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S&P: U.S. State Debt Levels May Be More Sustainable Than the Condition of the Nation's Infrastructure.

U.S. state tax-supported debt outstanding, in the aggregate, continues to increase but at a subdued pace. According to Standard & Poor's Ratings Services' calculations, total tax-backed state debt outstanding grew by just 1.9% in fiscal 2014. State debt balances have increased at anemic rates ever since the onset of the Great Recession (not including 2010 when there was a surge of issuance under the Build America Bond program). Given the widely acknowledged inadequacy of U.S. infrastructure, it's tempting to summarily conclude that the slow pace of new debt issuance, which has persisted through an extended period of low interest rates, represents a missed opportunity. In our view, however, this interpretation of recent state debt trends is simplistic.

U.S. states navigated the Great Recession adroitly, for the most part, with their credit profiles intact. Policymakers have managed this difficult environment by maintaining a sustained focus on their states' fiscal margins, which — already narrow — are likely to remain tight in the years to come. The Urban Institute reported that — as of February 2015, when states were crafting their budgets — aggregate revenue growth was expected to remain slow. The states anticipated revenue growth of just 1.7% and 1.2% for fiscal years 2015 and 2016, respectively, which would be well below the long-term growth rate of 2.5% (in real terms). (1) Likely in response to this slow revenue growth, lawmakers have recognized that the cost of new debt goes well beyond additional debt servicing costs and includes taking on new operations and maintenance (O&M) expenses.

Overview

- Current state debt levels are sustainable, in Standard & Poor's view.
- State infrastructure needs top what states can currently finance in traditional ways if they are to maintain credit quality.
- States' lower-than-normal funding of infrastructure projects may be because of the increased ongoing O&M costs such projects would require.

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