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Fitch: Personal Income Spike Leads to Fall in Liability Metric for U.S. States

Fitch Ratings-New York-08 November 2021: Liability metrics for U.S. states fell for a fifth straight year in fiscal 2020, with a surge in personal income the primary catalyst, according to Fitch Ratings in its latest annual report. Actual liabilities remain largely unchanged over the past five years, however, indicating slow progress in addressing outstanding states' outstanding long-term obligations.

Federal measures to support individuals, businesses, and the economy at large helped spark the largest median state personal income jump in 14 years (6.3%). This resulted in Fitch-adjusted net pension liabilities (NPLs) as a percentage of personal income declining to 4.7% in fiscal 2020, from 5.2% as of fiscal 2019 across all states.

"Rapid personal income growth is likely to continue in 2021, given additional federal pandemic aid enacted early in 2021 and the broader economic recovery, with gains in 2022 likely to slow as federal aid expires," said Senior Director Doug Offerman. "Combined with rebounding investment markets, state liability burdens are likely to see further near-term declines."

Although their rankings shifted slightly compared to last year, the five states with the highest burdens remain unchanged, including Connecticut, Illinois, Hawaii, New Jersey and Alaska. Except for Alaska, the highest burden states have long-term liabilities above 20% of personal income. Fitch's data also shows 43 states with carrying costs below 10% of governmental expenditures in fiscal 2020, which Fitch views as low. Two states (Connecticut, Illinois) have elevated carrying costs in excess of 20% of governmental expenditures.

"States by and large avoided reductions to pension contributions as they addressed budget gaps with surging revenues and federal relief limiting fiscal damage from pandemic shutdowns," said Offerman. "Solid contribution practices look to continue at least in the near term, given the expansive fiscal flexibility provided by the economic rebound and the continued availability of federal pandemic relief funds available to offset other state needs."

Over the five years since changes to pension accounting resulted in more consistent reporting, the ratio of state pension assets to liabilities has barely changed. Adjusted to reflect a standard 6% investment return, the ratio stood at 61.7% in fiscal 2020, up from 60.4% in fiscal 2016. The stability of this ratio over time suggests that the state pension changes intended to improve sustainability have not yet meaningfully lowered pension burdens.

"State Liability Burdens Shrink in Fiscal 2020" is available at www.fitchratings.com.

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