, I will then in the rest of this thesis focus on the politics of debt. This because, as Lazzarato (2012: 24) argues, “reducing finance to its speculative function neglects its political role as representative of ‘social capital’ (Marx),

which industrial capitalists will not and cannot concede, as well as its function as ‘collective capitalist’ (Lenin), which, through governmental practices, bears on society as a whole.” Centering the politics of debt therefore also centers the crucial power relation that underpins today’s financialized condition. In the next two chapters I will examine the most important market institutions to which cities need to demonstrate their creditworthiness, the credit rating agencies. These organizations act as proxies for the bond market as a whole. They are the principal agents of investor scrutiny and debtor discipline. The power of credit rating is, however, not limited to bridging informational asymmetries nor does it simply descend upon cities from above. In Chapter 4, I will examine the co-construction of creditworthiness in the interactions between rating agencies, local financial professionals and state oversight bodies. Next chapter will, however, first take the readers inside the “machinery” of the rating process. Here I will examine its crucial role of holding the bond market together, not just facilitating investment decisions by providing information about concrete credit risks, but crucially making the uncertainties of local fiscal relations commensurable, to enable their exchange as risk-bearing financial securities.

Chapter 3: Searching for commensurability: Municipal bond rating and the commodity abstraction

3.1 Introduction

On December 21, 2011, the credit rating agency Moody's confirmed that the creditworthiness of the outstanding General Obligation bonds of the City of Camden, New Jersey was rated Ba2 (Moody's, 2011). Nearly five years later, on September 5, 2016, Orkuveita Reykjavíkur, a municipal energy and utilities company in Iceland on the other side of the Atlantic Ocean, was upgraded to a similar Ba2 rating (Moody's, 2016b) while in August 16 the same year ArcelorMittal, one the world's largest steel producers, received the exact same rating (Moody's, 2016a), two notches below what is generally considered to be a safe investment grade. A city struggling under years of white flight and deindustrialization, a municipal energy company finally benefitting from the post-recession recovery of the Icelandic economy, and a private manufacturing corporation faced with declining demand from the Brazilian market and increased competition from Asia. Three different entities, facing different challenges and operating under different conditions, all reduced to the same Ba2-symbol. A symbol representing their status as "junk" in the global financial market. A symbol that managers will agonize over when going into debt negotiations and investors will pour over when determining if they should buy or sell. A symbol standing in for everything that make these entities real and distinguishable, reducing their contingent social relations to an abstract combination of letters and numbers. A symbol comparing the seemingly incommensurable.

In *Intellectual and Manual Labour*, Sohn-Rethel (1978: 19) writes that "the form of commodity is abstract and abstractness governs its whole orbit." Drawing on the first chapter of

Marx's *Capital Vol. 1*, what he alludes to is how for a heterogeneous set of objects to become exchangeable commodities in the market place, the exchange process must abstract away from the unique properties of each object to ensure commensurability between apples and oranges. This because, as Marx (1990: 127-128) writes, "the exchange values of commodities must be reduced to a common element, of which they represent a greater or lesser quantity" so that "[a]s use-values, commodities differ above all in quality, while as exchange values they can only differ in quantity, and therefore do not contain an atom of use-value." For Marx, the common element necessary for this process of transforming qualitative particularities into quantitative relations is human labor as it is only this labor that all commodities have in common. It is, however, not in the embodied concrete labor of specific tasks that makes it possible to exchange the one for the other, rather it is "human labour in the abstract" (ibid: 128) a labor reduced to its "socially necessary labour time" (ibid: 129) where one commodity can be directly compared to another by comparing the hours that goes into their production regardless of the qualitatively different natures of that labor. As such, the commodities assume a dual character, "only appear[ing] as commodities ... in so far as they possess a double form; i.e. natural form and value form" (ibid: 138).

Capitalist society, whose economy (as Marx (ibid: 125) opens his investigation with) is dominated by "an immense collection of commodities," is therefore a society crucially subject to the processes of abstraction and commensuration out of which commodities and value appear. While this fundamental commodity abstraction, Sohn-Rethel (1978: 20) argues, only exists in the minds of people it does not simply arise out of their consciousness, but from the actions of exchange themselves. Thus, "[w]hile the concepts of natural science are thought abstractions, the economic concept of value is a real one. It exists nowhere other than in the human mind but it

does not spring from it. Rather it is purely social in character, arising in the spatio-temporal sphere of human interactions” (ibid). As pointed out by Espeland & Stevens (1998: 315), however, the generalized social commensuration processes, the “expression or measurement of characteristics normally represented by different units according to a common metric,” that permeates society also beyond the sphere of the commodity “requires enormous organization and discipline that has become largely invisible to us.” Rather than an simple property of the commodity, in the words Bigger & Robertson (2017: 71), “value is found, affirmed, realized, or destroyed through ongoing social performances of comparison and measure.” The work of commensuration in the market place, the “social synthesis” that keeps commodity-producing societies together by unifying the individualized acts of production and consumption (cf. Sohn-Rethel, 1978), must therefore be examined not as an unconscious result of simple exchange relations but by unpacking the enormous organizational efforts that go into the creation of commensurable entities through processes of abstraction.

In this chapter I will examine one such effort, one that has become fundamental for the circulation of cities as commodities under financialized capitalism. This abstraction, and consequential commensuration, is the one produced by credit rating agencies in their assessment of the creditworthiness of municipal bonds. These agencies are private corporations assessing the creditworthiness of financial securities on a scale from AAA to C/D (see Table 3.1). The sector is dominated by the “big three” agencies of Standard & Poor’s (S&P), Moody’s and Fitch who in 2015 together accounted 87% of all credit analysts employed in Nationally Recognized Statistical Rating Organizations (NRSRO) while being responsible for 96.5% of all outstanding ratings (SEC, 2016: 11, 16). As an elusive process establishing the background fiscal conditions for urban governance, municipal bond rating has to date primarily been examined with regards to

Moody's	Standard & Poor's	Fitch
<i>Prime</i>	<i>Prime</i>	<i>Prime</i>
Aaa	AAA	AAA
Aa1	AA+	AA+
Aa2	AA	AA
Aa3	AA-	AA-
A1	A+	A+
A2	A	A
A3	A-	A-
Baa1	BBB+	BBB+
Baa2	BBB	BBB
Baa3	BBB-	BBB-
<i>Speculative</i>	<i>Speculative</i>	<i>Speculative</i>
Ba1	BB+	BB+
Ba2	BB	BB-
Ba3	BB-	B+
B1	B+	B
B2	B	B-
B3	B-	CCC
Caa1	CCC+	CC
Caa2	CCC	C
Caa3	CCC-	RD/D
Ca	CC	/
C	C	/
/	D	/

Table 3.1. The rating scale (adapted from: Fitch, 2017; Moody's, 2017; S&P, 2016)

the effects of their rating judgements on heavily indebted municipalities (see Chapter 4). The internal “machinery” of the municipal bond rating process has, however, been relatively overlooked. Given the more high-profile role that credit rating has played in, for example, the melt down of the asset-backed securities sector in the 2007-2008 crisis, it might for some seem surprising to put the *municipal* rating process at the center of attention. Government securities, however, account for the large majority of outstanding ratings⁹ and while there are some good studies that get inside the sovereign rating process (e.g. Paudyn, 2014), the municipal sector,

⁹ 77.9 % of all outstanding NRSRO ratings are for government securities as compared to 8.3 % for asset-backed securities, 7.5 % for financial institutions, 5.3 % for corporations and 0.9 % for insurance companies (Securities and Exchange Commission, 2016: 10-12).

long viewed as a financial backwater, has been relatively neglected.

Therefore, by investigating the criteria, processes and organizational practices of municipal bond rating, this chapter opens up the “black box” of the rating process (cf. MacKenzie, 2005). Firstly, I will introduce the agencies themselves. Here I will examine two competing approaches to their significance, one emphasizing the role of rating agencies in overcoming (spatial) barriers to knowledge in expansionary moments of capitalist development and the other which argues that their institutional significance instead can be found in the “regulatory license” they have received from the federal state. In the post-crisis period, however, both these explanations appear limited. Secondly, I will therefore present an alternative explanation, one that focus on the role of credit rating in overcoming barriers to commensuration. Here, I will draw on recent attempts to rethink the relationship between value and finance, engaging arguments that under current historical conditions of financialized expansion, it is abstracted risk, not just labor, that constitutes a central feature of value as a generalized social relation of “equivalence and substitutability” (c.f. Mann, 2010: 177). How this is achieved will be the examined in the third section where I will unpack the methodologies and processes that support the rating analysts in transforming contingent, localized fiscal uncertainties into a commensurable rating symbol. Thereafter, I will focus on two moments in the last decade where the limits of this commensuration become particularly visible: the push towards rating transparency and standardization after the 2007-2008 subprime mortgage crisis and attempts by the agencies to “recalibrate” their rating scales to ensure commensurability across public and corporate finance. The conclusion will thereafter sum up the argument, interrogating the socio-political consequences of the abstraction and commodification of local fiscal relations.

3.2 Logics of credit rating: from knowledge production to “regulatory license”

The mainstream view of the agencies is that they are simply a natural outgrowth of a market always striving towards efficiency. Kruck (2014: 27), for example, argues that “the basic function [credit rating] perform in the global political economy is to lower inefficient transaction-costs and to reduce informational asymmetries between borrowers and lenders.” Similarly, Alcubilla & Del Pozo (2012), two rating agency experts with long experience in the Spanish Securities and Exchange Commission, cite a Bank of England report from 2007 arguing that the rating agencies (i) help mitigate information asymmetry between issuers and investors, (ii) help solve “principal-agent” problems by allowing principals (i.e. investors) to steer the agent acting on their behalf (e.g. pension or mutual fund managers) towards less risky investments by steering them towards certain minimum ratings, and (iii) help solve collective action problems where credit downgrades can signal to dispersed investors to take action.

Following this, Sylla (2002) has explained the specific American origins of credit rating by looking to the sheer continental scale of the American economy. Throughout the 1800s, this economy was in dire need of railroad investments that could connect distant parts of the country with each other. As the railroad companies from the 1850s and onwards pushed beyond already settled lands to spread the colonial economy to the interior they faced increasing problems of financing. Previously they had been able to rely on bank loans and the selling of stocks, but as the geographical barriers between creditors and debtors increased such financing system based on local and state banks’ lending to people with prior personal connections became a limitation. In Sylla’s (ibid: 23) words this barrier was, however, not limited to the debt market, but a generalized condition in an expanding capitalism were “[a]s the scale and geographical scope of transactions expanded in a large economy in which resources, human and other, were mobile, the

need for information on suppliers and customers of whom a businessperson had no personal knowledge increased.” The first rating agencies *Standard & Poor’s* (“S&P”) and *Moody’s Investors Services* (“Moody’s”) would be two of the institutions developing out of attempts to respond to this imperative, starting to rate municipalities in late 1920s and 1919 respectively (Poon, 2012: 11).

Sylla’s (2002) history illustrates how the rating agencies developed out of the pressures “time-space compression” (Harvey, 1989) put on the American financial market. In *The Condition of Postmodernity*, Harvey (1989: 228) argues that the development of capitalist production has been driven by an inescapable logic to reduce the turn-over time of capital and to speed up its movement across space so that “[i]nnovations dedicated to the removal of spatial barriers ... have been of immense significance in the history of capitalism, turning history into a very geographical affair” (ibid: 232). Investments in infrastructures for movement and interconnectivity, such as railroad, airports and telecommunication networks, to achieve an increasingly “shrinking” world consequently have deep roots in capitalism. The rating agencies entered the historical stage as yet another infrastructure to produce and manage this “time-space compression.” By emerging alongside the expansion of the railroad system, credit rating developed to manage the increased stretching of (financial) social relations across a vast infrastructural network, but was also an infrastructure of time-space compression in its own right, “shrinking” the world of the debt market. Moving from 19th century western expansion to today, a similar (although much more critical) approach to the geographical role of the agencies has been developed in several contributions by Sinclair (1994, 2000, 2005). He is particularly interested in the dramatic expansion of the credit rating business in the context of globalization and financial market “disintermediation,” where the judgment of which securities are safe to

Year	
1869	Henry V. Poor's published his first <i>Manual of the Railroads of the United States</i> , allowing subscribers to gain insights into the finances of the country's major railway companies (issuing their first rating 1916).
1900	John Moody & Company publishes its first <i>Manual of Industrial Statistics</i> .
1906	Standard Statistics Bureau is founded by James L. L. Blake (incorporated as Standard Statistics Company in 1914 and issuing their first rating 1922).
1908	John Moody leaves John Moody & Company.
1909	John Moody & Company issues the very first credit rating.
1919	Poor's Publishing Company is founded out of the merger between John Moody & Company and Poor's Railroad Manual Company.
1913	Moody's Investment Service is formed by John Moody (incorporated 1914).
1914	Fitch Publishing Company is formed (issues its first rating 1924).
1931	Credit ratings make their first appearance in the Federal Government's 'safety and soundness'-regulation when banks are required daily record the price/value of lower rated bonds ("mark-to-market").
1941	Standard & Poor's Corporation is formed by the merger of Standard Statistics Company and Poor's Publishing Company.
1975	The SEC designates Nationally Recognized Statistical Rating Organizations (NRSRO).
2010	Dodd-Frank mandates federal agencies to remove all references to ratings in their regulation and establishes the Office for Credit Ratings within the SEC.
	Moody's and Fitch "recalibrate" municipal ratings to their corporate rating scale.
2012	S&P adopts new municipal rating criteria to make them comparable with their corporate rating scale.
2015	Credit rating agencies are mandated to move towards "default-based" ratings.

Table 3.2. Timeline of significant moments in the development of credit rating (Partony, 2002; Sinclair, 2005; White, 2002)

invest in have been taken out of the hands of banks.

These "less socially embedded capital markets" call for some other infrastructure of credit intelligence and "ratings increasingly become the norm as capital markets have displaced bank lending and as the trust implicit in these older systems have broken down" (Sinclair, 2005: 5, see also Kruck, 2011). Under these conditions, rating agencies as "embedded knowledge networks"

assume the role of legitimate organizers of financial knowledge by market participants that are constantly being overwhelmed with all sorts of data regarding investment risks and market development (Sinclair, 2005: 15). These networks are embedded by virtue of being seen as endogenous to the financial system. They therefore receive their legitimacy largely from the market actors themselves for their service to that market so that “rating agencies have to be considered important financial market actors because market participants and policy makers act as if they are important” (Sinclair, 2010: 92). This is an understanding of the credit rating agencies as knowledge producers and market coordinators where one crucial logic of credit rating has been to overcome spatial barriers to knowledge, regardless if these present themselves in the early 20th century American railroad system or have expanded to a global scale. By providing distant creditors with knowledge on localized investment risk the agencies play the key role of bridging space. The status and quality of this knowledge has, however, become hotly contested in recent years, posing the question of whether knowledge production *per se* really is the central role of the agencies.

One commentator challenging this view is Partnoy (2002: 65) who argues that:

Credit rating poses an interesting paradox. On one hand, credit ratings are enormously valuable and important. Rating agencies have great influence and even greater market capitalization. Credit rating changes are major news; rating agencies play a major role in every sector of the fixed income market... On the other hand, there is overwhelming evidence that credit ratings are of scant informational value.

This paradox is unavoidable when one talks to representatives of the “buy-side” of the municipal bond market. Deeply discredited for their involvement in the meltdown of the sub-prime mortgage market in 2007-2008 (SEC, 2008; Sinclair, 2010; White, 2009) they were humiliated

most recently in the 2015 Wall Street movie *The Big Short*, where the self-righteous protagonist pressures one of their representatives (partially blinded after an eye surgery) about how they could rate collateral debt obligations (CDOs) that were clearly of junk status so highly, even giving them AAA-ratings. Pushed into a corner, the S&P employee admits that they had no other choice because they rely on issuer fees for their profits and “if we don’t give them the ratings they go to Moody’s, right down the block!” Many buy-side practitioners deeply distrust the actual research that goes into the credit ratings, referring to the agencies as too slow to change ratings,¹⁰ too dependent on issuer-fees,¹¹ and in generally ill-suited for the “forward looking work of investing.”¹² As one recently retired independent municipal credit researcher with over 25 years of experience on the buy-side argued: “the ratings are not even instructive future indicators anymore ... their criteria are all over the place, the ratings are more divergent than then ever, they are less useful than ever.”¹³ This poses a crucial question: why do credit ratings agencies matter in a market where investors actually distrust their judgements?

Partony (2002: 66) ascribes this to the “regulatory license” the agencies have received from the federal state, arguing that “put simply, credit ratings are important because regulators say they are. Credit ratings are valuable as keys to unlock the benefits (or avoid the costs) of various regulatory schemes.” Rather than the dominant “reputation-based view,” he argues that while the reputation of the agencies to provide accurate assessment of risk might have been important in an early era with relatively marginal agencies in a competitive market, as the credit-rating business has expanded and the agencies become more influential the informational value of the ratings

¹⁰ Interview 13, 15-06-2016, former credit rating analyst now working in a major bank.

¹¹ Interview 21, 19-07-2016, former credit rating analyst now working in a major bank.

¹² Interview 18, 05-07-2016, former credit rating analyst now working in a major bank.

¹³ Interview 22, 19-07-2016, retired municipal market research consultant.

have, paradoxically, declined. Explaining this involve two regulatory moves. Since 1931, bond rating has been part of the “safety-and-soundness” regulation that aims to limit the riskiness of bank assets by either prohibiting the holding of too low rated securities or gear capital requirements in accordance to ratings (Partony, 2002; see also White, 2002). This, however, posed a problem: if ratings were to guide financial regulation, whose ratings would be considered legitimate? Responding to this question, the Securities and Exchange Commission (SEC) decided in 1975 to give a few agencies the designation Nationally Recognized Statistical Ratings Organization (NRSRO). Limiting new entries into the business and requiring financial institutions to rely on ratings, these regulations effectively gave the “big three” rating agencies of S&P, Moody’s and Fitch’s “a product to sell regardless of whether they maintain credibility with the investor community” (Partnoy, 2002: 78), leading to what White (2002) argues to be abnormally high profits. Moody’s net income/total assets-ratio during 1995-2000 was, for example, on average 42.1% (ibid, 49).

The growth of the rating agencies since the 1930s despite their limited ability to provide valuable information is in this view explained by the preferential treatment they have received by regulators. Since the subprime mortgage crisis, however, the regulatory conditions under which they operate have dramatically changed. Later in this chapter I will discuss how this has changed the rating process itself, but sufficient to note here is that, due to the widespread concerns with investors overreliance on credit rating, the *Dodd-Frank Wall Street Reform and Consumer Protection Act* of 2010 (“Dodd-Frank”) effectively initiated all federal agencies to remove references to reliance on ratings in their regulations (Dodd-Frank, 2010). The SEC thus removed ratings from its rules so that while investors may still rely on ratings there is no longer an explicit requirement that they do so. This, Kruck (2011: 159-160, emphasis in original) argues:

Entails a significant shift in terms of formal attribution of responsibility and an attempt to prod investors to conduct more credit analysis on their own. Since financial market actors are no longer *obliged* to rely on credit ratings to the same extent as before the crisis, responsibility for incorrect assessment of investment quality can formally be attributed more clearly to investors, rather than the credit rating agencies, whose legal liability is limited, or even to the SEC, which sanctioned the use of ratings but failed to clearly define responsibilities for grave failures in risk assessment.

The regulatory license that had been provided to the agencies was effectively removed and we need to search for other reasons to explain their persistent importance in the municipal bond market. This will be done in next section.

3.3 Machineries of commensuration: rethinking value in financial time

Finance is composed of processes that make debt valuable.
(Poon & Wosnitzer, 2012: 253).

When buy-side professionals are prompted on why credit rating still matters despite their own devastating critique of the agencies, they usually answer by referring to its role for pricing. While their traditional influence as knowledge producers in the retail-investor dominated municipal bond market (cf. SEC, 2012a) might still be higher relative to other markets, even for institutional investors credit ratings are important because they are still “the number one determinant of relative price.”¹⁴ In this sense, the rating agencies are not so much supplying an

¹⁴ Interview 21, 19-07-2016, former credit rating analyst now working in a major bank.

“accurate” assessment of default risk, but by providing a credit rating that can stand as a benchmark for all market participants these institutions “play a crucial role in constructing markets in a context of less than perfect information and considerable uncertainty about the future” (Sinclair, 2005: 15). The rating outputs become important because although the analysts might think that an A- rating really is an BBB one, the market will not price it as such.¹⁵ The role of the active institutional investor becomes to try to “outperform [those] benchmarks by avoiding securities that might be overrated and invest in underrated”¹⁶ and in that way acquire relative secure bonds for a lower price.¹⁷

So, while the individual rating may still matter for retail investors and still plays a host of other roles in the market,¹⁸ they have relative little value on their own. Investors increasingly distrust the quality of the research that goes into rating judgments and are encouraged to do so by the SEC. Instead, it is the relative standing of one credit’s rating vis-à-vis all other credits that matters. Indeed, “[i]nherent in the definition of ratings as indicators of *relative* credit risk is the notion that they are an ordinal measure of risk, but not necessarily a cardinal one” (Kruck, 2011: 20, emphasis in original). The individual rating means nothing, while the rating scale is

¹⁵ Interview 22, 19-07-2016, retired municipal research consultant.

¹⁶ Interview 18, 05-07-2016, former credit rating analyst now working in a major bank.

¹⁷ As explained by one former credit rating analyst now working in a major bank: “if you own a bond and the credit rating changes it's going to impact the value.... So you care, [but] a lot of times [investors] care more about what they think the rating agencies are going to do than they actually care about what the rating agencies say. Meaning, I'm not going to buy because the rating agencies says it's AA, I'm going to buy it because I think it's AA. But I think the rating agency is close to downgrading it [and] I'm only going to buy it to a price that reflects the effects of what I think that downgrading is going to be. I'm not going to pay more than I think it's worth.’ And so a lot of my overall evaluation as institutional investor is to think about are other ratings likely to be stable or are they in flux in some way and how is that going to affect the pricing of bonds, because [the rating] is kind of out there as the one publically shared credit information” (Interview 13, 15-06-2016).

¹⁸ For example, the independent assessment that credit ratings ensure liquidity in the secondary market while many structured financial products have rating triggers and requirements written into the contracts (Carruthers, 2013; Poon, 2012).

everything. It is the infrastructure that enables bonds to be priced in relation to each other.¹⁹

Beyond knowledge production and “regulatory license,” a third approach to explaining the persistence of credit rating can look to recent developments in *value theory* for inspiration. It is value that ties the “immense collection of commodities” together by equalizing qualitatively different use-values as bearers of different quantities of abstract labor (Marx, 1990: 125), but traditionally thinkers drawing on Marx’s *labor* theory of value have been reluctant to treat financial instruments (like municipal bonds) as bearers of value. Disaggregating capitalism into a sphere of production and a sphere of circulation, the argument goes that while value is produced in the former it is merely realized in the latter. It is only labor that produce value while financial instruments have instead been defined as “fictitious capital,” only containing a future claim to value not value itself (c.f. Harvey, 1982). Under present day financialized conditions this orthodoxy is, however, increasingly being questioned. Bryan et al (2015: 308), for example, argue that “if theories of value cannot incorporate finance in a central role they are disengaged from the frontiers of capital accumulation” while Marazzi (2010: 48) contends that “financialization is not an unproductive/parasitic deviation of growing quotas of surplus-value and collective saving, but rather the form of capital accumulation symmetrical with new processes of value production.” For Mann (2009: 122), then, “[financial] securities, as values, are as real as any value is.”

Defining value as “a form of social wealth constituted by a spatially and temporally generalizing social relation of equivalence and substitutability,” Mann (2010: 177, 175-176)

¹⁹ Take one former senior analyst’s reflection: “we are lucky in [the municipal bond market] because we have so few defaults, so how do you know if you’re wrong? ... You are really calibrating to a very narrow infrequent event which is default ... so all the difference, all those fine gradations and trying to rate a credit make a difference, but at the end of the day they make a difference in terms of relative value, because otherwise you would say that everything is pretty much in AA and AAA because it doesn’t default” (Interview 10, 06-06-2016).

draws on Postone (1993) to argue that:

An historicised notion of value that recognises capitalism's own dynamism must re-examine value theory's attachment to its 'labour' predicate, to recognise that the historical specificity of value is not only to capitalism in all its forms, but to each capitalism. To see value as historically determined is also to understand that – while value remains 'value', the organizing principle of capitalism – as capitalism changes, so too will the way in which value operates.

So, while Marx's emphasis on abstract labor as the essence of value might have held true under the conditions of industrial capitalism when he theorized it, Mann (ibid) argues that under contemporary financialized conditions value has escaped these circumscribed bounds. Rather than distinguishing "real" from "fictitious" value, or for that matter trying to dig into the labor process of the financial sector to figure out if investment bankers and financial advisors constructing financial instruments are undertaking value-producing labor, he therefore argues for abandoning attachments to "labor" and refocus attention on the generalized processes of "equivalence and substitutability" that characterizes all capitalist commodity production, that of physical commodities as well as financial instruments.

While Marx's commodities are commensurable bearers of value by virtue of all being products of labor, investment risk is the only thing financial instruments have in common. As de Goede (2004) has shown, the concept of risk as "naturally" occurring but rationally calculable emerged to demarcate modern financial speculation from simple gambling as the more legitimate strategy of generating profits on the basis of future uncertainties. As such, risk still sits at the very center of finance. It constitutes "the pivotal locus of value and profit opportunities" (Christophers, 2015b: 6). Christophers (2016: 7) hence argues for the need to attend to how

financial risk, just as with “abstract labor,” becomes abstracted from its concrete specificities, pointing to how while “[t]he future uncertainty priced as risk by financial instruments comes ... in myriad shapes and forms ... [its commodification] is only possible if such uniqueness is successfully abstracted from to produce commensurability.” By unpacking the socio-technical systems of catastrophe risk modelling, Johnson (2013) has in this vein, for example, investigated how a wide range of heterogeneous natural uncertainties, from hurricanes and earthquakes to pandemics, are packaged into the unified and commensurable risk-bearing commodity of the catastrophe bond. This is a process that effectively brings financial risk into being and Marazzi’s (2010) critique of notions of finance as an unproductive parasite on the “real” production process becomes useful for understanding this commodification.

Arguing that value production has “externalized” beyond the factory gates onto the “immaterial labour” process of the entire lived experience, Marazzi (ibid: 48) contends that we have seen “a transformation of valorization processes that witness the extraction of value no longer circumscribed to the place dedicated to production of goods and services, but that extends beyond factory gates so to speak, in the sense that it enters directly into the sphere of *circulation* of capital ... extending the process of value extraction to the sphere of reproduction and distribution.” Web-based capitalists such as Facebook and Google, who extract value from the everyday activity of their users, are the most obvious examples of this process. But it also enables us to understand how financialization has been complementary, rather than antagonistic, to a transformed process of accumulation that “no longer consists, as in the Fordist period, of investment in constant and variable capital ..., but rather of investment in *apparatuses* of producing and capturing value produced outside directly productive processes” (ibid: 54, emphasis in original).

With regards to risk, we can in this way see that while the uncertainties attached to investing in a financial instrument are produced through the entire lived experience of, for example, inhabiting a city, for these uncertainties to be commodified as risk in the form of a municipal bond their “myriad shapes and forms” needs to be abstracted from. Read through the lens of a financialized value theory, municipal bonds, just as physical commodities, can therefore be understood as having a “double form” of both possessing a set of qualitative fiscal uncertainties (“natural form”) while simultaneously being the bearer of a certain quantitative of risk as measured in the incremental steps of the rating scale (“value form”). The rating process can be understood as fundamentally trying to grapple with this “double form,” pivoting around a key tension between on the one hand understanding the concrete uncertainties associated with investment in place while on the other being able to compare investment risk across space. This process circulates around a need to transform the unique sums of place-specific economic histories, local political contestations and municipal financial practices into a measure of “abstract risk.” This is a term used by LiPuma & Lee (2004: 23) to describe how risk under financialized capitalism has “become abstracted from the relatively concrete uniqueness of uncertainties.” In a capitalism dominated by processes of circulation, this “abstract risk” is increasingly assuming the role of social mediation played by “abstract labour” in Marx’s production process (ibid). It has become central in the contemporary “generalizing social relation of equivalence and substitutability” that makes up the value relation (Mann, 2010: 177).

LiPuma & Lee (ibid: 30) are particularly making their argument with regards to financial derivatives, a financial instrument they see as abstract “not only in the conventional sense of being removed from immediate ordinary reality (such as the risk of nuclear war or air pollution) but in the historically specific sense of objectifying different, globally distinct, and

incommensurable social relations as a single priced thing” (see also Sotiropoulos, Milios, & Lapatsioras, 2013). The notion of abstracted risk is, however, useful for understanding credit rating as well. As such, value production in the form of a generation of fiscal uncertainties that can be exploited by the financial community is “externalized,” but its extraction by the financial sector requires the construction of “apparatuses” of risk assessment (cf. Marazzi, 2010). This because “specific phenomena are not inherently fungible as abstract risk; rather, they are *made to be so*” (Johnson, 2013: 32, emphasis in original). Distinguishing the relative “simple” existence of value as “the quality of being measurable and comparable with other things” from the “complex” processes of valuation here becomes helpful (Bigger & Robertson, 2017: 68). The uncertainties of local fiscal relations are not intrinsically valuable. Rather, “abstract risk” is “found, affirmed, realized” (ibid: 71) when “by condensing the highly complex contingencies of credit risk into a single measure, rating agencies contribute to transforming uncertainty into calculable risk” (Kerwer, 2002: 43).²⁰ These rating agencies, while not directly responsible for producing the uncertainties that the financial community exploits, are central to their commodification as value, entering the scene as “calculative devices of risk” (Langley, 2008: 469; see also Poon, 2007) so as to “authorize the commensurability of different regimes of contingency within the domain of financial exchange” (cf. Johnson, 2013: 31).

In addition to bridging barriers to knowledge, so pertinent during the expansion of the American railroad or in the disintermediated financial market of today, credit rating therefore fundamentally helps to overcome barriers to commensuration. They are tools that enable the very exchange of financial commodities, because “[o]nce commensurated in a single rating scale, borrowers bec[ome] comparable; they c[an] be ordered (from most to least creditworthy),

²⁰ Robertson’s (2012) account of the abstractions necessary in commodifying eco-systems services provides a useful parallel here.

categorized, labeled and counted” (Carruthers, 2013: 527). Above all, however, they can be exchanged. This because without a common metric there would be no way for the market as a whole (rather than its individual actors) to judge whether the bonds of Paterson, NJ with its temporary shutdown of all non-essential government services in the summer of 2016 (Pinto, 2016a) should be exchanged for a higher or lower price than those of Harrison, NJ which is still in court to reclaim withhold taxes from the newly developed Red Bull Stadium.²¹ As infrastructures of time-space compression, the agencies are fundamental in enabling the stretching of capitalist social relations across space, “synchronically condense heterogeneous fiscal conditions, in a simple fashion, in order to select, price and trade various securities” (Paudyn, 2014: 160; cf. Langley, 2010).

Credit rating can in this way be understood as being all about the question of abstract, commensurable risk, where the unique uncertainties of local fiscal relations are judged in terms of creditworthiness on a scale from AAA (most safe) to, depending on the agency, C or D (the latter indicating that the issuer is in default). Between these extremes, each rating scale has a 19-22 finer gradations and these are often combined with an indication of whether the future rating outlook is positive, negative or stable (see Table 3.1). It is these combinations of letters and numbers that conversations in the bond market circulate around, with abound references to AAA-(“triple A”), Baa1- and BBB-credits as if these were free floating entities completely removed from their local context. Comparing the seemingly incommensurable is, however, more easily said than done. The enormous organizational effort that goes into this task will be the focus of next section.

²¹ Interview 7, 01-06-2016, CFO of Harrison, NJ.

3.4 Overcoming the paradox of commensuration: it's all in the methodology

In their daily work credit rating analysts are faced with a paradox. On the one hand, they know that each credit has its own set of unique risk factors. On the other hand, their ratings would be useless for investors if they were not able to compare these factors with all other credits, if they were unable to reduce them to one of the symbols on the rating scale. While the literature will point this out, referring to the process as an “onerous search for ontological equivalence in fluid fiscal relations where none exists” (Paudyn, 2014: 20), this paradox does not escape the analysts themselves. They are (at least if they have been in the business a while) well aware of the vanity of their task. Take, for example, the frustrations expressed by one former analyst with about two decades’ experience in senior positions in one of the larger agencies. Asked to reflect on what makes municipal bond rating such an interesting place to work in, she pointed towards the complexities analysts need to grapple with every day:

Muni[cipal] finance is so complicated because all of these different issuers are just lumped together because of the tax exemption, but you have different state laws, you have different security structures, different types of issuers. What means something in one state doesn't mean the same thing in another so it's very complex ... Then, you know, what powers does certain types of entities have? For example, New York City handles its school district [while] Chicago has a separate entity. So, *you can't even compare city to city* because they have different services that they are providing even at like levels of government.”²²

The analyst admits that “you can’t even compare city to city,” and yet that is what the job is all about, putting cities into a rating scale that allows investors to compare investment opportunities. The way this rating becomes possible, how risk is abstracted from the uncertainties of its local

²² Interview 10, 06-06-2016, emphasis added.

context and made commensurable, is by relying on clearly specified criteria for evaluation of different risk factors and the development of organizational practices that ensure consistency across space. It is all in the methodology, to paraphrase one rating analyst.²³

3.4.1. Initiating a rating

The municipal bond rating process starts when a municipality or municipal entity such as an improvement authority, often in consultation with a financial advisor, decides to issue a bond.²⁴ Approaching a rating agency, the bond issuing municipality provides them with a draft “official statement” (OS), a document outlining technical details of the credit like maturities, principal, the security for the bond and basic financial information such as budgets and audits. The OS also contains an extensive description of the municipality including demographics, information on governance structure, tax collection rates and major employers. As one senior rating analysts points out, the official statement is really a “marketing document” where the municipality is telling its “story.” The work of the rating analyst then becomes the creative task to “think about that story and figure out if that’s the whole story or part of the story and what’s the other parts of the story might be.”²⁵

Diving beneath the surface appearance of a city’s credit story requires the analyst to draw on a broad combination of quantitative and qualitative data while always making sure to relate

²³ Interview 3, 18-05-2016, rating analyst.

²⁴ Municipal bonds come in various shapes depending on their legal structure and security pledge for debt repayment. A General Obligation (GO) bond pledges the ‘full faith and credit’ of the municipality, in principal meaning that it will put all its resources and full taxing power towards ensuring debt repayment. A revenue bond, on the other hand, only pledges the income from a particular revenue source, such as the tolls from a toll road, as security (see Chapter 2 for an extended discussion). Here I focus on GO bonds as these most clearly illustrates the need for the rating process to abstract from the complex factors determining an entire city’s economic and financial health.

²⁵ Interview 12, 14-06-2016, senior rating analyst and head of public finance at a major rating agency.

that local story to the larger story of municipal credit risk at state and national level as well as macroeconomic risk on a global scale more generally. In this task, the rating process relies on the issuer’s own financial information, general economic and demographic data gathered from public data bases and indicators of management performance in the form of, for example, comparisons between budgets and actual financial statements so as to judge financial planning, but also conversations with local management in conference calls and site visits.²⁶ These occasions, in particular the site visits, are highly staged performances where the issuer tries to tell its story and make the best case possible for the credit’s quality while the rating analysts try to dig deeper behind the hard numbers, asking questions about debt structure, further plans for

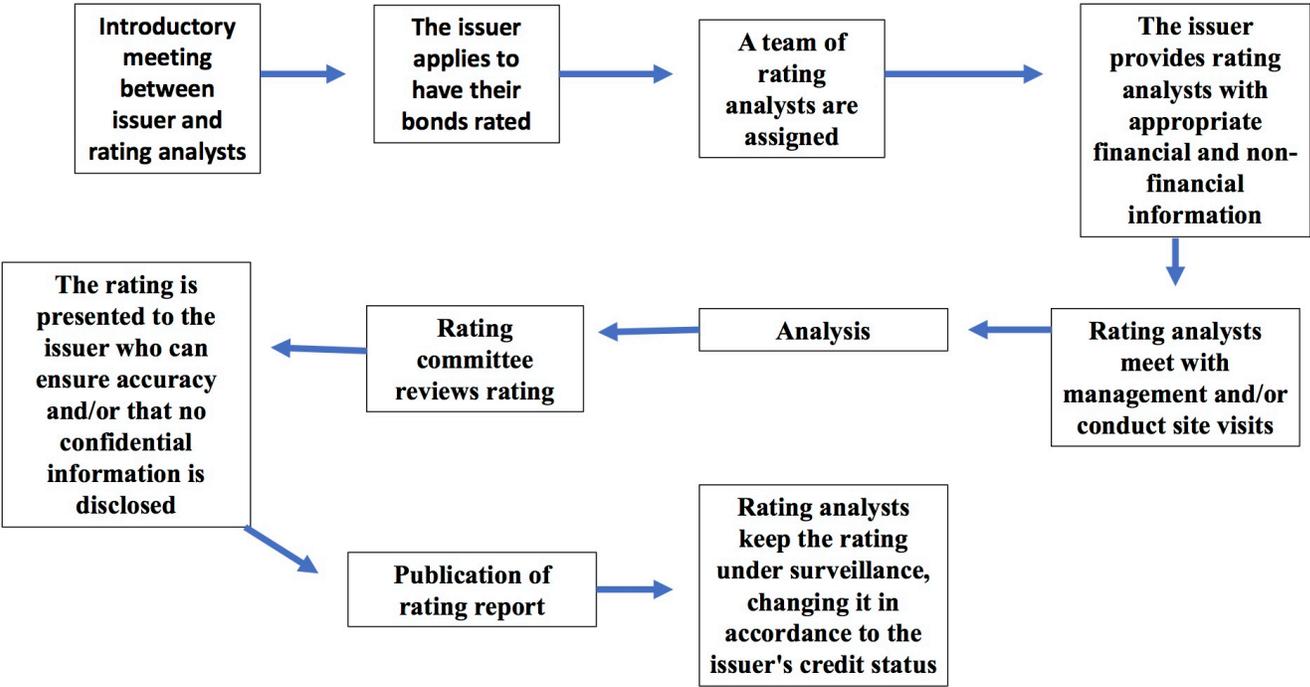


Figure 3.1. The rating process

²⁶ Interview 3, 18-05-2016.

issuance of debt and generally trying to get a feel for the place's economic and management.²⁷

Whereas some municipal officials put high trust in their ability to increase their ratings through these site visits,²⁸ seasoned rating analysts are well aware of their staged nature and look upon them with skepticism preferring the “objectivity” and standardization of the rating methodology.²⁹

²⁷ A former Chief Financial Officer (CFO) in Newark, NJ describes how these sites visits can look like, highlighting their staged nature: “[When issuing bonds] we would always meet with the rating agencies ... Almost every time we did an issuance we would meet with them, but we would have them to come to different parts of the city to see improvements that were made. We had meetings with them at the Newark Museum, we had meetings with them at the Devils' Stadium, [we had meetings with them at the] Prudential Center after that was built showing them that, we would have meetings at some of the corporate headquarters around the Prudential Center or at some of the major hotels, [we had meetings with them at the] Seton Hall Law School... Obviously you would take a tour of the museum or a tour of the Athletics Center, wherever we were, and talk to them about development that was ongoing and plans for the city, how that was going to stabilize tax rate going forward, ... and almost always the mayor would be there... So there was a big, big press on giving the rating agencies the information they needed to make a rating, show them the graphics, show the long-term budget projections, and give them a sense of the stability of the revenue structure and whatever strides were being made. Obviously, development was a major component so [we would show] any big development plans that went on. We also would do bus tours of the city where we would take them to different developments underway or completed. So, it was really a lot of information being passed to the rating agencies. They would obviously look at our financials and we would have conference calls with them going over questions on audits or whatever questions they had on general financial conditions and we would talk to them about those things on an ongoing basis” (Interview 17, 28-06-2016).

²⁸ Take for example the account of the CFO of the City of Elizabeth, NJ:

“**Question:** And you take [the agencies] to see these [economic development] sites as well?”

Answer: Oh yes, we take them for a dog and pony show. We take them out for lunch and then we go to the Mall and we go to the properties involved here

Q: What's the importance of that fieldtrip so to speak?

A: To just see this is it, this really works. It's a form of communication, just keeping them [informed]. If you see a location like Midtown they can come over here and they see the College and the train station and we show them all [redevelopment schemes] and the redevelopment financial revenue and say this it's what it's going to be so they have feel of what the city is about, what it's going to look like. We use to have them here every three years, so they will probably be here next year and we got all these [redevelopment] plans so next year they will be in the building stage so they can see [them]. It's something you visually can see and see that we're not making anything up.

Q: So it's kind of making them more confident?

A: Yeah, especially when you get to the Mall you can see the property involved down there which is enormous and down by the Mall the parking is busy. They can see that this is real, when you're driving down for 20 minutes looking for a parking spot then you really know that there is a lot of activity going on, a lot of revenue being generated.” (Interview 6, 27-05-2016).

²⁹ Interview 12, 14-06-2016.

3.4.1 The rating methodology: breaking apart

Asked what the greatest challenge in assigning a “correct” rating is, one senior analyst suggests the challenge is not so much the individual rating itself, but rather consistency.³⁰ The rating methodologies are therefore designed so as to “break things apart and figure out: what is [it] that lead you to a certain conclusion [in one place] and why would it lead you to a different conclusion in another place[?]”³¹ This is a strategy of abstracting away from the particular local complexities when assessing risk, where rather than comparing each unique combination of risk factors, disaggregating them into more manageable units. This because while it might be difficult to straight up compare the cities of Newark, NJ and San Francisco, CA, one can at least compare their relative levels of debt, their tax collection rates or their median family income against a common metric. Similarly to a financial derivative’s decomposition of any kind of asset into component parts that are then traded, it is this process of breaking apart that “enables the attributes of any [city] to be configured as universally recognizable and generic” (Martin, Rafferty, & Bryan, 2008: 126), regardless of its unique position in rounds of uneven development, its particular political contestations and its municipal financial practices. Clearly specifying relevant credit risk factors, breaking them down into smaller sub-factors and, sometimes, giving them different weights in accordance to their importance is what the rating methodologies are all about.

Firstly, there is the basic economic health of the locality. This matters because it is the

³⁰ The challenge being “making sure that if we say that in Texas that this is a strong revenue framework that we look at the same thing in, you know, Massachusetts. That we’re assessing it the same way, making sure that the differences and similarities are accurately reflected, ... Making sure that if this one is AA- that one is also AA- if they’re really similar” (Interview 12, 14-06-2016). Another former rating analysts stressed the need for “consistency, transparency and accuracy” arguing that “the rating is supposed to predict whether it’s going to be a default, but if you’re assigning ratings without any consistency and transparency what’s the value?” (Interview 21, 19-07-2016).

³¹ Interview 12, 14-06-2016.

strength of the local economy that provides the taxes that constitute the ultimate basis for debt repayment. Fitch (2016: 1) argues that the economic base of a municipality “serves as the foundation for the key rating factor assessments that place the credit within and sometimes outside the expected rating range.” Here the attention is to the structural position of the locality in relation to global flows of capital, rounds of uneven development and spatial divisions of labor. Secondly, however, local governments need to be able and willing to translate local economic strength into revenues. In the words of Moody’s (2016: 8), they need to be able to “translate economic weight into credit strength.” Investigating factors related to financial performance therefore provides an ability to measure the municipality’s ability to manage its finances in the face of the structural processes affecting its economic prosperity. The factors themselves are wide ranging, from economy and tax base to financial operations and management and are each broken down into several sub-factors that each get a score in relation to its relative performance. It is important, however, to not take these factors at face value. As Moody’s (2016: 7, emphasis added) points out, they should rather be understood as “quantitative measures that act as *proxies* for a variety of different tax base characteristics, financial conditions, and governance behavior that can otherwise be difficult to measure objectively and consistently.” Similarly, while the rating judgment is forward looking, that is concerned with how the municipality is going to be able to service its debt in the future, the agencies can only judge performance based on historical data, seeing the municipality’s historical ability to manage finances as a proxy for its future performance. This disjuncture between what is really of interest and what is possible to measure structures the entire rating process.

In particular, the proxy-nature of the rating factors poses the question of for what they actually are proxies? Here, when rating agencies look at the creditworthiness of a municipality,

what they arguably look at across all factors of the analysis is the municipality's budget flexibility with regards to debt repayment. That is, the rating analysts want to figure out the city's ability to adjust its financial operations so as to be able to repay the debt regardless of external economic shocks or other financial commitments. The proxy-indicators that are the rating factors are therefore generally concerned with revealing this underlying flexibility, judging the resilience of local finances in face of economic and political pressures. This search for flexibility is particularly evident in Moody's (2016: 9) rating methodology where, for example, a large and diverse tax base is favorable because it indicates less vulnerability to recession-induced shocks and higher median family income is a credit positive because it allows for "relative flexibility to increase property taxes in order to meet financial needs."

Further, financial position is measured as an indicator of a municipality's "cushion against the unexpected, its ability to meet existing financial obligations, and its flexibility to adjust to new ones" so that large and consistent cash reserves and other financial trends express the municipality's "ability to adjust to changing circumstances" (ibid: 11). Similarly, if the municipality is exposed to "outsized risk" by, for example, guaranteeing the debt of an enterprise this reduces its budgetary flexibility. The same goes for "labor contracts that materially affect credit strength," heavy fixed costs or limited ability to raise revenue and control expenditure (ibid: 14). Also with respect to the factor of "management" this flexibility is key. Here, the state's "institutional framework" in which a municipality operates "shapes its ability and flexibility to meet its responsibilities" while, for example, presence of organized labor, pension liabilities and tax caps further reduces its flexibility to respond to bondholder needs first and foremost (ibid: 14). This search for "flexibility" is crucially concerned with one thing, and one thing only, the municipality's "flexibility" to revise all other commitments that could stand

between bondholders and the debt service in event of a fiscal crisis. The debt service itself, however, is an inflexible, absolute commitment. Both Fitch (2016) and S&P (2013) emphasize a similar flexibility so that Fitch's (2016: 6, 10) factors include the municipality's "[i]ndependent legal ability to raise operating revenue without external approval" as well as its "spending flexibility" to determine its ability to respond to economic changes with revenue increases or expenditure cuts while S&P (2013: 16) argues that "a government's ability to implement timed and sound financial and operational decisions in response to economic and fiscal demands is a primary determinant of near-term changes in credit quality."

3.4.2 "Objectifying" risk: reassembly

After breaking apart the credit profile of a municipality into rating factors and sub-factors,³² the final assignment of a rating entails the reassembly of all these individual factors into a single indicator of investment risk. This is the final step in the process whereby risk, in the words of LiPuma & Lee (2004: 24), becomes "objectified." That is just, as Marx's (1990) labor *process* is objectified in the *thing* that is the commodity, the translation from concrete uncertainties to abstract, commensurable risk is achieved through a "process by which the contemporary financial community ... concretizes a complex amalgamation of social, economic, and political relations into a single recognizable object ... that then appears to be independent of these social relations because they are not part of the manifest appearance of the object or instrument" (LiPuma & Lee, 2004: 24). You cannot look at a Ba2-rating and get any sense what is going on beneath surface, the "manifest appearance" of the rating (that is the particular combination of

³² Moody's scorecard, for example, has four general factors, 13 sub-factors, 11 opportunities for "below-the-line-adjustments" and at least 19 other considerations not included in the scorecard but which can lead to further adjustments (Moody's, 2016c).

letters and numbers) does not reveal the political dynamics, economic histories and financial expertise of the locality. Yet, it is just what it is supposed to indicate. In order for the rating scale to fulfill its purpose, however, the rating needs to abstract from each unique combination of concrete fiscal uncertainties so as to enable easy comparisons.

The reassembly of all individual factors, sub-factors, “below-the-line adjustments” and other considerations into one single object (representing relative credit risk that can be priced and exchanged on the bond market) is the final step of the process. Here, the agencies have different strategies. Moody’s (2016) and S&P (2013) choose to weight the different factors according to a set percentage, but Fitch (2016) refuses to do this as they believe the relative importance of the different rating factors varies depending on the individual credit. Regardless of their approach to this standardization-specificity problem, however, the agencies crucially rely on creating credit profiles of incommensurable places by combining individually comparable risk factors into unique wholes that can be compared with other unique wholes by virtue of being composed of similar relative risk factors. By doing this, they abstract from the specificities of both these underlying factors and the particular fiscal social relations of a place for which these factors were supposed to represent “proxies.”

After the rating analysts have undertaken their analysis, it is presented in front of a rating committee made up of senior analysts. This committee monitors that the original analyst has closely followed the methodology, not being carried away by, for example, a particular successful site visit. It also, however, makes sure to impose spatial, as well as temporal, consistency on the rating process. The committee is set up so that it always includes at least one representative from outside the particular region where the municipality is located. The benefits of this is that the committee can always relate the individual rating to the municipal bond market

at large.³³ While the standard practice in an individual state might in the end override concerns of suspicious outsiders,³⁴ this committee structure ensures that the local rating is always sensitive to how it is made elsewhere.

Similarly, by being made up by more senior rating analysts, it also helps to transfer expertise across generations. The rating committee might accept or revise the analyst's suggested rating, which, together with a report explaining its rationale, goes out for review to the issuer who, while they cannot contest the rating itself, will check the material for inaccuracies and confidential information. As a final step, a press release is written and the rating is published. This concludes the transformation of the city from a lived place to an exchangeable commodity. It is, however, a process fraught with the inevitable contradictions of abstraction, where the concrete character of the financial commodity can never fully be escaped. Two moments in the post-crisis era illustrate this particularly clearly and in the next section I turn to them to examine the increasing standardization of the rating process as well as the recent push to "recalibrate" the municipal rating scale.

3.5 Limits to commensuration: standardization and global recalibration

Breaking apart followed by reassembly is what the rating methodology is all about. What makes the municipal bond rating process so complex, however, is that unlike, for example, the corporate credit market which have relatively few issuers with standardized financial reporting practices, municipal bonds are not uniform in this way. Analyzing their creditworthiness

³³ As explained by one senior rating analyst: "If you're only looking at Illinois credits you might say, 'Oh, that's how they do it in Illinois' but somebody from outside will say, 'But aren't you worried about that for this and this reason? because they don't do that in New Jersey'" (Interview 12, 14-06-2016).

³⁴ Interview 10, 06-06-2016.

consequently requires much more personnel and more qualitative judgment.³⁵ It is therefore particularly difficult to develop a purely standardized approach to municipal bond rating. Moody's (2016: 2, 7) are in their rating methodology documents keen to point this out, writing that "[t]he scorecard is not a calculator" and the "rating process involves a degree of judgment, or consideration of analytical issues not specifically addressed in the scorecard, that from time to time will cause a rating outcome to fall outside the expected range of outcomes based on a strict application of the factors presented herein."³⁶ Credit rating methodologies therefore need to introduce different mechanisms for accommodating the analytical (and indeed inevitably subjective) judgements necessary for assessing individual credit quality.

In the case of Moody's, these are represented by additional "below-the-line" adjustments that can notch a rating up or down. It is here "analytical judgment comes into play" and while, for example, a fund balance as percentage of revenues above 30% will indicate a Aaa-rating, if the analysts deem the municipality's revenue structure to be particularly volatile this can have a negative impact on the rating (ibid: 7). S&P (2013: 8-9, 18) on the other hand refer to positive and negative "overriding factors" such as "sustained large positive fund balances" or "lack of willingness" to pay obligations that can notch ratings up or down or cap them at a certain level while Fitch's (2016) unwillingness to apply a standardized weighting to its different factors speaks to a similar need to keep the process open to potential local anomalies. This becomes particularly true when it comes to local political dynamics which by their very nature are

³⁵ Interview 18, 05-07-2016, former credit rating analyst now working in a major bank.

³⁶ To exemplify this point, consider the story of Chicago's, IL sluggish rating performance: "Take out Chicago's pension problem and Chicago is like a AA rated credit. Its economy is very good, it's very diverse, people want to live there, they got great educational attainment in the city, they got all of these really good factors that you would say make them a good credit, [but] their pensions are dragging them down in such a way ... that now they are sub-investment grade by most rating agencies... So if you would take that kind of [qualitative judgment out of the rating process] you would miss it because pensions might have 10% weighting but I would say that the influence of the pensions on Chicago's rating is probably more like 80-90%" (Interview 10, 06-06-2016).

difficult (if not impossible) to statistically model. Thus, the rating agencies emphasize the need for qualitative analysis as much as statistical comparison, because, as S&P (2013: 4) puts it “[v]ariables such as economic conditions, debt levels, and financial performance can suggest when difficult decisions to restore fiscal balance might become necessary, but do little to suggest whether prudent decisions will be made.” While introducing possibilities for analytical adjustments into the methodology, this speaks to how the rating agencies constantly need to grapple with a tension between standardization for the sake of commensurability on the one hand and understanding particularities on their own terms to be able to accurately judge localized credit risk on the other.

This tension between standardization and particularities never reaches equilibrium, but with the Dodd-Frank regulations it is the former that has increasingly come into focus. Criticizing the rating agencies’ to be “inaccurate” in their ratings of structured financial products like Mortgage Backed Securities, Dodd-Frank called for more stringent accountability and transparency across the credit rating sector. Central to this was the empowerment of SEC to prescribe rules requiring all credit ratings to be undertaken in accordance with predetermined criteria and methodologies and to ensure that changes to these methodologies and processes were applied consistently. This pushed rating agencies to disclose reasons for changing methodologies and to notify users of ratings of which methodology a rating is based on, when this methodology is changed, when an error is identified in the methodologies and when that error might impact the rating. At the same time, each rating publication is to be accompanied with information that clearly discloses the underlying assumptions of the ratings, the data relied upon in the rating process as well as generally disclose information that makes it easier for users to understand the ratings (Dodd-Frank, 2010).

As Sinclair (2010) points out, increased transparency has long been a way for the agencies to legitimate themselves after crises, but while Moody's, for example, on their own initiative became significantly less secretive in the wake of the 1997-1998 Asian crisis and 2001-2002 Enron bankruptcy, Dodd-Frank explicitly asked the agencies to open up the "black box" of the rating process. While the concern with rating transparency in particular focused on structured finance, this regulatory response has spilled over to municipal ratings. Here the agencies have become increasingly concerned that their ratings are defensible with reference to a published methodology, use more data points to justify their case and document when a rating deviate from what would be expected using the standard formula.³⁷ The SEC does not explicitly call for the standardization of ratings *between* rating agencies, something Dodd-Frank asked the commission to look into but which they recommended against in a 2012 feasibility study (SEC, 2012b). In practice, however, its increased focus on rating transparency has pushed the rating process to *internally* become more uniformly applied to all issuers, regardless of local particularities. One former analyst explained the consequences of this:

[The rating process] has become a lot more bureaucratic and with the Dodd-Frank and SEC now regulating [the rating agencies] they are very driven by those methodologies. The exceptions are very difficult to achieve and identify and it's an unintended consequence, meaning that they have ten criteria that you follow and if you have something that is unique about yourself that's not in those ten that should compensate for them that's very difficult to do. So, it's a lot more what I refer to as rating by numbers as opposed to incorporating the subjective factors ... It's just squeezing everybody to the norm so to speak and I think it take away a lot of the opportunities either higher or lower [rating]

³⁷ Interview 10, 06-06-2016.

differences to occur.³⁸

While this has had its intended purpose, for some bond-market professionals, by enhancing transparency,³⁹ others are critical of it for reducing what was previously a creative task of figuring out a particular city's unique credit profile into a simple ticking of boxes. As another former analyst argued, the process has become much more mechanical. The agencies increasingly "rates to the criteria," with the methodology driving the rating rather than the actual credit quality of the issuer.⁴⁰ This diminishing "creativity" of credit rating in favor of its standardization should, however, not be interpreted as simply a new feature of increasing regulation (as perceived by the market participants) but rather puts the finger on the central problem of the rating agencies very business model: the difficulty to once and for all resolve the tension between the concrete and abstract inherent in the "double form" of the commodity. Seeking to commensurate the incommensurable, the rating process always needs to incorporate elements of standardization *as well as* "creativity," moments where the rating analyst can say "this credit is different" and processes for recalculating that difference into to the standardized grid of the rating scale. This tension has further become particularly evident in another post-crisis change to the rating process: the so called "global recalibration" of municipal credits to the corporate rating scale.

Mann's (2010: 177) definition of value as "a form of social wealth constituted by a spatially and temporally generalizing social relation of equivalence and substitutability" puts

³⁸ Interview 21, 19-07-2016, similar sentiments were expressed in interview 13, 15-06-2016 & interview 16, 23-06-2016. This is ironically leading to more "split-ratings" where different rating agencies assign different ratings because they are now so closely following their own methodologies and giving less attention to how the other agencies rate.

³⁹ The same former analyst goes on to say that although "the unique opportunities sort of become marginalized today" it is probably still better than 20 years ago when there was less consistency (Interview 21, 19-07-2016).

⁴⁰ Interview 13, 15-06-2016, former rating analyst now working in major bank.

emphasis not only on the relations of commensurability between commodities, but also on their substitutability to each other. This is because “equivalence alone is insufficient to explain the value-relation, because it does not specify the movement that must constitute value, which consists not only in equivalence, but also in the unfolding process of substitution, of one commodity for another, of one production process for another, of one capital for another” (ibid: 177). The value relation is one in constant movement, where capital needs to be able to move seamlessly not only across space, but across different forms of commodities: jumping from one commodity to another, buying and selling them in accordance to the changing market conditions of the day. In the context of credit rating, this movement was, however, long encountering a barrier. This is the barrier between municipal credits and corporate credits.

For many decades, the municipal bond market was characterized as an isolated financial backwater. As late as before the subprime mortgage crisis municipal bonds were therefore still rated on a separate rating scale, a separation that in the case of Moody’s, for example, went back all the way to 1918 (Ackerman, 2010). Throughout the last decades, however, investor crossovers have become more commonplace (in particularly with regards to structured financial products such as Credit Default Swaps (CDS), but also the Build America Bonds-program (BAB) initiated through the American Recovery and Reinvestment Act of 2009). With these crossovers came a greater need for rating commensurability.⁴¹ With this growing market interest

⁴¹ Two senior rating analysts who both were intimately involved in the recalibration process in their respective agencies explain these changes in the market:

- A) “Now you have changes in the financial system happening and more crossing over so bankers, issuers, counterparties all wanted ratings to be comparable because imagine you enter into a [credit default] swap and you're AA+ rated Goldman Sachs and I'm like some A- rated local government, what you want to be able to do is to put them on parity so that the triggers can be the same and it means the same thing and that in collateral postings you want to insure you got a balance, symmetrical credit risk” (Interview 10, 06-06-2016).
- B) “The reason that [the recalibration] happened around the same time for [Moody’s and Fitch was] the federal government’s Build America Bonds-program ... [This program provided] a tax break for municipal

in comparing across different kinds of credit it was soon realized that the actual default risk of municipal bonds as compared with corporate was minimal, but as they were rated on a separate scale they would often look much riskier. In an default study Moody's (2010c: 1), for example, found that 1970-2009 only 54 of Moody's rated municipal securities had defaulted so that while the default rate for speculative-rated municipal credits was 3.4% for corporate credit that rate was 21.4%. Here we can see an historical irony: while credit rating developed to overcome barriers to commensuration, as the financial sector grew increasingly sophisticated the practice of separating municipal ratings from corporates created a new barrier to this commensuration.

For corporate investors used to understand risk in terms of historical levels of default, the incommensurability between the municipal and corporate rating scales presented itself as an absurdity such that, in the words of bond market journalist Robert Slavin (2015: 1), a BBB municipal bond could be safer than a AAA corporate bond because “[a]t any given point of the rating scale, munis have less history of default than do corporates.” Financial market actors and their representative, such as the Securities Industry and Financial Markets Association (SIFMA), would thus increasingly push for the comparability across asset classes, arguing that “we need to make sure that there’s harmonization across groups, so that a corporate triple-A rating versus a municipal triple-A versus a structured finance triple-A rating versus some sort sovereign debt triple-A rating doesn’t mean different things” (Ackerman, 2009: 1). Similarly, municipal bond market researcher Natalie Cohen (2009: 1) argued that “what is missing is a spectrum of ratings

bonds so you could sell taxable bonds but the buyers would be made whole for that tax ...they subsidized municipal bonds so they could open up the market to other buyers who [previously couldn't] take advantage of a tax exemption.... [If you can't take advantage of the tax exception you] don't tend to buy municipal bonds because you get lower yield [and] if you can't take advantage of the tax exemption then getting a lower yield is not at all appealing. So, the BAB-program ... [subsidized municipal bonds] so now you had people who generally bought corporate bonds being interested in munis” (Interview 12, 14-06-2016).

on a single scale that accurately reflect [sic] the default research – municipal at the higher end of the scale with corporate ratings further down – in line with their relative risk.” This push from investors coincided with increasing public outcry from government officials at what they perceived as the rating agencies “discrimination” against municipal bonds by putting them under greater scrutiny than their corporate equivalents, resulting in higher borrowing costs and potential waste of tax payers’ money (Ackerman, 2009).

Under increasing pressure from investors as well as issuers and legislators to move towards default based ratings,⁴² Moody’s and Fitch would increasingly take steps to “recalibrate” their municipal ratings to the corporate rating scale in April 2010 (Fitch Ratings, 2010; Moody’s Investors Service, 2010a). S&P, on the other hand, would initially argue that their ratings did not need a recalibration, but would in 2012 eventually adopt a new municipal rating methodology to overcome problems of comparability (Cherney, 2012). This involved moving municipal credits up the rating scale to represent their lower default risk. It should, according to the agencies themselves, not be seen as a rating upgrade per se since the underlying credit quality has not changed. Rather it is merely a “recalibration.” This is not, however, necessarily how it has been interpreted in the market.⁴³ Furthermore, while many market actors have been positive about the change, since the recalibration rating analysts are “more forgiving in the AAA-space” when rating municipal bonds,⁴⁴ it is not a process that has been universally welcomed. As Ashton (2009: 1438) has argued with regards to the subprime mortgage market, “the key concern for financial institutions and investors is not the lowering or managing of credit risk per se but the

⁴² In regulation this would cumulate in a 2015 Dodd-Frank ruling “to adopt procedures designed so credit rating weigh default risk “in a manner that is consistent” for all rated obligors and securities” (Slavin, 2015: 1).

⁴³ Interview 22, 19-07-2016.

⁴⁴ Interview 10, 06-06-2016.

search for yield.” With less “stratification” between securities some investors therefore believed that the recalibration would “strip value” or make it harder to extract interest rate and fees on lower rated bonds (Albano, 2010).

If the process of commensuration *between* municipal bonds requires “enormous organization and discipline” (Espeland & Stevens, 1998: 315), this process of commensuration *across* asset classes would entail an gigantic task. Moody’s (2010: 3), for example, would in stages be adjusting 70,000 ratings of 18,000 issuers while Fitch would recalibrate more than 38,000 ratings (Seymour, 2010). But, of course, how do you compare local governments to corporations? Through the recalibration, sought by so many financial market actors, the paradox of comparing the incommensurable would return with a vengeance. In Moody’s (2010) three-step recalibration plan, municipal ratings first had to be “benchmarked” against the “global rating scale,” secondly different recalibrations would be developed for different municipal sectors (states, local governments, healthcare, etc.) before, thirdly, the new, recalibrated ratings were published, including an upwards notching of 1-3 steps for most investment grade ratings (rated Baa3 and upwards). Assembling cross-sector committees where public, corporate and sovereign finance analysts together analyzed a sample of “representative” ratings to develop benchmarks in which risk did not only had to be abstracted from the specificities of local fiscal relations, but also from the specificities of local government all together to achieve comparability with all other credits. Similar to how the rating committee is designed so as to ensure that each rating analysis is rated to an equal standard, these committees would then ensure that the “myriad shapes and forms” of local uncertainties were commodified as abstract risk, commensurable

with all other forms of financial uncertainties.⁴⁵ As such, the recalibration process is the final step allowing for equivalence and substitutability not only across space but also across sectors, enabling investments to flow relatively seamlessly across the globe and value to be extracted from the totality of everyday life.

3.6. Conclusion: from commodity abstraction to “abstract domination”

In this chapter I have attempted to open up the “black box” of the municipal bond rating process. Building on renewed discussions of value theory in the wake of financialization, I have argued that credit rating agencies have become key institutions for the commodification of cities as sources of value extraction. Grappling with the “double form” of municipal bonds as always possessing qualitatively heterogeneous concrete uncertainties of default while also being the bearer of a quantity of abstract risk that make them tradable on in the financial market, the rating process relies on creating credit profiles of incommensurable entities by breaking them down into individually comparable risk factors and then reassembling them to unique wholes that can be compared with other unique wholes by virtue of being composed of similar relative risk factors. It’s all about breaking apart followed by reassembly, allowing the agencies to “objectify” heterogeneous local fiscal relations into a single rating enabling their market circulation as a commensurable commodity in form of the municipal bond (cf. LiPuma & Lee, 2004). By doing this, however, they abstract away from the specificities of these underlying rating factors as well

⁴⁵ As explained by one former analyst: “we went through a number of cross-departmental committees where credits were presented to bench mark were they would fall, where corporate analyst would rate them, and the public finance person would provide counterbalances so if they said there is no cash [we would say] 'you have the tax base, consider that to be an untapped reserve and the taxes are relatively low in the city', whatever, so it was that type of conversation that would happen and ultimately credits were pin-pointed against sovereigns and against corporates and then there was the assumption that our ordinal scale was correct and that enabled moving credits into different categories” (Interview 10, 06-06-2016).

as the unique social relations of place for which these factors are proxies.

Mackenzie (2005: 570) has admitted that the fine-grained understanding that method of “opening the black box” provides does indeed, as many critics claim, have the tradeoff of “blunting oppositional political passions.” This because the necessarily close interaction with the research subjects can make condemnation difficult. Understanding credit rating as a form of commodity abstraction, however, gives us a set of tools to further understand and contest its power by clarifying what is at stake in the process. Thus, in a critique of those who, by interpreting abstract labor as merely a thought abstraction, treat the equalization of commodities as unproblematic, Colletti (1972: 84) writes that “in the reality of the world of commodities ... individual labour powers are equalized precisely because they are treated as abstract or *separate* from the real empirical individuals to whom they belong” such that “[a]bstract labour’, in short, is *alienated* labour, labour separated or estranged with respect to man [sic] himself.” Similarly, the “abstract risk” of the rating scale is alienated risk, risk that is estranged from the local communities whose lived interactions in the city produce the concrete socio-political uncertainties of default that the rating process assesses and packages into a unified, commensurable commodity. By conceptualizing credit rating as a process of commodification we can see thus see how just as with Marx’s (1990: 165) fetishized commodity, which has “absolutely no connection with the physical nature of the commodity” nor to the social relations of its production, the commodification of cities and local government entails stripping them of their embeddedness in the social relations of place, alienating them from their own residents and as commensurable entities making them substitutable to all other credits. In this way, cities lose everything that makes them concrete, living places and are put into circulation through a time-space “marked by homogeneity, continuity and emptiness of all natural and material content...

[where] the exchange abstraction excludes everything that makes up history... [and] the entire empirical relate [sic] of facts, events and description by which one moment and locality of time and space is distinguishable from another is wiped out” (Sohn-Rethel, 1978: 48-49).

This abstraction, fundamental to capitalism, has far-reaching consequences for local politics. It is namely the commodity abstraction that gives social domination under capitalism a very different character from that of the social forms preceding it: where “social relations ... exist not as overt interpersonal relations [like the relation between a feudal lord and his serfs] but as a quasi-independent set of structures that are opposed to individuals, as sphere of impersonal “objective” necessity and “objective dependence” ...[making capitalism] a system of abstract, impersonal domination ... [where] people appear to be independent; but they actually are subject to a system of social domination that seems not social but “objective”” (Postone, 1993: 125). Understanding credit rating as commodification, then, puts the neoliberalizing influence of the rating agencies on urban governance into new light. It shows how while this sometimes takes the character of highly visible confrontations with the agencies and their ratings by mayors and other local political figures who resent them for their unaccountable powers, on a day to day basis the influence of credit rating is commonly of a much more “objective” and abstract character, internalized in public finance norms co-produced in the interaction between rating analysts and local financial professional. From this chapter’s account from inside the agencies, I will therefore in the next chapter turn to their relation to the municipalities that they rate. There I will focus on the case of New Jersey, the scene of a far-reaching rating crisis, to examine the local dynamics of credit rating and unpack the (non)politics of “creditworthiness” as a fundamental component of contemporary financialized urban governance.

Chapter 4: “I consider them another boss:” Bond rating, accountancy urban governance and the limits to creditworthiness

Newark has got to improve its bond rating and the only way I can see us doing that is to work with my council to do even greater cuts to municipal spending.

Cory Booker (quoted in Kaske, 2010: 1).

The creditor-debtor relationship shapes all social relations in neoliberal economies.

Maurizio Lazzarato (2012: 35).

4.1 Introduction

Since the Great Recession, critical analysts have been increasingly concerned with the dynamics of debt as key drivers of socio-political development. While Marx (1990: 233) long ago wrote that “[t]he class struggle in the ancient world ... took the form mainly of a contest between debtors and creditors,” contemporary commentators such as Graeber (2011) have argued that this contradiction is equally pronounced today, if not an even more so as the economy has been thoroughly financialized (cf. Krippner, 2005). One of the most ambitious arguments to this regard has been presented by Lazzarato (2012) who in *The Making of the Indebted Man* asserts that rather than chiefly being characterized by increasingly sophisticated techniques for speculation (such as the Residential Mortgage-Backed Securities (RMBS) and Collateral Debt Obligations (CDOs) that brought the subprime mortgage crisis), the era of neoliberal financialization has more significantly been marked by the increasing importance of the social relation of debt as a centerpiece of politics. Indeed, “[d]ebt creation, that is, the creation and

development of the power relation between creditors and debtors, has been conceived and programmed at the strategic heart of neoliberal politics” (ibid: 25).

In this chapter I will engage with the politics of this debt relation, stepping outside the “machinery” of the credit rating process to explore its effects on urban politics and administration. As such I will examine how the debt relation is negotiated in the interactions between rating agencies, local financial professionals and municipal finance regulation in the State of New Jersey. Building on the work of Hackworth (2002, 2007), Sinclair (2005) and others who have investigated the politics of municipal bond rating, I will argue that although this sometimes takes the character of a “shock doctrine” (cf. Klein, 2007) when spectacular credit rating crises bring forth the neoliberalization of urban governance, on a day-to-day basis the influence of credit rating practices is much more mundane. Beyond the “roll-back” moments of neoliberalism (cf. Peck & Tickell, 2002), cities increasingly have to “roll-with” (Keil, 2009) a politics of credit rating that, in some respects, has become business as usual. In addition to the highly politicized moments of crises and rating downgrades that have received much attention, the relationship between credit rating and local politics is often mediated through the technocratic discourse of “accountancy urban governance” (Merrifield, 2014: 416) characterized by the “combination of bond-market discipline, applied at a distance, and state-level interventions, imposed from on high” (Peck, 2017: 349).

The case of New Jersey is particularly illustrative in this regard. This because the state is widely perceived as a particularly outstanding example of municipal financial prudence. And yet, also in New Jersey, crisis is always just below the surface as the state is home to many older industrial cities that have long struggled in fiscal terms. During my field work, this was most clearly illustrated by the high profile Atlantic City budget crisis (cf. Peck, 2017). This instance

provided an indication of the weaknesses of a supposedly robust system, but it only tells one side of the story. To get beneath the surface of financialized urban governance, there is a need to go beyond such abject moments of crisis. Instead of directly focusing on the outbreaks of crises, this chapter therefore attends to all those cases where crisis might never come but where the power of finance and credit rating yet makes itself present.

To make this argument, the chapter will proceed in three steps. Firstly, I will provide an overview of the literature on municipal credit rating. This tends to read as a series of snapshots of the outbreak and resolution of crises, as moments where the contested politics of urban governance become particularly visible. While, as “exceptions,” these local financial crises can help us understand the more general “rule” of regulation by financial means, I will argue that it is necessary to step back from these crises if we are to understand the often smoothly functioning operations of the everyday politics of creditworthiness. Consequently, in the next section I will examine the making of Merrifield’s (2014: 416) “accountancy urban governance” in New Jersey. Such an exercise puts other methodological demands on the researcher. There is a need to probe elements of the urban system that is less understood while exploring how the institutional “rules of the game” materialize in actual practice. As a complement to the secondary-source analyses that have dominated accounts of municipal credit rating, I will therefore draw on interviews with local government financial professionals and other municipal actors to examine how the politics of creditworthiness are *co-constructed* in the interactions between rating agencies, municipal actors and state regulators.

Rather than an arena of contestation, credit rating here becomes a constrained “politics of limits” producing shared norms of what “good public finance” looks like through discourses of budgetary flexibility and financial expertise. This is not an entirely smooth process, however,

and the last section of the chapter will examine two cases where the limits to creditworthiness and accountancy urban governance become particularly pronounced: The Town of Harrison's rating crisis of 2010-2011 and the ongoing trickle-down effects of the State of New Jersey's rating crisis through its Municipal Qualified Bond program. A conclusion will thereafter sum up the argument of the chapter and reflect on what insights can be drawn for a wider understanding of the nature of local state agency in the context of financialization.

4.2 Municipal debt politics and the power of credit rating

With the return of the urban fiscal crisis in the post-recession period and the normalization of "austerity urbanism" (Peck, 2012) as a widely shared local policy condition of ever-leaner governments, the dynamics of municipal debt has come to occupy the center of American urban politics (see Chapter 2 for an extended discussion). Most significantly this is highlighted by the municipal bankruptcies sweeping the country from Stockton and Vallejo in California via Alabama's Jefferson County and, the biggest of them all, the Detroit default of 2013. In these bankruptcies, the contradictions of the municipal debt relation between bondholders, pensioners, service users and municipal employees have been fought out in courtrooms and closed-door negotiations, with bankruptcy filings often being used in a strategic manner so as to be able to rewrite labor contracts that are seen as crippling local governments (cf. Davidson & Kutz, 2015). In this sense, just as cities have been key strategic sites for neoliberalization (cf. Brenner & Theodore, 2002), urban politics after the Great Recession can be seen as ground zero for an emergent condition of debt politics.

It is here rating agencies makes their appearance in urban governance, Peck & Whiteside (ibid: 248) arguing that "[t]here are few more potent symbols of these changed times than the

inordinate significance attached to the ratings of cities and states provided by a handful of credit scoring firms.” In urban political economy, these rating agencies were first examined by Hackworth (2002, 2007) who argued that, through processes such as the rollback of inter-governmental fiscal transfers, the rise of large institutional investors and financial disintermediation, these agencies had become increasingly important players in urban governance. More recently, a similar argument has been made by Biles (2015: 2) who contends that “sensitive to the expectations and values of Wall Street institutions and desperate to acquire or maintain high ratings, cities have tailored their policies accordingly.” The rating agencies are here seen as being central institutions pushing for the increasing neoliberalization of urban governance, effectively holding local governments “hostage” (Ross, 2017: 25) in a never-ending search for *creditworthiness*. This is a politics Sinclair (2005: 65-66) defines as:

Both a causal belief – being creditworthy means that debt issuers are likely to repay their debt – and a principled belief, in that placing a priority on repaying debt is morally right and obligatory ... [which] becomes embedded in rules and norms, that is, institutionalized, acting like other beliefs in the manner of ‘invisible switchmen’ to ‘constrain public policy’ by ‘turning action onto certain tracks,’ thus obscuring other tracks from view.

In urban political economy, this shift has been portrayed in terms of a deeply contested global-local politics with rating agencies descending from above onto big city administrations,⁴⁶ enabling the hammering through of fiscally conservative politics. These politics of credit rating takes the character of Klein’s (2007) “shock doctrine,” with rating downgrades being

⁴⁶ Hackworth (2002, 2007) focuses on the cases of New York, Philadelphia and Detroit, Biles (2015) on Chicago, Philadelphia and Detroit, while Sinclair (2005) attends to the latter two only and Mitchell & Beckett (2008) relates the experience of New York to that of Mexico.

instrumentalized by local and extra-local actors to drive through “tough” reforms that would be politically impossible in normal times. The account of New York City’s fiscal crisis by Mitchell & Beckett (2008) exemplifies this narrative. Here, the downgrades of the city’s bonds by S&P in April 1975 and by Moody’ in October that same year gets to represent “the worst moments of the crises,” rating the city’s debt as speculative and “essentially making them unmarketable and instantly bankrupting the city” (ibid: 82). It was in this moment that the range of non-local agencies that had been established to restructure the city’s finances (including the Emergency Financial Control Board and the Municipal Assistance Corporation) “were essentially given carte blanche in their municipal rescue” and, in this way, the rating agencies “were key to the ensuing loss of autonomy for the city” (ibid).

In this kind of narrative, the focus has primarily been on the first of Peck & Tickell’s (2002) interplaying “roll-back” and “roll-out” moments of neoliberalization, where the institutionalized pressures of the rating agencies have secured the roll-back of localized Keynesian commitments to service provision and secure public employment. The Cory Booker quote that opened this chapter provides a clear example of the salience of this process, but, as Paudyn (2014) has pointed out, the influence of these financial institutions cannot be reduced to such explicit moments of spectacular rating intervention. It rather “derives from how persuasively they manage to constitute [a] neoliberal notion of *budgetary normality* as the hegemonic discourse against which democratic governments are judged and governed” (ibid: 5, emphasis added). The singular attention to high-profile crises-moments that has dominated critical accounts of municipal bond ratings is therefore at risk of overlooking how for many cities the politics of creditworthiness instead resembles a “roll-with-it” neoliberalization predicated on the “normalization of neoliberal practices and mindsets” (Keil, 2009: 232), Here, rather than

neoliberal reform being brought onto the scene by external actors (as in Mitchell & Beckett's (2008) account of New York City's crisis), "neoliberal subjects of all kinds co-construct, sustain and also contest a now normalized neoliberal social reality" (Keil, 2009: 232).

This requires a closer engagement with the intersections between credit rating and local actors, one that can draw inspiration from Weber's (2010) account of the financialization of urban redevelopment. Contesting approaches to finance capital that characterize it as something that simply descends upon cities from above, Weber (ibid: 257, 270) maintains that municipal governments rather are "active agent[s] of financial liberalization and integration" so that: "cities [are] not just arbitrarily selected for investment [by finance capital] as a result of a game played far above their heads; their local government representatives play[...] a critical role in constructing the conditions under which capital [can] be channeled into locally embedded assets." Similarly, an understanding of the everyday power of credit rating in urban politics needs to carefully position high-profile cases of big-city rating crises and contestations to examine how on a day-to-day basis the politics of creditworthiness is *co-constructed* in the interactions between local and extra-local actors.

Such a conceptualization of credit rating shifts the focus from publically visible "shock politics" where local elected officials see their democratic legitimacy being undermined by private financial institutions. Instead, it sees credit rating as "the internal form of governmentality involved on the promotion and reiteration of a neoliberal *politics of limits* underpinning virtually all budgetary relations" (Paudyn, 2014: 7, emphasis added). It is this notion of a "politics of limits" that really gets to the heart of the credit rating process. It specifies rating agency power not as providing the initial "shock" (cf. Klein, 2007) that justifies direct intervention into urban politics, but as setting "the parameters defining the budgetary realities

facing governments” (Paudyn, 2014: 200). That is, credit rating more fundamentally creates the background conditions under which all municipal actors must operate. There is a need, then, to balance the analysis of exceptional events like local financial crises with the more general normalization of financialized relations and practices. That is the purpose of this chapter’s empirical contribution, where the next section will examine the case of municipal finance in New Jersey and the central role played in the politics of creditworthiness by an often-neglected local actor: the municipal financial officer.

4.3 Accountancy urban governance: co-constructing creditworthiness in New Jersey

In addition to overlooking the everyday normalization of credit rating in local government, one unintended consequence of the form of secondary-source analysis of high-profile rating crises that has previously dominated urban political economy is that the focus almost by default becomes on local elected officials and their battles with the rating agencies. This tends to overlook how municipal finance, although indeed political, is very much the purview of a highly professionalized set of municipal employees. Further, it renders the politics of credit rating in terms of an unhelpful dichotomy between “external” financial institutions and the local state. This unhelpful because while with credit ratings the actions of the state are indeed “circumscribed by actors who sit outside its own body,” senior government professionals are deeply involved in this process (Lemoine, 2017: 27–28). The co-construction of creditworthiness as a form of “budgetary normality” consequently calls attention to the relations between external and internal actors in the normalization of the financial logics of credit rating.

Responsible for the processes of budgeting, tax collection and debt issuance, local financial professionals (in New Jersey uniquely led by a State-certified Chief Financial Officer)

play a key role in municipal management. Yet, with its focus on growth politics and its actors (including mayors, business leaders and labor representatives), urban political economy has rarely afforded them much attention. With post-crisis austerity pressures, however, there is a case to be made that the technocratic actors principally responsible for managing constrained municipal budgets warrant critical attention. Most significantly, inspiration can be drawn from *critical studies of accounting*, which has followed Tinker's (1985: xv–xvi) landmark argument that we need to understand accountants “not as harmless bookkeepers, but as arbiters in social conflict, as architects of unequal exchange, as instruments of alienation, and as accomplices in the expropriation of the life experiences of others.” By contesting the “objective” nature of accounting, this is a field that seeks to politicize accounting practices and insert accountants as important socio-political actors (see Dillard (1991) and Morgan (1988) for other early contributions as well as Potter (2005) for an overview). As such, it points towards the critical potential in researching the role of local financial professionals in urban politics.

In an earlier context of localized austerity, Clarke & Cochrane (1989; see also Cochrane, 1998) investigated the rise to influence of treasurers within the British municipalities to argue that these became central to local politics both in terms of setting the rules of the game for other municipal departments and for providing creative accounting strategies to minimize the impact of central funding cuts. This was crucially not problematized by other municipal actors as “the influence of accounting practice is taken so much for granted that no one noticed it anymore, and it is rarely challenged because it is simply part of the environment within which decisions are made and policies are shaped” (Clarke & Cochrane, 1989: 46). Similarly, jumping forward to the post-recession British coalition government's austerity politics, Merrifield (2014: 423, 421) in a spirited commentary denounce the rise of “accountancy urban governance,” in which

accountants, often employed by global consulting firms, “have a massive and growing stake in the delivery and management of Britain’s public services” such that more “services that are now driven by accountancy exigencies rather than peoples’ real needs.”

While Merrifield uses the term as an exploratory phrase rather than a neatly defined concept, for our purposes accountancy urban governance can be understood as the mediation of local fiscal politics through the practices of accounting. In this way, fundamental political questions of societal priorities become transformed through the discourses and practices of the public finance profession so that a social relation (like the debt relation) takes on the appearance of a technocratic relation between those that produce “good fiscal practice” and those that judge it. The accountants involved on both sides of the rating process exemplify Tinker’s (1985: xvi) portrayal of “arbiters in social conflict,” negotiating the contradiction between the debtor municipality and its creditors. Their interactions set the rules of the municipal fiscal game while their search “for technical rather than political solutions to financial problems” (cf. Clarke & Cochrane, 1989: 45) obscures the inherently contested politics of credit rating. Instead, they portray creditworthiness as a merely technical matter of accountancy common-sense and professional insight into the mysteries of the bond market.

Further, the need to ensure creditors that the debt will be honored above all other social considerations, is left unquestioned as in the accountant’s world “financial measures are seen as normal practice and the ‘objective’ monitoring of the organization using financial measures [such as credit rating criteria] is not seen as unreasonable – indeed it is presented as evidence of its ‘rationality’” (ibid: 47). Focusing on the role played by local financial professionals in municipal debt politics while embedding them within the hierarchal relations of the bond market and state regulation (cf. Peck, 2017) becomes key to understand the “roll-with-it” logic of credit

rating. Drawing on interviews with municipal Chief Financial Officers (CFOs), the rest of this section will examine this in detail. First I will, however, introduce my case study of the municipal rating landscape of New Jersey.

4.3.1 Credit rating in New Jersey

The reemergence of the urban fiscal crisis in the wake of the Great Recession has in particular affected older industrial “legacy cities,” which although already struggling took an additional hit in the wake of the Great Recession (Mallach & Scorsone, 2011: 10). New Jersey is a state that has felt this impact, being the home of several older struggling cities like Newark, Camden, Trenton and Paterson. Interested in the role credit rating played in urban fiscal crises I travelled back and forth between such cities and New York, exploring the relationship between the Wall Street based global rating agencies and local municipal actors. Targeting places which bond ratings recently had changed in a downgrading process sweeping the state, my primary data in the form of interviews with municipal professionals is by no means a representative sample, but I was able to follow the credit rating process to a range of places where it has played a significant role, from large struggling cities like Newark and Trenton to the booming city of Hoboken (see Table 1 for a brief overview). These were all municipalities large enough to rely on bond issuing and several of them had recent experience with localized fiscal and rating crises. Harrison, for example, had its credit rating slashed in 2010-2011 when a large sports-led redevelopment project went sour, Paterson’s fractured politics had made it unable to pass budgets on time, and Kearney had been downgraded by Moody’s after an ill-fortuned year forced the town to temporarily seek state aid. My sample also, however, included relatively highly rated cities like Elizabeth.

Municipality	Credit Rating as of 2016 (Moody's, except for Hoboken)	Population (2010)	Median Household Income (2011-2015)
Newark	Baa3 (negative)	277,140	\$33,139
Paterson	Ba1 (negative)	146,199	\$32,915
Elizabeth	Aa3 (stable)	124,969	\$43,568
Trenton	Baa1 (stable)	85,913	\$34,257
Perth Amboy	A3 (no outlook)	50,814	\$44,024
Hoboken	AA+ (S&P)	50,006	\$114,381
Plainfield	A1 (negative)	49,808	\$54,500
Kearny	Baa1 (negative)	40,684	\$60,015
Harrison	Baa1 (stable)	13,620	\$56,713

Table 4.1 List of field sites (Compiled from Moody's and S&P's websites and U.S. Census Bureau (2017)).

While the low-interest rate environment of the summer of 2016 made some municipal officials skeptical as to whether the rating actually mattered for their debt service payments,⁴⁷ most agreed that in the long term they were crucial, since they determined how much of the budget would be eaten up by interest rate payments over the years. As explained by the CFO of Hoboken (who had formerly served in a similar role for the City of Newark):

[The credit rating is] very important especially in terms of how well your bonds are received in the market place and the interest rates you receive. That's the critical thing. *The lower interest rates you can receive, especially on the 20 or 30 year bonds, means a lot to your community and to your tax payers ...* Right now, I think that some people are maybe a little complacent about it because interest rates are so low, so the difference between 1% and 1.5% isn't much, but when you figure it out thorough the amortization

⁴⁷ Interview 15, Business Administrator in Newark, 22-06-2016.

schedule it can be significant. When you are busily trying to put your budget together you're trying to cut down every dollar you can, so even if [the interest payments] is [just] \$50,000 it makes a difference in your budget.⁴⁸

When asked how they had sought to mitigate the impact of credit rating, however, local financial officials tended to avoid the more politicized questions of service reductions and workforce cuts. An exception was the Business Administrator of Newark, who recalled that when he worked in Jersey City he had to reduce that city's workforce by 350 staff, more than 10% of the total, in order to mitigate the effects of bad credit rating.⁴⁹ More typical was the resort to accounting solutions to the problem, such as making sure to clean up balance sheets; bundling smaller debt ordinances for investments with similar "useful lives" together in one debt issuance in order to access the market under more favorable condition;⁵⁰ relying on the bonding power of a County Improvement Authority;⁵¹ or working with financial advisors to refinance debt taken under worse market conditions.⁵²

Here, local CFOs occupy a contradictory position, however, because while representing the interests of the local political body they are also representatives of the accounting profession. This shapes their view of good budgetary practice. Hence, in contrast to the emphasis on the

⁴⁸ Interview 17, CFO in Hoboken, 28-06-2016, emphasis added.

⁴⁹ Asked about strategies to mitigate the effects of credit rating, he argued that "*obviously*, you would want to [reduce] your number of employees. When I was in Jersey City it was unsustainable to think that we were going to be able to keep the same amount of employees and get taxes under control, especially since government is probably 75% employee related costs. Taxes had gone through the roof; their revenue stream became very limited based on the downturn of the economy and we watched very closely the number of employees. They had probably 3300 employees when I started and 2950 when I left. Newark went through something similar, they had more than 4000 employees and we have 3350 employees right now. So, it's about keeping the head count under control because employee pensions, health care and [other] employee related costs are very high" (Interview 15, Business Administrator in Newark, 22-06-2016, emphasis added).

⁵⁰ Interview 20, CFO in Plainfield & Former Director of New Jersey's Division of Local Government Services, 08-07-2016.

⁵¹ Interview 4, CFO at the Hudson County Improvement Authority, 24-05-2016.

⁵² Interview 15, Business Administrator in Newark, 22-06-2016.

politically charged rating conflicts that have dominated the urban political economy literature, financial professionals in these localities were, with few exceptions, reluctant to discuss the political dynamics of their work. Instead they argued for the common-sense nature of the credit rating criteria, sometimes advocating “creative accounting” strategies devised to gain market access and favorable interest rates.

In instances when pushback against the agencies occurred, this typically came from non-financial municipal professionals,⁵³ or took the form of disputes over the technical matters in the rating process. Both the CFOs of Harrison⁵⁴ and Perth Amboy,⁵⁵ for example, complained that the agencies were unable to understand New Jersey municipalities, primarily because municipal accounts in the state do not follow General Accepted Accounting Principles (GAAP). Kearney’s CFO also criticized Moody’s inability understand his small blue-collar suburb which, although in temporary reception of “Transitional Aid” from the state, was clearly a quite different animal from larger cities like Newark and Camden whose long-term financial challenges rendered them reliant on such aid. As he explained:

The rating agencies ... don't look at towns individually. They like to lump us together... We [only] took the Transitional Aid for 2014-15, but these rating agencies what they do is that the minute they see you in that program they come to the conclusion that ‘you guys are basically junk and you can't manage your finances’ and they put us in that category like Camden, Newark, Paterson and they fail to realize the big difference

⁵³ Newark’s Business Administrator, for example, “dislik[ed]” the rating agencies because although the city had “made great strides in improving the city’s fiscal conditions,” Moody’s (in particular) ‘extremely conservative approach’ meant that they were still on the credit watch list (Interview 15, Business Administrator in Newark, 22-06-2016).

⁵⁴ Interview 7, CFO in Harrison, 01-06-2016

⁵⁵ Interview 9, CFO in Perth Amboy, 06-06-2016

between those cities and this community.⁵⁶

These technical disagreements aside, local CFOs tended to naturalize the creditworthiness criteria of the rating agencies as good financial practice, internalizing them as administrative common-sense. Next I will explore this.

4.3.2 Discourses of creditworthiness

The internalization of the politics of creditworthiness was most starkly exemplified by the Finance Director of Elizabeth (New Jersey's highest rated major city) when asked to account for their successful track record with the agencies. While emphasizing new economic development projects and the administration's long experience, this respondent gave particular credit to his continuous "close dialogue" with the agencies. Outlining how he made sure to keep them updated on the fiscal health of the community, he stated that "*I consider them another boss, another entity I have to report to. I report to the mayor, I report to [the] council, I report to directors [and] I keep Moody's informed also ... because they are the bond raters and it translates to a lot of dollars.*"⁵⁷ This vivid portrayal of the rating agencies as "another boss" was contested by other CFOs, however, but who saw the agencies "almost as auditors" or "advisors," as:

Somebody else that you in effect have to cater to, you have to take their recommendations seriously and you have to think of when you are structuring your budgets and financial statements. What impact is it going to be when the rating agencies look at this, when are we going to undertake these capital projects, how is this going to

⁵⁶ Interview 8, CFO in Kearny, 03-06-2016.

⁵⁷ Interview 6, Director of Finance in Elizabeth, 27-05-2016.

appear in our records?⁵⁸

This is a clear example of how, as argued by Lemoine (2017: 5), senior professionals become crucial for inserting the monitoring practices of credit rating into the daily workings of government administrations where “the criteria and modes of evaluation promoted and shared by private investors and financial actors transform the [local] state’s routine representations and practices as they adapt to these modes of calculation.”

By presenting Moody’s and other rating agencies in terms of “another boss” or an “advisor,” these financial professionals naturalized the rating agencies as unproblematic players in local administration, while reinforcing the notion that municipal debtors should monitor themselves according to these standards. In other words, perform a politics of creditworthiness. This often took the character of a general acceptance of the rating criteria as public-finance common-sense. Probed on the impact credit rating has on local administrations, the CFO of the City of Plainfield argued that: “to the extent that the guidelines that the credit rating agencies are looking for [represent a form of] *financial responsibility*, I think that it informs policy within a lot of municipalities.”⁵⁹ Similarly, while the rating agencies themselves repeatedly emphasize that their rating reports *do not* offer policy recommendations for improving the rating but simply indicate possibilities for rating change,⁶⁰ local financial professionals often took these as advice

⁵⁸ The CFO of Hoboken, for example, pushed back on the notion of the agencies as a boss and suggested the less strong term “advisor” instead, arguing that “I don’t see them maybe not as a boss but certainly as somebody that you want to influence in the right way ... to me they are almost like auditors ... So, I think it’s more advisory than being a boss, but I could see why you would think that because it’s obviously somebody who’s suggestions and recommendations you take seriously, work to improve to meet” (Interview 17, CFO in Hoboken, 28-06-2016).

⁵⁹ Interview 20, CFO in Plainfield & Former Director of New Jersey’s Division of Local Government Services, 08-07-2016, emphasis added.

⁶⁰ Interview 3, rating analyst, 18-05-2016.

(or “guidelines”) for future improvement.⁶¹

In particular, the concern of the part of the agencies with long-term financial planning and “healthy surpluses” so as to ensure a “budgetary flexibility” and to insure against unexpected events was seen as a generalizable principle of financial prudence. As explained by the CFO in Elizabeth:

The whole key for Moody's is keeping the surplus balance and generating surplus on going ... If you dip too low, then you lose your bond rating ... So, we're very candid with Moody's, we tell them 'ok, we're going to have problem in this particular year and we have reserves that we could tap into that we have built up over the years in order to maintain our surplus balance.' The other thing that Moody's places very highly is the ability to raise taxes, so we are raising taxes as much as we [can], 2%, 3%, 4%, whatever, over the year, plus we will be tapping into our reserves until we have *stable surplus balance*, which means that in some cases we're going to be downsizing some of our staff over the next few years. There are a lot of retirements planned to police and fire and, in some cases, that's not going to be replaced. We're going to tighten up on our cost controls and on our staffing ... These are the balances that are needed to enjoy a rise of [receipts from] taxes and to keep the surplus up there.⁶²

⁶¹ The CFO for Hudson County Improvement Authority put this most clearly:

Question: So how can you break out of a vicious circle of credit downgrades?

Answer: Generally in the rating reports they will tell you the things that had an upward pressure on a rating and a downward pressure on rating and that's what they are looking for and you got to try to implement that as much as you can...

Q: So the rating reports the give some guidance?

A: Yes they do, they actually do

Q: So would you look at that and follow the suggestions?

A: Yes, I would say that anybody that is looking to move their rating they are going to have to look at those and it may be not an easy fix. Maybe they are going to say that the debt load is too high, that means you are going to have to try not to issue and that isn't always easily done ... but if that was a recommendation you got to have to start looking at the other things, possibly getting grants” (Interview 4, CFO in the Hudson County Improvement Authority, 24-05-2016).

⁶² Interview 6, Director of Finance in Elizabeth, 27-05-2016, emphasis added.

This proactive approach to financial planning, including the use of five-year financial forecasting, was favored by Moody's (2014b: 1) which cited "the city's closely managed financial operations which have maintained healthy and stable financial reserves that are augmented by funds in external accounts" as key to their 2014 upgrade of its GO-bonds to Aa3. Reflecting on Paterson's rating experience, on the other hand, its former CFO argued that the city was "unable to plan, *it got a reactionary government which the bond market hates*. [The rating agencies] like [it] when you're in sound financial condition and plan for contingencies. They want to be able to say to people 'your money is safe, you are going to get your money back', that there's a good degree of certainty."⁶³

This view of the importance of financial planning for budgetary flexibility has become a governing axiom for many municipal finance professionals. As explained by Hoboken's CFO:

[The rating agencies) are big on surplus generation, and not using too much of your surplus ... [you need to make sure that you have] the ability to show that you have that kind of *flexibility in your finances* where you have some surpluses ... so that if something crazy with the post-employment benefits, pension system or the state's ability finance state aid because of their own pressures [you are able to handle that].⁶⁴

This planning for "flexibility" is further being promoted by the Government Finance Officers Association (GFOA) which emphasize five- or ten-year financial planning as key to resilient public finance and due recognition on the rating scale (Kavanagh, 2011). Long term planning for

⁶³ Interview 19, Former CFO in Paterson (now retired), 07-07-2016, emphasis added.

⁶⁴ Interview 17, CFO in Hoboken, 28-06-2016. As further emphasized by the CFO of Harrison "I think the biggest thing [in terms of good fiscal management] is really setting up reserves. Those are the tools that are set up for towns to deal with [contingencies]. There's a lot of things that even if you can't predict that are foreseeable. If there is a big change whether it's with pensions or with health insurance or with payouts or you are going to have an exodus of people, you need to be able to deal with that" (Interview 7, CFO in Harrison, 01-06-2016).

budgetary flexibility stands as an expectation of prudent of financial stewardship, both as a credit rating requirement and a code of the public finance profession. As discussed in previous chapter, however, the rating agencies understanding of budgetary flexibility and resilience is not politically unproblematic. This because while they rate municipalities in accordance their ability to service debt in the face of contingencies such as economic downturns or state funding cuts (Fitch, 2016; Moody's, 2016a; S&P, 2013), the central underlying assumption is that responsibility for this flexibility lies with the municipal debtor. The debtor should be able to neglect social needs that compete with debt repayment while the promise to the bondholders is an absolute, inflexible commitment.

By internalizing these guidelines for fiscal health and flexibility, in their role as arbiters in the creditor-debtor social conflict (cf. Tinker, 1985), local CFOs also naturalized the discourse of creditworthiness, effectively melding the monitoring practices and performance standards of the rating agencies with the internal procedures and priorities of municipalities. Consequently, the key to a good credit rating becomes the constant self-policing of local finances with the agencies in mind,⁶⁵ building up surpluses to ensure that the ability to service debt would be resilient to future political-economic contingencies, while “addressing the needs of the community in a responsible fashion.”⁶⁶ That is, in a way that is responsible with regards to the city's creditworthiness although this might contradict its workforce and collective consumption responsibilities.

⁶⁵ As Elizabeth's CFO puts it: “what I like to do is to keep in *constant contact* with Moody's. Anything good or anything bad I like to report to them. I'm constantly sending them estimates on our surplus status, what it's going to be for year round and what it's going to be the half year round, that type of thing. Every time anything major comes up I let them know. If it's good it's one thing, if it's bad I tell them how we are going to cure it ... *I put a lot of time in answering to Moody's*” (Interview 6, Director of Finance in Elizabeth, 27-05-2016, emphasis added).

⁶⁶ Interview 20, CFO in Plainfield & Former Director of New Jersey's Division of Local Government Services, 08-07-2016.

Another way that this discourse of “responsibility” was (re)produced concerned the widespread resentment among CFOs of what was perceived as too strong “political” involvement in fiscal affairs, something they believed should be left to the professionals. Many of the challenges municipalities face in terms of credit rating were in this way framed as problems of over-politicization of revenue collection or service provision, of an encroachment of the “irrational” world of politics into the rational practices of public finance administration. One example of this was presented by the former CFO of Paterson. During my field work, Paterson’s budgeting process had been severely interrupted by a struggle between the mayor, who was seeking to raise property taxes, and elected councilors, who were resisting this (Pinto, 2016b). As a consequence, the city had to shut down all non-essential government services for a day and Moody’s (2016d) reported this as a “credit negative” just a few days later. While Patterson had long been struggling with a declining tax base, in explaining the city’s long brewing fiscal crisis the former CFO kept coming back to the irrationality of the local administration’s unwillingness to introduce user fees for its recreational facilities. This was something which could give them “millions of dollars” but which was politically too sensitive. So, while the city had brought in a financial consultant suggesting ways to increase revenues and cut cost, these recreational facilities were still draining budget resources because “politics drives the boat, Paterson is a political city.”⁶⁷

This way of framing politics as a problem was based on a sharp demarcation between the local electoral process (“politics”) and everyday financial practice (“administration”), two zones that were rendered incompatible with each other. In this sense, the logics of financial

⁶⁷ As he explains: “In my mind there is a basic premise that there are core services that should be funded by taxes while others pay for themselves ... I’m shocked how many towns don’t [charge fees for e.g. public pools] ... The City of Paterson does not charge for anything recreational, it’s normal, it’s politically great, [but it] doesn’t help the city one bit, [because it] drains resources” (Interview 19, Former CFO in Paterson (now retired), 07-07-2016).

technocratic administration are seen to override “political” consideration, the latter being regarded as disruptive or even illegitimate. Such view was widespread among the CFOs and credit rating analysts alike, representing a shared discourse of technocratic public finance common-sense. Reluctance on part of elected officials to raise taxes⁶⁸ or to restructure public finance through the introduction of user fees were seen as impediments to a higher credit rating. Indeed, the CFOs often saw it as their duty to be the guardians of financial prudence *against* the local political body. In a city like Newark where local councilors “want to use every penny” even going so far as to “very busily hide [budget surpluses] in the financial record.”⁶⁹ This technocratic approach to fiscal politics does not simply develop spontaneously in the credit rating agency-CFO interactions, however, but is conditioned by the state’s regulation of municipal finance. Next I will therefore turn to the institutional arrangements in which the local politics of creditworthiness are embedded.

4.3.3 “They save us from ourselves:” the role of state oversight

While American municipalities have relatively high levels of autonomy they are ultimately “creatures of the state,” subject to rules and regulations laid out by state governments. Consequently, creditworthiness is not just co-constructed by localized municipal officers and globalized rating agencies. Rather, it is continuously mediated through the municipal finance regulation of the state, where concerns around local fiscal health allow for a level of constrained

⁶⁸ The CFO of Kearny, for example, points out how local political dynamics provide an obstacle in the way of the financial professionals’ quest for creditworthiness: “the rating agencies like having tax increased because for them it’s basically additional revenue, so if you tell them that you’ll have a 10% tax increase they will love it because it allows you to build up surplus, it allows you to build up reserves. Getting the mayor and council to do a 10% increase is going to be impossible. I’ll be lucky if I can get a 2-3% [increase]” (Interview 8, CFO in Kearny, 03-06-2016).

⁶⁹ Interview 17, CFO in Hoboken (formerly Newark), 28-06-2016.

local autonomy that would be unthinkable in most other policy fields in a country ostensibly committed to “home rule” (Nickels, 2016). This particularly holds true for local debt financing which, as Sbragia (1996: 85) points out, “is characterized by a more inflexible set of controls than other areas of local government activity.” In the post-recession “return” of the urban fiscal crisis this state control has moved to the center of attention. While critical commentators, such as Peck (2014), have argued that states are essentially “pushing austerity” downwards where budgetary retrenchment politics under fiscal federalism is characterized by the *offloading* of crisis onto the state system and the subsequent *downloading* of that crisis onto its lower tiers, many legal scholars and policy makers see the states not as the originators of local fiscal stress, but as its resolvers. Investigating crisis narratives in four cities, Hinkley (2017: 2133) has argued that this belief has displaced the origins of the financial crisis away from the market onto “irresponsible” local governments and, with the need to make “tough decisions” of adjustments, “the growing exercise of state power over cities has been a defining feature of this recession.”

Most significantly, attention has been on particularly interventionist programs such as the municipal financial “emergency management” laws existing in 13 states, where the state has the power of putting local governments under the control of a state-appointed control board or receiver (Scorsone, 2014). As essentially overruling principles of home rule, these laws have sparked heated debate among legal scholars, one critic of whom characterizes Michigan’s and Rhode Island’s particularly aggressive take-over laws as “an intrusion so deep into local governance that it constitutes temporary dissolution of local democracy” (Anderson, 2011: 622). Conservative proponents like Gillette (2014), however, are more positively likening fiscal take-over with the extraordinary appointment of dictators in the Roman republic. Indeed, according to this increasingly hegemonic view the spill-over effects of localized fiscal crisis on other

municipalities' credit rating and access to bond markets legitimate state take-over through financial control boards or receivers. Furthermore, "immunized" from local "interest groups" by being state appointed, these are promoted as the best instrument to drive through necessary long-term structural changes since "the dictatorial character of take-over boards allows them to ignore, or at least resist, interest that have exercised disproportionate influence during periods of normal politics and that drive expenditures inconsistent with majoritarian preferences" (Gilette, 2014: 1435).

In comparison to, on the one hand, municipal bankruptcies that essentially shifts risk and cost of fiscal stress to bondholders and, on the other hand, creditor remedies shifting them to local tax payers, Kimhi (2008: 656) has therefore argued that the state should be seen as the "superior risk bearer" when it comes to municipal finance and that its close involvement is preferable because of an ability to intervene in fiscals crisis that both bondholders and local residents lack. Hence, Kimhi (ibid) argues that while the legal community have primarily been concerned with the spectacular moments of bankruptcy, permanent state finance boards provides a more effective means to resolve local fiscal crisis. This is particularly the case because a finance board can be proactive, something that "sends a signal to the credit markets and to the credit rating agencies: the state show its commitment to preventing local crisis, and its refusal to let municipalities default" (ibid: 678). Indeed, as Gao, Lee, & Murphy's (2016: 3) quantitative study suggests: "investors prefer to purchase local municipal bonds from states that proactively asses municipalities that exhibit signs of stress."

New Jersey is often held up as a particularly good example of such proactive financial oversight, as the state, famously, refuses to allow municipalities to file for bankruptcy and default on their debts (cf. Peck, 2017). This policy was particularly clearly articulated in a 2014

panel discussion on state oversight and municipal defaults at the annual conference of the National Federation of Municipal Analysts (NFMA) where Thomas Neff, then director of New Jersey's Division of Local Government Services (DLGS), outlined the state's approach to local public finance, centered on a refusal to allow "municipalities to go bankrupt or walk away from their obligations" (Lipitz, Fehr, Neff, & Kannel, 2015: 63). While New Jersey indeed has the possibility to appoint a receiver/emergency manager in particular distressed cases, this is not necessarily the most effective method since it can send negative signals to the bond market; as demonstrated by the rating downgrade Atlantic City received when former Detroit emergency manager Kevin Orr was appointed to help restructure the city's finances in January 2015 (Peck, 2017). Instead, at the heart of New Jersey municipal finance regulation are publically much less visible institutions: The Local Finance Board (LFB) and the Division of Local Government Services (DLGS).

With origins in the Municipal Finance Commission (MFC) of 1933 as well as the Local Government Supervision Act (LGSA) of 1947, passed in response to widespread municipal defaults in the aftermath of the Great Depression, the New Jersey's Division of Local Government Services is a state agency operating under the authority of the governor-appointed Local Finance Board with responsibility for monitoring municipal finance (Nickels, 2016). Overseeing the finances of 21 counties and 566 municipalities (Coe, 2008: 762), the DLGS and the board get involved in moments of crisis and has with the Municipal Rehabilitation and Economic Recovery Act of 2002 (MRERA), designed to allow intervention in Camden's fiscal crisis, strengthened powers to take over local governments if deemed necessary (ibid). Principally, however, they take on the more proactive role advocated by Kimhi (2008), relying on laws requiring municipalities to regularly report their finances and allowing regular points of

intervention where they, for example, “may order any item required by law to be raised by taxation for municipal, county or school purposes which has been omitted in whole or part from any budget to be included in the budget” (N.J.S.A., 2016c: §52:27BB-24). This close monitoring of “each budget in detail, line item by line item”⁷⁰ makes New Jersey unique. Indeed, as explained by one former director of DLGS:

[New Jersey is] the only state that requires a state agency to approve the budgets of all local units. Every county, every local authority, every fire district, and every board of education. That provides bondholders assurance that things will be budgeted as they are supposed to be and our agencies will remain solvent so they have enough money to repay the debts.⁷¹

While this budget scrutiny used to take place annually, since the 1990s the DLGS has been downsizing its staff so that for qualifying municipalities that meet certain performance criteria they now only have the capacity to do so every third year, relying on self-reporting in the off years (Coe, 2008). Cities that do not meet these criteria, however, are still under close scrutiny. Most significantly the LFB has the authority to impose “special restraints upon municipalities in, or in danger of falling into, unsound financial condition and in this way forestall serious defaults upon local obligations and demoralize finances that burden local taxpayers and destroy the efficiency of local services” (N.J.S.A., 2016c: §52:277BB-54). With these cities, the LFB receives far-reaching powers.⁷²

⁷⁰ Interview 20, CFO in Plainfield & former Director of New Jersey’s Division of Local Government Services, 08-07-2016.

⁷¹ Interview 1, Former Director of New Jersey’s Division of Local Government Services, 06-05-2016.

⁷² Including: powers to limit the city’s ability to issue bonds, make purchases or enter into contracts, mandate to approve collective bargaining agreements, ability to dismiss managers and employees and to fix their hours and

In addition to these extraordinary cases, however, also non-distressed cities that want to exceed the legal debt limit of 3.5% of their equalized property value needs to seek approval from the board. Applying to the board, the debt issuing plans are scrutinized with regards to its effects on local finances and homeowners and the LFB has the right to refuse approval if it deems them unsustainable. As another former head of DLGS explains:

Let's say you have a mayor that is adamant he is not going to raise taxes, but yet he wants to spend and maybe what he has done is that he doesn't want to raise taxes and he wants to borrow and he doesn't have the ability to pay back what he is borrowing. An application like that would not pass because *we are not going to allow him to borrow if he doesn't have a plan on repayment*. So, as part of the application we will take a look at 'here's your plan, what's the impact on the residents, what's the impact on business', because *you don't want to see them make such bad decisions that they jeopardize the financial health of the community*.⁷³

In this sense, in addition to the co-construction of accountancy common sense in the interactions between local financial professionals and rating agencies, the state takes upon itself the role of the paternalistic protector of “good fiscal practice” of municipalities that cannot help themselves but to transgress the rules of creditworthiness (whether this is with regards to a political unwillingness to raise taxes or too lax spending habits). And with the threat of state takeover always looming in the background, habits of debtor self-policing become firmly instituted in the local political culture as local government representatives “are very hesitant to do anything that

terms as well as to nominate a Fiscal Control Officer to be appointed, authorize liquidation of municipal liabilities, restrict expenditure beyond available cash or, if the political body refuses to allow for this, directly take over the city's administration (N.J.S.A., 2016c).

⁷³ Interview 20, CFO in Plainfield & former Director of New Jersey's Division of Local Government Services, 08-07-2016, emphasis added.

would *bring in the state*, like missing a [debt service] payment.”⁷⁴ Just as with regards to the rating agencies, while some local CFOs would be critical of the LFBs “very conservative” approach⁷⁵ others welcomed state budget oversight as necessary controls that “save us from ourselves.”⁷⁶ This co-construction of creditworthiness is, however, not a smooth, unproblematic process. Rather in the context of austerity urbanism’s new normal and with no signs of structural improvement of municipal finances, technocratic accountancy solutions tend to see increasingly diminishing returns. Here, the techniques adopted to achieve good credit rating start to not only contradict other policy goals such as low taxes, but also their own purposes. I will discuss such limits to creditworthiness next, unpacking two episodes of failure in the regime of accountancy urban governance.

4.4 Limits to creditworthiness: self-fulfilling ratings and trickle down rating crisis

For fiscally struggling cities, credit rating (in the words of a former rating analyst) “kicks you when you’re down.”⁷⁷ Economists refer to this as the *procyclical* nature of credit rating and it has provided the basis for one of the discipline’s most significant critiques of the agencies, prominently put forward by Ferri et al (1999) with regards to role of their role in exacerbating the 1997 East Asian crisis. Related to the widely-held buy-side belief that rating agencies are

⁷⁴ Interview 4, CFO in the Hudson County Improvement Authority, 24-05-2016, emphasis added.

⁷⁵ Kearney’s CFO, for example, argued the seeking permission for bond ordinances as a Transitional Aid community could be an “administrative nightmare” while “sometimes they don’t look at the uniqueness of the project. For example, if you are doing a park and playground improvement for \$500,000 they will just look at it [and say] ‘oh, you are getting Transitional Aid, why are you putting money into this?’ not realizing that that part of the community might not have seen a park and playground improvement in the last 20+ years ... so sometime they fail to go beyond the numbers” (Interview 8, CFO in Kearny, 03-06-2016).

⁷⁶ Interview 5, Director of Finance in City of Trenton, 25-05-2016. Similarly, Perth Amboy’s CFO credits the state putting “their foot down” as central to initiating a move away from long-term habits of using “budget gimmicks” to more sustainable local financial practices (Interview 9, CFO in Perth Amboy, 06-06-2016).

⁷⁷ Interview 18, former rating analyst now working at major bank, 05-07-2016.

generally too slow to react⁷⁸ the notion of the procyclical nature of ratings holds that while a crisis indeed might catch the rating agencies off-guard, this subsequently gives them “an incentive to become more conservative, so as to recover from the damage that these errors caused them and to rebuild their own reputations” (ibid: 336-337). Initial tardiness, or conservative incrementalism, with governments precede sharp downgrades which effectively amplify fiscal stress by further increasing borrowing costs. Rating agencies can in this way magnify fiscal and macroeconomic cycles by being unduly generous in good times only to “overly downgrade” in bad times (ibid: 347). This, ultimately, means that rather than comments from the sideline, ratings are performative. That is, the rating agencies do not just report on fiscal cycles but their judgments foment and amplify crises. In particular, by cutting off necessary market access for fiscally strained governments whose very ability to manage their outstanding debt might be dependent on continuing short-term borrowing. This was something the Town of Harrison, NJ got to experience in 2010-2011 when Moody’s nine notches downgrade brought its credit rating down to Ba3-“junk” levels, described by one commentator as “on par with Detroit and one notch below Portugal” (Beeson, 2011).

Despite the professional predicament to manage fiscal crisis through more or less creative accounting tricks, most local financial professionals are well aware of the relative limited long-term effect of these. While they might think that a particular rating judgment is too harsh, they usually do not contest the fact that their demographic profile or economic development prospects do not speak in their favor. As the grimly realistic CFO of New Jersey’s long struggling capital Trenton puts it:

⁷⁸ See Chapter 3.

There's really not much you can do, we need more services, you can't lay anybody off, you can't downsize the budget, and until we have some legitimate redevelopment we are not going to increase the tax base. So, it's really a catch 22 ... The numbers don't support whatever optimism that we try to have ... It's not much we can do about it, until we get some redevelopment we are going to continue to struggle.⁷⁹

Similarly, Paterson's former CFO would emphasize the crucial need for local economic development since cutting back on expenditures, introducing user fees, cleaning up balance sheets, selling bonds through the County and other accounting tricks only go so far in a stagnating local economy. As he explains, "the only thing controllable is the budget and taxes and you risk other things by cutting budgets and raising taxes, so the answer has to be redevelopment."⁸⁰ Redevelopment itself can, however, also be detrimental for a municipality's quest for creditworthiness, as experienced by Harrison, a suburban town of 13,620 people (U.S. Census Bureau, 2017) located in New Jersey's Hudson County just across the Passaic River from Newark and a short Path Train ride from New York City.

Struggling to reinvent itself after deindustrialization, the town's median household income stands below New Jersey's average (\$56,713, compared to the state's \$72,093, (ibid). In 2010-2011 the town experienced a significant fiscal and credit rating crisis. It was, however, not so much its long-term socio-economic profile that had brought this crisis to the town, but a soccer stadium development stalled in the wake of the 2007-2008 recession. In 2006 the town administration had taken help from the Hudson County Improvement Authority to issue

⁷⁹ He continues: "I think [the rating agencies] are fair to us. They can penalize us more, but I they see we are working hard at it and trying to control costs. But we are stuck at this point. Demographics and lack of ratable growth doesn't help any. They treat us well. They understand what we are trying to accomplish. They are responsible for the rating and they have to give a fair rating... It's hard to be positive when you don't see any growth, but they realize we manage it the best we can ... they think we are well managed and we get points for that" (Interview 5, Director of Finance in City of Trenton, 25-05-2016).

⁸⁰ Interview 19, Former CFO in Paterson (now retired), 07-07-2016

redevelopment bonds of \$39.4 million to buy land on which to develop a 25,000 seat stadium for the New York Red Bulls soccer team (Beeson, 2011). Designed as “triggers to bring about other redevelopment” whose PILOTs (payments in lieu of taxes) would be used to for debt service,⁸¹ the Harrison bond issue was nothing extraordinary. It was merely another “entrepreneurial” bet on the future of the kind Harvey (1989a) identified 30 years ago, trying to capitalize on a nationwide push within *Major League Soccer* to move teams to purpose-built, often suburban, stadiums, (deMause, 2015). But it was a bet that was not well placed in this instance.

Eager to attract the soccer team, Harrison gave the Red Bulls a sweetheart deal, allowing them to rent the stadium for \$1/year in addition to \$125,000 in annual PILOTs, because the plan being that property development around the stadium would spur economic growth, and thereby subsidize the \$3 million requirement for annual debt service payments. With the financial crisis of 2007-08, however, the stadium was delayed, expected additional redevelopment halted and the additional PILOTs never came through.⁸² Having to rely on short-term borrowing to make up for this revenue shortfall at the same time as having their state aid cut by \$4.7 million in 2010, Harrison effectively deplete its reserves in 2009-2010 and reduced its budgetary surplus from \$3.9 million to \$26,000 (ibid: 2). When the debt service for the stadium redevelopment then came online the town found itself stuck in what its CFO calls “the perfect storm.” On top of this, the Red Bulls renegaded on their agreement, appealing their PILOTs and withholding the payments. With declining collection rates, but still needing to redistribute the mandated funds to the local school district and Hudson County, the town was forced to issue short-term notes just to meet its first \$3.1 million debt service payment. This prompted Moody’s to downgrade their A1

⁸¹ Unless stated otherwise, this account is drawn from a 01-06-2016 interview with Harrison’s CFO

⁸² Rather than receiving the projected payment increases of \$2.3 in 2008 to \$11.5 million in 2011, the town only collected \$2.98 million 2008-2010 (Moody’s, 2010)

GO-rating to Baa1 and assign a “negative outlook,” citing “the town’s likely difficulty in meeting debt service obligations over the near-term without borrowing in an environment of limited revenue growth” (Moody’s, 2010: 1).

Going from A1 to a Baa1 rating is a significant dip, but Harrison was still rated as investment grade. Only five months later, however, another dip to Ba3 followed (Moody’s, 2011). In the words of Moody’s 2011 rating judgment, the fall-out of the stadium redevelopment had produced “outsized enterprise-related risk” leading to a “sharp erosion of financial flexibility,” where Harrison not only had abnormally high levels of debt service (16% of the 2011 budget), but also exhibited weak liquidity, dependence on debt financing for cash flow and, crucially, *limited market access* (ibid: 1-2). This poor access to capital markets had become notable in early 2011 when the commercial bank that previously bought Harrison’s short-term notes suddenly declined to buy any more. Thus, the town only managed to receive one other bidder on each note issue when it went out for, first, Bond Anticipation Notes (BANs) in March and, later, Tax Anticipation Notes (TANs) in April (ibid). Since this short-term borrowing was central for Harrison’s ability to pay the annual debt service on its outstanding stadium redevelopment debt, the agency deemed this poor market access so significant that its second downgrade brought the town down below the “investment grade”-threshold (ibid).

In their characteristically dry tone they argued that “[w]ith only one bidder on each note from the same investor, uncertainties arise around the town’s ability to secure access to the market in fiscal 2012 and ahead. Given stressed fiscal 2012 cash flow projections, we believe a failed TAN sale in 2012 would severely challenge the town to make timely debt service without

alternative funding” (ibid: 2).⁸³ While paying \$250,000 in interest payments on TANs alone in 2012, this final downgrade would provide the catalyst for a through restructuring of Harrison’s budget where the municipal finance department had to use all its inventiveness to reestablish its budgetary “flexibility.”⁸⁴ Debt management became front and center of local politics and slowly the town managed to regain the confidence of the rating agencies, being upgraded each year from 2012 until it eventually achieved a Baa1 rating in November 2016. In this sense, Harrison exemplifies the shift from entrepreneurial to financialized urban governance logics highlighted by Peck & Whiteside (2016; see also Davidson & Ward, 2014). Entrepreneurial speculation in the bond market was predicated on the need to reinvent a struggling local economy, but this backfired as real economic growth contracted, refocusing urban administrators onto the defensive management of debt rather than proactive strategies for growth.

The catalytic 2011 rating judgement was not without its ironies, however, because while citing “a recently demonstrated poor access to the capital markets” as a central negative rating factor (Moody’s, 2011: 1), it was Moody’s very own downgrade in 2010 that had crucially reduced this market access by making investors less willing to bid on the town’s 2011 notes. As Harrison’s CFO explains in frustration when reflecting on the agency’s continual emphasis on market access, “one [rating] indicator is access to the market, but *how can I access the market if*

⁸³ This despite the town’s actual ability (as a complement to the one private bidder) to access financing through the state and the Hudson Improvement Authority. The town’s CFO explains: “[in 2011] we had to go out for TANs and I’m sure we had to roll-over BANs because we only permanently finance in 2012. It was difficult to secure financing for those things, but we have tools, right? We have the Hudson County Improvement Authority that has a very good note pool program so we were able to utilize that resource. We had a short cash deficit because of the timing of the roll-over of the stadium debt and the state was able to bridge that for us and we did have private financing for rolling over BANs and some other things. Like I said, our credit rating didn’t speak much for us ... but we accessed it, we were able to do it.”

⁸⁴ This was achieved by building up reserves for debt service and possible further tax appeals from the Red Bulls, reducing the municipal workforce by 37% (Larkins, 2014: 20) through layoffs and early retirements, raising taxes with \$1400 on the average household, renegotiating collective bargaining agreements to reduce long-term benefits as well as seeking help from the state in form of financial aid and admittance to its municipal credit enhancement program.

you tell them that I'm not investment grade? It's like what comes first, the chicken or the egg? You're the ones that are representing to the market that I'm no good, so how can you now judge me on what my access to the market is?" So, while Harrison's CFO is now positive that the town is in a better financial position, its 2010-2011 rating crisis strikingly demonstrates the limits to the politics of creditworthiness. It shows how rather than a neutral process guiding local fiscal policy in accordance to best public finance practice, credit ratings are routinely self-fulfilling and pro-cyclical, kicking you when you are down.

In this case, in the absence of the projected PIOLTs from additional redevelopment, Harrison's very ability to ensure timely repayment of its outstanding redevelopment bonds was predicated on its short-term access to financing vehicles. As such, when Moody's in 2010 penalized the town for relying on these short-term notes it effectively limited the market access so crucial for its future ability to honor its long-term debt. By dropping its rating below investment grade in 2011, Moody's effectively punished Harrison for the agency's own rating judgment. The town received a poor credit rating because as already poorly rated it was struggling to find investors for its debt. Next, I will turn to another instance where the technocratic politics of creditworthiness has failed, illustrating the limits to state involvement in local finance.

Previously in this chapter I have discussed the role of state *oversight* in the co-construction of creditworthiness in New Jersey's municipal-finance system, where focus has been on the tight regulation of what local actors can and cannot do in terms of debt and local finances more generally. The role of the state extends beyond the imposition of extra-local control, however. Rather, as these systems of control are closely attached to programs that often *do* work in the interest of local administrations, they are indeed paternalistic in the true sense of

the word, although not without their contradictions. The case of Harrison's 2010-2011 rating crisis illustrates this clearly in that while the crisis was overdetermined by a state-wide consolidation of municipal aid,⁸⁵ when the rating crisis broke out the state worked closely with the local administration to reconstruct its creditworthiness. Appointing a "fiscal oversight officer" to help restructure its finances, having the director of DLGS assist in meetings to boost the confidence the rating agencies and helping the town to bridge a temporary cash deficit with a short-term interest-free loan, New Jersey's strong financial oversight model was ultimately instrumental in regaining the confidence of the bond market. It was one financial trick, however, that stood out as central for the town's ability to regain market access and refinance its outstanding redevelopment bonds in 2012. This was the so called Municipal Qualified Bond (MQB) program. This program is concerned with enhancing the creditworthiness of municipalities under stress, but in recent years it become central in the transmission of rating crisis across the state's municipalities. In this sense, it provides another illustrative case of the failures accountancy urban governance.

Similarly to how credit rating, as illustrated in the case of Harrison, actually can aggravate fiscal stress rather than just report on it, in recent years New Jersey's municipal finance regulation has shown signs of aggravating the credit rating pressures that it was designed to alleviate, exhibiting at least three kinds of failure. Firstly, while the politics of local fiscal stress has traditionally occupied the closed quarters of the LFB's monthly meetings and the bureaucracy of the DLGS, the most serious recent case of municipal financial distress, Atlantic City, has occupied front and center of state politics. It has taken the public character of a highly

⁸⁵ Harrison went from receiving \$5.3 million in Special Municipal Aid in 2009 to only \$1.5 million in Transitional Aid in 2010 as well as a cut in Consolidated Municipal Property Tax Relief Aid from \$1,049,894 to \$511,940 (Larkins, 2014: 2).

politicized battle where Republican governor Chris Christie has been pitted against Democratic state legislators and local politicians. Sparked by a nation-wide overcrowding of the casino and gambling market and involving threats of a bankruptcy filing, appointment of emergency management and eventually full on state takeover (Peck, 2017), the Atlantic City crisis illustrates a form of failure predicated on the state's digression from its own system of local finance regulation. As explained by a former director of DLGS:

[In New Jersey] we are well respected for our [financial oversight model], respect earned over 70 years, and now thrown out of the window. *We violated our own rules*, the politics got deeply involved which it hasn't been before. You never had this kind of drama before. The system worked. Procedures and rules made it work ... and we can't predict now what the short, medium and long-term effect will be on the state and its reputation.⁸⁶

The rating consequences of this digression from established technocratic, depoliticized procedures has been the cause of great concern for the integrity of New Jersey municipal credit in the bond market and a fear among local representatives that the state's handling of Atlantic City is going to have negative spill-over effects on local ratings state-wide.⁸⁷

If the case of Atlantic City represents a divergence from the State's own rules, a second kind of failure occurs when the quest for creditworthiness runs into other state regulations that

⁸⁶ Interview 1, Former Director of New Jersey's Division of Local Government Services, 06-05-2016, emphasis added.

⁸⁷ An representative of New Jersey League of Municipalities stressed the sensitivity of municipalities to how the politicization of municipal finance in the case of Atlantic City will affect the State's bond market more generally, arguing that: "if it looks like the state isn't working hand-in-glove with communities who are in trouble, then both the [rating] agencies and investors are going to get more nervous about New Jersey municipalities ability to repay [their debt] which will drive up their costs of borrowing... Sometimes [the state] want to use political leverage to get municipalities to do something, state legislators will use their language to force municipalities to do one thing or another, but they have to be careful when they talk about this because it makes the rating agencies or the underlying investors nervous of whether New jersey municipalities are going to be continuing to be under the scrutiny that they are under now and continue to bet on the support and resources and guidance that they are getting from the state" (Interview 11, Director of the New Jersey League of Municipalities, 09-06-2016).

contradict this. One example of this is the relationship between limitations on tax increases and the rating agencies emphasis on “budgetary flexibility.” In 2010, Republican Governor Chris Christie lowered the municipal property tax cap from 4% to 2% annual increases to make New Jersey more “affordable” (Dopp, 2010). While this cap technically puts no limitations on increasing taxes if needed to fulfill debt obligations (N.J.S.A., 2016b), it has resulted in a limited ability to further downsize operations and cut expenditures so as to ensure the “flexible” budgets with sizable surpluses that the rating agencies favor. As Plainfield’s CFO explains:

[Although it is technically exempt from the tax cap,] debt service is part of the overall budget ... [and] when the Christie administration took away the possibility of municipalities to raise taxes ... that’s when the rating agencies said: ‘Hey wait a minute, you can no longer raise taxes and you no longer have additional revenues, you are not going to be able to meet your needs the way you used in the past, we are downgrading you!’⁸⁸

Here, just like as a reduction of municipal aid since 2010 has jeopardized the confidence of the rating agencies in the state’s struggling cities (Sherman, 2015), the quest for creditworthiness is undermined by municipal financial regulation that seeks to lower taxes and restrict local government spending since this eats away the crucial budgetary surpluses necessary for a strong credit rating.

A third and paradoxical kind of failure posing a more fundamental limit to the politics of

⁸⁸ Interview 20, CFO in Plainfield & former Director of New Jersey’s Division of Local Government Services, 08-07-2016. See also Paterson’s former CFO who highlights the more long-term impact of tax caps: “[in order to get market access despite a speculative rating, you will] definitely try to reduce expenditures, [but that is] very difficult because of our appropriation cap has been in place for so long. I would say every town is pretty much down to the bare bones... [Different kinds of tax caps have] been there for 15-20 years, so people that had a lot of money in the budgets that was maybe not needed but was there for just in case all of that money is gone” (Interview 19, Former CFO in Paterson, 07-07-2016).

creditworthiness, however, emerges neither in the digression from the system nor from the contradictions between its constituent parts, but when the *functional* workings of a program produces *dysfunctional* results. This is amply illustrated by the role that the MQB-program has played since 2011 in transmitting rating downgrades across New Jersey municipalities by downloading the budget woes of the state onto municipal ratings. As such it presents a complementary case to the “pushing” of fiscal stress downwards the administrative hierarchy of the states identified by Peck (2014): the trickle-down of rating crises.

In bond market terms, the MQB-program is a “credit enhancement” program which, like similar programs in 24 other states across the U.S. (Schankel, 2011), is constructed “to provide a credit substitute to an otherwise weaker underlying government unit when there is a need for the local unit to access the capital markets” (Burger, 2008: 1135). Specifically, it works as a *pre-default state aid intercept program* (Ely, 2012; Moody’s, 2013; S&P, 2008) that pledges state municipal aid⁸⁹ as a guarantee for debt service payment. If taking part of the program, a municipality can issue “qualified bonds,” backed not only by its own GO-pledge but by state aid funds. These are money supposed for other purposes that are effectively withheld from the municipality by the state and transferred to a trustee who pays the debt service on its due date if the municipality would be unable to do so.

The benefit for the bondholders is that they do not need to put their trust in the local administration’s promise of debt repayment, as this is guaranteed by the trustee holding on to the aid funds. As Moody’s (2014: 1) puts it, this prevents “debt service obligations from competing with other local expenditure priorities.” In this sense, it operates as a guarantee from the state on

⁸⁹ Including, “business personal property tax replacement revenues, gross receipts tax revenues, municipal purposes tax assistance fund distributions, State urban aid, State revenue sharing and any other funds appropriated as State aid and not otherwise dedicated to specific municipal programs” (N.J.S.A., 2016a: §40A:3-7a).

the behalf of local government that the interest of the bondholders will be protected in the event of fiscal conflict. It takes state aid out of the space of political struggle between competing social priorities and effectively redefines the boundary between local democracy and public finance expertise. As such, it has provided a key vehicle for fiscally stressed cities to access capital, allowing them to issue bonds to which the rating agencies assigns two ratings: one underlying rating of the municipality and a second rating of the enhanced bond that is notched 1-3 steps below the higher GO-rating of the state (Moody's, 2013).

With roots in the fiscal crisis of the 1970s, New Jersey's program was created with the enactment of the Municipal Qualified Bond Act of 1976 (N.J.S.A., 2016a).⁹⁰ Since then, it has been crucial for boosting the ratings of struggling cities. This because, by issuing bonds under the program, these cities get to enjoy interest rates far below what their underlying credit weakness would otherwise allow them (although, while seeing stricter surveillance from the state and the reduced cash flexibility that comes with withholding of state aid).⁹¹ In recent years, however, the program's very ability to leverage state credit strength to the benefit of municipalities has backfired, allowing the rating-effects of the state's own public pension crisis to trickle down to its most struggling cities.

As Hinkley (2017: 2132) points out, much attention with regards to the post-recession urban fiscal crisis has been on the long term sustainability of government pension plans, where concerns over "underfunded" pensions have impaired the credit rating of local governments across the country and become "a justification for exerting greater control over cities' fiscal autonomy." While many pension plans indeed took a hit from the Great Recession, this looming

⁹⁰ According to a former CFO of the city, the act was written for Newark when "the city had not been able to enter the debt market in a long time because finances was in a somewhat disastrous state ... [and] they were trying to renew some notes [but] had nobody bidding on them" (Interview 17, CFO in Hoboken, 28-06-2016).

⁹¹ Interview 17, CFO in Hoboken, 28-06-2016.

pension crisis has been reinforced by the rating agencies themselves, which in a series of rating methodology revisions have attached greater significance to the “implicit liability” of pensions (ibid; see also Lemoine, 2017). Like municipal governments, states have been confronted with the problem of managing pension plans because, as argued in a recent S&P (2016: 2) report, “[w]hen public pension plans assume a lower rate of return, all else being equal, governments must dedicate greater proportion of their revenue to pension contributions to meet the higher estimated pension liability.” Most states, however, have been reluctant to make those higher contributions and as of the end of Fiscal 2015 the median funded ratio of state public pension plans was only 74.6%, with New Jersey’s 37.8% funded pension plan being among the most imperiled in the country (ibid: 5, 15).

As an effect of these underfunded pension liabilities, the product of a decade’s long bipartisan practice of balancing the state budget on the back of its pension contributions (Volcker Alliance, 2015), the credit rating of New Jersey has steadily dropped since 2010, receiving its 11th downgrade when Moody’s (2017: 1) cut it down to A3 citing “the continued negative impact of significant pension underfunding, including growth in the state’s large long-term liabilities, a persistent structural imbalance, and weak fund balance.” As tied to the state’s rating, these downgrades have been transmitted to the MQB-program, which credit rating successively has dropped as the state’s credit deteriorated.⁹² Affecting 16 cities taking part in the program, these downgrades might make some relatively highly rated municipalities like Jersey City (Aa3) and Bayonne (A3), whose underlying rating exceeds the rating of the program, to opt out of issuing qualified debt, but for long struggling places like Newark (Baa3), Paterson (Ba1) or Trenton (Baa1), the space of fiscal maneuver will only be further circumscribed.

⁹² Moody’s has, for example, been downgrading the program from Aa3 in 2010 to A1 in 2011, A2 in 2014, A3 in 2015 and finally to Baa1 in 2017, only two notches above “junk” status.

As such, the increasing inability of the MQB-program to produce adequate remedy to local fiscal stress illustrates how as the fiscal crises of the states get worse, the models of strong and paternalistic municipal fiscal oversight that have been lauded as the solution of the new urban fiscal crisis are increasingly strained. Rather than serving as the guardians of local creditworthiness and prudent fiscal practice, states in the present conjuncture are pushing austerity as well rating crises down their administrative hierarchies. This further exposes cities to the risks of the bond market and the discipline of the rating agencies. As such, the sweeping downgrades of cities in New Jersey's MQB-program represent yet another peculiar instance of failure in the regime of accountancy urban governance.

4.5 Conclusion

Building on previous work examining the growing importance of debt dynamics and the subsequent influence of credit rating agencies in urban politics, I have in this chapter argued for the need to attend to how on a day-to-day basis the politics of creditworthiness is *co-constructed* in the interactions between local and extra-local actors. In particular, I have argued that this takes the form of “accountancy urban governance” where fiscal politics are mediated through the discourse of accounting. Through this politics, local financial professionals are central in inserting the values and monitoring practices of bond rating into the heart of municipal administrations. This remakes the contested politics of the debt relation into a technical question of public finance “best practice.” In this sense, I second Clarke & Cochrane's (1989) argument that radical scholars and social movements that seek to challenge urban austerity need to give greater attention to the role financial professionals play in local politics. As Merrifield (2014: 424) argues, we need to “point the critical finger at this new nobility, of its select committee of

accountants and administrators, the middle managers who reside over our privatized public sector, and who pull the strings in our fast-emerging rentier and creditor society.” We also, however, need to understand how they are embedded in hierarchal relations of power.

In his account of the use of financial derivatives by Italian municipalities, Lagna (2015) argues against Foucauldian notions of financialization as a disciplinary power internalized and performed by all actors as an all-encompassing, depoliticized and technocratic common sense. Such approaches, he claims, fail to appreciate agency and power asymmetries between actors. Instead he proposes an agent-centered account that interprets how local governments in Italy have used financial derivatives as a conscious political strategy to circumvent austerity measures imposed from above. As such, financial innovations do not diffuse evenly across space, but “specific political struggles shape [their] global growth ... into a complex and uneven process” (Lagna, 2017: 208) where “governments often exercise statecraft by deploying the methods and instruments of financial innovation” (Lagna, 2016: 168). Like Weber (2010), this argument highlights the proactive role taken by local states in their own financialization process, emphasizing how municipalities have “been active, financialized participants ..., seeking investments that would provide them with a regular income stream” (cf. Pani & Holman, 2014: 214).

Examining the co-construction of creditworthiness in New Jersey municipal finance I have in this chapter, however, shown that this local state agency is a circumscribed one, preconditioned on the “politics of limits” (Paudyn, 2014: 7) that characterize credit rating as well as the state’s regulation of municipal finance. The discipline of the rating agencies does not simply descend from above and their influence relies on local actors, but this does not mean that municipalities are fully able to steer their own course. They may be able to employ speculative

financial instruments, but the scope of these is circumscribed by the limits put upon them in the search for budgetary flexibility. This “flexibility” is the mechanism of normalized credit rating power, one that has been accepted by local financial professionals as good public finance practice. As such, it is indeed co-constructed but crucially preconditioned on the neoliberalization of inter-governmental relations, where budget cuts and downloading of responsibility and risk to local governments have created an ever-increasing need to manage the dynamics of local debt. These techniques in the search for “creditworthiness” are, however, increasingly running up to their own limits also in the supposedly most robust corners of American municipal finance, highlighting the diminishing returns of financialized forms of urban governance.

Chapter 5: Conclusion: The violence of municipal debt

This thesis, has sought to develop what I in the introduction called a “bond market optic” on contemporary urban political economy. That is, it has tried to situate and contextualize the conditions of “austerity urbanism” (cf. Peck, 2012) in the context of the municipal bond market, its actors, practices and institutions. This market optic has the benefit, as Sbragia (1983) contends, of positioning cities within some of the multiple local and extra-local relations that shape everyday urban life. Specifically, focus has been on following one such bond market relation, that of credit rating. Thinking through this relation allows us to draw together the always asymmetric interactions between finance capital, local actors and state and federal regulators. It highlights the co-construction of a politics of creditworthiness that is increasingly steering American urban governance. The bond market optic allows us to see the multiple institutions and actors in play to sustain municipal finance as a form of metagovernance characterized by the dual powers of bondholders and state intervention (cf. Peck, 2017), but always mediated through the technocratic expertise of local financial professionals.

Three chapters have explored this system of municipal finance. Firstly, following Kirkpatrick’s (2016) argument that the post-Great Recession “return” of the urban fiscal crisis needs to be understood in the context of an increasingly large and speculative municipal bond market, Chapter 2 sketched the general features of this market. By way of background, the technical details of municipal bonds were outlined before reviewing how they have become an increasingly central object for the study of the financialization of urban governance. This process is making municipal finance (and, in extension, local politics) increasingly speculative and risk-prone, while it exposes cities to harsher discipline from bondholders and their representatives (including rating agencies). Thereafter, the chapter tracked this market development from the

urban fiscal crisis of the 1970s up until today in order to explore how cities have been put under increasingly close investor scrutiny and how this has differentiated what was previously a rather homogenous market. In this new market, local governments that are already doing well are privileged while those that struggle are further punished.

The credit rating analysts are key agents of this differentiated investor scrutiny. Chapter 3 therefore opened the “black box” of the rating process. Building on a renewed interest in value theory under the conditions of financialization, it argued that this process pivots around a central tension between on the one hand understanding the concrete uncertainties of investing in place while on the other hand needing to transform these uncertainties into a measure of “abstract risk” so as to make commensurable commodities out of cities and their debt. Drawing on interviews from within the agencies as well as close reading of rating methodologies, it explored how rating analysts seek to negotiate this tension before it concluded by examining two crucial limits to commensuration. Stepping outside the credit rating machinery, Chapter 4 further explored its interactions with municipal actors. Unpacking the mechanisms of credit rating power, it argued that rather than simply descending from above, the politics of creditworthiness is co-constructed in the interactions between rating agencies, local financial professionals and state oversight bodies. This dispersed “accountancy urban governance” is, however, conditioned on the circumscribed room of maneuver of local agents, a “politics of limits” that operates through local acceptance of the common-sense of technocratic accountancy. This includes the need to ensure “budgetary flexibility” as well as the sharp demarcation of municipal financial administration from local politics. It is, however, not an absolute process. Rather it is increasingly showing signs of cracking, even in one of the most robust corners of municipal finance.

Thinking through the bond market allows us to connect these multiple actors and institutions, but it also has its blind spots. In particular, it positions the analysis on a level of abstraction that easily overlooks the “local stuff” of urban politics (cf. Sbragia, 1983). Indeed, some readers who have made it this far might find the thesis just too abstracted from urban everyday life. And they may be right. While exploring the details of the rating process and its interactions with local financial administrations, it says little about the actual, material consequences of speculative municipal indebtedness and credit rating for the people who inhabit my research sites. The analysis unpacks the bureaucratic labyrinths of municipal finance, but rarely ventures outside into the world. Indeed, readers might ask, what is the critical significance of such exercise in an era when American metropolises have once again been gripped by social upheaval in the wake of structural racism and police brutality (Taylor, 2016)? The rest of this conclusion seeks to offer a partial response to these concerns.⁹³

In *Capital*, Marx (1990: 925–926) famously argued that “[i]f money ... ‘comes into the world with a congenital blood-stain on one cheek,’ capital comes dripping from head to toe, from every pore, with blood and dirt.” Exploring the processes of the co-called “primitive accumulation,” including land dispossession, enclosure, colonialism and slavery, *Capital*’s abstract unpacking of the commodity form, fetishism and the nature of money are here resolutely concluded by debunking the claim that capitalism was simply born out of human genius and ambition. Instead, Marx argues that its birth was a deeply violent process, where laborers were forcibly separated from their means of production in order to create the doubly “freed” working class needed to fill the factories of English mill towns. As such, *Capital*’s concluding chapters firmly put violence in its place within capitalism. Taking issue with Marx’s denotation of this as

⁹³ These concluding reflections draw on an on-going collaboration with Sage Ponder. The responsibility for the particular arguments presented here is, however, mine alone.

a “primitive” process (that is, as being located in capitalism’s pre-history), Harvey (2003) has further elaborated on the ongoing violence of capitalism to argue that in its contemporary guise it is similarly characterized by processes of “accumulation by dispossession.” This includes a privatization of formerly public assets not unlike Marx’s enclosure of the commons, but in an era of financialization, in particular, “the speculative raiding carried out by hedge funds and other major institutions of finance capital [becomes] the cutting edge” (Harvey, 2003: 124).

With this conceptualization of financialization as form of contemporary accumulation by dispossession, Harvey (ibid) highlights the often overlooked “violence of financial capitalism” (Marazzi, 2010: 3). Just as Marx (1990: 919) commented that “public debt becomes one of the most powerful levers of primitive accumulation,” this violence is never far away in the municipal debt politics of contemporary America. Indeed, Detroit’s settlement with its creditors, for example, resembles a classic case of accumulation by dispossession, including the privatization of land and infrastructure in exchange for debt relief. Similarly, the reduction of pension commitments to avoid creditor haircuts in the bankruptcy of Central Falls, RI illustrates yet another example of such unequal redistribution (see Chapter 2, Table 2.2). The violent character of this process, however, becomes particularly evident in all those instances where financial discipline clearly articulates with deep rooted racism, a violent phenomenon in its own right, best understood as “the state-sanctioned or extralegal production and exploitation of group-differentiated vulnerability to premature death” (Gilmore, 2007: 28). A striking illustration of this can be found in the case of Flint, MI.

In 2011, the City of Flint had been placed under financial “emergency management” by Michigan’s republican governor Rick Snyder. Tasked with restructuring the struggling city’s finances and to return it to fiscal solvency, the appointed emergency manager was given

overriding authority of the city's operations, effectively dissolving local democracy (cf. Anderson, 2011; Peck, 2012). As Kirkpatrick & Breznau (2016) have shown, Michigan's black majority cities are particularly at risk of being placed under emergency management, and in Flint this would catalyze a deeply violent production of premature death (cf. Gilmore, 2007). Eager to save money on the city's water and sewage account, the Flint emergency managers choose to disconnect its crumbling water system from nearby Detroit and instead join a newly formed regional water authority proposing to establish an independent connection to Lake Huron (Highsmith, 2016). Until this connection was constructed, however, Flint's water would be taken from the local river, a source heavily polluted after decades of industrial activity. This polluted water would have a corrosive effect on the city's many older and ill-maintained pipes, delivering lead contaminated water straight into the homes of Flint's residents. While this could have been avoided, since the emergency management had decided to not use the anticorrosive agents that for a cost of \$100/day could have hindered pipes to erode (Pulido, 2016: 5) nearly 9000 children younger than six years old are instead suspected to have been exposed to dangerous levels of lead, contaminating their brains and entire nervous systems (Ranganathan, 2016: 18).

As Pulido (2016: 1) argues, this localized crisis of environmental regulation needs to be understood in the larger picture of capitalism's devaluation of black and other non-white populations, groups that under the context of austerity urbanism has become "so devalued that their lives are subordinated to the goals of municipal fiscal solvency." In this sense, the Flint lead poisoning scandal was just one of many acts in an unfolding drama of racism and structural discrimination. Just as the urban fiscal crisis needs to be understood in the context of financialization, it was also a particular financialized form of violence. As Tabb (2014: 92) notes, "[f]inancialization involves the use of state power to enforce collection of debt" and

techniques like Michigan's emergency management program crucially need to be understood in this context. They are through their "strategic, targeted deployment of the exception... [a] set of tools for enforcing financially leveraged value extraction" (Kirkpatrick & Breznau, 2016: 31). That is, a form of accumulation by dispossession. Disciplined as a debtor, albeit a particular racialized one, Flint was through discourses of austerity "framed and punished as if it were a financially reckless individual, while the structural and historical causes of its financial duress [were] thoroughly masked" (Ranganathan, 2016: 27). The city therefore represents a particular spectacular moment when the violence of racism and the violence of financialization come together. There might be no necessary need to understand the intricate details of the municipal bond market to put Flint in the context of long standing processes of "environmental racism" (Pulido, 2016; Ranganathan, 2016). But while the city's fate became narrated as a national tragedy, including the highly staged intervention by President Barack Obama, the everyday violence of municipal debt does not usually reach the news headlines. Rather than being spectacular events with clearly identifiable causes and perpetrators (the decision to switch water supply by named emergency managers), financialization induced austerity is more commonly characterized by forms of violence that are both "slower" (Nixon, 2011) and more "abstract" (LiPuma & Lee, 2004).

Nixon (2011: 2) coined the term "slow violence" when he spoke to the need to take understandings of violence beyond the word's association with explosive, immediate events to instead "engage a different kind of violence, a violence that is neither spectacular nor instantaneous, but rather incremental and accretive." Such violence, like the slowly unfolding catastrophes of climate change or pollution, often operates out of immediate sight, with the relation between cause and effect obscured through the passing of time (ibid). It is, however,

central if we want to understand the violence of austerity urbanism in places like Flint. Indeed, as Paulido (2016) highlights it was not just the contamination of the Flint river that produced the poisoning disaster. Neither was it simply the result of the specific, immediate decision to use that river as the new water source. Rather, the preconditions of the Flint water crisis were produced in the much slower “politics of abandonment” leading to decades of deterioration of the city’s water and sewer infrastructure (ibid: 5). The case of Flint is therefore a clear illustration of Nixon’s (2011) slow violence, because “[t]he decision to neglect infrastructure so that it becomes toxic must be seen as a form of violence against those who are considered disposable” (Pulido, 2016: 5). This slow processes of neglect and environmental disaster, however, needs to be put in the context of a particular form of “abstract violence” that characterize the global financial system (LiPuma & Lee, 2004).

With the concept of abstract violence, LiPuma & Lee (ibid) highlight how in a capitalism increasingly dominated by processes of circulation (epitomized in the proliferation of financial derivatives), dominant forms of global violence are decoupled from sovereign power. Instead of being brought about by military force and colonialism, “it never appears directly; rather it mediates and stands behind local realities – such as interest rates, food costs, and the price of petroleum” (ibid: 26). This is a violence that like Nixon’s (2011) slow violence is hard to pin down. A violence internal to the financial system that cannot simply be attributed to a clearly defined perpetrator, not simply stemming from the “Caesar-like” (Peck, 2017: 329) sovereignty of Flint’s emergency managers or Michigan’s governor who appointed them. Rather, “[i]ts effects are violent because it damages and endangers the welfare and political freedom of those in its path, [but it] does so without ever revealing itself. Lacking any sensible qualities, the harm

brought about by, for example, exchange rate volatility seems to materialize out of thin air” (LiPuma & Lee, 2004: 28).

In the municipal bond market, this abstract violence is the violence of credit rating. It “mediates and stands behind” local realities of austerity urbanism. Rating downgrades might bring about the neoliberal restructuring of local governments (Biles, 2015; Hackworth, 2002, 2007; Mitchell & Beckett, 2008; Sinclair, 2005). More importantly, however, it is the internalization of the norms of “budgetary flexibility” that divert funds from needed service provision to keep the budget surpluses high, it is the dangers of being downgraded because of too much debt that keeps municipal managers from borrowing to maintain their infrastructures, and it is the interest rate costs eating away at the operating budget that make local financial professionals advise against socially necessary capital projects. In short, it is the everyday vigilance of the debtor seeking to “live within its means” that structures austerity urbanism as a violent and redistributive project of offloading the costs of financialization onto the city’s most vulnerable residents (Peck, 2014; Peck, 2012). Compared with emergency managers, this is a harm that is difficult to mobilize against. Like exchange rate volatility, it indeed “seems to materialize out of thin air” (LiPuma & Lee, 2004: 28).

The municipal bond market is therefore difficult to politicize. Like the commodity form in general, it appears as a particularly abstract form of social domination (cf. Postone, 1993) with a violence that is not immediately attributable to a single cause or a named perpetrator. Instead it mediates the entire lived experience of inhabiting the city, but largely without making itself directly visible. It is because of this actually existing abstract violence that close-up accounts of the present urban condition and the concrete realities and struggles of its people are not enough. We also need accounts that seek to expose and critique the financial conditions of existence that

structure these realities and shape their struggles. We need to defetishize the spaces from which these market abstractions originate, unpack the labor processes, bodies, techniques and discourses that bring them into existence. This is the political contribution I have tried to make in this thesis.

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Appendices

Appendix A: List of interviews

Respondent	Location	Date
Interview 1, former Director, New Jersey's Department of Local Government services.	Restaurant	06-05-2016
Interview 2, municipal bond market analyst, major bank.	Café	16-05-2016
Interview 3, rating analyst, major credit rating agency.	Café	18-05-2016
Interview 4, Executive Director/Chief Financial Officer, Hudson County Improvement Authority, NJ.	Respondent's office	24-05-2016
Interview 5, Director of Finance, City of Trenton, NJ.	Respondent's office	25-05-2016
Interview 6, Chief Financial Officer, City of Elizabeth, NJ.	Respondent's office	27-05-2016
Interview 7, Chief Financial Officer, Town of Harrison, NJ.	Respondent's office	01-06-2016
Interview 8, Chief Financial Officer, Town of Kearny, NJ.	Respondent's office	03-06-2016
Interview 9, Chief Financial Officer, City of Perth Amboy, NJ.	Respondent's office	06-06-2016
Interview 10, municipal bond market analyst, major bank (former rating analyst).	Respondent's office	06-06-2016
Interview 11, Director, New Jersey League of Municipalities.	Respondent's office	09-06-2016
Interview 12, Director, public finance department, major credit rating agency.	Respondent's office	14-06-2016
Interview 13, municipal bond market analyst, major bank (former rating analyst).	Respondent's office	15-06-2016
Interview 14, rating analyst, major credit rating agency	Respondent's office	21-06-2016
Interview 15, Business Administrator, City of Newark, NJ.	Respondent's office	22-06-2016
Interview 16, senior manager, major bond insurance firm.	Respondent's office	23-06-2016
Interview 17, Chief Financial Officer, City of Hoboken, NJ.	Respondent's office	28-06-2016
Interview 18, municipal bond market analyst, major bank (former rating analyst).	Respondent's office	05-07-2016.
Interview 19, former Chief Financial Officer, City of Paterson.	Restaurant	07-07-2016
Interview 20, former Director, New Jersey's Department of Local Government Services, & Chief Financial Officer, City of Plainfield, NJ,	Phone interview	08-07-2016
Interview 21, Executive Director, fixed income & commodities, major bank (former rating analyst).	Respondent's office	19-07-2016
Interview 22, retired consultant municipal bond market analyst.	Café	19-06-2016.