U.S. States' Fiscal 2023 Liabilities: Stable Debt, With Pension And OPEB Funding Trending Favorably

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Key Takeaways

- Based on our 50-state survey, total U.S. state net direct debt decreased 1.3% in fiscal 2023, while the combined state share of net pension and OPEB liabilities declined 8.8% compared with fiscal 2022.
- On average, state debt metrics remain low to moderate compared with most economic and state budgetary measures and will likely remain so as states took advantage of federal funding and pursue paygo funding for capital needs that have traditionally been debt-funded.
- Pension funded ratios improved slightly in fiscal 2023 relative to fiscal 2022 and we expect continued improvement in fiscal years 2024 and 2025.

Although State Debt Levels Were Steady In 2023, Waning Federal Stimulus And Lower Borrowing Costs Could Increase Borrowing In Coming Years

U.S. state debt levels remained relatively flat in fiscal 2023 compared with 2022, declining a modest 1.3%. S&P Global Ratings attributes this year-over-year decline to a combination of factors, including elevated borrowing costs and inflation-induced cost pressures, record-high liquidity levels due to large budget surpluses, and substantial COVID-19 relief stimulus that could be used for one-time purposes, making pay-as-you-go (paygo) funding of capital expenditures a more attractive alternative to debt financing.

By the numbers: U.S. states' 2023 debt

1.7%
Net direct debt as a share of personal income

1.4%
Net direct debt as % of gross state product

0.2%
Net direct debt as a share of governmental expenditures

16
States with increased debt levels in 2023 vs. 2022

$1,067
Net direct debt per capita

1.3%
Decrease in total net direct debt outstanding

Source: S&P Global Ratings.

The rate-cutting cycle in the U.S. began with a 50-basis-point cut at the Sept. 18, 2024, Federal Open Market Committee meeting. S&P Global Economics believes that the Fed will continue easing monetary policy in the coming year through a regular series of interest-rate cuts. Our baseline outlook envisions a steady, spaced-out series of rate cuts that will help the Fed engineer a soft landing--where demand stays close to potential while the last bit of excess inflation evaporates. We believe the federal funds rate will fall to 3.00%-3.25% by the end of 2025 from the current 4.75%-5.00%, with another 50 basis points (bps) of cuts by the end of 2024 and 100 bps of cuts anticipated in 2025. For more information see "Economic Outlook U.S. Q4 2024: Growth And Rates Start Shifting To Neutral," published Sept. 24, 2024, on RatingsDirect.

Before the September cut, the Fed's 5.25%-5.50% target range challenged states to achieve significant savings through financings; however, lower rates in light of recent Fed actions and those anticipated continue to make the issuance environment more favorable. Given that the higher rate environment has reduced traditional refunding opportunities, some states have opted for optional extraordinary redemptions and tenders to redeploy cash and realize savings. New sale issuances have accelerated in 2024 because states have needed to balance the objective of funding critical state programs with long-term debt while striving to maintain rainy-day funds and other liquidity, thereby providing stability to state finances if an economic slowdown were to occur.

Inflation has begun to moderate in part due to the Fed's actions although it continues to adversely affect costs. Project costs have often increased well above the overall rate of inflation, with some states reporting they have revised project estimates upward by more than 30%. States have not made significant adjustments to their capital plans in general and, where possible, have leveraged American Rescue Plan Act (ARPA) and Infrastructure Investment and Jobs Act (IIJA) funds that will continue to flow into the economy over the next several years. ARPA dollars must be obligated by December 2024 and spent by the end of December 2026. The IIJA, which authorized $1.2 trillion for transportation and infrastructure spending, requires that $550 billion be spent before 2026. For example, Tennessee and Georgia have both funded their respective capital budgets with cash on hand, reducing their debt issuance expectations for fiscal years 2024 and 2025.

Since 2019, State Debt Burdens Have Generally Declined As A Share Of Real GSP And Personal Income

When evaluating a state's debt burden, S&P Global Ratings generally begins with a review of historical data. The trend of historical results and our understanding of the reasons for those trends inform our view of whether the debt burden will go up or down. We also consider a state's economic environment, our expectations for its economic growth, and that growth's likely impact on the debt burden in the future. Table 1 shows that, since 2019, the median state's debt burden has modestly decreased by most measures, including debt to personal income, debt as a percent of expenditures, and debt to real gross state product (GSP). On average, net direct debt per capita has increased modestly over the same period. This metric could increase over time if capital plans are not appropriately scaled as some states' population growth slows or declines. The five states with the most debt outstanding--are California, New York, New Jersey, Massachusetts, and Illinois--hold approximately 49% of state net direct debt outstanding (and account for about 26% of the U.S. population).

Table 1

U.S. state debt affordability over time

	2019	2020	2021	2022	2023
Net debt service as a % of governmental expenditures	3.7	3.7	3.3	3	2.9
Net direct debt as a % of personal income	1.9	1.8	1.7	1.7	1.7
Net direct debt as a % of real GSP	1.6	1.7	1.6	1.5	1.4
Net direct debt per capita (mil. $)	940	932	1,000	1,006	1,067

GSP--Gross state product. Source: S&P Global Ratings.

S&P Global Economics' most recent forecast projects that U.S. GDP growth will slow to 1.8% in 2025 from 2.7% in 2024. States have a historically high level of liquidity that can be used to fund capital projects on a paygo basis, which will likely mitigate the negative impact that slowing economic growth would otherwise have on debt metrics. Therefore, we generally expect ratios will remain stable in the near-to-medium term. Many states, particularly those with larger debt burdens, employ robust debt management strategies and adhere to affordability requirements, all of which support our forward-looking view of stability when looking at median state debt burdens. We view a state's debt capacity and ability to pay debt service as correlated to its economic output, as taxes and fees generated by economic activity are the primary source to pay debt service. If generally favorable tax revenue trends reverse and the growth of state debt burdens begins to outpace growth of the revenue streams servicing them, it could suggest fiscal stress and a decreasing capacity to service debt. This is something we continually monitor throughout economic cycles.

State Current Costs For Debt, Pension, And OPEBs Tend To Correlate With The Size Of A State's Economy

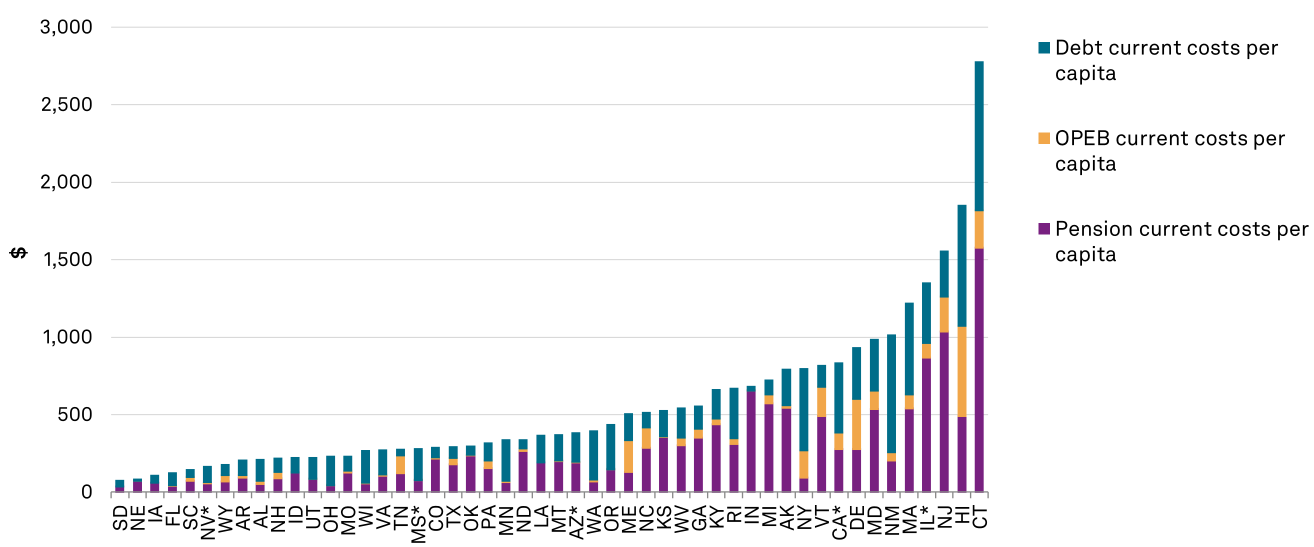
States with high fixed costs, including debt, pension, and other postemployment benefit (OPEB) payments, typically have less flexibility to make necessary budget adjustments during periods of financial stress. We also expect that states with more rapid economic growth that have greater capital needs can generally support higher debt and liability levels.

Some states have increased debt burdens because they provide higher support for programs and projects that generally receive a greater proportion of funding from local governments. For example, Hawaii directly runs the public school, university, and community college systems. And Connecticut, in our view, generally provides a higher level of support to local needs resulting in a lower debt profile at the city and county level. Many states also have either constitutional or statutory requirements, or court-mandated minimums, to provide adequate educational funding, which can also lead to higher debt burdens because it can be difficult for many states to reduce funding for these programs from a legal standpoint.

Charts 1 and 2 show fiscal 2023 combined debt, pension, and OPEB current costs relative to state population and general fund revenues. On a per capita basis, South Dakota, Nebraska, Iowa, Florida, and Wyoming have the lowest current costs, with all states below $120 per capita. Six states--New Mexico, Massachusetts, Illinois, New Jersey, Hawaii, and Connecticut--had carrying costs in excess of $1,000 per capita in 2023. The median carrying cost per capita among states was $365, meaning that 25 states were below this threshold, and 25 were above it (chart 1).

Chart 1

U.S. state current costs per capita, fiscal 2023

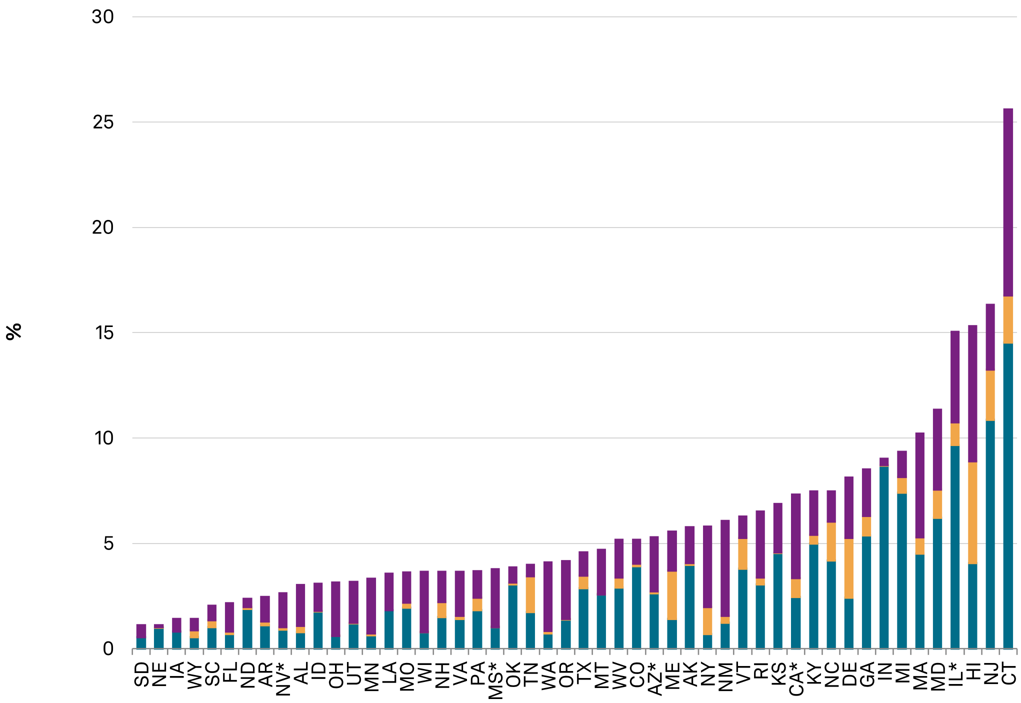


*The 2023 annual comprehensive financial reports are unavailable for Arizona, California, Illinois, Mississippi, and Nevada, so we used 2022 data. OPEB--Other postemployment benefits. Source: S&P Global Ratings.

As a percentage of general fund revenues, four states had current costs representing 2% of revenues or lower (South Dakota, Nebraska, Iowa, and Wyoming), while six states had current costs that exceeded 10% of revenues (Massachusetts, Maryland, Illinois, Hawaii, New Jersey, and Connecticut) (chart 2). The median current cost as a percentage of revenues was 4.4%, meaning that 25 states were above and 25 were below this level.

Chart 2

U.S. state current costs as a percentage of fiscal 2023 revenues



*The 2023 annual comprehensive financial reports are unavailable for Arizona, California, Illinois, Mississippi, and Nevada, so we used 2022 data. Source: S&P Global Ratings.

By the numbers: U.S. states' pension and OPEB medians, fiscal 2023

		Funded ratio (%)	Net liability (Bil. $)	Aggregate net liability per capita ($)	Median net liability as % of GSP (%)	Median net liability as % of personal income (%)
Pension medians						
	2023:	**75.1** ▲	**4.4** ▲	**1,165** ▼	**1.6**	**1.8**
	2022:	73.6	3.7	1,241		
	2021:	81.2	2.7	702		
OPEB medians						
	2023:	**11.2** ▲	**1.4** ▼	**248** ▼	**0.4**	**0.7**
	2022:	9.7	1.5	321		
	2021:	6.1	2.1	407		

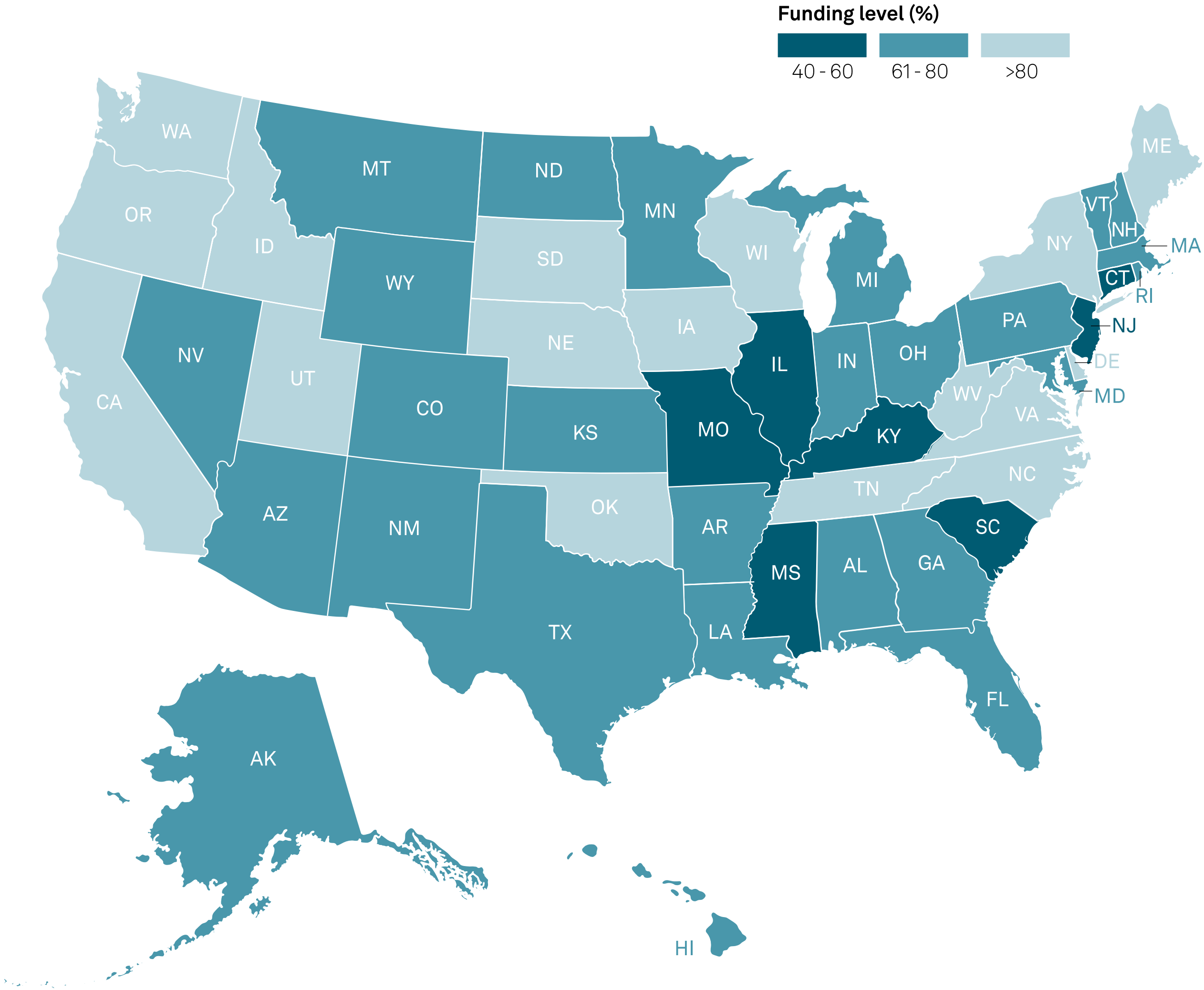
OPEB--Other postemployment benefits. GSP--Gross state product. Source: S&P Global Ratings.

Combined proportionate state net pension and OPEB liabilities declined 8.8% in fiscal 2023 relative to fiscal 2022 levels. The decline in net pension liabilities and the associated improvement in pension funded ratios are largely due to positive investment returns estimated at 12% for fiscal 2023. S&P Global Ratings expects asset performance will spur notable improvement in U.S. public pension funded ratios for the fiscal year ended June 30, 2024 (July 1, 2023-June 30, 2024), with an expected 16%-17% return, adding to the positive returns for fiscal 2023. Given the typical one-year delay from pension measurement to reporting, we expect to see the positive credit impact play out over the next two years. For more information, see our report, "Pension Brief: U.S. Public Pension Funded Ratios Continue Improvement In 2024," published July 25, 2024.

Median net OPEB liabilities also declined to 0.4% of GSP in fiscal2023, from 0.5% in fiscal 2022 but increased to 0.7% as a share of personal income from 0.6% in fiscal 2022. Net OPEB liabilities per capita declined 22.7% to $248 from $321. Since most U.S. OPEB plans fund retiree medical benefits on a paygo basis, they are exposed to higher liability and cost volatility than they would be if they were prefunded. States might improve OPEB funding by adding assets, reducing liabilities, or both. Since states differ in their legal flexibility to manage liabilities, options for some to contain rising costs could be limited. Some face legal restrictions in their ability to prefund an OPEB trust, forcing claims volatility and cost escalation to directly affect these states' budgets.

Chart 3

Aggregate U.S. state pension funded ratios 2023



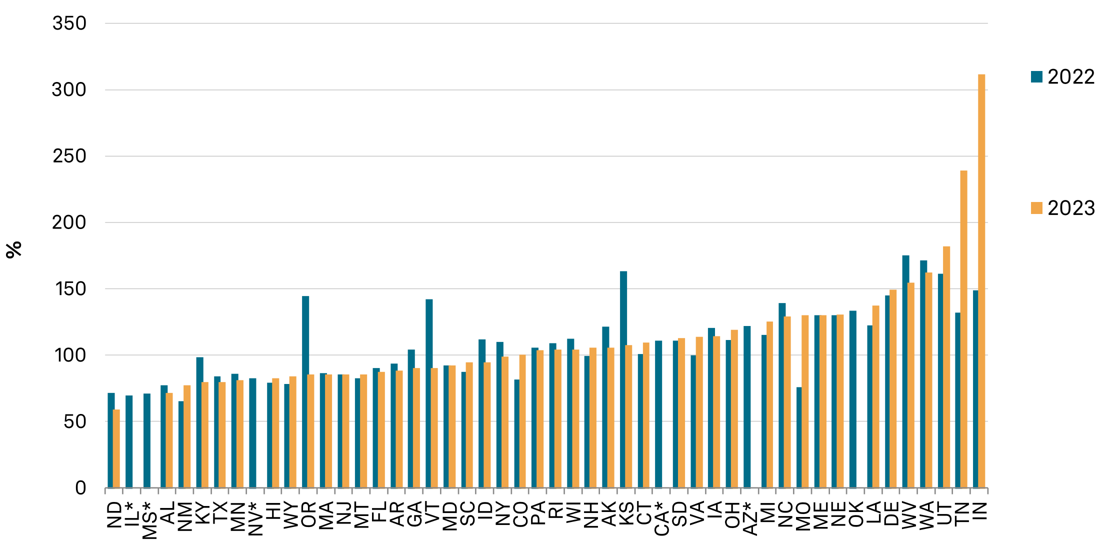
For most plans, data aligns with the state's 2023 fiscal year. For some plans, data aligns with the state's 2022 fiscal year depending on data availability. Plans with calendar year-end reporting periods are incorporated within the state's respective fiscal year (e.g., reports ending Dec. 31, 2022, are counted within the state's 2023 fiscal year). Source: S&P Global Ratings.

Many States Still Fall Short Of The Minimum Funding Progress, Though Some Show Improvement

Despite efforts to improve funding discipline, many states are falling short of making meaningful progress on their aggregate pension and OPEB liabilities. Many are funding their retirement liabilities on an actuarial basis; however, if the underlying actuarial assumptions are not consistently met or if contribution methods are weak, actuarially determined contributions (ADCs) could fail to make meaningful funding progress. Our minimum funding progress (MFP) metric is an amount that we consider meaningful progress for a given year. Actual contributions exceeded MFP for 20 states in fiscal 2023, compared with 27 states in fiscal 2022. In fiscal 2023, notable excess contributions were made in Indiana, which directed $2.5 billion of reserve balances to reduce its pre-1996 teachers plan pension liability. Tennessee has made additional proactive contributions through its budget, totaling $500 million in 2023 and $550 million in 2024, to pay its net pension liability and OPEB liabilities, in excess of the ADC level and significantly above our MFP calculation. OPEB plan funding generally stands in contrast to funding for state pension plans. Most states continue to fund OPEB liabilities on a paygo basis in which annual funding is equal to the benefits distributed; assets are not set aside to accrue returns and help offset future costs.

Chart 4

Actual pension contributions as a percent of MFP for top two plans, 2022-2023



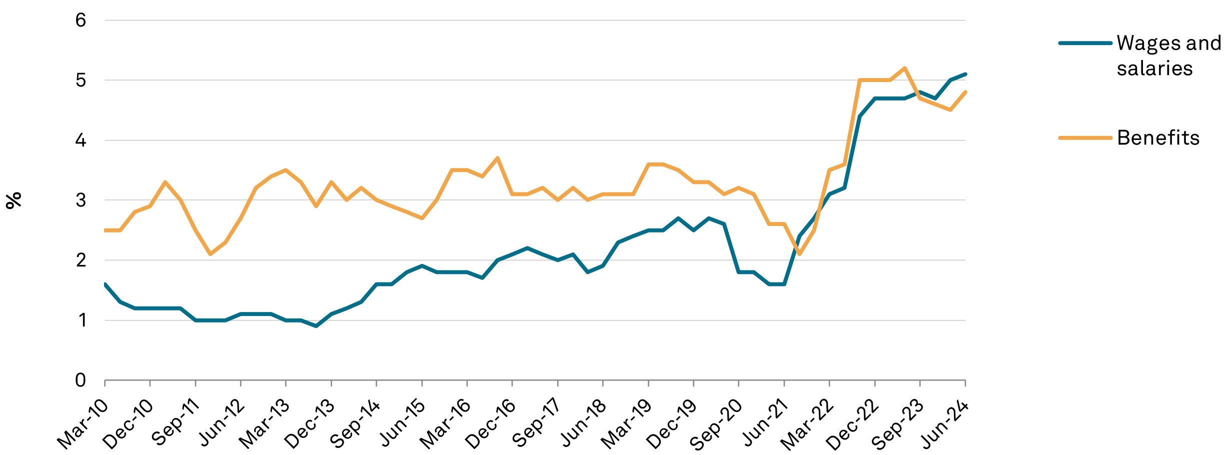
*The 2023 annual comprehensive financial reports are unavailable for Arizona, California, Illinois, Mississippi, and Nevada. MFP--Minimum funding progress. Source: S&P Global Ratings.

Since mid-2021, wage growth has caught up with benefits because inflation and associated effects, as well as tight labor market conditions, have spurred state and local employers to increase wages to attract and retain workers. From 2019 to 2023, average annual wages per state government employee increased 21.5%, to $76,359 from $62,830. To offset the resulting rising pension costs due to higher wages, states and local governments have instituted less expensive pension plan tiers for new hires, with increasing employee contributions serving as one reform method that lessens the burden on employers. We believe that because of attraction and retention pressures, demand for wage growth will outpace the limited, or spent, ability of plans to add cheaper new benefit tiers, which could lead to rising budgetary stress from pension costs.

So far, the closing gap between wage and benefits growth does not appear to have affected state and local government hiring. The U.S. Bureau of Labor Statistics reported that state and local governments added an estimated 23,000 jobs in August 2024, marking the 31st consecutive month that state and local government employment was stable or increased. So far, reductions in future retirement benefits for new state and local government hires have not impeded employment growth in the sector, but we continue to monitor how states consider the effects of recent wage increases on the future growth of postretirement benefit costs.

Chart 5

Wages/salaries and benefits for state and local government, 12-month % change, not seasonally adjusted



Sources: Bureau of Labor Statistics and S&P Global Ratings.

Robust liquidity positions, strong revenue performance, federal stimulus, and strong management controls allowed states to improve pension and OPEB funding and fund capital projects in fiscal 2023 without having to increase debt levels in aggregate. We expect economic growth to slow in 2025; however, many states citing the pursuit of growth have cut taxes and could face pressures should financial forecasts not hold, or if there is a pullback in consumer spending. Although upcoming elections could cause shifts in governmental budget and policy priorities, S&P Global Ratings believes that record-high liquidity will cushion state credit stability as current costs for debt and liabilities remain manageable. Strong asset performance in fiscal 2024 and thus far in fiscal 2025, along with an ongoing focus on funding discipline, will continue to support funding progress in the near term.

Table 2

State net direct debt statistics for fiscal 2023

State	Fiscal 2023 (mil. $)	Rank	Per capita ($)	Rank	As a % of personal income	Rank	As a % of GSP	Rank	Debt service as a % of general spending	Rank
Alabama	5,724	21	1,139	23	2.1	19	1.9	19	3.7	22
Alaska	892	40	1,216	22	1.7	24	1.3	27	1.6	39
Arizona*	1,593	36	214	46	0.3	46	0.3	46	0.7	45
Arkansas	829	42	270	44	0.5	41	0.5	41	3.0	25
California*	80,973	1	2,078	12	2.6	17	2.1	17	3.5	23
Colorado	4,365	25	743	31	0.9	33	0.8	33	1.9	35
Connecticut	26,568	6	7,345	1	8.4	2	7.8	2	16.4	1
Delaware	2,803	29	2,717	8	4.2	5	3.0	9	5.4	11
Florida	12,703	11	562	34	0.8	36	0.8	34	3.2	24
Georgia	10,628	14	964	28	1.6	26	1.3	28	5.1	14
Hawaii	9,293	17	6,475	2	9.9	1	8.6	1	11.4	2
Idaho	743	43	378	39	0.6	37	0.6	37	0.5	48
Illinois*	34,521	4	2,751	7	3.9	9	3.2	7	6.2	7
Indiana	1,276	39	186	47	0.3	47	0.3	47	0.7	44
Iowa	555	46	173	48	0.3	48	0.2	49	0.3	49
Kansas	3,820	26	1,299	20	2.0	21	1.7	22	2.7	28
Kentucky	4,955	24	1,095	25	2.0	22	1.8	21	2.2	32
Louisiana	7,136	20	1,560	16	2.7	15	2.3	16	5.3	12
Maine	1,450	38	1,039	26	1.6	25	1.6	23	2.7	27
Maryland	14,192	9	2,296	10	3.1	13	2.8	12	5.8	9
Massachusetts	41,103	3	5,871	3	6.7	3	5.6	3	6.4	6
Michigan	8,838	18	880	29	1.5	28	1.3	26	2.3	31
Minnesota	7,417	19	1,293	21	1.8	23	1.6	24	4.6	16
Mississippi*	5,609	22	1,908	13	4.0	8	3.8	5	6.8	5
Missouri	2,238	30	361	40	0.6	40	0.5	40	2.5	30
Montana	177	49	157	49	0.2	49	0.3	48	0.7	46
Nebraska	33	50	44	50	0.0	50	0.0	50	0.2	50
Nevada*	2,063	33	646	32	1.0	32	0.9	31	1.7	37
New Hampshire	686	44	489	37	0.6	39	0.6	38	2.6	29
New Jersey	30,925	5	3,329	4	4.1	6	3.9	4	8.5	3
New Mexico	3,286	27	1,554	17	2.9	14	2.5	15	4.7	15
New York	62,181	2	3,177	5	4.0	7	2.9	11	3.9	21
North Carolina	5,435	23	502	36	0.8	35	0.7	36	2.0	34
North Dakota	877	41	1,119	24	1.5	27	1.2	29	0.6	47
Ohio	9,474	16	804	30	1.3	30	1.1	30	4.1	19

Table 2

State net direct debt statistics for fiscal 2023 (cont.)

State	Fiscal 2023 (mil. $)	Rank	Per capita ($)	Rank	As a % of personal income	Rank	As a % of GSP	Rank	Debt service as a % of general spending	Rank
Oklahoma	2,136	32	527	35	0.9	34	0.8	32	1.9	36
Oregon	11,717	13	2,768	6	4.2	4	3.7	6	5.3	13
Pennsylvania	18,818	8	1,587	19	2.1	18	1.9	18	4.2	18
Rhode Island	1,987	34	1,813	14	2.7	16	2.6	14	5.7	10
South Carolina	1,485	37	276	43	0.5	43	0.5	42	0.9	43
South Dakota	414	47	451	38	0.6	38	0.6	39	1.6	38
Tennessee	1,746	35	245	45	0.4	45	0.3	45	1.4	40
Texas	9,890	15	324	42	0.5	42	0.4	44	1.3	41
Utah	2,170	31	635	33	1.0	31	0.8	35	4.0	20
Vermont	634	45	980	27	1.5	29	1.5	25	2.1	33
Virginia	12,999	10	1,492	18	2.0	20	1.8	20	4.2	17
Washington	20,833	7	2,667	9	3.3	10	2.6	13	7.0	4
West Virginia	2,909	28	1,332	15	3.1	12	2.9	10	2.8	26
Wisconsin	12,559	12	2,125	11	3.3	11	3.0	8	5.8	8
Wyoming	197	48	337	41	0.4	44	0.4	43	1.0	42
Median	4,093	--	1,067	--	1.6	--	1.4	--	2.9	--

*The 2023 annual comprehensive financial reports were unavailable for Arizona, California, Illinois, Mississippi, and Nevada, so we used 2022 data. GSP--Gross state product. Source: S&P Global Ratings.

Table 3

States pension and OPEB liabilities and statistics for fiscal 2023

	Pensions			OPEBs		
State	Aggregate state share of NPL (mil. $)	Aggregate pension funded ratio (%)	State NPL per capita ($)	Aggregate state share of NOL (mil. $)	Aggregate OPEB funded ratio (%)	State NOL per capita ($)
Alabama	4,792	62	938	1,518	32.8	297
Alaska	4,389	72	5,984	(1,166)	100	(1,590)
Arizona	4,381	75	590	671	59.8	90
Arkansas	2,525	79	823	1,542	0	503
California	64,063	81	1,585	97,377	4.3	2,499
Colorado	14,575	61	2,480	262	38.6	45
Connecticut	38,010	54	10,508	17,102	12.3	4,728
Delaware	1,783	86	1,728	7,421	7.7	7,192
Florida	7,596	79	336	7,843	0	347
Georgia	11,280	76	1,023	3,066	47.5	278
Hawaii	7,392	63	5,150	6,848	37.2	4,772

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States pension and OPEB liabilities and statistics for fiscal 2023 (cont.)

	Pensions			OPEBs		
State	Aggregate state share of NPL (mil. $)	Aggregate pension funded ratio (%)	State NPL per capita ($)	Aggregate state share of NOL (mil. $)	Aggregate OPEB funded ratio (%)	State NOL per capita ($)
Idaho	706	85	360	(128)	95.4	(65)
Illinois	148,596	43	11,632	21,867	1.2	1,742
Indiana	6,509	76	948	85	76.2	12
Iowa	986	90	307	428	0	133
Kansas	7,344	71	712	0	0	0
Kentucky	28,137	49	6,217	988	67.4	218
Louisiana	6,301	73	1,378	6,768	0.0	1,480
Maine	2,315	86	1,659	1,601	25.1	1,147
Maryland	22,268	73	3,603	11,869	3.8	1,921
Massachusetts	42,771	64	6,109	14,203	13.8	2,029
Michigan	17,585	67	661	2,009	75.4	200
Minnesota	2,419	82	422	732	0	127
Mississippi	4,487	56	1,242	110	0.2	38
Missouri	8,275	56	1,336	2,637	6.8	426
Montana	2,611	74	2,305	67	0	60
Nebraska	439	92	222	27	0	13
Nevada	3,042	76	952	913	0	286
New Hampshire	1,079	67	769	1,675	0.5	1,195
New Jersey	76,660	47	8,251	74,932	0	8,065
New Mexico	6,754	66	3,194	335	40.7	159
New York	11,120	93	568	58,219	2.1	2,975
North Carolina	4,206	83	388	5,319	10.7	491
North Dakota	1,030	68	1,314	50	62.7	64
Ohio	6,808	78	578	365	94.8	31
Oklahoma	2,446	81	603	(111)	100	(27)
Oregon	4,907	82	1,159	(70)	65.6	(16)
Pennsylvania	45,692	62	3,401	9,866	5.9	1,198
Rhode Island	2,816	65	2,569	340	51.2	311
South Carolina	3,971	60	739	2,524	11.2	470
South Dakota	(2)	100	(2)	0	0	0
Tennessee	830	94	117	1,357	46.1	190
Texas	58,774	73	1,927	48,613	4.5	1,594
Utah	973	95	285	(28)	99.4	(8)
Vermont	3,016	62	4,659	1,658	11.1	2,561

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States pension and OPEB liabilities and statistics for fiscal 2023 (cont.)

	Pensions			OPEBs		
State	Aggregate state share of NPL (mil. $)	Aggregate pension funded ratio (%)	State NPL per capita ($)	Aggregate state share of NOL (mil. $)	Aggregate OPEB funded ratio (%)	State NOL per capita ($)
Virginia	6,180	81	709	1,424	16.6	163
Washington	(6,192)	100	(793)	4,250	0	544
West Virginia	2,072	90	1,170	(126)	100	(71)
Wisconsin	1,520	96	257	614	59.3	104
Wyoming	589	75	999	200	0	299
Median	4,438	75	1,011	1,391	11	282

For most plans, data aligns with a state's 2023 fiscal year. For some plans, data aligns with a state's 2022 fiscal year depending on data availability. Plans with calendar year-end reporting periods are incorporated within a state's respective fiscal year (for example, reports ended Dec. 31, 2022, are counted within a state's 2023 fiscal year). Funded ratios are capped at 100%. We exclude various OPEB plans that do not offer medical benefits. The majority of these benefits resulted in relatively small liabilities but these benefits are sizable for some states. Kansas and South Dakota do not report even an implicit liability for retiree health care benefits. We are calculating Nevada's aggregate OPEB funded ratio as negative because the state's plan reported gross benefit payments that exceeded contributions and income in fiscal 2022. We are calculating a NOA for Utah's OPEB plans although the state's aggregate OPEB funded ratio is below 100% due to how we aggregate OPEB data across state plans. OPEB--Other postemployment benefits. NPL--Net pension liability NOL--Net OPEB liability. NOA--Net OPEB asset. Source: S&P Global Ratings.

Related Research

- Economic Outlook U.S. Q4 2024: Growth And Rates Start Shifting To Neutral, Sept. 24, 2024
- Pension Brief: U.S. Public Pension Funded Ratios Continue Improvement In 2024, July 25, 2024

This report does not constitute a rating action.