STANDARD & POOR'S RATINGS SERVICES
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Summary:
Washington; Appropriations; General Obligation

Primary Credit Analyst:
Sussan S Corson, New York (1) 212-438-2014; sussan.corson@standardandpoors.com

Secondary Contact:
Gabriel J Petek, CFA, San Francisco (1) 415-371-5042; gabriel.petek@standardandpoors.com

Table Of Contents

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Credit Profile		
US$536.985 mil var purpose GO rfdg bnds ser R-2016B due 07/01/2033		
Long Term Rating	AA+/Stable	New
US$145.71 mil motor vehicle fuel tax GO rfdg bnds ser R-2016C due 07/01/2033		
Long Term Rating	AA+/Stable	New
Washington GO		
Long Term Rating	AA+/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AA+' long-term rating and stable outlook to the State of Washington's series R-2016B various purpose general obligation (GO) refunding bonds, and series R-2016C motor vehicle fuel tax GO refunding bonds.

At the same time, Standard & Poor's affirmed its 'AA+' long-term rating and underlying rating on the state's existing GO and motor vehicle fuel tax (MVFT) GO debt and its 'AA' rating and stable outlook on the state's existing appropriation-backed debt. The outlook on all ratings is stable.

The ratings reflect our view of the state's:

- Relatively well-educated workforce and good income indicators;
- Sales tax-based revenue structure that, although somewhat less sensitive to economic cycles than income tax-reliant states, is following a decades-long stagnating trajectory as a share of total revenue;
- High cost of housing, especially in key economic centers that could impede long-term growth prospects;
- Good internal access to sources of liquidity in the treasury and treasurer trust funds;
- Strong financial policies and practices, including statutory provisions requiring that the state's biennial budget and projected subsequent two fiscal years' spending plans be balanced; and
- Moderately high per capita debt burden but well-funded pension plans.

The state's full faith, credit, and taxing powers secure the state's GO bonds. The state's MVFT GO bonds are first payable from state excise taxes on motor vehicle and special fuels. The refunding bonds are being issued to refinance some of the state's existing debt.

Washington will have about $17 billion of GO bonds, net of reimbursements, outstanding after the current offering. Of this, about $6.4 billion of the state's net GO debt is payable first from excise taxes on motor vehicles and special fuels or from toll revenue. The state also has about $886 million of certificates of participation and other appropriation-backed debt outstanding as of February 2016.

In November 2015, the state's Economic and Revenue Forecast Council (ERFC) released an updated forecast that reflects revenue growth $245 million above budgeted estimates and 10.5% growth in 2015-2017 general fund revenue compared with the previous biennium. Washington's reliance on retail sales and business and occupation (gross receipts) taxes for a combined 63% of general fund tax revenues (on a budgetary basis) typically affords more revenue stability than other states that rely on personal income tax revenues. Projected fiscal 2016 year-over-year growth in retail sales tax and business and occupation tax revenue is strong at 4% and 7%, respectively, although legislative changes in the 2015-2017 biennium session contribute in part to the business and occupation tax forecast. Although employment, personal income, housing, and GDP trends remain positive, the slowing global economy and a strong dollar's effect on exports remain mitigating risks to Washington's revenue forecast.

Despite higher revenue trends, expenditure costs have also increased more than expected since the enacted budget. In December 2015, Governor Inslee released his 2016 proposed supplemental budget that includes more than $500 million in additional expenditures since the enacted biennium budget, or a small 1.4% of total general fund expenditures through fiscal 2017. Higher-than-expected costs include those related to severe wildfires ($178 million), as well as rising Medicaid and health care costs, such as increasing pharmaceutical expenses ($180 million), human service program ($63 million) caseloads, and corrections ($23 million). Higher proposed expenditures also include more spending on mental health services ($137 million). In addition, the governor has introduced legislation to raise teacher salaries, which he proposes will be funded through the elimination of certain tax exemptions. The proposed 2015-2017 general fund two-year budget totals $37.9 billion, compared with the enacted $37.5 billion after incorporating assumed reversions of almost $173 million.

The supplemental budget proposes using $178 million from the budget stabilization account (BSA) to cover emergency fire costs, for an estimated ending balance of $714 million at the close of the biennium, compared with $894 million in the enacted budget. Based on the proposal, the projected general balance combined with the BSA would total $961 million, or 2.5% of biennium expenditures, which we view as adequate. On an annualized basis, which is more comparable to other states, the ending biennium balance, as proposed, would equate to a good 5.0% of expenditures budgeted for the year, although this is lower than the previously projected 7.2% of annualized expenditures. Fiscal 2015 combined balances were about $1.5 billion, or a strong 11.0% of state general fund expenditures, compared with previously estimated 8.5% of annualized spending.

Education funding continues to pose fiscal pressures for the state. The Washington State Supreme Court's 2012 decision (the McCleary ruling) deemed that the state has systematically underfunded its public education system. The 2015-2017 biennium budget made some progress in raising education spending to address a portion of the state's obligations under the McCleary ruling; however, Washington remains in violation of the ruling and there continues to be pressure for education reform to address education inequality. The state supreme court issued an order in August 2015 to fine the state $100,000 per day, paid into a segregated account for basic education until Washington adopts a complete compliance plan to fully fund all elements of basic education by 2018. The governor's 2016 proposed supplemental budget includes $16 million for the fine, or a very small 0.04% of the biennium spending.

Washington's economy has sustained above-average rates of growth with real GDP and employment expanding at 3.0% and 2.8%, respectively, in 2014, outpacing the nation's 2.2% and 1.9%, respectively. The state's November 2015 Economic and Revenue Forecast Council (ERFC) forecasts baseline 2.8% employment growth in 2015, which still exceeds that of the nation but is a hair lower than previous forecasts due to flat construction employment.

Transportation equipment exports declined 1.9% year-over-year through the third quarter of 2015 due to the strong dollar. The ERFC's forecasted 2015 personal income growth is particularly strong at 5.4%, which is relatively consistent with our view, in which we project the state's personal income will grow at 5.1% in 2015 (based on IHS Connect's modeling), which would be considerably faster than what we anticipate for the nation (2.6%). The ERFC projects slightly slower 4.8% personal income growth in 2016 that would still exceed projected national growth rates. The state's personal income has historically increased faster than overall state tax revenue, even after adjusting for various tax-rate changes. The ERFC reports that, from 1998-2014, the average annual growth rate in state tax revenues of 3.5% has lagged that for personal income, which is 4.8%. In our view, the divergence in the growth rates indicates relatively stronger economic activity among the higher value sectors in Washington and partly reflects the fact that the state does not levy a personal income tax.

In general, we consider Washington's approach to financial management strong, as reflected in our financial management assessment and budget management scores. Well-established economic and revenue forecasting and increasingly refined debt management practices and oversight served the state's credit quality well during the recession and its aftermath. Forward-looking state policies facilitate budget practices we view as prudent, including minimal reliance on payment deferrals or other one-time responses to anticipated budget gaps.

For November 2015, the state treasury and treasurer's trust fund's month-end cash balance was $5.3 billion, up somewhat from the $4.4 billion at the same point in December 2014. Investments are conservative, in our view, with an average of 66% of funds invested in U.S. treasuries and agencies in November 2015. In addition to Washington's investment guidelines, state policies require that collateral in repurchase agreements (of which the state currently has none) for U.S. treasury, agency, and money market instruments be priced at 102% of market value. Mortgage-backed repurchase agreements of more than seven days are subject to a higher, 105% requirement.

As of fiscal year-end 2015, the state's gross direct tax-supported debt burden was $19.7 billion in GO and appropriation-backed bonds outstanding but a somewhat lower $18 billion when accounting for self-supported debt. Tax-supported debt was moderately high, in our opinion, at $2,584 per capita (based on the U.S. Census 2014 state population of 7.1 million), 5.4% of total personal income (2014), and 4.4% of state GDP (2014). Debt pay down remains average, in our view, with about 50% of principal outstanding amortized over 10 years. Gross GO and lease appropriation-backed debt service is moderate, in our opinion, at 5.65% of the funds' expenditures from which it pays debt service. However, portions of the state's debt are funded from self-supporting or reimbursable sources. Considering just the general fund, adjusted for these offsetting revenues, we estimate that debt service was 6.6%, moderate in our view. Washington projects that it could issue approximately $530 million in new GO and MVFT GO bonds in February 2016. The state also estimates that it might issue another $730 million in GO and MVFT GO bonds through the fall of 2016.

Long-term state liabilities include those related to the state's pension system and retiree health care. Washington's pension liability profile has improved somewhat as of its fiscal 2015 audited financial statements because of the lower reported net pension liability based on the state's allocation across 11 pension systems. The state adjusted the discount rate applied to its liabilities to 7.8% from 7.9% in the current biennium and the rate is scheduled to decline further to 7.7% in the 2017-2019 biennium. According to the fiscal 2015 comprehensive annual financial report, Washington's share of the net pension liability across 11 pension plans (not including a share of the school employees retirement system liability) totaled $1.53 billion, or $217 per capita (using 2014 U.S. Census population figures), which is low in our view. Relative to total personal income, the state's share of the net pension liability was 0.4%, which is also what we consider very low. The aggregate funded ratio across plans is good, in our view, at more than 90% although funding has historically fallen short of actuarially determined contribution levels. With its biennial budget process, the state legislature appropriates pension contributions every two years. Although contributions have historically been set to equal the required contribution, they frequently fall short of the actuarially determined contribution because they are not adjusted after the budget is adopted.

Other postemployment benefits (OPEB) are funded on a pay-as-you-go basis. The state's OPEBs produce an implicit liability by allowing retired employees to purchase health, life, and vision insurance in the same pool as current employees at a subsidized rate.

Based on the analytic factors we evaluate for states, we have assigned Washington a composite '1.7' on a on a four-point scale whereby '1.0' is the strongest and '4.0' is the weakest.

(For additional information on the state's general credit, see published full report published Sept. 18, 2015, on RatingsDirect.)

Outlook

The outlook is stable, reflecting that the state continues to benefit from above-forecast end-of-biennium revenue trends. Nevertheless, we expect that significant upward pressure on spending originating in legal- and voter-approved mandates will remain a soft point in the state's credit profile. However, legal requirements that Washington enact budgets that not only balance for the current biennium but also project balance through the following biennium help facilitate a structural approach. That, coupled with the state's ongoing discipline vis-à-vis funding its budget reserves should help insulate the state rating from unanticipated economic or revenue weakening. Potential for upward movement would likely entail a more permanent fix to Washington's education funding challenges and, potentially, revenue trends that better keep pace with the state's underlying economic growth rates.

Given that Washington's previous projected budget gap was solved with stronger-than-expected revenues, downside pressure on the state rating would likely have economic origins. Sustained weak demand for key state exports, fueled in part by a strong U.S. dollar, slower-than-expected growth from China, and a sharp falloff in the housing market could all contribute to such a scenario. State policymakers' response to a downside economic scenario--whether it's timely and structurally oriented--would likely dictate any impact on our rating on the state. If lawmakers delayed taking corrective action or relied extensively on one-time solutions to mid-biennium budget gaps, allowing the state's reserve balances to decline precipitously, this could result in downward pressure on the state rating.

Related Criteria And Research

Related Criteria

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
- USPF Criteria: Special Tax Bonds, June 13, 2007
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011

Ratings Detail (As Of January 11, 2016)		
Washington certs of part (Washington St Dept of Gen Admin Tacoma Co-Location Proj) dtd 12/01/1996		
Long Term Rating	AA/Stable	Affirmed
Washington go & motor veh fuel tax ser 1992B AT-7 III-g EE-1 dtd 06/01/92 due 03/01 & 06/01/1993-2012 2017 03/01/2013		
Long Term Rating	AA+/Stable	Affirmed
Washington motor vehicle fuel tax GO bnds ser 2015C due 02/01/2040		
Long Term Rating	AA+/Stable	Affirmed
Washington motor veh fuel tax GO bnds ser 2008D dtd 01/22/2008 due 01/01/2009-2033		
Long Term Rating	AA+/Stable	Affirmed
Washington motor veh fuel tax GO bnds ser 2010B dtd 07/28/2009 due 08/01/2010-2032 2034		
Long Term Rating	AA+/Stable	Affirmed
Washington motor veh fuel tax GO rfdg bnds		
Long Term Rating	AA+/Stable	Affirmed
Washington motor veh fuel tax GO rfdg bnds ser R-2015D due 07/01/2030		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO bnds ser 2008B dtd 09/26/2007 due 07/01/2008-2030 2032		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO bnds (Build America Bnds) taxable ser 2010D dtd 10/22/2009 due 08/01/2020-2024 2029 2039		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO bnds (SR-520 Corridor Program -Toll Rev) ser 2012C dtd 10/31/2011 due 06/01/2017-2033 2041		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO rfdg bnds		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO rfdg bnds ser R-2010C dtd 10/28/2009 due 01/01/2012-2026		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax GO rfdg bnds ser R-2014B dtd 10/24/2013 due 07/01/2014-2021		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh Fuel Tax GO bnds ser 2007D dtd 02/06/2007 due 01/01/2008-2030 2032		
Long Term Rating	AA+/Stable	Affirmed
Washington various purp gen oblig bnds		
Long Term Rating	AA+/Stable	Affirmed

Ratings Detail (As Of January 11, 2016) (cont.)		
Washington various purp GO bnds ser 2006D dtd 02/07/2006 due 01/01/2007-2031		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington var purp GO bnds ser 2007A dtd 08/01/2006 due 07/01/2014-2031		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington var purp GO bnds ser 2007F dtd 05/30/2007 due 07/01/2008-2029 2032		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington var purp GO rfdg bnds ser R-2007A dtd 11/14/06 due 01/01/2007-2026		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington var purp GO rfdg bnds ser R-2015G due 07/01/2032		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO bnds		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO bnds (Motor Vehicle Fuel Tax) ser 2004B dtd 08/06/2003 due 07/01/2004-2028		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO comp int bnds ser 1999S-2 dtd 05/20/1999 due 01/01/2017-2019		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO Mtr Veh Fuel Tx		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO & mtr veh fuel tax rev bnds ser 1993B DD-12 CC-9 dtd 05/01/1993 due 03/01/1994-2010 2018 & 05/01/2005-2010 2018		
Long Term Rating	AA+/Stable	Affirmed
Washington GO & mtr veh fuel tax (MBIA/National)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (wrap of insured) (AMBAC) (ASSURED GTY - SEC MKT)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (wrap of insured) (FGIC & AGM) (SEC MKT)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (Motor Vehicle Fuel Tax)		
Long Term Rating	AA+/Stable	Affirmed
Washington Various purp GO bnds ser 2007C dtd 02/06/2007 due 01/01/2008-2032		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington Washington St Var Purp #2 dtd 2-1-83		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed

Ratings Detail (As Of January 11, 2016) (cont.)		
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
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Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington certs of part rfdg (Dept of Ecology St Office Bldg Proj) ser RE-2003-B		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Washington GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Aberdeen, Washington		
Washington		
Aberdeen (Washington) APPROP		
Long Term Rating	AA/Stable	Affirmed
FYI Properties, Washington		
Washington		
FYI Properties (Washington) APPROP		

Ratings Detail (As Of January 11, 2016) (cont.)		
Long Term Rating	AA/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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