Fitch Ratings 2024 Outlook: U.S. Public Finance Compendium

Outlook Compendium Report

Fitch's Sector Outlook: Deteriorating

Three of eight sectors (Not-For-Profit Hospitals, Life Plan Communities and Higher Education) in Fitch Ratings' U.S. Public Finance (USPF) portfolio continue to have 'deteriorating' sector outlooks for 2024, indicating our expectation that credit pressures will worsen this year amid persistent labor and cost pressures. Three of the sectors (States & Locals, Public Power and Water & Sewer) have improved to 'neutral' this year, from 'deteriorating' last year. The outlooks for Community Development & Social Lending (CDSL) and Transportation continue to be 'neutral,' as they were in 2023.

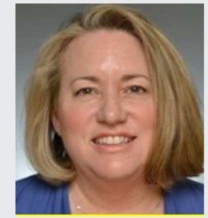
Rating Outlook Distribution

Overall, the distribution of Rating Outlooks continues to reflect the credit stability typical of USPF. Approximately 91% of USPF ratings overall have Stable Rating Outlooks, 5% have Positive Rating Outlooks and only 3% have Negative Rating Outlooks. Water & Sewer utilities have the highest proportion of Positive Rating Outlooks (10%) of any USPF sector, largely reflecting improving leverage profiles despite incorporating higher capex and operating costs. Conversely, Not-For-Profit Hospitals and Life Plan Communities share the highest percentage of Negative Rating Outlooks, both at 11%.

What to Watch

- Economic performance that is better or worse than the slow growth forecast in Fitch's December 2023 Global Economic Outlook could materially alter the sector outlook for US Public Finance credits. In particular, a deep and prolonged recession could lead public finance entities toward credit negative budget choices such as sustained pension funding deferrals or delays in payments.
- Continued dampening of inflation, paired with a more favorable labor market environment, could cause the outlooks to improve for those sectors with 'deteriorating' outlooks (Not-For-Profit Hospitals, Life Plan Communities and Higher Education); however, a rekindling of higher inflation could exacerbate expenditure pressure, both for materials/supplies and labor, putting pressure on ratings.
- An increase in labor productivity and operating income along with positive equity and housing market performance could cause improvement in the outlook for the 'deteriorating' sectors. Conversely, a weakening of the equity/housing markets or a further tightening of the labor market (absent material increases in labor productivity) could put pressure on ratings in those sectors.

Arlene Bohner, Managing Director
Head of U.S. Public Finance



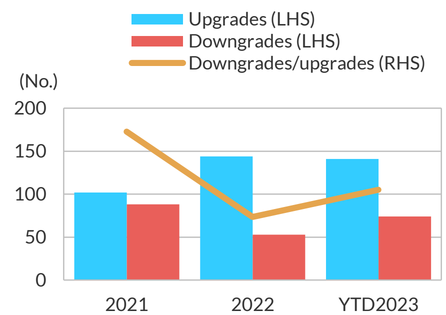
"The US economy is entering 2024 showing a surprising level of resilience, even in the face of higher interest rates. Consumers continue to spend down household savings, providing support for revenue growth across public finance, and this should continue well into 2024. On the expense side, labor and cost pressures remain pivotal concerns for credit quality."

Core Credit Drivers: U.S. Public Finance

		Revenues			Expenditures				Financial Profile		
Subsectors	Outlooks	Personal Income/ Afford-ability	Real-Estate Values	Demand/ Volumes	Labor Costs	Labor Avail-ability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves & Liquidity
States and Local Governments	Neutral	↘	↔	N.A.	↔	↔	↔	↔	↔	↔	↔
Hospitals	Deteriorating	N.A.	N.A.	↗	↘	↘	↘	↔	↔	↘	↔
Life Plan Communities	Deteriorating	↘	↔	↗	↘	↘	↘	↔	↔	↘	↔
Education and Nonprofits	Deteriorating	↘	↔	↔	↘	↔	↘	↔	↔	↘	↔
Community Development & Social Lending	Neutral	↘	↔	↗	↔	↔	↘	↘	↔	↘	↔
Public Power	Neutral	↘	N.A.	↔	↔	↔	↔	↔	↘	↘	↔
Water & Sewer	Neutral	↘	N.A.	↔	↔	↔	↔	↔	↘	↘	↔

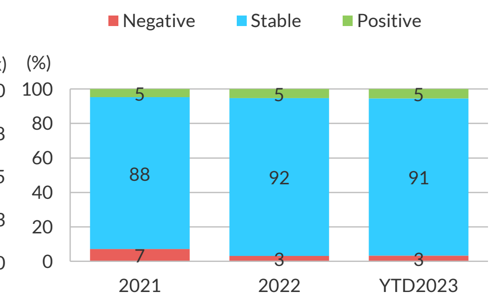
N.A. – not a material driver of credit quality in sector; ↑ improving - high relevance; ↗ improving - moderate relevance; ↔ neutral; ↘ deteriorating - moderate relevance; ↓ deteriorating - high relevance.
Source: Fitch Ratings

U.S. Public Finance — Rating Changes



Source: Fitch Ratings

U.S. Public Finance — Rating Outlooks



Source: Fitch Ratings

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Core Credit Drivers: North America Transportation Infrastructure

		Volume			Price	Costs		Financial		
Subsectors	Outlooks	Economic Environment	End-User Afford-ability	Industry Growth Prospects	Regulatory and Political Environment	Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves and Liquidity
Airports	Neutral	↘	↔	↔	↔	↘	↘	↔	↘	↗
Toll Roads	Neutral	↘	↔	↔	↔	↘	↘	↔	↘	↔
Ports	Neutral	↘	↔	↔	↔	↘	↘	↔	↘	↔

N.A. – not a material driver of credit quality in sector; ↑ improving - high relevance; ↗ improving - moderate relevance; ↔ neutral; ↘ deteriorating - moderate relevance; ↓ deteriorating - high relevance.
Source: Fitch Ratings

U.S. Economic Forecast

(%)	Annual Avg. 2017–2021	2022	2023F	2024F	2025F
GDP Growth	2.2	1.9	2.4	1.2	1.4
Consumer spending	2.6	2.5	2.2	1.3	1.2
Fixed investment	2.8	1.3	0.2	-1.4	2.2
Net trade (end-year)	-0.5	-0.5	0.5	0.0	-0.2
CPI inflation (end-year)	3.6	6.5	3.3	2.6	2.4
Unemployment rate	4.9	3.6	3.6	4.6	4.8
Policy investment rate (end-year)	1.40	4.50	5.50	4.75	3.50
Exchange rate	0.88	0.94	0.93	0.93	0.93

F – Forecast
Source: Fitch Ratings

U.S. States and Local Governments Outlook 2024

Fiscal Capacity to Withstand Slowing Economy

Fitch's Sector Outlook: Neutral

Economic growth will cool in 2024 but overall macro conditions will remain relatively neutral for U.S. states and local governments, and credit quality will remain stable and strong given governments' prudent efforts in recent years to bolster financial resilience. A combination of strong reserves, significant liability reductions and other prudent budget management measures leaves state and local governments well positioned.

Employment, income, and GDP growth will all slow next year, but the U.S. should avoid an outright recession. Uncertainty about commercial office space demand given the seemingly permanent shift to some form of hybrid work, along with hawkish Federal Reserve policy will pressure values and suppress real estate market transactions. State and local governments built 2024 budgets on expectations of slower tax revenue growth, or even declines in some cases.

Rating Outlook Distribution

The vast majority of state and local government Rating Outlooks are Stable. This is consistent with 2022 and an improvement from the 2021 and especially 2020 distributions, which were heavily affected by pandemic-driven challenges. The stability in 2023 reflects the fundamental strengths of state and local governments, including broad and diverse revenue bases, control over revenues and spending, moderate long-term liabilities and sound financial cushions.

Over 2023, Fitch took a limited number of positive rating actions on state and local governments, and almost no negative actions. This reflects both a favorable post-pandemic macro-economic environment and governments' generally forward-looking approaches to utilize the fiscal benefits. In 2023, state and local governments continued to consolidate fiscal gains and build additional fiscal buffers that will prove important as sector conditions moderate in 2024.

Eric Kim, Senior Director

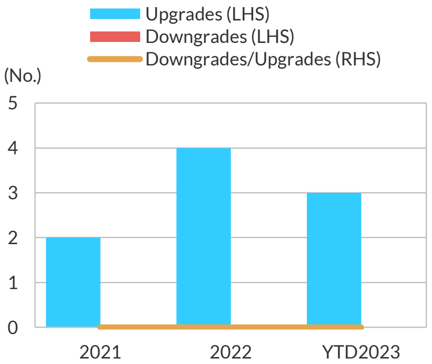
"A combination of strong reserves, significant liability reductions and other prudent budget management measures leaves state and local governments well positioned."

Core Credit Drivers: State and Local Governments

	Revenues			Expenditures				Financial Profile		
Sub-Sectors	Personal Income/ Affordability	Real-Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves & Liquidity
State and Local Governments	↘	↔	N.A.	↔	↔	↔	↔	↔	↔	↔

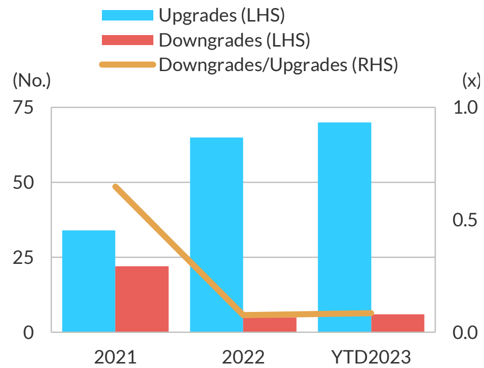
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance. ↓ Deteriorating — High relevance. N.A. – Not a material driver of credit quality in the sector.
Source: Fitch Ratings

State IDRs — Rating Changes



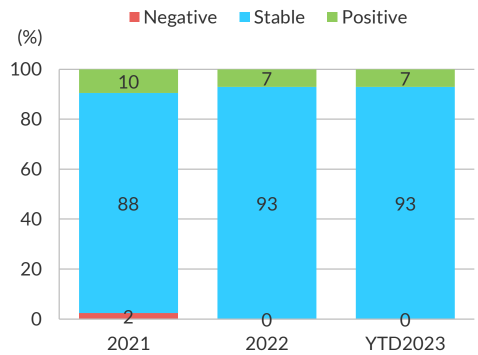
Source: Fitch Ratings

Local Government IDRs — Rating Changes



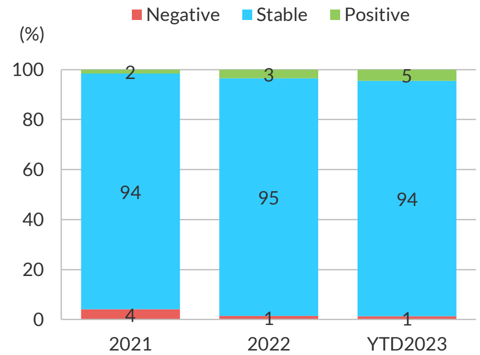
Source: Fitch Ratings

State IDRs — Rating Outlooks



Source: Fitch Ratings

Local Government IDRs — Rating Outlooks



Source: Fitch Ratings

What to Watch

- A deep and prolonged recession could lead governments toward credit negative budget choices such as sustained pension funding deferrals or payment delays.
- Persistent labor and wage inflation putting pressure on expenditure bases to fiscally challenging levels.
- Unexpectedly sharp housing market deterioration.
- Unexpectedly deep revenue declines and resulting budget challenges for those states that are implementing significant tax policy changes enacted in recent years.

U.S. Not-For-Profit Hospitals and Health Systems Outlook 2024

Signs of Life After Challenging 2022–2023 but Margins Will Remain Pressured

Fitch's Sector Outlook: Deteriorating

Fitch Ratings continues to expect core credit drivers for the sector to remain challenged for the sector writ large again in 2024, coming off a generationally challenged period in 2022 and 2023. The industry continues to struggle with labor shortages and salary/wage/benefit pressure that is still compressing margins for a sizable portion of the sector, even as other core credit drivers, specifically volumes and overall liquidity, begin to improve.

As the largest single expense for healthcare providers, managing salary, wages and benefits has emerged as the single most meaningful differentiator between operational success and failure. Organizations that have successfully attracted and retained staff at all levels, not simply nursing, have experienced reductions in both usage and cost per hour of external contract labor (ECL), as well as more new hires compared to "leavers". These are all positive signs and contribute to cost savings and, perhaps more importantly, to quality and patient safety.

The larger macroeconomic headwinds, specifically the labor supply shortage, became highly pronounced in calendar year 2022 and remained a pressure point, with operating metrics challenged for many providers in 2023, some significantly. Fitch believes this pressure will remain for the foreseeable future yet slowly resolve, with the expectation for added incremental operational recovery in 2024. Fitch also expects a number of health providers to lag significantly behind any recovery.

Fitch's 2022 prediction that break-even operations on a month-to-month basis would return sometime in 2023 did largely occur, albeit perhaps later in the year and to a lesser extent than originally anticipated. A select few health systems continue to enjoy strong operating margins, which is a mark of distinction amid the current sector landscape. Another subset of the industry has continued to struggle in 2023, with the most direct impact seen at the lower end of the rating scale in the form of three multi-notch downgrades in the 'BB' category or lower YTD.

While liquidity has provided a significant rating cushion for multiple years and should still allow most providers to weather the current environment, unrestricted liquidity levels remain subdued from sector highs seen in 2021. Liquidity levels have begun a rebound of sorts with this year's market improvement, yet larger market uncertainty in 2024 continues to loom large over the sector.

Fitch continues to predict a period in which downgrades and Negative Rating Outlooks will outpace upgrades and Positive Rating Outlooks (currently 3-to-1 and 2.3-to-1, respectively, in 2023 YTD) but to a lesser extent compared to this year. Fitch also remains steadfast on not calling for downgrades en masse across the entire sector.

Kevin Holloran, Senior Director

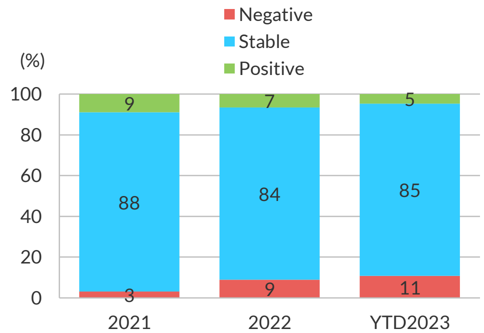
"The last several years have proven very challenging for most of the sector, which is now facing the ongoing 'labor-demic' with significant staff shortages, intense wage pressure and heightened inflation. While staffing issues have started to attenuate, salary and wage expenses appear to have been reset at a new, higher level for many — directly impacting operating margins over the near term. This year (2023) was a turning point for many to the positive, particularly on a month-to-month basis; however, 2024 will remain challenging and will be yet another make or break year for a sizable portion of the sector."

Core Credit Drivers: Hospitals

	Revenues			Expenditures				Financial Profile		
Subsectors	Personal Income/ Affordability	Real Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves and Liquidity
Hospitals	N.A.	N.A.	↗	↘	↘	↘	↔	↔	↘	↔

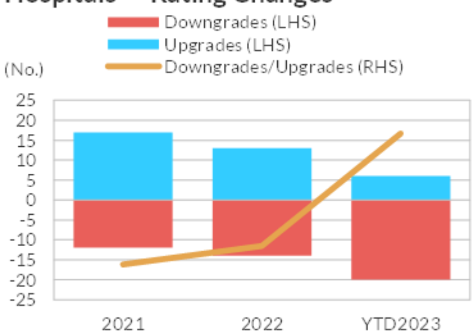
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance.
↓ Deteriorating — High relevance. N.A. – Not a material driver of credit quality in the sector.
Source: Fitch Ratings

Hospitals — Rating Outlooks



Source: Fitch Ratings

Hospitals — Rating Changes



Source: Fitch Ratings

Rating Outlook Distribution — Rating Changes and Outlook Revisions

Rating Changes

Despite a second year of considerable expense pressure, affirmations remained the most common rating outcome in 2023. Rating actions in 2023 YTD indicate downgrades have outpaced upgrades by roughly 3-to-1, compared to just 1.1-to-1 one year prior, while affirmations still represent 88% of all rating actions in 2023. The sector continues to demonstrate considerable resiliency due to previously accumulated financial cushion and, despite the 2022 market downturn chipping away at that cushion, gradual market recovery in 2023 has restored some of it.

Rating Outlook Status

As shown in the accompanying chart, while the vast majority of Rating Outlooks remain Stable (at 85%), another notable shift has occurred yoy, with Negative Rating Outlooks increasing to 10.7% (YTD) from 8.9% one year prior. Additionally, Positive Rating Outlooks declined to about 4.7% in 2023 YTD, compared to 6.6% in 2022. The overall negative shift in ratings and Rating Outlooks is not surprising given the pattern of financial results over the TTM, particularly for health systems with operating margins lagging the general industry recovery. Although the odds of a full operational recovery in 2024 are deemed remote, we anticipate continued improvement. However, should gradual operational improvement in 2024 fail to materialize, an acceleration in downgrades and Negative Rating Outlook revisions would be expected.

What to Watch

- A sector outlook reassessment would likely require significant improvement in labor productivity given the current scarcity of available labor industrywide and for clinical positions in particular, which historically have been in high demand but short supply. Gains in labor productivity will likely be achieved only through redesigned labor processes, possibly through technology and artificial intelligence (AI) advancements. Recent years have seen enhanced recruitment and retention efforts, emerging as one of if not the single most meaningful differentiator between operational success and failure.
- A sector outlook revision to neutral would necessitate more widespread sector wide improvement to operating income, particularly in the wake of a very challenging 2022 (with an essentially break-even median operating margin) and an equally challenging 2023.
- Equity market stability and a return to materially positive returns yoy could restore and increase rating headroom, in turn signaling a higher likelihood of a sector outlook revision as greater credit stability is amassed.
- Though not expected to be a widespread event, a second year of debt service covenant (DSC) violations are of particular concern this year. Second year violations, which would occur in calendar 2024 as late fiscal 2023 and early 2024 audits are finalized, may intensify the potential for bondholders to declare an event of default and accelerate bond payments.

U.S. Not for Profit Life Plan Communities Outlook 2024

Sector Headwinds to Continue

Fitch's Sector Outlook: Deteriorating

Fitch Ratings expects the general operating environment for life plan communities (LPCs) to remain negative in 2024. While demographic trends should continue to support healthy demand for LPCs, Fitch has a weaker outlook on many of the other key drivers of fundamental credit quality that have not improved since 2023; decelerating real estate price growth and inflationary operating expense pressure are among the most notable examples. Fitch expects that these headwinds may continue to stall the sector's recovery in 2024.

The LPC sector continues to experience a number of expense pressures, particularly with staffing. Positive trends in occupancy and the demographic strength of LPCs' underlying resident base have supported the sector's ability to pass through most of this cost escalation to their revenue base of entrance and monthly service fees over the last two years. However, occupancy and demand could soften if rate increases continue above historical norms or if cost-cutting erodes service quality. Decelerating growth in real estate pricing may also slow the current strong pace of independent living unit (ILU) sales and limit an LPC's ability to raise entrance fees to absorb cost inflation and pay refunds.

A sector outlook revision to neutral would require demonstrable improvement in labor availability, demonstrated efficacy of higher than average rate increases to counteract inflationary cost pressures and expectations for stable or improving real estate market performance.

Rating Outlook Distribution

Fitch's net outlook balance deteriorated to negative 7 in 2023, compared to negative 2 in 2022, reflecting deterioration in LPC operations, which led to an uptick in Negative Rating Outlooks compared to the previous year.

What to Watch

- A heightening of regulatory requirements, particularly minimum staffing ratios, would add to already increased operating costs and exacerbate the headwinds in the LPC sector.
- Mergers & Acquisitions, provider affiliations and industry consolidation are going to remain key themes as providers seek the benefits of economies of scale.

Margaret Johnson, CFA, Senior Director

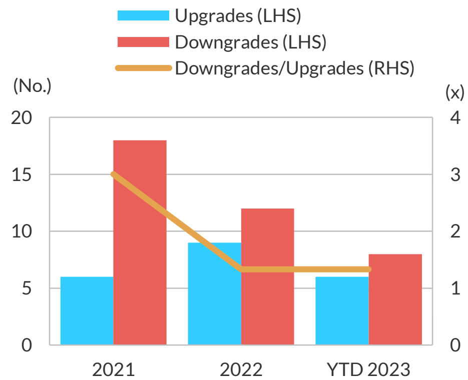
"While Fitch expects demographic trends to continue to support healthy demand, decelerating real estate price growth and cost inflation are significant headwinds that will continue to stall the sector's recovery."

Core Credit Drivers: Life Plan Communities

	Revenues			Expenditures				Financial Profile		
Sub-Sectors	Personal Income/ Affordability	Real-Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves & Liquidity
Life Plan Communities	↘	↔	↗	↘	↘	↘	↔	↔	↘	↔

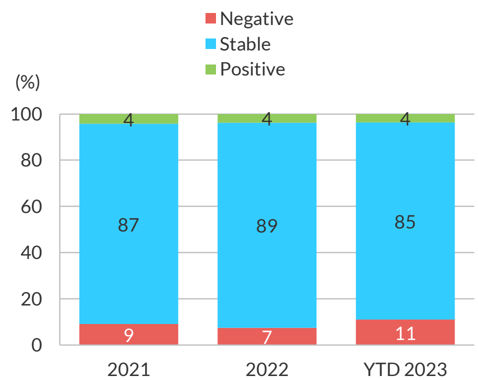
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance. ↓ Deteriorating — High relevance. N.A. – Not a material driver of credit quality in the sector.
Source: Fitch Ratings

Life Plan Community — Rating Changes



Source: Fitch Ratings

Life Plan Community — Rating Outlooks



Source: Fitch Ratings

U.S. Higher Education Outlook 2024

Credit Gap Widens Further

Fitch's Sector Outlook: Deteriorating

Fitch Ratings anticipates a deteriorating credit environment for U.S. public finance higher education in 2024 relative to 2023. Fundamental credit factors will be challenging across the sector, with meaningful macroeconomic headwinds, including labor and wage pressure and elevated interest rates, along with a mild and very uneven recovery in enrollment. All of these challenges could weaken operating margins and strain financial flexibility in 2024. Limited increases in tuition are unlikely to be sufficient to mitigate elevated operating costs. Sector bifurcation will continue to widen the credit gap between larger, more selective institutions versus their smaller, less selective and more tuition-dependent counterparts.

Rating Outlook Distribution

Despite these conditions, Rating Outlooks remain Stable for most Fitch-rated institutions and widespread downgrades are not anticipated. There were 10 upgrades versus six downgrades YTD November 2023. However, Outlook revisions have been decidedly negative, with 10 unfavorable revisions against just four favorable revisions. The key factor generally driving downgrades and unfavorable Outlook revisions was enrollment pressure, often resulting in diminished operating performance and eroding liquidity.

What to Watch

- A sector outlook revision to neutral would require evidence of steady net tuition growth prospects. Revenue growth prospects are limited as tuition increases have been muted for most non-selective institutions and a competitive pressure point. These concerns remain heightened in due to elevated expenses related to higher labor and benefit costs in a still-tight labor market.
- Further improvement in macro conditions (namely labor market pressures and equity market performance) sufficient to support longer-term operating stability could support a sector outlook revision to stable. While inflation continues to wane, most higher costs related to labor/benefits will have a long tail into 2024 and possibly beyond.
- Further stabilization in enrollment across student groups and institution types could also warrant a favorable revision in the sector outlook. Total enrollment is showing signs of stabilization but at a new post-pandemic low and with limited prospects for meaningful growth as demographic conditions continue to trend downward.

Emily Wadhwani, Senior Director

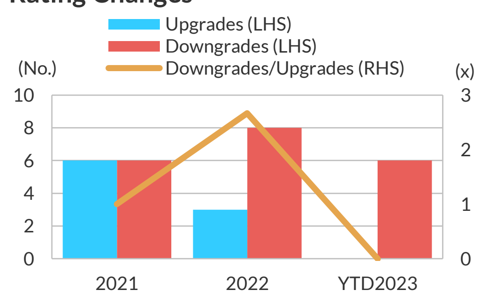
"Fundamental credit factors will be challenging across the sector, with meaningful macroeconomic headwinds including labor and wage pressure, elevated interest rates, and a very uneven recovery in enrollment. Sector bifurcation will continue to widen the credit gap between larger, more selective institutions versus their smaller, less selective and more tuition-dependent counterparts."

Core Credit Drivers: Higher Education

	Revenues			Expenditures				Financial Profile		
Subsectors	Personal Income/ Affordability	Real Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves and Liquidity
Higher Education	↘	↔	↔	↘	↔	↘	↔	↔	↘	↔

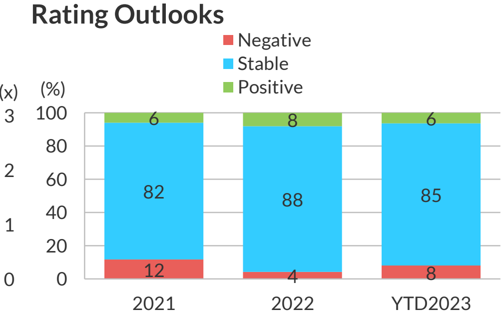
↑ Improving – High relevance. ↗ Improving – Moderate relevance. ↔ Neutral. ↘ Deteriorating – Moderate relevance. ↓ Deteriorating – High relevance.
Source: Fitch Ratings

Education & Non-profits — Rating Changes



Source: Fitch Ratings

Education & Non-profits — Rating Outlooks



Source: Fitch Ratings

U.S. Community Development & Social Lending Outlook 2024

Strong Credit Profiles Support Sector as it Faces Ongoing Uncertainty

Fitch's Sector Outlook: Neutral

While the U.S. economy has remarkably averted recession thus far, the U.S. Community Development & Social Lending (CDSL) sector is not out of the woods just yet. Although Fitch is no longer forecasting a recession in 2024, the U.S. economy is expected to slow sharply as higher interest rates and a slowdown in bank credit weigh on consumer spending and private investment. However, Fitch believes that CDSL issuers are well-positioned to face these headwinds, given their strong financial profiles, conservative risk management practices, the effective oversight provided by their underwriting and servicing teams, and their long, successful track record of executing loss mitigation strategies. In addition, many CDSL issuers, particularly state housing finance agencies (HFAs), hold loan portfolios that benefit from federal government guarantees, insurance, and other forms of support such as excess overcollateralization, which insulate them to a large degree from the worst effects of economic downturns.

Despite the perceived higher risk and lower credit quality of their loan portfolios and borrowers relative to the prime borrowers served by mainstream banks and other financial institutions, the loan portfolios of CDSL issuers have experienced generally low delinquency, default, and loss rates. This strong loan performance is directly attributable to the prudent risk management and effective oversight provided by CDSL issuers. As such, even if macroeconomic and housing market conditions deteriorate in 2024, Fitch expects any loan losses to remain manageable.

Rating Outlook Distribution

There were 19 downgrades and one upgrade to the sector's ratings in 2023. Sixteen of the 19 downgrades were driven by direct linkages of HFA loan programs to the U.S. IDR, which Fitch downgraded on August 1, as these 16 credits are primarily secured by mortgage-backed securities (MBS) issued by Ginnie Mae, Fannie Mae and/or Freddie Mac. The three other downgrades were related to two military housing projects with declining operating performance, and the upgrade was related to an HFA IDR. As of November 30, 2023, approximately 96% of CDSL ratings had Stable Rating Outlooks and 4% had Negative Rating Outlooks.

What to Watch

- Deteriorating U.S. macroeconomic conditions, leading to rising unemployment, increased inflationary pressures, and/or worsening housing affordability.
- Ongoing heightened financial market volatility, further limiting market access.
- Reduction in external support for the sector, evidenced by decreased federal funding and/or declining support from banks and other private sector organizations.

Karen Fitzgerald, CFA, Senior Director

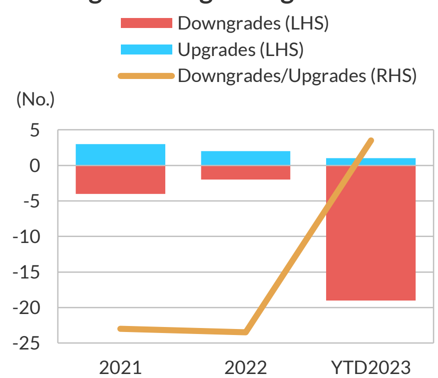
Issuers in the Community Development & Social Lending (CDSL) sector have repeatedly demonstrated their resilience and adaptability during turbulent economic times. Given their strong financial profiles, conservative risk management, effective oversight, and successful track records, Fitch expects CDSL issuers to remain steadfast as they face ongoing uncertainty and the continuing challenges of housing unaffordability and limited market access in 2024.

Core Credit Drivers: Community Development & Social Lending

	Revenues			Expenditures				Financial Profile		
Subsector	Personal Income/ Affordability	Real-Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves & Liquidity
Community Development & Social Lending	↘	↔	↗	↔	↔	↘	↘	↔	↘	↔

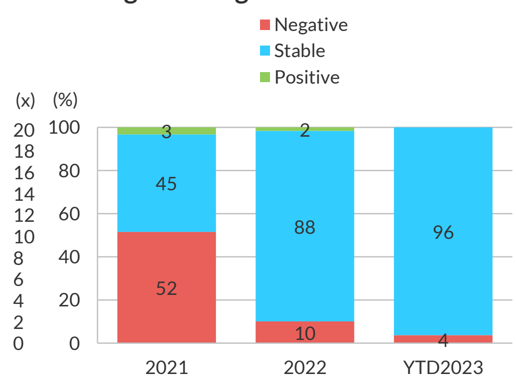
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance.
↓ Deteriorating — High relevance.
Source: Fitch Ratings

Community Development & Social Lending — Rating Changes



Source: Fitch Ratings

Community Development & Social Lending — Rating Outlooks



Source: Fitch Ratings

North American Transportation Infrastructure Outlook 2024

Softer Economic Conditions Drive Subdued Performance in 2024

Fitch's Sector Outlook: Neutral

The sector outlook for 2024 is neutral with expectations for overall stable credit conditions and a limited range of volatility in volume activities. Risks to financial positions related to capex borrowings are a leading concern, along with the combined effects of a slowdown and inflation pressures throughout 2024.

Absent any major economic shocks, the broader operating environment for transportation should be less volatile than in the past couple of years. U.S. and Canadian airports have largely reached pre-pandemic passenger levels and mild additional growth is expected under Fitch Ratings' base case scenarios. Port volumes also should also see more stable operations following a couple of years of outsized volatility. Toll road projects have had a more steadier growth profile in recent years, and Fitch believes this trend should continue in 2024.

With several new mandates, public-private partnerships for the transportation sector remain highly relevant for project delivery and risk sharing . While projects in operating phases are performing well, Fitch notes that construction period risks are areas of concern. Some projects with material delays in completion dates, or taking on upward cost adjustments, have resulted in challenges with grantors to resolve differences and could result in negative rating actions.

Rating Outlook Distribution — Stable Across Airports, Toll Roads and Ports

The portion of Stable Outlooks across the transportation sectors is very high and compares closely with 2022 as well as with the time frame shortly before the pandemic created greater Rating Outlook movements. Fitch views the Outlooks to be more reflective of the stabilized operating environment where credits are well positioned to maintain operating and financial profiles consistent with the current rating levels.

What to Watch

- Longer than expected economic slowdown, leading to revenue and volume underperformance, could result in a deteriorating sector outlook due to weaker coverage or leverage indices.
- Inflation that drives higher operating costs, and either weaker operating income or further pressures pricing to end users, could drive a negative sector outlook.
- Capacity expansion and/or redevelopment could further increase debt borrowings and increase leverage profiles on sustained bases and lead to a negative sector outlook.
- Delays in construction schedules as well as unplanned budget increases could limit embedded flexibility in project delivery.

Seth Lehman, Senior Director

"Airports, toll roads and ports remained remarkedly resilient in the face of a more volatile economy in the last few years and are in a better fiscal position overall heading into 2024 as the operating environment stabilizes."

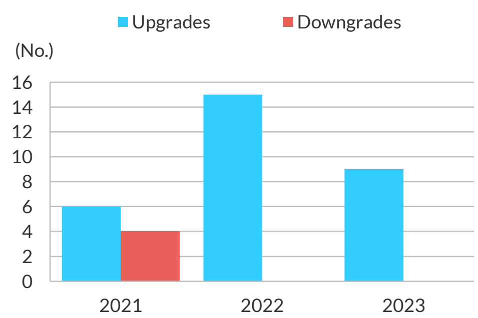
Core Credit Drivers: North America Transportation Infrastructure

	Volume			Price	Costs		Financial		
Subsectors	Economic Environment	End-User Affordability	Industry Growth Prospects	Regulatory and Political Environment	Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves and Liquidity
Airports	↘	↔	↔	↔	↘	↘	↔	↘	↗
Toll Roads	↘	↔	↔	↔	↘	↘	↔	↘	↔
Ports	↘	↔	↔	↔	↘	↘	↔	↘	↔

N.A. – Not a material driver of credit quality in sector. ↑ Improving – High relevance. ↗ Improving – Moderate relevance. ↔ Neutral. ↘ Deteriorating – Moderate relevance. ↓ Deteriorating – High relevance.
Source: Fitch Ratings

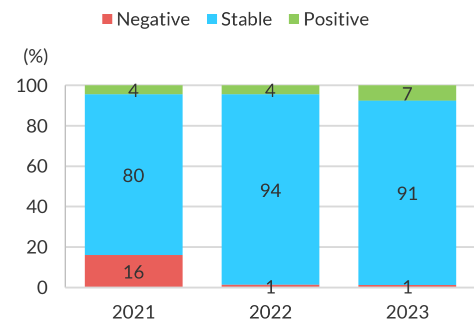
North American Transportation Infrastructure — Rating Changes

As of Nov. 22, 2023



Source: Fitch Ratings

North American Transportation Infrastrtucture — Rating Outlooks



Source: Fitch Ratings

U.S. Public Power and Electric Cooperatives Outlook 2024

Stabilizing Cost Pressures Support Operating Performance

Fitch's Sector Outlook: Neutral

Fitch Ratings' neutral outlook for the Public Power and Electric Cooperatives sector reflects our expectation that economic and business conditions will remain relatively stable in 2024. The operating environment will remain challenging, but we do not expect conditions to weaken further. There were fewer general inflationary pressures and natural gas costs stabilized at lower levels, but slower economic growth and persistently high interest rates could contribute to lackluster operating performance. Credit quality across the sector is likely to remain stable as efforts to manage operating costs and increase rates to preserve margins continue.

Rating Outlook Distribution

Rating Outlooks throughout the sector remain overwhelmingly Stable and we do not expect many rating changes in the sector next year. Approximately 93% of Public Power and Cooperative ratings Fitch assigned maintained a Stable Outlook. Roughly 4% of the ratings maintained a Positive Outlook or Watch and 3% a Negative Outlook or Watch.

The ratio of downgrades to upgrades remained largely unchanged in 2023 from 2022 at roughly 2.0x. However, given the small sample sizes, the ratios do not portend a broader trend of financial performance across the sector. Rating reviews that resulted in an affirmation or no action dominated the landscape of activity in 2023 as issuers managed cost pressures and benefited from stronger economic activity that were more favorable than originally anticipated. We do not expect this balance to change in 2024.

Ratings and Outlooks for pre-paid energy issuers were largely unchanged in 2023, driven by the rating stability exhibited by the financial institutions acting as supply counterparties. However, pre-paid energy issuers are excluded from the sector rating metrics, as ratings are predominately driven by the credit quality of the counterparties.

What to Watch

- More challenging operating cost environment, including higher natural gas prices and long-term interest rates.
- Accelerated imbalance of capacity and demand.
- Improved affordability of electric service.
- Expanded implementation of emissions limits.
- Significant capital cost pressures and higher spending requirements.

Kathy Masterson, Senior Director

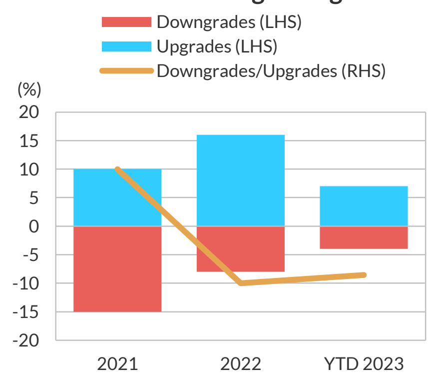
"The operating environment for the Public Power sector are likely to remain relatively stable in 2024 as lower inflation and fuel prices could help sustain financial margins despite slower economic growth and persistently high interest rates. Capacity constraints and proposed environmental rules are increasing long-term concerns that could dampen performance over time."

Core Credit Drivers: Public Power

	Revenues			Expenditures				Financial profile		
Sub-sectors	Personal income/ affordability	Real estate values	Demand/ volumes	Labor costs	Labor availability	Non-labor operating costs	Capital input costs	Leverage	Cost of debt	Financial reserves and liquidity
Public Power	↘	N.A.	↔	↔	↔	↔	↔	↘	↘	↔

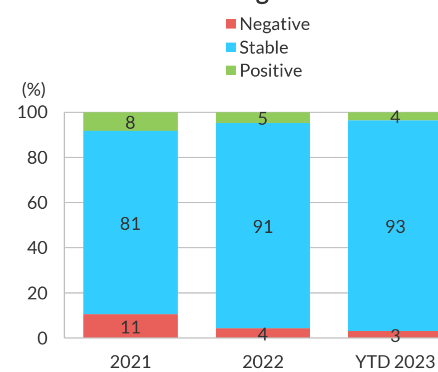
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance. ↓ Deteriorating — High relevance. N.A. – Not a material driver of credit quality in the sector.
Source: Fitch Ratings

Public Power — Rating Changes



Source: Fitch Ratings

Public Power — Rating Outlooks



Note: Excludes pre-paid energy issuers.
Source: Fitch Ratings

U.S. Water and Sewer Outlook 2024

Inflationary Pressures Easing

Fitch's Sector Outlook: Neutral

Fitch Ratings' outlook change for the water and sewer sector to neutral from deteriorating reflects the stabilization of business conditions over the past 12 months, allowing for greater certainty in 2024 with respect to budgeting capital and operating costs. Although headwinds related to general inflationary pressures have eased, they have led to a "new normal" operating environment whereby utilities sectorwide have had to account for higher costs. Positively, the rates of increase related to chemical, labor and power costs have normalized and are now generally in line with expected revenue rates of increase. The distribution of Rating Outlooks across the portfolio is predominantly Stable and most utilities retain headroom for absorbing higher costs and increased capital spending.

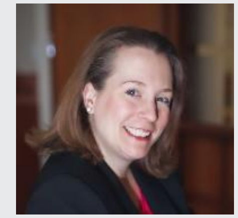
Rating Outlook Distribution

Fitch expects limited rating changes in 2024; however, a narrowing of financial margins is possible as capital programs increase. As of Nov. 8, 2023, 87% of water and sewer ratings assigned by Fitch maintained a Stable Rating Outlook. Approximately 10% have a Positive Rating Outlook or are on Rating Watch Positive and 3% have a Negative Rating Outlook or are on Rating Watch Negative. Ratings trending positive are dominated by utilities with improving leverage profiles despite incorporating higher capex and operating costs. Conversely, ratings trending negative are predominantly driven by utilities with rising leverage due to increasing operating expenses or capex without offsetting rate support.

What to Watch

- Utilities managing to a new higher cost environment.
- Capital spending to continue rising.
- Impacts of federal funding.
- The regulatory environment and effects on capital programs and operations.
- Trends in service affordability.

Audra Dickinson, Senior Director



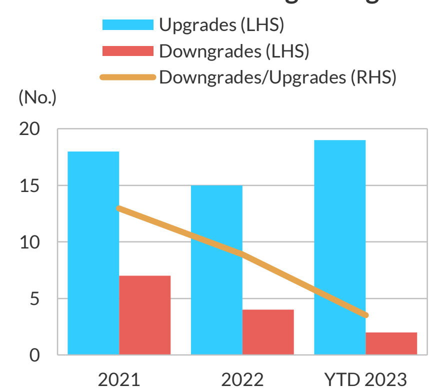
"Cost and inflationary pressures have eased and utilities have now incorporated higher operating and capital costs into their budgets. Relative to one year ago, the operating environment has normalized and our water and sewer systems seem to have greater certainty around budgeting for the upcoming year."

Core Credit Drivers: Water-Sewer

	Revenues			Expenditures				Financial Profile		
Sub-Sectors	Personal Income/ Affordability	Real Estate Values	Demand/ Volumes	Labor Costs	Labor Availability	Non-Labor Operating Costs	Capital Input Costs	Leverage	Cost of Debt	Financial Reserves & Liquidity
Water-Sewer	↘	N.A.	↔	↔	↔	↔	↔	↘	↘	↔

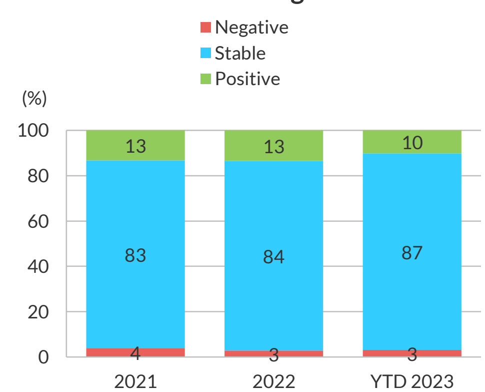
↑ Improving — High relevance. ↗ Improving — Moderate relevance. ↔ Neutral. ↘ Deteriorating — Moderate relevance. ↓ Deteriorating — High relevance. N.A. – Not a material driver of credit quality in the sector.
Source: Fitch Ratings

Water & Sewer — Rating Changes



Source: Fitch Ratings

Water & Sewer — Rating Outlooks



Source: Fitch Ratings

Outlooks and Related Research

2024 Outlooks
Global Economic Outlook
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2023 State Liability Report (November 2023)
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State Tax Cut Wave Has Peaked with Modest Revenue Effects for Most States (August 2023)
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The Road Ahead for U.S. State Gas Taxes and Transportation Bonds (June 2023)
Controlling Labor Costs Will be Key to NFP Hospital Margin Improvement (October 2023)
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Early NFP Hospital Medians Show Expected Deterioration; Will Worsen (March 2023)
US Not-for-Profit Hospital Cyberattacks Could Signal Greater Risk (February 2023)
Investment Value Declines Erode Not-for-Profit Hospitals' Liquidity (January 2023)
Life Plan Communities Able to Manage Nursing Staff Requirements (September 2023)
Life Plan Communities Labor Tracker (September 2023)
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More U.S. Higher Ed Consolidation, Trimming or Closures to Come (September 2023)
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Global Housing and Mortgage Outlook (December 2023)
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Strong Financial Profiles and Loan Oversight Support CDFI Credit (May 2023)
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Peer Review of U.S. Managed Lanes (November 2023)
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U.S. Airport and Toll Road Traffic Monitor (July 2023)
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Major U.S. Airports Brace for Renewed Traffic Growth with Big Spending Plans (October 2023)
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Public Power Utilities' Cyber Investment Key to Mitigate Greater Risk (October 2023)
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US Water Utilities' Debt Would Increase Under Proposed PFAS Rule (April 2023)

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