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Moody's: U.S. Local Governments Outlook Remains Stable Due To Steady Revenue Growth, Healthy Reserves.

New York, December 07, 2016 — The outlook for US local governments will remain stable as the majority of the sector is underpinned by solid property tax revenues and healthy reserves, Moody's Investors Service says. The outlook indicates fundamental business conditions over the next 12 -18 months.

Property taxes, the bedrock of local governments, remain healthy and will continue growing in 2017 owing to broader local tax base growth returns to pre-recession levels.

"A combination of property value growth and tax rate increases drove revenues 5.1% higher in the first half of 2016. We expect these factors will continue to support revenue growth of 3%-5% in 2017," according to Moody's Analyst Sarah Jensen.

Moody's says reserve levels remain healthy for most local governments and provide budget flexibility. Most local governments will continue to actively raise revenues or cut spending as needed to maintain these reserves through 2017. Reserves provide flexibility for local governments in times of unexpected economic stress and unpredictable expenditures.

While manageable for most, overall fixed costs and growing balance sheet liabilities are a long-term drag on the sector. Fixed costs such as pension liabilities, debt service and other post-employment benefit (OPEBs) contributions could, if unaddressed, begin to crowd out essential services.

Infrastructure needs are becoming more pressing, and rising fixed costs could hamper the ability to issue debt to address this issue.

Despite general stability across the sector, there is a growing portion, roughly 5% -10% of issuers, facing numerous challenges pressuring their credit profiles. These local governments face revenue stagnation combined with growth in fixed costs, leading to a trend of credit deterioration.

Moody's would change the outlook on the sector to positive if strong property tax revenue growth continues at 4%-5% and is accompanied by a stabilization of fixed costs and maintenance of healthy reserves. The sector outlook could change to negative if property tax revenue growth weakens to 1-2% or growth is outpaced by the increase in long-term liabilities and fixed costs.

"Financial challenges at the state level, particularly in states hit by low energy prices or budget imbalances, could impact some municipalities and school districts as states could either cut aid or shift fiscal responsibilities to local governments," said Jensen.

"Local Governments — US: 2017 Outlook - Strong Tax Revenues, Healthy Reserves Drive Stability for Most." Is available to Moody's subscribers at

https://www.moody's.com/researchdocumentcontentpage.aspx?docid=PBM_1045982.

This report is part of a series of 2017 Credit Outlooks that provide insight into next year's credit conditions across all sectors. See more at www.moodys.com/2017outlooks

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