

The Potential of Countercyclical Fiscal Policy in New York City

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About the author

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Executive Summary

In New York City, there is growing debate on how to pay for the expanded social services promised by Mayor Zohran Mamdani, given the profound absence of federal support under President Trump. This debate resonates far outside New York as other U.S. cities face similar challenges.

Given the tension between federal and local governments, this paper makes the case for New York City enacting countercyclical fiscal policy to strengthen its economy and navigate downturns.

Countercyclical fiscal policy generally means a government uses its own spending and taxation power to smooth out business cycle fluctuations. During a recession, for example, a government would increase or maintain its spending while reducing taxes – actions that help stabilize demand, employment, and income, while reducing “economic scarring.”

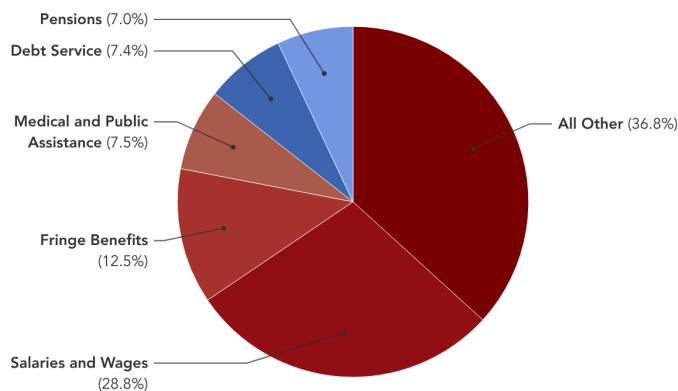
Countercyclical fiscal policy is not widely promoted at the local level, especially given New York’s significant borrowing and spending constraints since the 1970s fiscal crisis. This report lays out how it is in fact a viable solution and powerful tool in a downturn.

The government can spend when households and businesses can’t or won’t, but the type of spending matters. I argue the first step in effective countercyclical fiscal policy is to increase or at least maintain “multiplier” spending during a downturn. Multiplier spending, like spending on salaries, wages, and public assistance, can directly help reduce the duration, severity, and general pain of a recession (see Figure 1). This isn’t the case for “non-multiplier” spending, which does not help stabilize incomes or demand, like spending on pensions and debt service.

Figure 1:

NYC expenditures (FY 2027 adopted budget)

Multiplier spending (reds) directly stabilizes demand, incomes, and employment, while non-multiplier spending (blues) does not.



The expenditure data is from all funding sources, not just city funds.

Source: New York City Office of the Comptroller

The report delves into the challenges of taxation as a countercyclical tool and believes that targeted, progressive tax *increases* can bring in revenue to maintain multiplier spending. It also outlines different strategies for the City to free up funding, including reducing the size of its asset positions, using alternative metrics to assess pension fund sustainability, and utilizing short- and long-term borrowing to the extent necessary.

Capital spending could be made into an even sharper tool for countercyclical fiscal policy if budget officials and policymakers incorporate countercyclical considerations into their debates, discussions, and projects.

In that vein, there are 10 recommendations under two guiding principles:

- New York City and New York State policymakers should bring a countercyclical perspective to their work.
- New York City's countercyclical fiscal policy toolkit should contain a variety of tools.

Short-term recommendations include:

1. Increase or at least maintain multiplier spending.
2. Stop the prepayment of future expenses.
3. Draw down available reserves as needed, within legal limits.
4. Issue revenue anticipation notes (RANs) and tax anticipation notes (TANs) to help cover short-term revenue shortfalls.
5. Utilize long-term borrowing capacity to maintain capital project spending throughout a downturn.

Medium-term recommendations include:

6. Implement targeted, progressive tax increases.
7. Deficit finance during the next recession if the City decides the benefits outweigh the costs.

And long-term recommendations include:

8. Identify the types of spending that can be legally rerouted to multiplier spending during a downturn.
9. Explore metrics other than the funding ratio to assess the sustainability of public pension funds.
10. Create a committee within the Mayor's Office of Management and Budget (OMB) to study the costs and benefits of a full or partial pay-as-you-go funding for the City's pension funds.

Introduction

In New York City, a striking fiscal challenge exists. President Trump, since his inauguration, has cut, or threatened to cut, federal funding to states and cities which he accuses of not cooperating with his policies on diversity, equity, and inclusion, as well as immigration (Egelko 2026). In New York, his administration seized over \$80 million legally awarded by the U.S. Federal Emergency Management Agency to support the influx of asylum seekers, then froze \$18 billion meant for infrastructure projects due to “unconstitutional DEI principles” (Mann 2025).

In sharp contrast, Mayor Zohran Mamdani won his election on the promise of expanding what the City can do for its residents, from universal child care to public grocery stores. But a debate persists on how to pay for expanded social services given the profound absence of federal support. This debate resonates far outside New York as other U.S. cities face similar challenges.

This report argues that New York City could expand – or at least maintain – its spending during a downturn and in a political environment where inadequate federal assistance will likely continue. To do this, the City must turn to countercyclical fiscal policy. If the federal government can’t or won’t provide it, states and cities should.

Countercyclical fiscal policy generally means a government uses its own spending and taxation power to smooth out business cycle fluctuations. For example, during a recession a government would increase or maintain its spending while reducing taxes. These actions help stabilize demand, employment, and income, while reducing “economic scarring” which is associated with long-term unemployment and even depression, divorce, and suicide (Sperling 2025).

The substantial countercyclical fiscal policy that took place over Covid-19 – and resulting anger when that support was taken away – demonstrates the difference robust government spending can make in people’s lives.

Going into the pandemic, many policymakers believed the federal government’s response to the 2008 recession was too small and hoped to correct course with more generous spending policies. This resulted in the quickest economic recovery in recent history, but coincided with above-average inflation. Going into the next recession, policymakers may seek to correct course by estimating stimulus needs more conservatively. Undershooting would not guarantee low inflation but would almost certainly lead to higher-than-necessary unemployment.

Given the federal climate, and that policymakers might underestimate the amount of federal aid needed by cities and states to get through the next recession, state and

local governments should invest in strategies to independently stimulate their local economies.

This paper outlines how that might look in New York. It breaks down types of spending with the most countercyclical power, the challenges of using taxation as a countercyclical tool, and how countercyclical fiscal policy power could come from adjustments in asset positions. It argues why New York City should reconsider the use of deficit financing to shift toward countercyclical fiscal policy. It concludes with 10 explicit recommendations to make this fiscal policy shift.

Shifting political tides, and growing pressure for socialized government services, offers New York City policymakers a distinct opportunity. Implementing and expanding City capacity for countercyclical fiscal policy would not only support the promises of the Mamdani administration; it would pave the way for stronger local economies in cities across the country.

1. Expanding Countercyclical Power

The majority of policymakers believe economic stabilization to be the responsibility of the federal government. One primary reason is that state and local governments have constraints the federal government does not. All states (except Vermont), and many large cities have balanced budget rules. New York City is legally required to have a balanced budget at the beginning and end of the fiscal year according to generally accepted accounting practices (GAAP) (New York City Office of the Comptroller 2023). This makes countercyclical spending difficult since revenues generally fall during a recession and balanced budget rules put pressure on spending to fall with revenue.

Almost all states and many large cities also have limits on general obligation debt (Volcker Alliance 2022). New York City's debt limit is set at 10 percent of the five-year average of the full valuation of real estate located in the City (New York City Office of the Comptroller 2024). Sometimes debt limits are set in conjunction with debt service limits, meaning that if a government is below their debt carrying capacity, their debt service limit might prevent further borrowing. While New York City does not have a legal debt service limit, it aims to keep debt service payments below 15 percent of annual tax revenue. The City is also constrained by the State Constitution's operating limit. It restricts the amount of real property tax the City can levy for operating purposes to 2.5 percent of the five-year average of the full market value of taxable real estate. Balanced budget rules, debt limits, operating limits, and debt service limits all constrain state and local government budgets to the point where policymakers do not usually think about acting countercyclically.

The rejection of state and local governments as countercyclical agents can lead to longer recessions. Figure 1 shows real state and local government spending over the economic recoveries from the 2008 and 2020 recessions. Spending is indexed to 100

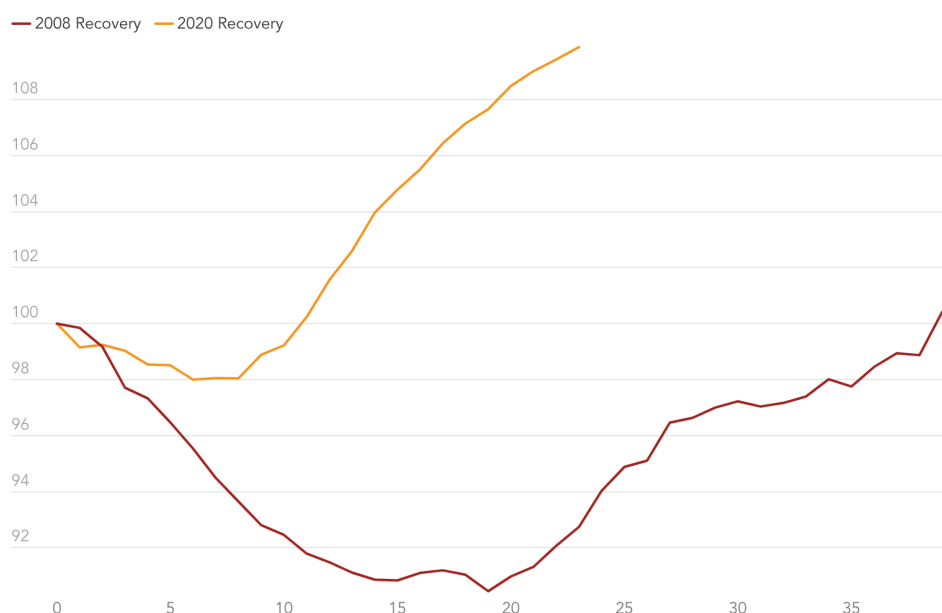
at the end of the recession, as identified by the National Bureau of Economic Research (NBER). The figure shows that real state and local government spending took almost ten years to return to its pre-recession level in 2008. This means that instead of acting as a stabilizing force, state and local spending was a drag on the 2008 recovery.

Conversely in 2020, when substantial attention was given to stabilizing state and local government revenue, state and local spending experienced minimal reduction, never dropping below 97 percent of its level at the end of the recession. This demonstrates, for at least these two case studies, that the spending of state and local governments can make a difference in the speed and strength of economic recoveries.

Figure 1:

Real state, local government spending during recoveries

Number of quarters to return to level of real spending since start of each recession (indexed to 100)



It took 39 quarters (9.75 years) for state and local spending to return to pre-2008 levels; it took 11 quarters (2.75 years) to return to pre-2020 levels.

Source: FRED, "State and Local Consumption Expenditures and Gross Investment" [SLCE] and "Government consumption expenditures and gross investment: State and local (implicit price deflator) [A829RD3Q086SBEA]

We should use state and local government spending to shorten recessions because extended recessions have harmful long-term effects. Deep extended downturns can lead to slower future growth (Mason 2017). Figure 2 shows real GDP in 2000 dollars and two CBO projections of potential GDP. After the 2008 recession, real GDP never returned to its projected potential (yellow line). However, after the 2020 recession, real GDP not only returned to its projected potential (blue line), but surpassed it. In this case, a quicker recovery means stronger, faster future growth.

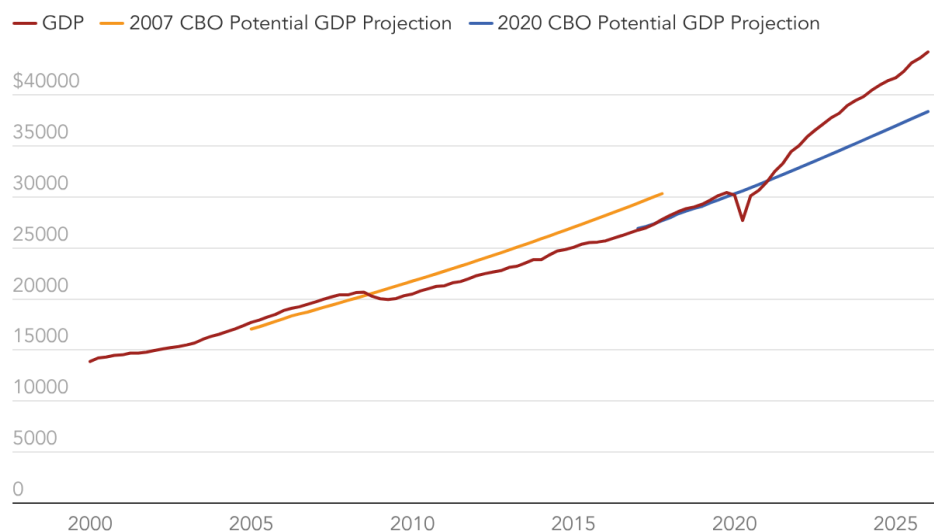
A severe downturn can leave “economic scars” in the form of increased long-term unemployment and higher unemployment rates for younger workers just entering the labor market. As noted in *“Tragedy” of a One-Sided Biden Critique*, economic scarring can lead to higher rates of depression, divorce, and suicide (Sperling 2025).

It is likely that state and local government aid during the next downturn will be underestimated. This could lead to the 2008 recovery scenario where state and local spending makes the recovery slower and weaker, producing long-term economic scarring. To avoid this, policymakers should aim for the 2020 recovery scenario in which state and local spending helped produce a faster, stronger recovery. Without adequate federal government assistance, this will require states and local governments to think hard and creatively about increasing their capacity for countercyclical action.

Figure 2:

Real GDP vs. CBO projections of potential GDP

Billions of dollars (\$ in 2000)



"CBO" and "GDP" stand for Congressional Budget Office and Gross Domestic Product, respectively.

Source: FRED and CBO

2. Spending for Countercyclical Purposes

Not all government spending is helpful for reducing the duration, severity, and pain of a recession. This section examines New York City's spending, categorizes it into “multiplier” and “non-multiplier” spending, and argues that multiplier spending should be increased, or at least maintained, during a downturn.

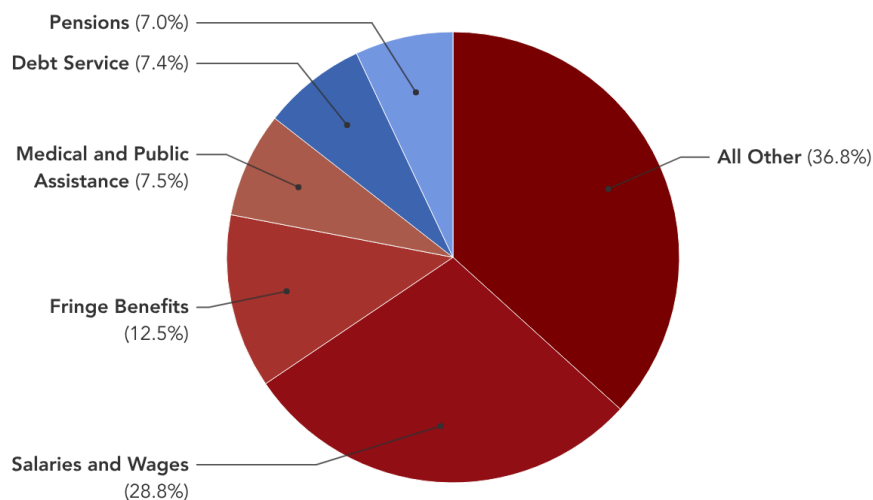
Figure 3 shows the bulk of New York City's spending is multiplier spending. About 42 percent of the fiscal year (FY) 2027 adopted budget is spent on salaries, wages, and fringe benefits (New York City Office of the Comptroller 2026). Reducing compensation expenditures either through layoffs, reduced hours, or benefits would directly lower incomes, demand, and aggregate spending. This could lead to further job loss, income reduction, and loss of demand. The point of countercyclical fiscal policy is to prevent this vicious cycle.

The biggest budget component in Figure 3 is "All Other" – spending on materials, equipment, utilities, and operating costs of smaller city agencies. These expenditures are helpful from a stimulus standpoint. Those purchases provide revenue for businesses to keep employees on, which stabilizes their incomes and maintains demand for other products and services. By maintaining multiplier spending over a recession, the City could better stabilize incomes, demand, and employment.

Figure 3:

NYC expenditures (FY 2027 adopted budget)

Multiplier spending (reds) directly stabilizes demand, incomes, and employment, while non-multiplier spending (blues) does not.



The expenditure data is from all funding sources, not just city funds.

Source: New York City Office of the Comptroller

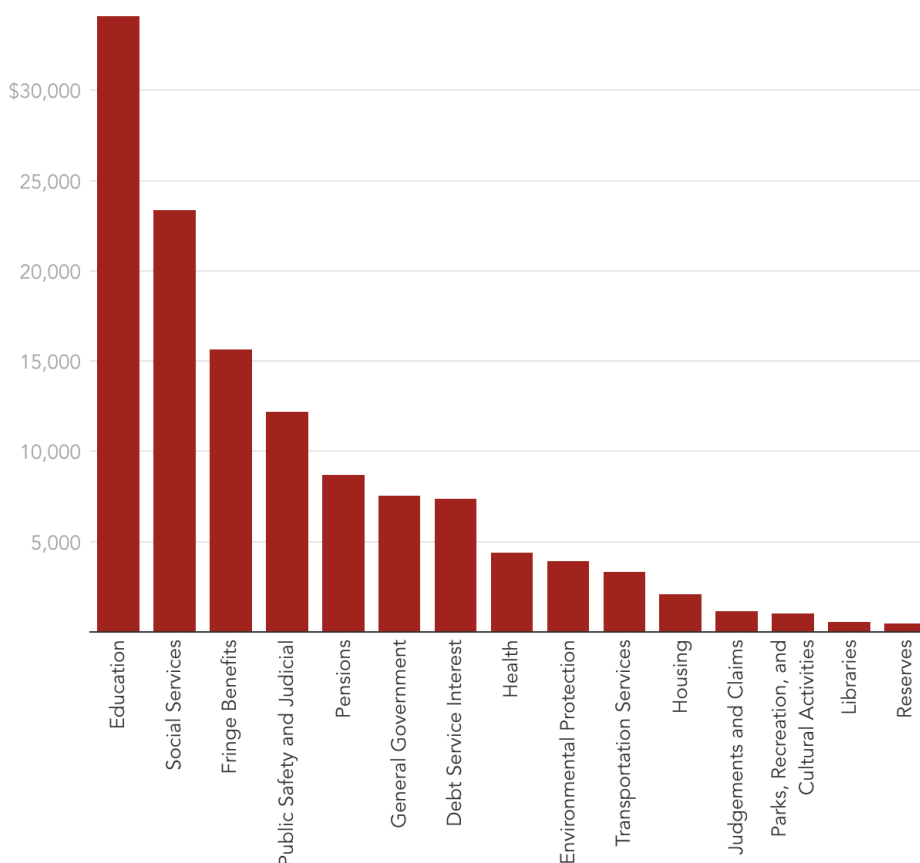
Multiplier spending is desirable not just for its stimulative benefits. It often represents spending on essential public goods and services. As Figure 4 shows, New York City plans to spend \$125.8 billion in FY 2027 to provide such goods and services. Education and social service spending makes up almost half of the FY 2027 budget. The City contributes to Medicaid and spends to ensure residents have greater access to affordable housing, healthcare, transportation, public parks, and libraries. Cutting

spending in these areas during a downturn is harmful for residents' quality of life, in addition to being counterproductive for stimulus.

Figure 4:

NYC expenditures, FY 2027 adopted budget

Billions of dollars (nominal)



Source: New York City Office of the Comptroller

Non-multiplier spending is any City spending that doesn't help stabilize incomes or demand. Figure 3 shows two non-multiplier categories: pensions and debt service, contributing to 14 percent of the FY 2027 adopted budget. This represents a sizable opportunity. If these funds could be rerouted to maintain multiplier spending, it could reduce the duration, severity, and overall pain of the recession. However, New York City is legally obligated to pay its debt service and pension contributions. This means the City lacks the flexibility to reroute unhelpful, non-multiplier spending to helpful, multiplier spending. While asking for flexibility in debt service payment is taboo in virtually all policymaking, academic, and financial circles, there may be flexibility with pension contributions (see Section 3).

Takeaway: The first step in effective countercyclical fiscal policy is to increase or at least maintain multiplier spending during a downturn.

When a recession occurs, demand falls, unemployment rises, and incomes shrink. Multiplier spending, like spending on salaries, wages, equipment, and public assistance, can directly help reduce the duration, severity, and general pain of a recession, while non-multiplier spending does not. The City should explore the desirability and legality of rerouting non-multiplier spending to multiplier spending.

3. Taxation as a Countercyclical Tool

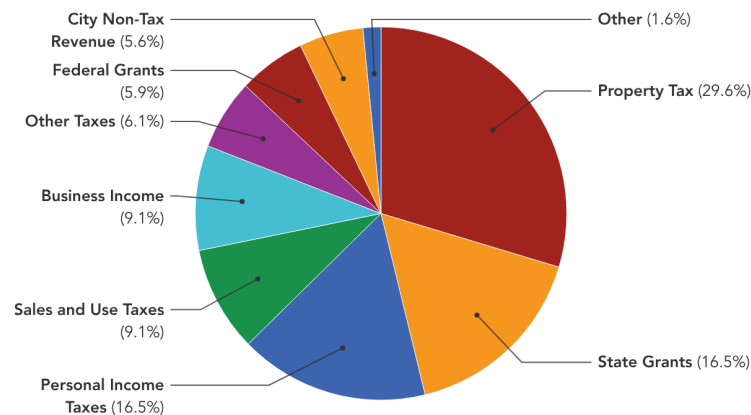
Countercyclical fiscal policy aims to ensure people have money to spend, creating demand for goods and services, and giving employers a reason to keep employees on the payroll. In terms of taxation, countercyclical fiscal policy usually means lowering taxes. Lowering tax burdens increases households' disposable income, meaning it leaves more money in their pockets for them to spend. This may be good for stimulus and households, but it lowers government revenue.

As Figure 5 shows, the majority of the City's revenue (about 70 percent) comes from taxes. The second biggest category (about 23 percent) is funds from the state and federal government. We assume that federal government aid will decrease. This means reducing tax burdens for New Yorkers during a downturn might lower tax revenue, preventing the City from taking additional steps to stimulate the local economy.

Figure 5:

NYC revenue by source

City Fiscal Year 2027 Adopted Budget



Source: New York City Office of the Comptroller

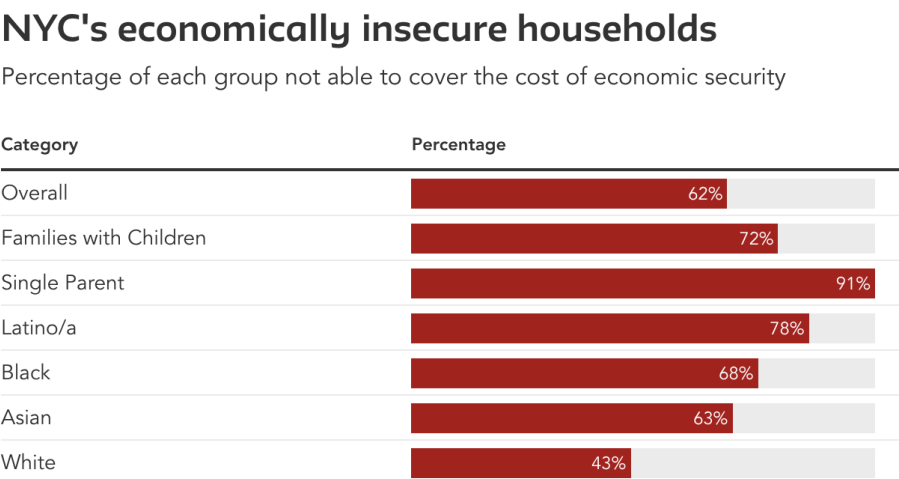
Targeted, progressive tax *increases* are a better tool for countercyclical action. In terms of stimulus and equity, it's best to increase taxes on individuals and businesses that can and will keep spending even if their tax bill rises. For example, it is hard to imagine high-income households (making \$1 million or more in adjusted gross income per year) cutting back spending due to small tax rate increases.

During Covid-19, the State of New Jersey raised the personal income tax rate on earnings between \$1 million and \$5 million by two percentage points, in addition to maintaining a surcharge set to expire on the income of top-earning businesses (Reitmeyer 2020). If New York City applied tax rates of 4.2 percent to incomes between \$1 and \$5 million, and a 4.4 percent tax rate to incomes over \$5 million, the City could raise roughly \$1 billion (Center for New York City Affairs 2026). New Jersey's 2.5 percent surtax on the State's most profitable businesses raised about \$1 billion each year for the government's coffers (Biryukov 2024).

Targeted, progressive tax increases could raise a significant amount of countercyclical stimulus funds. One remaining issue with tax increases as a countercyclical tool is that even when New York City is not in a recession, it faces problems requiring additional revenue. Figure 6 shows over 60 percent of households are economically insecure, largely driven by high housing and child care costs (Federation of Protestant Welfare Agencies 2025).

The Mamdani administration has proposed social service programs requiring new revenue sources to permanently fund. It means that while tax increases can be an excellent countercyclical tool, there will be competing uses for that revenue. For this reason, it may not be wise to rely solely on tax increases for countercyclical fiscal policy.

Figure 6:



Source: FPWA

Takeaway: New York City should utilize targeted, progressive tax increases during a downturn, in addition to other tools.

Conventional countercyclical fiscal policy says governments should lower taxes to increase disposable income, but it has the potential effect of less government revenue. Increasing taxes brings in revenue to maintain multiplier spending. In terms of stimulus and equity, it is best to increase taxes on high-income individuals and businesses that can and will keep spending even if their tax bill rises.

4. Finding Countercyclical Capacity in City Assets

This section explores three ways the City could adjust its asset positions to generate funds for countercyclical action: redirect prefunding of future expenses; draw down reserve accounts; and advocate for more flexibility in pension contributions.

Stop prefunding and draw down reserves

The fear of a 1970s fiscal crisis, along with a desire to maintain a strong credit rating, forged a tradition of conservative budget practices in New York City. Ever since the implementation of the balanced budget rule, the City has found creative ways to save while complying with the law. These saving vehicles can and should be used as a source of funds for countercyclical action during the next downturn.

The Budget Stabilization Account (BSA) – otherwise known as “the roll” – takes any surplus in the current budget year and uses it to prepay some of next year’s expenses (New York City Office of the Comptroller 2026). Most City budgets since the 1970s use prepayments from the current fiscal year to balance the upcoming year’s budget. The City usually prepays expenses like debt service, subsidies to libraries, health and hospitals, the MTA, and pay-as-you-go retiree healthcare costs. The roll has prepaid debt service more than one year in advance. The roll is substantial: the account peaked in FY 2023 at \$6.1 billion. The FY 2026 BSA totaled \$2 billion (New York City Office of the Comptroller 2026).

Another savings vehicle is the retiree health benefits trust (RHBT). Before the RHBT, the City used pay-as-you-go funding for retiree health benefits out of the current operating budget. The RHBT allows the City to set aside money to help pay for these long-term expenses. The funds can only be used to pay for retiree health benefits, so the potential amount for countercyclical stimulus is limited to the current year’s liability for those benefits (Rosenberg 2020). For example, in 2020 the de Blasio administration estimated the RHBT contribution would be \$2.2 billion. If the City wanted to “borrow”

\$1 billion, it would pay \$1.2 billion into the trust and deplete the savings already in the trust by \$1 billion, which would free up \$1 billion in the current budget. As of FY 2025, the RHBT totaled \$5.2 billion.

In 2019 New York City residents voted to amend the City Charter to allow a Revenue Stabilization Fund (also known as the Rainy Day Fund or RDF) which was approved by State legislators in 2020. The fund formally allows the City to set aside resources for hard times, as the RHBT was an informal way to save. The only rule in the RDF's initial conception was not to withdraw more than 50 percent of the fund in any given year unless the Mayor cites a "compelling fiscal need" (New York City Office of the Comptroller 2022). The NYC Commission on Government Efficiency (COGE) held public hearings to discuss reforms to the RDF structure, suggesting a target amount of 12 percent of City tax revenue and the development of formal deposit rules. As of FY 2027, the level of the RDF is \$2 billion.

The City has two smaller reserves, the General Reserve fund and Capital Stabilization Reserve fund. Although the General Reserve is technically a reserve fund, it functions more like a short-term savings account, plugging gaps as they arise in the current year. Fund contributions are usually a flat amount, allocated without an intent to redistribute funding in good times to bad times (New York City Office of the Comptroller 2022). The Financial Emergency Act requires a minimum of \$100 million general reserve at the start of the year; the City usually contributes more in good years. The fund peaked in FY 2023 at \$1.5 billion. As of the FY 2027 adopted budget, the City plans to contribute \$450 million in FY 2027 and \$1.2 billion in subsequent years.

The Capital Stabilization Reserve pays for capital project costs that cannot legally be paid for by issuance of bonds. Functionally, the reserve supplements the General Reserve. There is no legal minimum for the fund and the City usually makes small contributions. As of the FY 2027 executive budget, the Capital Stabilization Reserve is \$0, with contributions set to increase to \$250 million from FY 2028 to 2030.

Going forward, the BSA may become a less important tool for saving (Perry 2026). Now that the City can legally save its surplus in a rainy day fund, it no longer needs the BSA as a de facto reserve fund. Instead of prepaying future expenses with surplus funds, the City can deposit surplus funds to the rainy day reserve.

Figure 7 provides a summary of the City's savings vehicles. The second column shows the current balances of these vehicles as of September 2026. The third column lists the limits of each vehicle as far as obtaining funds for countercyclical fiscal policy.

Figure 7:

NYC savings vehicles: balances and limitations

Savings Vehicle	Balance	Limitations
Budget Stabilization Account (BSA)	\$2 billion (FY 2026)	Amount of funds limited to amount of prepayment done in prior year
Retiree Health Benefits Trust (RHBT)	\$5.2 billion (FY 2025)	Amount of funds limited to current-year liability for benefits
Revenue Stabilization Fund (i.e. Rainy Day Fund)	\$2 billion (FY 2027)	Withdrawal amount limited to half of fund balance unless Mayor declares “compelling fiscal need”
General Reserve	\$450 million (FY 2027)	Funds typically used as “in-year” reserve for unforeseen contingencies
Capital Stabilization Reserve Fund	\$0 (FY 2027)	Funds allocated for capital project costs that cannot be funded by bonds

Source: New York City Office of the Comptroller 2026

Takeaway: New York City can implement countercyclical fiscal policy by reducing the size of its asset positions.

The City could stop prepayment to the Budget Stabilization Account and use that money to stabilize incomes and ensure people have access to basic necessities. It would not make sense for the City to pay for its future debt service bills while laying off teachers and reducing public assistance. The City can also draw down other reserves, with the major savings vehicle being the Rainy Day Fund.

Increase pension flexibility

The City uses substantial budget resources to prefund future pension obligations. As of FY 2026, the City paid \$10 billion to its pension funds, about nine percent of the overall budget. The City’s five major pension funds, known as “the Systems,” are the fourth largest public pension plan in the United States, managing \$328.87 billion in assets as of May 2026. For FY 2027, the Systems’ reported funded ratio was above the national average at around 85 percent. It is worth asking if prefunding is necessary, and if so, to what extent. By moving away from 100 percent prefunding, the City could leverage countercyclical fiscal power while not impacting pension fund sustainability.

Pension fund contribution is based on a target of 100 percent prefunding. The actuarially required contribution (ARC) covers not only the “normal cost” (pension cost

for an additional one year of service credit) but also the amortized unfunded accrued liability (UAL) (New York City Office of the Actuary 2025). The ARC is set by the City Actuary to close the UAL over time, such that the present value of future assets is enough to pay the estimated cost of future benefits. In other words, the City's contribution is set with the intention to make the pension plans 100 percent fully funded. Before the FY 2027 executive budget plan to re-amortize UAL payments, the City was set to reach fully funded status across all its major pension funds after 2032 (New York City Independent Budget Office 2025). The newest FY 2027 executive budget re-amortization proposal aims to pay off the UAL by 2037 (Perry 2026).

Credit rating agencies also put pressure on state and local governments to fully fund pensions, using a variety of metrics to rate the funding. For example, Fitch Ratings states a funded ratio of 70 percent or more to be adequate, while S&P assigns a strong rating for funding ratios 90 percent or more. Typically the more fully funded the plan, the better the rating and outlook for the City's debt rating. S&P notes that "overall, the higher the funded ratio, the more likely that accumulated assets will be able to support annual benefit obligations. Generally, S&P Global Ratings will favorably view a pension fund with a funded ratio trend that is stable or increasing. Funded ratios that are 100 percent or higher are viewed most favorably" (S&P Global 2007).

Prefunding at 100 percent is not necessary to ensure all future pension obligations are met. Whether the City has a funding ratio of 100 or 50 percent, the legal obligation to pay benefits due is the same. As long as total contributions cover the present value of benefits accrued by all employees for an additional year of service (i.e. normal cost) and inflation, then the unfunded liability should not grow. In other words, the pension fund can be sustainable at levels well below 100 percent. For example, Social Security has effectively operated for decades at very low levels of prefunding in its trust (Sgouros 2017). Related, while actuaries use 20-year periods to amortize UALs, the actual time to "catch up" could be decades longer.

Small changes in long-term assumptions can drastically reduce funding ratios for otherwise healthy plans. For example, when New York State lowered the City's pension funds assumed rate of return from eight percent to seven percent after the 2008 financial crisis, it created a multi-billion dollar brand new (unfunded) liability (Perry 2026).¹ The City had to address this newly-created unfunded liability by making legally required contributions to pay it down over a 20 year period.

Full prefunding is not necessary to avoid reduction or discontinuation of pension benefits. Politicians may use underfunding to argue for a reduction in current or future pensioner benefits. If a pension plan is underfunded enough, policymakers may argue the system is unsustainable and must be replaced by a defined contribution plan. Both arguments rest on the idea that 100 percent prefunding is necessary. As argued above, pension funds with low funding ratios can be sustainable and thus there is no reason to

¹ Some liability comes from pension funds underperforming, not just the assumed rate of return change.

cut benefits or switch to defined contribution plans just because a fully funded ratio is out of reach. Furthermore, there's a convincing argument that closing a pension fund or switching to a defined contribution plan is not riskless and could potentially leave a government in a more dire situation due to the loss of contributions flowing into the system (Sgouros 2017).

Instead of focusing on a 100 percent funding ratio, alternative metrics can better assess the long-term sustainability of pension plans. Funding ratios tell policymakers how much money the plan has to pay off its debt tomorrow, but virtually all plans will not close tomorrow. A more useful metric might be computing the year in which the pension fund will run out of money given current trends (Sgouros 2017). The fund would be considered sustainable if each year the date advanced.

Louise Sheiner of the Center for Retirement Research argues that pension plans that stabilize their debt-to-GDP ratio can be sustainable even if not fully funded (Sheiner 2023). Using this metric produces required contributions less than the 100 percent funding ratio, without giving up plan sustainability. This means more funds could be available to address current needs. For example, in FY 2026 the City paid \$10 billion to its pension funds, an amount determined based on a long-term target of 100 percent prefunding. If the City paid 90 percent of this actuarially determined amount, then it would have paid \$9 billion, freeing up \$1 billion for current needs².

Public pension plans were historically funded on a pay-as-you-go basis out of the City or State's current revenue (Urban Institute). 1974's Employee Retirement Income Security Act set standards for retirement plans in private industry; 1984's Government Accounting Standards Board (GASB) set standards for state and local governments to report benefit obligations and pension fund assets. State and local governments then moved towards prefunding with many setting legal requirements for contributions.

Given this, it is worth analyzing the benefits of the pay-as-you-go system. Annual pension withdrawals historically grow at a slow, stable rate and thus are relatively predictable. It is easier for the City to budget for expenses like this year-to-year.

Another argument for a full or partial pay-as-you-go system is that it would directly connect and hold policymakers accountable for pension related decisions. For example, better benefits would increase current expenses, so policymakers advocating for them would have to fund them. Conversely, policymakers arguing for a reduction in benefits would have to answer to pensioners in real time (Sgouros 2017).

² This gives a sense of the stakes involved lowering the funding ratio target, not a formal estimation.

Takeaway: The City should reassess pension fund sustainability.

New York City built up considerable pension assets relative to its obligations. Achieving such a high level of prefunding requires forgoing a substantial amount of current resources. By using metrics alternative to the funding ratio, the City may find long-term sustainability can be achieved by lower contributions, thus freeing up current resources for countercyclical purposes. The City could create a committee within the Mayor's Office of Management and Budget (OMB) to study the costs and benefits of a full or partial pay-as-you-go funding for the City's pension funds.

5. Rethinking Debt as a Countercyclical Tool

"What do you do if you don't have the option of some amount of borrowing? You have to do massive cuts, massive cuts to all city agencies," Mr. de Blasio said on Thursday. "That will undermine any possibility of the right kind of restart and recovery. So, borrowing the right way, it makes sense" (Ferre-Sadurni, Mays, and McKinley 2020).

Issuing debt to stabilize incomes and maintain public programs and services not only reduces the severity and length of a recession, but greatly improves people's material living conditions and keeps economic activity vibrant. Borrowing to cover within-year cash flow gaps and for long-term capital projects are generally accepted practices. However, the stigma around deficit financing has dissuaded policymakers from using it even at sensible times. New York City can expand its countercyclical fiscal policy potential by utilizing all its legal borrowing capacity and reconsidering the use of deficit financing during a downturn.

New York City has the legal capacity to borrow for operating expenses on a very short term basis. After the 1970s fiscal crisis, the Financial Emergency Act (FEA) imposed strict budgetary rules, including the stipulation of a balanced budget at the end of each fiscal year. During the fiscal year, the timing of revenues coming in and bills due does not match. To solve this, the City can issue within-year short-term debt. The maximum amount of tax anticipation notes (TANs) issued is 90 percent of the available tax levy, meaning total amount of City real estate taxes (New York City Charter), and must mature within the fiscal year they were issued in. Revenue anticipation notes (RANs) are issued in anticipation of a specific type of revenue. RANs are capped at 90 percent of available revenues (meaning revenues other than real estate taxes) and must mature within the fiscal year issued. RAN renewals can mature in the fiscal year following that of original issuance (New York City Office of the Comptroller 2024). Before 2004, it was quite common for the City to issue RANs to cover short-term cash

needs (New York City Office of the Comptroller 2004). During the next downturn, the City can utilize its ability to borrow on this short-term basis.

New York City can also legally borrow money to finance capital projects. In theory, the City could heavily increase its borrowing and stimulate the local economy by spending on large scale capital projects such as the building of new schools, libraries, or repairing roads and bridges. This particular route is promising because issuing bonds for capital spending does not require authorization from the State. The only legal limit is on debt capacity, which is tied to real estate valuation and personal income tax revenue (New York City Independent Budget Office 2026).

Not all bonds issued by New York City are counted against the general debt limit, such as the Building Aid Revenue Bonds (BARBs) issued by the Transitional Finance Authority or bonds issued by the Municipal Water Finance Authority (New York City Independent Budget Office 2026). As of June 2025, the City could legally borrow an additional \$44 billion to finance capital projects (New York City Office of the Comptroller 2025). This represents significant untapped countercyclical stimulus potential – the largest of all discussed here – to be considered carefully.

One significant problem with countercyclical capital spending is that the City's capital needs do not follow the business cycle. Capital needs are driven by growth and old infrastructure. If the City needs to build new schools for enrollment growth and repair crumbling bridges, it should not wait for the next downturn. My previous research found state and local policymakers do not try to "time the market," meaning the interest rate on debt is not a critical factor in deciding capital projects to engage in (Page-Hoongrajok 2021). Even though prices and interest rates are relatively high and state and local governments might not *want* to borrow to fund capital projects, they do because they feel they must.

Another problem with countercyclical capital spending is that shovel-ready projects are usually not shovel-ready. Countercyclical spending aims to get money to people to spend quickly. But projects that are truly shovel-ready already have funding in place. Any new funding the City obtains through bond sales will go to fund brand new projects, which then must go through an (often lengthy) development process.

Despite these challenges, countercyclical capital spending is still a worthwhile tool to consider, especially if state and local budget officials intentionally try to think in a countercyclical way. Even if timing and shovel-ready issues were not resolved, starting capital projects during a recession can still boost spending in future years, making a recovery stronger. The timing issue is less relevant to New York City because there are many capital projects. For example, if the City engages in large-scale projects during a boom due to need, there will still be other large-scale projects in the ten-year Capital Plan that the City can act on in the event of a recession.

In addition, there are capital projects like new bike and bus lanes, and replacing park benches, that are more straightforward (Perry 2026). If the City took countercyclical fiscal policy into account when capital planning, it could identify suitable projects to scale during a recession (Perry 2026). Furthermore, the City Council has discussed speeding up and streamlining construction projects. For example, contracting the same entity for the design and build of a capital project can reduce delays and minimize discrepancies between estimates of how much a project will cost and its actual cost (New York City Council, Finance Division 2026). Ideas like this can facilitate more shovel ready projects.

Another challenge in rethinking debt as a countercyclical tool is that borrowing for operational expenses is generally frowned upon for interrelated reasons. First, borrowing creates a long-term liability to pay for a short-term operating cost or need. This is considered unsustainable since the borrowing does not fix the underlying cause of the deficit. Second, a City's credit rating can suffer, leading to higher borrowing costs and increasing unsustainability. Third, there are concerns about shifting a current generation's debt to future generations. But when we apply these concerns to countercyclical deficit financing, the relevance diminishes.

According to the logic of deficit financing opponents, the best time to deficit finance is in a recession. If a state or local government is facing a revenue shortfall due to no fault of its own, it makes sense to borrow to make up for it. The government is not plugging structural operating gaps or doing it on a recurring basis. There is a critical difference between using deficit financing as a last resort and never using it at all.

State and local governments can successfully deficit finance without going bankrupt. When municipal bankruptcies occur they are covered heavily by the media. No such headlines cover state and local governments successfully paying back loans. This may lead to the belief that subnational bankruptcies occur frequently and successful repayment is the exception.

History shows this belief is backwards. For example, New York City deficit financed after 9/11 with "Recovery Bonds." The City has legal restrictions on borrowing (discussed in Section 1) but deficit financing is possible with approval from New York State. After 9/11, the City was authorized to issue \$2.5 billion in deficit financing bonds and issued about \$1.9 billion (Office of New York State Comptroller 2020). The issuance of debt allowed the City to address critical needs in a dire time. The City successfully paid down this debt as of FY 2023.

Over Covid-19, the State of New Jersey deficit financed to the tune of \$4 billion.³ The bond's interest rate was below two percent and there was strong demand for the

³ New Jersey also passed a law (A3971) that allowed municipalities and counties to issue "coronavirus relief bonds" that would cover revenue shortfalls caused by the pandemic. The Bergen Record reports that 86 towns, or about 15 percent of New Jersey municipalities, moved to authorize borrowing.

bonds among investors (Reitmeyer 2020). The state is repaying the debt over a 12 year period. A recent budget report stated the State is paying off the debt, with no mention of the debt putting undue pressure on the latest budget (Reitmeyer 2026).

Since the borrowing, New Jersey's credit rating has been upgraded eight times (State of New Jersey Office of the Treasury 2026). This means that deficit financing during a downturn does not doom a government to a permanently poor credit rating. While the rating did suffer from S&P and Fitch downgrades in the run up to the bond sale, it isn't clear the downgrades were a result of the intention to borrow. These drops may have occurred without deficit financing, since the credit agencies' main concern cited were structural deficits.

New York State borrowed \$10 billion from the federal government over Covid-19 to continue making unemployment insurance (UI) benefit payments and paid it back without issue (Center for New York City Affairs 2025). The spike in unemployment claims early in the pandemic completely overwhelmed many states and depleted New York's UI Trust Fund of \$2.5 billion, thus driving the need to borrow (New York State Office of the Governor 2025). The State then stabilized incomes and paid the loan back when the economy recovered. This is exactly the point of deficit financing. Borrowing longer term to pay for current bills is a fear of deficit finance opponents. However, there was little backlash when these mechanisms were at work during Covid-19.

In terms of nationwide borrowing, a 2021 Pew report examined 442 municipal bonds issued over \$100 million from August to December 2020. Anywhere from one quarter to one half were used for some kind of deficit financing (Pew 2021). Both borrowers that participated in the Federal Reserve's Municipal Liquidity Facility (State of Illinois and the Metropolitan Transit Authority) successfully paid back their loans.

Future New Yorkers benefit from present deficit financing. Opponents argue that current residents receive the benefits of borrowing, but the cost is spread to future generations who may not benefit. Given the timeframes of pandemic deficit financing, it is likely the generation that received borrowing benefits is the same generation paying it back. New Jersey towns wishing to borrow had to repay within five years (up to ten for special circumstances). New Jersey State borrowed with a repayment plan of 12 years. Even the longest repayment period, for New York City's Recovery Bonds, took about 20 years to repay.

Children directly and indirectly receive benefits from the sustaining of essential services. As Figure 4 showed, almost half the City budget goes to education and social service spending alone. Helping families avoid eviction, hunger, or health emergencies does not exclusively help adults.

Deficit financing can lessen a downturn's severity and duration, leading to strong economic growth and labor markets in the long-run. The long 2008 recession was associated with growth that never returned to trend, while the shorter 2020 recession

was associated with future growth that returned to pre-recession trend. Interrelated, using deficit finance to stabilize incomes and demand during a downturn can prevent prolonged weak labor markets, improving lifetime earnings of young people entering the labor force. Thus, future New Yorkers will experience better economic growth and employment prospects than they would have without deficit financing.

Future New Yorkers also benefit from a vibrant city with robust public services. Every year the City spends a substantial amount on public services. If the City refuses to use deficit financing while federal government assistance decreases, it is likely these essential services would be cut. When a city becomes an unattractive place to live and people move out, it erodes the city tax base, leading to further degradation of public services. As one New York Times article put it:

“The Financial Control Board forced the city to absorb drastic spending cuts: Workers were let go and hospitals were closed. Crimes and disorder rose; tens of thousands of residents fled the city, as New York turned into a national symbol of urban decay” (Ferre-Sadurni, Mays, and McKinley 2020).

Deficit financing during recessions would allow New York City to minimize spending cuts and keep critical services intact. In the long run this attracts more residents and businesses, leading to stronger growth and better employment opportunities.

Takeaway: During a downturn, the City should utilize short- and long-term borrowing to the extent necessary.

Debt can be a powerful countercyclical tool. New York City has the legal right to borrow on a short-term basis, and can legally borrow for capital projects. Capital spending could be made into an even sharper tool for countercyclical fiscal policy if budget officials incorporate countercyclical considerations into their debates, discussions, and projects. Policymakers should recognize that deficit financing has long-term benefits and does not automatically set the City on a path of unsustainable debt. Albany could validate this point by allowing New York City to deficit finance during the next recession.

6. Recommendations

Below are ten recommendations for implementing and expanding the capacity for countercyclical fiscal policy in New York City. Each is motivated by the arguments presented in this report. Short-term recommendations are actions the City can take swiftly and unilaterally. Medium-term recommendations are actions requiring State

government approval. Long-term recommendations are specific ways the City can explore long-term, meaningful expansion of its countercyclical capacity.

Guiding principles:

New York City and New York State policymakers should bring a countercyclical perspective to their work. State and local government officials often do not consider countercyclical fiscal policy their responsibility. This can lead policymakers to act in ways that exacerbate a recession instead of combatting it. If New York City budget officials and policymakers incorporate countercyclical considerations into their discussions, debates, projects, and overall work, the City's potential for countercyclical fiscal policy action would become clearer.

New York City's countercyclical fiscal policy toolkit should contain a variety of tools. Relying on one tool to weather a recession is unwise. New York City drew on a number of actions to get through the last three downturns (Office of New York State Comptroller 2020). Even flush rainy day funds may be inadequate to make up for revenue shortfalls. Targeted, progressive tax increases may raise significant funds but there will be other worthwhile uses for those funds. Ideally, New York City's countercyclical fiscal policy toolkit would rely on a mix of tools.

Short-term recommendations:

These are actions the City can take swiftly and unilaterally. In the event of a downturn, to implement countercyclical fiscal policy, New York City should:

1. **Increase or at least maintain multiplier spending.** Multiplier spending is spending that directly helps stabilize demand, incomes, and employment. For example, spending on salaries, wages, equipment, and public assistance are desirable because it can reduce the duration, severity, and general pain of a downturn. Countercyclical fiscal policy aims to increase or maintain this spending as much as possible during a recession.
2. **Stop the prepayment of future expenses.** To the extent that the Budget Stabilization Account (BSA) is still used, the City should stop the prepayment of future expenses during a downturn. This money should be used to stabilize incomes and to help ensure people have access to basic necessities. For example, it would not make sense for the City to pay for its future debt service bills while laying off teachers and reducing public assistance.
3. **Draw down available reserves as needed, within legal limits.** Since the capital reserve is small, the RHBT is limited to the current year's liability, and the general fund balance is volatile, the rainy day fund is likely the major savings vehicle going forward. When a downturn occurs, the City should withdraw savings from the rainy day fund and other reserves to maintain essential services.

4. **Issue RANs and TANs to help cover short-term revenue shortfalls.** New York City has the legal capacity to borrow for operating expenses on a very short term basis through revenue anticipation notes (RANs) and tax anticipation notes (TANs). During a downturn, the City should utilize their capacity to issue RANs and TANs to help cover short-term revenue shortfalls.
5. **Utilize long-term borrowing capacity to maintain capital project spending throughout a downturn.** As of June 2025, New York City was \$44 billion below its legal debt carrying capacity. The City should issue long-term debt to finance capital projects during a downturn. Policymakers could identify capital projects that could be implemented quickly to get money into people's pockets. Even longer-term projects are desirable to provide a boost of spending into the recovery period.

Medium-term recommendations:

Before a downturn occurs, New York City should increase its countercyclical fiscal policy power potential by making the case and advocating for changes that require State government approval. The State can enable the City to:

6. **Implement targeted, progressive tax increases.** Targeted, progressive tax increases would bring in revenue for the government to maintain multiplier spending while minimizing the overall impact on aggregate spending. The State of New Jersey used these tax increases countercyclically during the pandemic.
7. **Deficit finance during the next recession if the City decides the benefits outweigh the costs.** Deficit financing has long-term benefits and does not automatically set a city or state on a path of unsustainable debt. Studying the costs and benefits of deficit financing would allow State legislators to make more informed decisions if and when the City asks Albany's permission to borrow during a downturn.

Long-term recommendations:

New York City can evaluate conventional, institutionalized views on sound finance and research what changes could facilitate the most stimulus in the event of a downturn. Specifically, the City should:

8. **Identify spending that can be legally rerouted to multiplier spending during a downturn.** Non-multiplier spending is spending that does not directly help stabilize demand, employment, and income during a recession. This spending includes debt service, pension contributions, and tax expenditures. The City should identify all non-multiplier spending and explore the desirability and legality of rerouting those payments to multiplier spending.

9. **Explore metrics other than the funding ratio to assess sustainability of pension funds.** New York City spends a significant amount of money to stay on the path to a 100 percent funding ratio. 100 prefunding is unnecessary for pension fund sustainability. Much lower funding ratios could be consistent with long-term sustainability. The City should explore alternative metrics to assess the long-term health of their pension plans.
10. **Create a committee within the Mayor's Office of Management and Budget (OMB) to study the costs and benefits of a full or partial pay-as-you-go funding for the City's pension funds.** Historically, state and local governments paid pension obligations that were due out of their current revenues. It is worth asking what, if anything, was lost in the shift to prefunding. The OMB should convene a committee to study the costs and benefits of a full or partial pay-as-you-go funding for the City's pension funds.

Glossary

Assets: Things an entity (like New York City) owns that have value.

Asset side adjustments: When an entity (like New York City) makes deliberate changes that affect the size of its asset holdings. For example, if the City does not contribute to its Rainy Day Fund or its pension funds, it makes its asset position smaller than what it would have been.

Balanced budget rules: Legal rules that force state and city governments to limit expenditures to revenues collected in a fiscal year. To comply with these rules, governments may have to cut spending or raise new revenue.

Business cycle: The economy moving through phases of recession (lowest point), expansion, boom (highest point), and contraction.

Capital projects: Building or improving physical assets, i.e. buildings, transit etc.

Countercyclical fiscal policy: The government increases its spending when private households and businesses reduce their spending. The government acts to get money in people's hands so they spend it quickly. This helps stabilize demand, employment, and jobs.

Debt: Things that an entity (like New York City) owes, i.e. bonds, future pension obligations.

Debt side adjustments: When an entity (like New York City) makes deliberate changes that affect the size of its debt. For example, if the City issues more debt to finance capital projects during a recession, it is increasing the size of its debt position relative to what it would have been.

Disposable income: What households have left to spend after taxes.

Economic scarring: The harmful, long-term effects of a deep downturn and slow recovery. Examples include increased long-term unemployment, prolonged weak labor markets, and depressed growth.

Multiplier spending: Spending that directly helps stabilize demand, incomes, and employment. For example, spending on salaries, wages, equipment, and public assistance.

Non-multiplier spending: Spending that does not directly help stabilize demand, employment, and income during a recession. This type of spending includes debt service, pension contributions, and tax expenditures.

Pay-as-you-go: Paying for (pension) obligations with current revenues.

Procylical fiscal policy: When a government acts in ways that go with the business cycle instead of against it. For example, during a recession, private households and businesses tend to cut back their spending. Procylical fiscal policy would be a government also cutting their spending.

Stimulus funds / stimulate: When a government intentionally gives money to households and businesses in various forms in the hopes they spend it.

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