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Fitch: US State Budgets Poised for Slower Growth After Fed Rate Cuts

Fitch Ratings-New York-19 September 2024: U.S. states are settling into a new normal of slower revenue growth after the Federal Reserve's first interest rate cut in four years, according to Fitch Ratings analysts during a webinar yesterday. Fitch economists project a sizeable slowdown in growth for 2025 and a series of interest rate cuts through 2026. The labor market and job growth are already slowing down, and the same trend appears likely for for state budgets.

"Managing expenditures to revenues is nothing new to states, but the pandemic was an extraordinary outlier that states had to adjust to in the moment," said Senior Director Karen Krop. "States had already learned the importance of building fiscal resilience during good times from the global financial crisis, and this lesson helped them weather the pandemic."

By adding to their coffers in recent years, states have been able to head off negative peformance pressure and smoothly downshift from what Krop called "first booming, then slowing, then normal growth."

After cresting in 2023, the wave of new state tax cuts appears to be ending. Senior Director and U.S. state government group head Eric Kim pointed to California, Illinois and New Jersey as states that have recently raised taxes in part to address budget gaps.

Time will tell how the direction of the broader economy post-rate cuts will affect the state labor picture. Kim noted a wide range of disparity in terms of non-farm payrolls growth across the states; through July, Idaho and Utah grew over 10% growth above pre-pandemic levels, while Hawaii, Louisiana and Maryland were stalled below pre-pandemic employment levels.

Additional information is available in Fitch's state budget report at www.fitchratings.com.