

MASS TRANSIT: IS CREDIT RECOVERY ON SCHEDULE?

UNCLE SAM RIDES TO THE RESCUE

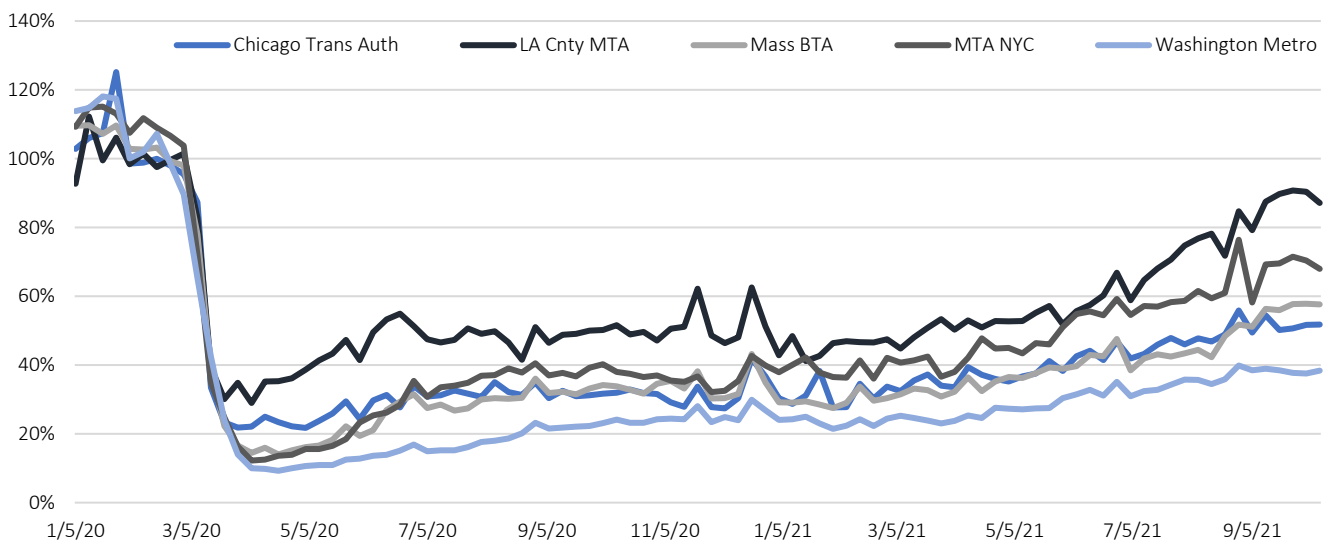
The social and economic fallout from the ongoing COVID-19 pandemic has been pronounced, and Mass Transit remains a sector of acute focus for tax-exempt credit analysts. While ridership levels were already under pressure before the pandemic, nationwide stay-at-home orders caused volumes to grind to a near halt in the Spring and Summer of 2020. This prompted credit concerns and a corresponding need for massive Federal aid. CARES Act funding, December's stimulus package, and the subsequent American Rescue Plan Account (ARPA) delivered funds that accounted for 4.9x pre-pandemic mass transit farebox revenue and 1.58x annual sector operating expenses.¹ Support of that nature is not expected to continue, which begs the question of how far along the recovery cycle things are and what that means for mass transit issuers.

TRANSPORTATION SYSTEMS GRAPPLE WITH AN AGE OF UNKNOWNNS

Ridership has steadily increased over the course of 2021, yet it remains suppressed relative to historic norms due largely to remote and hybrid employment practices, and lingering public health concerns. On the positive side, increased vaccination levels, easing COVID-19 restrictions, and a gradual return to the office have bolstered mass transit utilization, a trend we expect to continue. To what extent this ultimately occurs and how long it takes to get there are the key credit variables. It also bears emphasizing that although sector trends are informative, issuer specific analysis remains paramount.

Metro areas across the country have experienced a wide disparity in recovery rates to date. Los Angeles and New York have enjoyed the most significant rebound among the five largest transit systems, while Washington DC has lagged. Differentiating factors include distinct pre-pandemic ridership trends, travel modes, vaccination progress, and pace and magnitude of local economic recovery.

Weekly Ridership Trends v. 2019 Pre-Pandemic



Source: American Public Transportation Association

Although ridership trends are heading in the right direction, pandemic induced changes to employment and commuting patterns will likely prevent a complete recovery. S&P reports that return-to-work surveys suggest about 20% of the US workforce now has an ability to work from home, and one to two days per week is very likely going forward, leading to a potential 2 to 4% permanent loss in ridership.

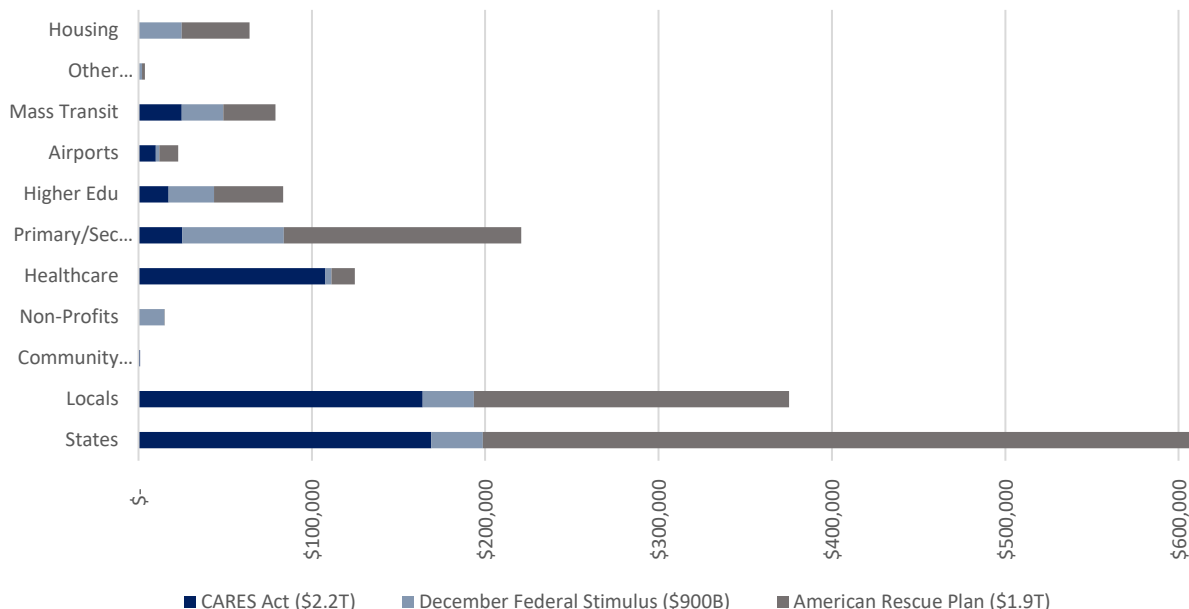
Accordingly, our evaluation of individual credits emphasizes management's ability to not only adjust service levels and operating expenses, but also more permanently align these measures with "new normal" usage levels. This is especially critical for bond issues that rely on fare box revenue to support debt service. Notably, most Mass Transit bonds that Appleton credit approves are not backed by ridership activity or fare box revenue. Our inclination is to instead invest in bonds from issuers that draw upon local sales taxes to service debt, as historically this revenue source has delivered more ample, stable cash flow.

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SEPARATING TRANSIT VALUE FROM POTENTIAL CREDIT DERAILMENTS

Ongoing challenges for mass transit systems remain, yet the sector benefits from several sustainable strengths that have long supported many issuers' credit fundamentals. Mass Transit systems are essential to the economy, generally enjoy strong voter support, and have been bolstered by generous state and federal aid. The largest issuer, the Metropolitan Transit Authority (MTA) has \$49 billion in debt outstanding and is widely viewed as integral to not only the NY Metro area but the US economy at large. While we see significant value in certain credits, many others have been avoided based on credit and/or relative value concerns. One size does not fit all, and our analysts are carefully analyzing ridership trends, the health of the local economy, and bond specific debt provisions, among other factors, when considering investments in Mass Transit bonds.

Federal Aid Has Bridged Pandemic Budget Gaps (\$million)



Source: JP Morgan

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