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INVESTORS SERVICE

CREDIT OPINION
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New Issue

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Washington (State of)

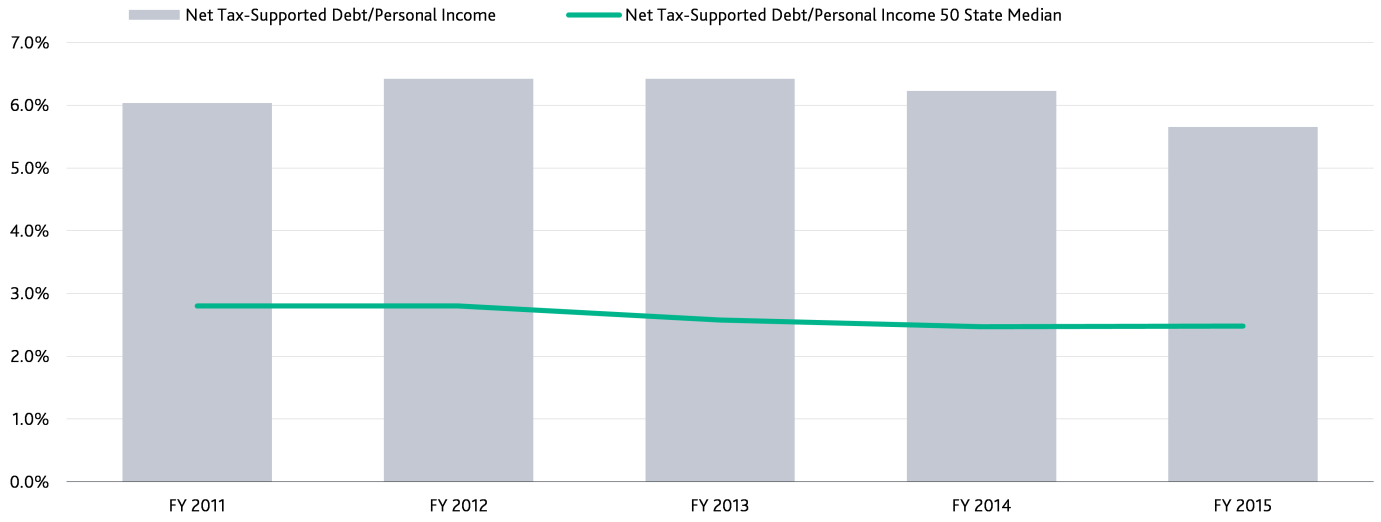
New Issue - Moody's assigns Aa1 to $1.3B Washington State GO bonds; outlook stable

Summary Rating Rationale

Moody's Investors Service has assigned Aa1 ratings to four series of the State of Washington's General Obligation Bonds: Various Purpose General Obligation Bonds, Series 2017A; General Obligation Bonds, Series 2017T (Taxable); Various Purpose General Obligation Refunding Bonds, Series R-2017A; and Motor Vehicle Fuel Tax General Obligation Refunding Bonds, Series R-2017B. The four series are expected to total approximately $1.3 billion. Following the issuance of these bonds, the state will have approximately $19.1 billion of general obligation bonds outstanding, including bonds additionally secured by fuel taxes and tolls, all rated Aa1. The outlook is stable.

Washington's Aa1 general obligation rating incorporates the state's sound management tools such as its quarterly consensus revenue forecasting process and demonstrated willingness to address budget shortfalls, along with an economy that is improving and expected to out-perform the nation over the long term. Revenue trends are positive, supported by employment gains and improvement in the state's housing market, and available reserves are increasing. These strengths are tempered by education spending mandates, exposure to the cyclical aerospace industry and other export markets, and above average debt ratios. Frequent voter initiative activity adds budget challenges although the state legislature has a history of responding effectively to maintain budget balance.

Exhibit 1
Washington's Debt Levels Exceed 50-State Medians



Source: Moody's Investors Service US State Debt Medians Reports

Credit Strengths

» Institutionalized governance practices such as consensus revenue forecasting, multi-year revenue and expenditure projections, and timely budget adoption

» Strong demographic trends

» Satisfactory overall liquidity levels maintained in pooled resources

» Healthy pension funding levels and modest retiree health insurance liability

» Increasing available reserves

Credit Challenges

» Significant future increases required in K-12 education funding

» Exposure to cyclical commercial aerospace industry and export market

» Above-average debt ratios

» Voter initiative activity adding element of fiscal uncertainty

Rating Outlook

Washington's rating outlook is stable, reflecting economic gains that are boosting revenues, an improving reserve position, and budget balancing solutions that are largely recurring. We expect that the state will continue to address any budget gaps that emerge, as it has in the past, and, over time, absorb the substantial increase in mandated basic education funding. Economic concentration in some industries that are historically volatile poses longer-term credit risk.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

Factors that Could Lead to an Upgrade

» Sustained trend of structural budget balance, plus maintenance of strong reserve levels

» Economic expansion and improved industry diversification

» Reduction of debt ratios to levels closer to Moody's 50-state medians

Factors that Could Lead to a Downgrade

» Employment erosion

» Protracted structural budget imbalance

» Increased reliance on one-time budget solutions

» Deterioration of the state's cash position

Key Indicators

Exhibit 2
Washington Has Rebuilt Reserves Since the Recession

Washington	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Operating Fund Revenues (000s)	16,252,763	16,099,012	17,067,211	17,765,292	18,789,958
Balances as % of Operating Fund Revenues	-0.7%	0.8%	2.4%	4.2%	7.9%
Net Tax-Supported Debt (000s)	17,677,697	19,425,533	20,386,128	20,422,165	19,800,626
Net Tax-Supported Debt/Personal Income	6.0%	6.4%	6.4%	6.2%	5.7%
Net Tax-Supported Debt/Personal Income 50 State Median	2.8%	2.8%	2.6%	2.5%	2.5%
Debt/All Governmental Funds Revenue	50.6%	56.4%	56.2%	52.7%	47.7%
Debt/All Governmental Funds Revenue 50 State Median*	22.7%	24.3%	23.8%	23.0%	20.4%
Adjusted Net Pension Liability/All Govt Funds Revenue	32.7%	25.2%	43.5%	56.7%	N/A
Adjusted Net Pension Liability/All Govt Funds Revenue 50 State Median	48.7%	63.9%	60.3%	59.2%	N/A
Total Non-Farm Employment Change (CY)	1.3%	1.6%	4.3%	2.8%	3.3%
Per Capita Income as a % of US (CY)	105.5%	107.0%	106.8%	107.7%	107.3%

*The 2015 governmental fund median number uses 2014 numbers for states that have not yet released their FY2015 audit

Source: State Audited Financial Statements with Moody's Investors Service Adjustments; Moody's Investors Service State Debt and Pension Medians Reports; US Bureau of Labor Statistics; US Bureau of Economic Analysis.

Recent Developments

In its latest revenue forecast, released June 15, the state increased its estimate of General Fund revenues for the 2015-17 biennium by $294 million and for the 2017-19 biennium by $126 million, compared to the February forecast.

Detailed Rating Consideration

Economy

Washington State benefits from a high-value-added, but often cyclical, commercial aircraft industry; a fast growing information technology industry; and above average per capita income and household wealth. Significant agriculture and timber sectors are vulnerable to volatile commodity prices and export demand. First quarter 2016 exports were down 15.6% from the first quarter of 2015. Transportation equipment exports (primarily The Boeing Company (A2 stable) airplanes) declined 17.4%. Exports other than transportation equipment declined by 12.8%. The state's unemployment rate has remained relatively stable over the past year, slightly above the US rate. The state's unemployment rate was 5.8% in April 2016, compared to 5.6% for the state one year earlier and 5.0% for the US in April 2016. The state's economic forecasts expect continued although slightly slower economic growth, with increasing employment in most sectors.

Finances and Liquidity

Driven by economic growth, state revenues have grown steadily since the recession. On a GAAP basis, the state's non-federal operating fund revenues grew at a compound annual rate of 5.1% from fiscal 2010 through 2015. In its June forecast, the state projects that General Fund revenues for the 2015-17 biennium will be $37.431 billion, an increase of 11.2% from the 2013-15 biennium and an increase of $294 million from the February forecast.

Due to rising revenues and expenditure controls, reserves, which fell to negative levels during the recession, have been gradually rebuilt to pre-recession levels. On a GAAP basis, available reserves, which consist of Unassigned General Fund Balance plus the state's Budget Stabilization Account increased from a negative $107 million (0.7% of revenues) at the end of fiscal 2011 to a positive $1,477 million (7.9% of revenues) at the end of fiscal 2015. In the February forecast, the state projects that total budget-basis reserves will decline slightly from $1,524 million at the end of fiscal 2015 to $1,487 million at the end of the 2015-2017 biennium, including $701 million in the Budget Stabilization Account.

The enacted budget for the 2015-17 biennium included a significant increase in K-12 education funding in response to the State Supreme Court's ruling in the "McCleary" case. The budget also includes additional funding for higher education. In conjunction with the approval of the budget, the legislature suspended for three years Initiative 1351 which would have required additional increases in K-12 funding. Subsequent to the adoption of the 2015-17 budget, the Supreme Court ruled that the state had still not complied fully with its ruling in the McCleary case and imposed a fine on the state of $100,000 per day. The legislature has not yet responded to the court's latest ruling.

LIQUIDITY

The state's overall liquidity is sound and has improved notably over the last four years with the improvement in GAAP-basis financial position. Average daily balances in the Treasury and Treasurer's Trust Fund were $4.4 billion for the 12 months from January through December 2015. The state does not issue cash flow notes.

Debt and Pensions

DEBT STRUCTURE

Washington's debt ratios are more than twice Moody's 2016 50-state median level; net tax-supported debt as a percentage of personal income is 5.7%, compared with Moody's 50-state median of 2.5%. Washington's net tax-supported debt per capita ($2,522) is more than twice the national median of $1,025. Annual debt service costs relative to revenue available for debt service (Moody's calculation) was also relatively high at 7.0% in fiscal 2015 versus a median of 4.3%.

DEBT-RELATED DERIVATIVES

The state has no variable rate debt and no debt-related derivatives.

PENSIONS AND OPEB

While debt ratios are above average, the state's aggregate pension funding is relatively strong. Based on the Washington's fiscal 2013 pension data, Moody's has calculated that the overall retirement systems' adjusted net pension liability (ANPL) was 43.5% of governmental revenues, well below the 50-state median of 60.3%. Other pension ratios such as ANPL to personal income, GDP, and population are similarly below the medians.

In Washington, retiree health benefits are set as part of the biennial budget process and funded on a pay-as-you-go-basis. As of January 1, 2015, the most recent date for which a full valuation was prepared, the actuarial accrued liability attributable to the state (after retiree contributions) was $5.274 billion. The annual required contribution (ARC) for fiscal year 2014 was $354 million, about 1.4% of the state's total governmental revenues, excluding federal aid.

Governance

The state has strong governance practices including a quarterly consensus revenue forecasting process, multi-year revenue and expenditure projections, timely budget adoption, and a demonstrated willingness to address budget shortfalls. Although frequent voter initiative activity can create budget challenges, the state legislature has broad powers to amend or suspend voter-approved initiatives.

Legal Security

The 2017A, 2017T, and R-2017A bonds are general obligations of the state, to which the state has pledged its full faith, credit and taxing power. The R-2017B bonds are also general obligations, but are additionally secured by and expected to be paid from motor vehicle fuel taxes.

Use of Proceeds

Proceeds of the 2017A and 2017T bonds will be used to fund various state capital projects and programs. Proceeds of the R-2017A and R-2017B bonds will be used to refund outstanding bonds for debt service savings.

Obligor Profile

Washington is the thirteenth largest state by population, at 6.9 million. Its state gross domestic product is fourteenth largest. The population is relatively wealthy, with per capita personal income equal to 107.3% of the US level and a poverty rate in the bottom third among states.

Methodology

The principal methodology used in this rating was US States Rating Methodology published in April 2013. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 3

Washington (State of)

Issue	Rating
Various Purpose General Obligation Bonds, Series 2017A	Aa1
Rating Type	Underlying LT
Sale Amount	$392,265,000
Expected Sale Date	06/28/2016
Rating Description	General Obligation
Various Purpose General Obligation Refunding Bonds, Series R-2017A	Aa1
Rating Type	Underlying LT
Sale Amount	$535,125,000
Expected Sale Date	06/28/2016
Rating Description	General Obligation
General Obligation Bonds, Series 2017T (Taxable)	Aa1
Rating Type	Underlying LT
Sale Amount	$101,345,000
Expected Sale Date	06/28/2016
Rating Description	General Obligation
Motor Vehicle Fuel Tax General Obligation Refunding Bonds, Series R-2017B	Aa1
Rating Type	Underlying LT
Sale Amount	$272,470,000
Expected Sale Date	06/28/2016
Rating Description	General Obligation

Source: Moody's Investors Service

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