

# NCSL's Fiscal Institute Symposium 2023

## Rating in Times of Volatility

November 16, 2023

1:30 – 2:10 p.m.



**S&P Global**  
Ratings

**Geoffrey Buswick**  
Managing Director &  
U.S. Governments Sector Lead

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# Understanding S&P Global's Ratings

- An issuer's *ability* and *willingness* to pay debt in a *timely* manner
- Credit ratings are *forward looking*
- S&P Global ratings are *opinions*, not guarantees of credit quality or exact measures of the probability that a particular issuer or particular debt issue will default
- The Ratings scale *is relative* and based on the creditworthiness of an issuer or credit quality of an individual debt issue, from strongest to weakest, within a universe of credit risk
- Criteria provide the analytic framework to derive the rating opinion

# Ratings 101 | S&P Global's Ratings Scale

## Investment-Grade

AAA	→	Strongest
AA+	}	Very Strong
AA		
AA-		
A+	}	Strong
A		
A-		
BBB+	}	Adequate
BBB		
BBB-		

## Speculative-Grade

BB+	}	Least Speculative
BB		
BB-		
B+	}	Speculative
B		
B-		
CCC	}	Highly Speculative
CC		
C		
D	→	In Default

Short-term U.S. Public Finance note ratings: **SP-1+, SP-1, SP-2 & SP-3**

# U.S. Public Finance (USPF) Q4 2023 Sector Summary -- States

## What we're watching

- With revenues slowing and inflationary pressures holding, we're watching for current and out-year budgetary challenges
- Federal criticism of Medicaid redetermination actions in some states could force a change in eligibility rolls

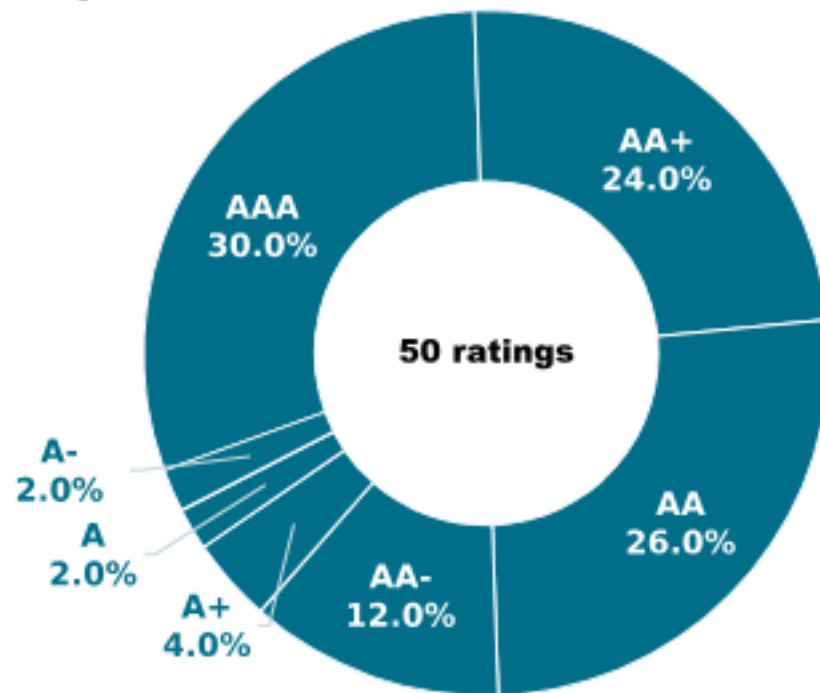
## Trends

- Reserves holding steady at all-time highs or even increasing in fiscal 2024
- Jobs are still hard to fill, and retention actions like benefit enhancements and across-the-board wage increases could have long-term budgetary impacts

## Rest of year expectations

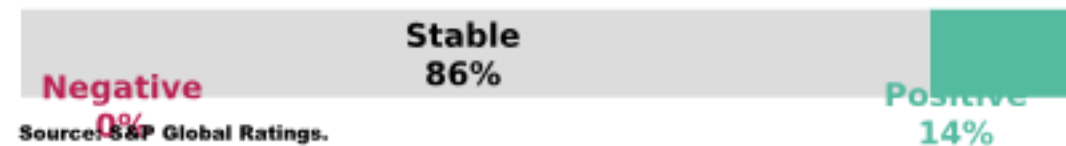
- The national economy will feel the effects of labor shortage and work stoppages and growth will slow, affecting state revenue collections
- Continued credit stability with some strengthening possible, as ratings on seven states have a positive outlook

Ratings distribution



Source: S&P Global Ratings.

Outlook distribution



Source: S&P Global Ratings.

# USPF | Credit Conditions: Fall 2023

## What we're watching

- Higher interest rates and inflation remain headwinds for most issuers from a debt issuance and operating/capital budget perspective
- Extreme weather events continue, requiring swift response and resource allocation. Cost and availability of property insurance are emerging as a challenge

## Trends

- Credit conditions have been largely stable, and upgrades have exceeded downgrades this year for most sectors
- The U.S. economy has been resilient, but we expect slower growth ahead. Federal budget deliberations and increased geopolitical tensions could further limit growth
- Federal stimulus and healthy financial reserves continue to provide significant flexibility

## Rest of year expectations

- Our baseline U.S. economic forecast is now for a shallower but more protracted slowdown rather than a recession; however, we don't expect this to disrupt credit stability for most issuers



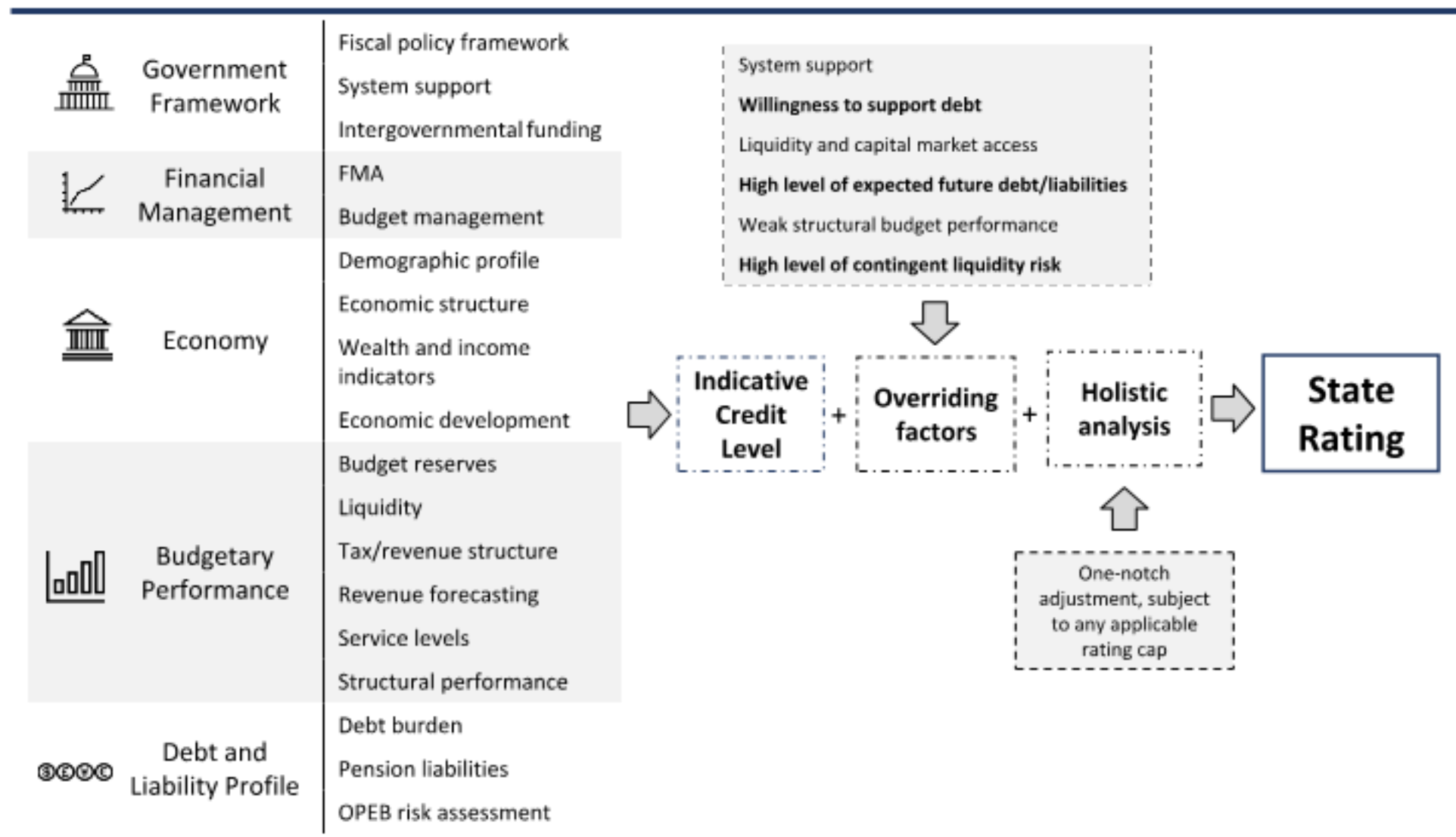
# S&P Global Ratings' U.S. Economic Forecast Overview

## Key indicators

As of September 2023	2019	2020	2021	2022	2023f	2024f	2025f	2026f
<b>Real GDP (annual average % change)</b>	<b>2.3</b>	<b>-2.8</b>	<b>5.9</b>	<b>2.1</b>	<b>2.3</b>	<b>1.3</b>	<b>1.4</b>	<b>1.8</b>
<b>Change from June (percentage point)</b>					<b>0.5</b>	<b>0.0</b>	<b>-0.1</b>	<b>-0.1</b>
<b>Real GDP Q4/Q4 (annual average % change)</b>	<b>2.6</b>	<b>-1.5</b>	<b>5.7</b>	<b>0.9</b>	<b>2.2</b>	<b>1.1</b>	<b>1.6</b>	<b>1.9</b>
<b>Change from June (percentage point)</b>					<b>0.9</b>	<b>-0.4</b>	<b>0.0</b>	<b>0.0</b>
<b>Consumer spending (annual average % change)</b>	<b>2.0</b>	<b>-3.0</b>	<b>8.3</b>	<b>2.7</b>	<b>2.5</b>	<b>1.4</b>	<b>1.5</b>	<b>2.1</b>
<b>Equipment investment (annual average % change)</b>	<b>1.3</b>	<b>-10.5</b>	<b>10.3</b>	<b>4.3</b>	<b>-0.8</b>	<b>1.4</b>	<b>1.7</b>	<b>2.2</b>
<b>Nonresidential structures investment (annual average % change)</b>	<b>2.3</b>	<b>-10.1</b>	<b>-6.4</b>	<b>-6.6</b>	<b>7.6</b>	<b>1.1</b>	<b>0.5</b>	<b>3.2</b>
<b>Residential investment (annual average % change)</b>	<b>-1.0</b>	<b>7.2</b>	<b>10.7</b>	<b>-10.6</b>	<b>-11.1</b>	<b>0.7</b>	<b>3.2</b>	<b>1.8</b>
<b>Core CPI (annual average % change)</b>	<b>2.2</b>	<b>1.7</b>	<b>3.6</b>	<b>6.2</b>	<b>4.7</b>	<b>2.6</b>	<b>2.3</b>	<b>2.3</b>
<b>Core CPI Q4/Q4 (annual average % change)</b>	<b>2.3</b>	<b>1.6</b>	<b>5.0</b>	<b>6.0</b>	<b>3.7</b>	<b>2.4</b>	<b>2.3</b>	<b>2.3</b>
<b>Unemployment rate (%)</b>	<b>3.7</b>	<b>8.1</b>	<b>5.4</b>	<b>3.6</b>	<b>3.6</b>	<b>4.1</b>	<b>4.7</b>	<b>4.8</b>
<b>Housing starts (mil.)</b>	<b>1.3</b>	<b>1.4</b>	<b>1.6</b>	<b>1.6</b>	<b>1.4</b>	<b>1.4</b>	<b>1.4</b>	<b>1.4</b>
<b>Light vehicle sales (mil.)</b>	<b>17.0</b>	<b>14.5</b>	<b>15.0</b>	<b>13.8</b>	<b>15.2</b>	<b>15.2</b>	<b>15.5</b>	<b>15.6</b>
<b>10-year Treasury (%)</b>	<b>2.1</b>	<b>0.9</b>	<b>1.4</b>	<b>3.0</b>	<b>3.9</b>	<b>4.0</b>	<b>3.6</b>	<b>3.6</b>

Note: All percentages are annual averages, unless otherwise noted. Core CPI is consumer price index excluding energy and food components. f--Forecast.  
Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, The Federal Reserve, S&P Global Market Intelligence Economic Simulink, S&P Global Ratings Economics' forecasts.

# U.S. States | U.S. State Ratings Methodology (GO)



Source: S&P Global Ratings U.S. States Ratings Methodology, October 17, 2016

# Governments | Post-COVID Landscape

## Key Risks – October 2023



### Inflation

Higher cost of living erodes income and potentially discretionary spending which could lower consumption-based taxes.



### Interest Rates

Higher borrowing costs have contributed to lower debt issuance while higher mortgage rates are increasing housing costs.



### Federal Policy

Diminished federal stimulus flows and the potential for a federal government shutdown loom large.



### Event Risks

Cyber attacks and extreme weather events will continue to challenge management. Cost and availability of insurance are emerging as a challenge.



### Demographics

The aging U.S. population will add to service delivery costs and continue to challenge government staffing.



### Real Estate

Fluctuations in commercial real estate values and housing affordability present potential revenue challenges over time.



# U.S. States | By The Numbers



Aggregate reserves  
130% higher than  
pre-pandemic



**5.1%**

U.S. (unadjusted) hourly  
wage gains in 2022



**81.7%**

Average state pension  
funded ratio for FYE 2021,  
expected to decline FY22

**0**

States with  
negative outlooks

**6**

States with  
positive outlooks

**Core CPI forecast**  
(% change)

FY23

**4.7%**

2022

**6.3%**



**18.7 mil.**

Medicaid and CHIP  
enrollment increase  
(or 26.4%) between  
Feb. 2020 and Aug. 2022



**20.8%**

State Fiscal  
Recovery funds still  
to be appropriated  
(as of Aug. 31)

**4.7 mil.**



More jobs open in Nov.  
than active job seekers  
(10.3 mil. open to 5.6 mil.  
actively seeking work)



**5**

Consecutive years with  
international migration  
to the U.S. declining



**25**

States in which deaths  
exceeded births in 2021

## Cyber | Headlines & Trends

Starting Dec. 18, 2023, the U.S. Securities and Exchange Commission (SEC) will require public companies to report material cyber security incidents on a Form 8-K within four business days of materiality determination.

**“The global average cost of a data breaches reached \$4.45 million in 2023--an all-time high and a 15% increase, compared with 2020.”** IBM Security's Cost of a Data Breach Report 2023

**“74% of all breaches include the human element, with people being involved either via Error, Privilege Misuse, Use of stolen credentials or Social Engineering.”** Verizon's 2023 Data Breach Investigations Report

**“69% of the 2,489 breaches reviewed in 2022 were done by organized crime (less than 10% nation-state or state-affiliated actors).”** Verizon's 2023 Data Breach Investigations Report

**“Sadly, too few organizations learn how valuable MFA is until they experience a breach.”** Jen Easterly, Director U.S. Cybersecurity and Infrastructure Security Agency

**“Artificial intelligence and machine learning, while great for research & analytics (i.e. ChatGPT). However, AI tools can also be used by hackers for advanced attacks.”** Forbes, March 5, 2023

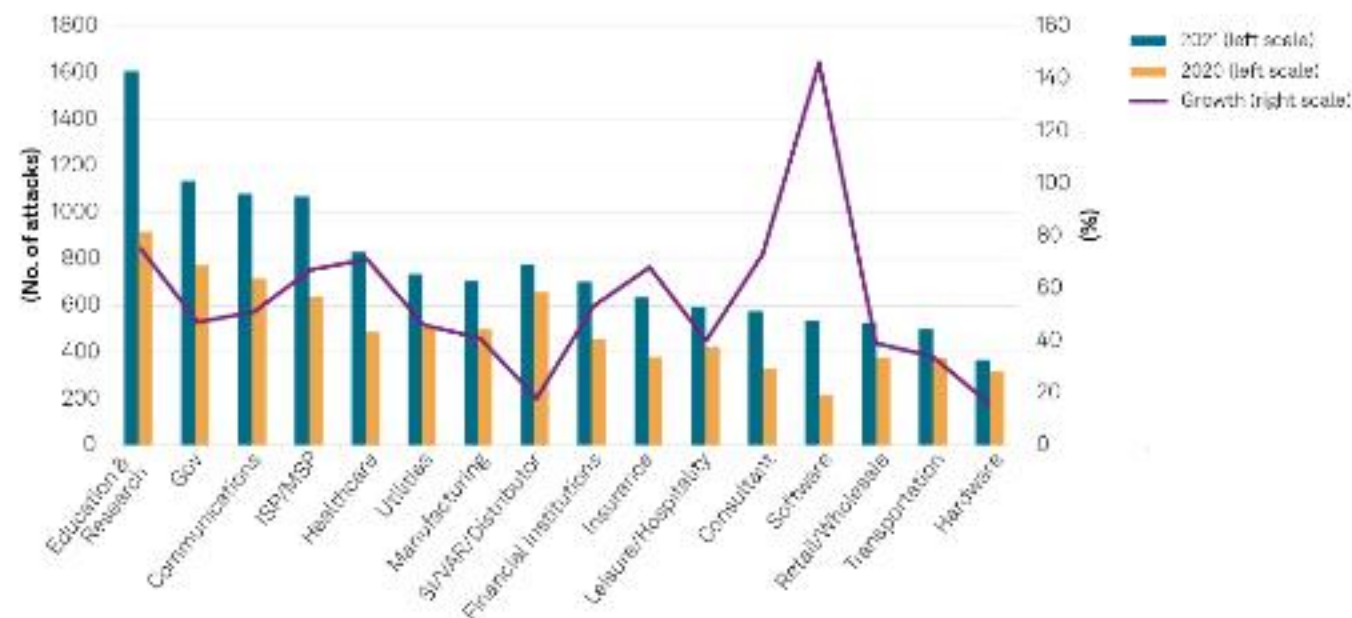
**“233 days.** The average time financial institutions took to detect and address data breaches.” Cloudwards, Dec. 12, 2022

**“The ransomware attack against Scripps Health that led to more than four weeks of electronic health record (EHR) downtime procedures and the theft of some patient data, resulted in \$112.7 million in estimated revenue loss and incremental expenses.”** Scripps, Aug. 10, 2021

# Cyber & Crypto | Risk Management

## Cyberattacks Increasing Across All Industries

Average Weekly Cyberattacks Per Organization By Industry



Source: Check Point Research  
 As Threats Rise, U.S. Public Finance Entities Take On Mounting Challenges To Secure The Digital Front Line, published Dec. 13, 2022

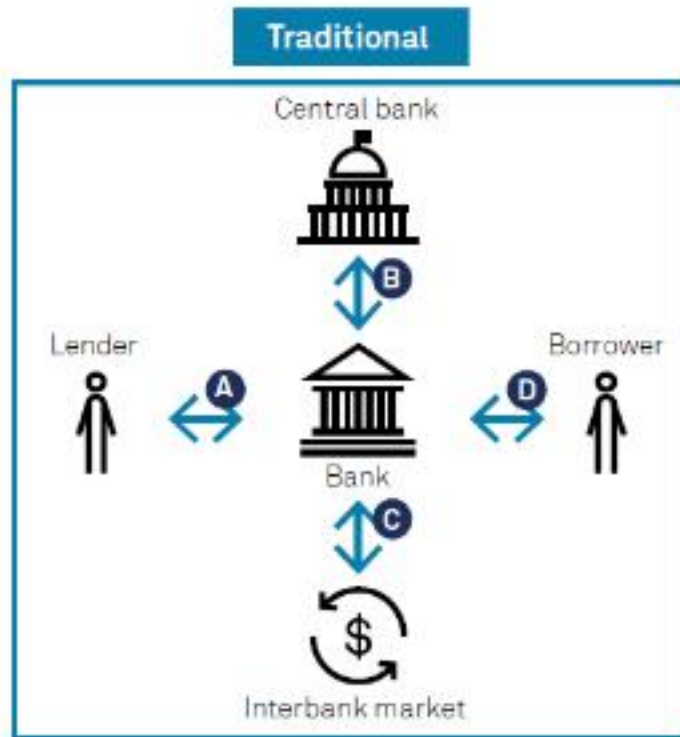
## Cryptocurrency and Decentralized Finance



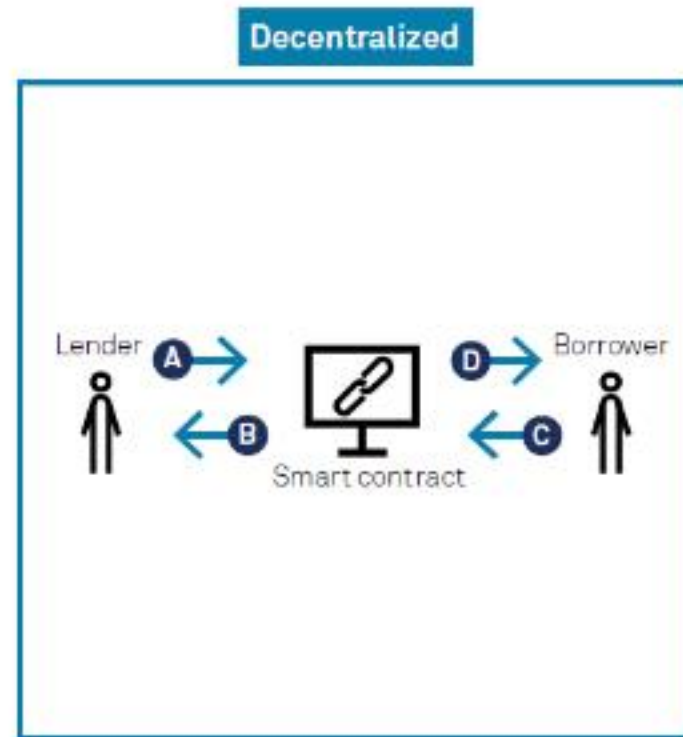
Source: Exploring Crypto And DeFi Risks In Credit Ratings, published June 30, 2022



# Disruptors | DeFi Uses Smart Contracts In Place Of Conventional Financial Risk Functions



- A** Lender deposits fiat money to receive interest
- B** Central bank provides liquidity to banks and sets interest rates based on inflation and other parameters
- C** Interest rates on bank loans affected by interbank market
- D** Loan approval and interest rate for borrower depends on collateral and borrower risk profile



- A** Provides eligible crypto assets as liquidity
- B** Receives tokens as determined by protocol as form of interest
- C** Provides other eligible crypto assets as collateral\*
- D** Receives a borrowed amount of crypto assets

# Q&A





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