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Fitch Ratings: U.S. Infrastructure Needs Federal Funding Commitment

Fitch Ratings-New York-15 May 2019: Any U.S. federal government plan for renewing infrastructure will need to provide for consistent, continued federal funding and more diverse funding sources to fully address the infrastructure deficit, says Fitch Ratings. The April meeting between the President and Democratic Congressional leaders in which they agreed to work toward a $2 trillion infrastructure plan was a first step in addressing infrastructure needs; however, the difficulty of hammering out the details may keep the plan from advancing. The second meeting between these parties, tentatively planned for the week of May 20, may provide more information regarding what level of federal funding the White House would back but ultimately Congress will need to get behind proposed legislation.

Federal funding will be an important factor in any plan's viability, as will private participation. The nation's significant infrastructure needs, encompassing not only transportation but also utilities, housing, and other social infrastructure, will require ongoing funding from various parties. Relying only on states and local governments will not be enough.

That said, with no federal plan currently in place, states have become increasingly proactive in raising necessary infrastructure money for themselves and local governments, primarily for transportation. Since 2013, 31 states raised gas taxes according to the National Conference of State Legislatures, including four in 2019 alone. Highway tolls were also used to pay for infrastructure not directly related to tolled roads and Fitch notes challenges to such policies have been rejected by the courts so far.

However, state and local governments are unable to raise adequate funds to fully address infrastructure needs on their own. State revenue growth since the end of the Great Recession has generally been slow, and coupled with rising costs for items such as pensions, Medicaid, and public education, states' budgets have limited headroom for additional spending on infrastructure. Local governments are similarly constrained with modest revenue growth and rising costs for pensions and other employee benefits, public safety and a varying tolerance for additional debt.

As an additional tool, a number of states, and increasingly municipalities, have turned to public-private partnerships (PPP) to procure a wide variety of projects, including roads and bridges, civic centers, courthouses and even public schools. While PPPs can impose long-term cost burdens for governments similar to traditional public procurements, in certain situations the PPP model can accelerate projects and has the potential to yield long-term savings if risks are appropriately managed. Given broad infrastructure demands, we anticipate continued growth in PPPs using private financing such as private activity bonds.

With details to be worked out, it may be hard to get any plan off the ground if Congress is unable to agree on the source of federal funding. Split control of Congress makes passage of such a large infrastructure bill tenuous. Disagreements exist over gas tax increases, reducing federal tax cuts and increasing the federal deficit. A plan proposed last year by the White House did not result in

legislation.

Any infrastructure plan should provide for the renewal and replenishment of the federal highway transportation fund (HTF), which is the primary source of existing federal infrastructure funding and is supported primarily by federal gasoline taxes. The HTF provides around $40 billion in highway spending and $10 billion in transit spending to states annually. Since 2008 the HTF required transfers from the Treasury's general fund to close its revenue gap. The Congressional Budget Office forecasts the HTF will be depleted in 2022 without another infusion of general fund dollars. Putting the HTF on a sustainable fiscal path would serve as a strong indicator of the federal government's commitment to long-term infrastructure investment.