
Fitch: Vaccine Mitigates Downside for US Public Finance; Risks Remain

Fitch Ratings-New York/Chicago-17 December 2020: Widespread availability of a coronavirus vaccine would help mitigate downside risk to US public finance (USPF) performance in the second half of the year, Fitch Ratings says. Extraordinary levels of federal economic stimulus have supported USPF credit quality throughout the pandemic, and vaccinations lessen the risk that support will end before business and consumer confidence leads to a sustained recovery. However, significant execution risks remain. Delays in vaccine availability or low inoculation rates would result in significantly weaker growth in 2021 and greater budget stress on credits.

We expect stagnant growth in 1Q21 with a surge in virus cases and hospitalization rates, the expiration of pandemic unemployment assistance at the end of 2020, and the initial limited vaccine distribution. Healthcare, higher education and state and local government credits will continue to see reduced revenues and increased expenses in 2021 and may rely on cost cutting, debt, and draws on liquidity and reserves. Renewed federal stimulus would help support the economy, but we do not assume additional direct aid in our USPF ratings.

Fitch's expectation for US GDP growth in 2021 has been revised upward by 50bps to 4.5% based on the large-scale dissemination of a vaccine, which is expected to bolster economic recovery in 2H21 with the easing of social distancing and shutdowns. Pfizer/BioNTech vaccine distribution began Monday and Moderna's vaccine is expected to be approved by the US Food and Drug Administration as early as Friday, with the Centers for Disease Control and Prevention recommending that health care workers and residents of long-term care facilities be first to receive vaccinations.

Not-for-profit hospitals and life plan communities (LPCs) will benefit from vaccine prioritization for its staff and, in the case of LPCs, residents. By reducing coronavirus hospitalization rates, inoculation will allow a return of elective procedures to pre-pandemic levels toward the end of 2021. Vaccination is expected to help bolster confidence in accessing health services, improving margins by driving volume and revenue increases, while alleviating labor cost pressures.

Widely available vaccines would help higher education student-driven revenues recover in fall 2021 and stabilize conditions for those schools that rely on non-recurring stimulus or expense cutting. As travel restrictions ease, we may see some recovery in international student interest. For those institutions that already exhibited weaker demand characteristics, enrollment may not return to previous levels. The coronavirus' lingering effects on revenues will require ongoing matching expense reductions, including cuts to staff, supplies and capital, which could increase in magnitude if net revenues remain pressured into FY 2022.

State and local governments should be able to lift lockdown restrictions as more people are vaccinated, boosting economic activity. The positive impact on sales and income tax revenues may not be felt until the next fiscal year for some credits, however, and in the meantime, a slow economic and jobs recovery will continue to squeeze budgets due to the lagged effect on finances.

The provision and administration of the vaccine may place logistical and financial burdens on state and local governments, adding to near-term pressures. Increased remote working and e-commerce, pre-pandemic trends that were accelerated will persist, affecting tax revenues long after the pandemic is contained. States and metro areas with large exposures to leisure and hospitality will see revenue erosion as a full recovery of this sector is unlikely in 2021, even with vaccinations.

Affordable housing and multifamily mortgage delinquency levels are currently low but may increase, particularly in areas with sustained high unemployment and slower economic recovery. In sectors that the coronavirus did not materially effect, namely public power and water and sewer, the vaccine should have limited positive upside.

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