

# **Bond Case Briefs**

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## **S&P U.S. Public Finance Mid-Year Outlook: The Heat Is On**

Ratings performance across U.S. public finance (USPF) remains stable despite continued high inflation, supply-chain issues, and a weaker economic outlook. While these economic conditions are all felt by USPF issuers differently, they have yet to materially weaken credit quality. Revenue growth remains positive due to relatively healthy employment and real estate conditions. Revenues have also benefited in the short term from inflation, but this won't be sustainable as the economy slows.

Federal stimulus and strong revenue performance have kept reserves at robust levels, which provides fiscal cushion. A significant amount of the \$350 billion in stimulus received by governments as part of the American Rescue Plan Act remains unobligated; while inflation and rising costs may affect the number or scope of projects that can be completed, a spending deadline of 2026 means it will continue to flow through the system for at least the next 18 months, generating jobs and supporting the economy.

Our recent North America credit conditions report ("Credit Conditions North America Q3 2022: Credit Headwinds Turn Stormy," published June 28, 2022, on RatingsDirect) highlights the U.S. suffering a "hard landing" as a top credit risk. As the Fed forges ahead with an aggressive cycle of monetary tightening, there's a growing risk that sharply rising interest rates, combined with a pullback by U.S. consumers in the face of nagging inflation, will push the world's biggest economy into recession (with an associated rise in unemployment). In a worse scenario, fuel and food inflation could remain high even if core inflation declines, leading to stagflation. All of this is compounded by the lingering effects of the pandemic.

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