THE BOND BUYER

Decrease in ridership may put pressure on transit financing

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A nationwide drop in mass transit ridership is cutting into fare revenue that transit agencies rely on for about one-third of operating costs, putting pressure on agencies' ability to borrow at attractive rates.

Between 2014 and 2018, the U.S. saw a 7.5% drop in ridership, according to a report by the libertarian think tank Cato Institute, with urban areas suffering larger declines. Transit agencies spent $46.9 billion on operations in 2016 and used $15.8 billion out of fare revenues to pay for them, Randal O'Toole, a senior fellow at Cato, wrote in his report.

The causes of the decline are varied, according to experts. Lower gas prices, remote working, easy driving and new competition from ride-share companies are taking slices of the pie.

However, O'Toole believes one cause inches above the rest.

"The growth of ride hailing is responsible for most, if not all the decline in transit ridership," O'Toole said.

Fare revenues don't cover many of the costs associated with public transportation, instead transit agencies rely on taxes and governmental aid to fund and maintain projects, softening the blow of decreased ridership. Agencies also may use sales tax revenues, for example, to back their bonds.

The Metropolitan Council and Metro Transit in the St. Paul/ Minneapolis area doesn't issue revenue bonds for its transit. Its financing is secured by property taxes, Kate Brickman, director of communications, wrote in an email. The region has seen a dip in overall ridership, but has experienced months of record ridership for its light rail system and bus rapid transit system, she wrote.

The Metropolitan Transit Authority of Harris County in Houston, Texas, has never issued a fare revenue bond, Chief Financial Officer Art Smiley wrote in an email.

"Our issuances have all been related in one way or another to sales tax revenues," Smiley said. However, the interest rate of a fare revenue bond would be higher than the rate on a general obligation bond issued by the same obligor, Smiley added.

If ridership were to fall to a level that indicated it was no longer viable as a business, Smiley wrote, then agencies would have a significant amount of difficulty in borrowing money.

In December 2018, Moody's Investors Service gave the Metropolitan Transportation Authority in New York a negative outlook because of its lower-than-expected ridership, driven by a decline in bus customers. MTA is still rated A1 with a negative outlook.

"In the U.S., most of our mass transit systems issue tax-backed bonds and where those economies are very strong, declining ridership really doesn't have an impact on pledged revenue growth," said Nick Samuels, Moody's vice president and senior credit officer.

However, for systems that are backed by enterprise revenues, where ridership and fare box collection matter more, the decrease in ridership would have an effect, Samuels said.

If ridership declines continue without agencies increasing fares, or coming up with alternative sources of revenue like congestion pricing, it could continue to have negative impacts on enterprise revenue backed systems, Samuels said.

"Long term, we'll have to see watch and see what the trend is and how that really impacts them," Samuels said. He added that no matter how agencies are funded, they will be looking for ways to enhance their revenue to keep riders.

Many transit agencies receive the majority of revenues from taxes and intergovernmental aid, and so are less vulnerable to the near-term revenue impacts of declining ridership, said Andrew Ward, a director at Fitch Ratings in San Francisco.

"Declining ridership has pressured operating budgets via reduced fare revenues and forced policymakers to adjust service levels and expenditures in the large urban transit agencies with the most ridership," Ward said. "Failure to adjust in a timely manner can be negative for credit quality but hasn't yet led to any downgrades in our portfolio."

Long-term, agencies may need to adapt, Ward said.

In the next 10 years, the pressure from decreased ridership could become greater, Ward said, but it's not clear that that trend will continue, since pressures now are cyclical.

To offset decreased ridership, agencies would need to increase fares or decrease expenditures, Ward said. To do so, some transit agencies will cut lines that have decreased ridership and put extra service where lines are busier, he said.

"If a transit agency can't come up with the political will to adjust service level and doesn't have the flexibility to adjust fares meaningfully, declines in ridership can erode their bottom line," Ward said. "That's the most negative outcome for financial stability."

The decline in ridership leads to investors thinking more about investing in autonomous vehicles, but since it's still just an idea, it hasn't taken hold quite yet, Ward said.

O'Toole believes that between 2020 and 2025 there will be driverless ride-hailing on a large-scale in major cities and added once it's perfected, the trend will spread fast. By taking the driver away, driverless cars will be less expensive than public transit, he said.

By 2030, transit agencies will exist solely to pay back their debts, O'Toole said, and to fulfill their unfunded pension and healthcare obligations. If they run transit at all, it's going to be just so that they can justify their existence to the voters because they're continuing to tax them, to pay off their debts and unfunded pension and healthcare obligations, he said.

"I would call them zombie transit agencies," O'Toole said. "They have empty buses and trains running around to justify paying back all these debts and unfunded obligations, but they're not really providing a useful service to anyone."