STANDARD & POOR'S
RATINGS SERVICES

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Summary:

Washington; Appropriations; General Obligation

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Credit Profile		
US$364.545 mil motor veh fuel tax GO rfdg bnds ser R-2013B		
Long Term Rating	AA+/Stable	New
US$338.725 mil various purp GO rfdg bnds ser R-2013A		
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 to the state of Washington's:

- $338.7 million various purpose general obligation (GO) refunding bonds, series R-2013A; and
- $364.5 million motor vehicle fuel tax (MVFT) GO refunding bonds, series R-2013B.

At the same time, we affirmed our 'AA+' long-term rating and underlying rating (SPUR) on the state's existing GO and MVFT GO debt. In addition, we affirmed our 'AA/A-1+' rating on the state's variable rate 1996 series A and B GO bonds.

The short-term rating reflects our short-term rating on the bank providing liquidity support to the bonds (Landesbank Hessen-Thueringen Girozentrale). Finally, we also affirmed our 'AA' rating on the state's appropriation-backed debt. The outlook on all long-term and underlying 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 exhibits sensitivity to economic cycles but to a lesser degree than those of states that rely primarily on personal and corporate income taxes;
- Good internal liquidity;
- Strong -- and strengthening -- financial policies and practices, including new 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 new and refunding series of GO bonds. The state's MVFT GO bonds are first payable from state excise taxes on motor vehicle and special fuels. The series R-2013A and R-2013B refunding bonds are being issued to refund certain outstanding GO bonds of the state for debt service savings.

The state will have a total of $18.05 billion of GO bonds outstanding after the current offering. Of this, $7.0 billion of the state's GO debt is payable first from state excise taxes on motor vehicle and special fuels. The state also has $568 million of certificate of participation (COP), appropriation-backed debt outstanding. Of this, $77.8 million is GO debt of various local agencies within the state and is a contingent obligation of the state government in the event of nonpayment by a local government agency.

An important element in our rating and outlook for the state is the way it has and continues to respond to fiscal imbalances, responses that are evaluated in our financial management assessment (FMA) and budget management scores. For its 2011-2013 biennial budget of $31.7 billion, the state confronted a $4.9 billion deficit. During the 2011 session, the legislature enacted $4.5 billion of ongoing fiscal adjustments. Still, in the midst of a weakened economy, the new budget fell out of balance and, by the fall of 2011, entailed a new, $1.9 billion shortfall. The legislature adopted measures fixing around $480 million of the gap in a special session in December 2011. Political and policy differences emerged during the regular legislative session that began in January, and the legislature was unable to reach agreement on the balance of the needed solutions. A key policy difference among legislators in the regular and two subsequent consecutive special sessions, lasting 30 days and one day, respectively, was whether and to what extent the budget solutions should include payment deferrals as part of the gap-closing effort for the fiscal 2011-2013 biennium. State fiscal pressure eased somewhat naturally due to a relatively small upward revision to the biennial revenue forecast of $96 million and a downward revision to the state's caseloads (mostly in Medicaid), saving $300 million. To eliminate the remaining approximately $1 billion deficit, the state legislature agreed to $475 million in other spending reductions, including $127 million to the Temporary Assistance for Needy Families (welfare) program. The state also adopted some nonrecurring measures to restore balance to the biennial budget. Most notable was the reduction of its working capital requirement, which freed up $238 million of funds on a one-time basis. The change reflects modernization of the state's cash management practices that allows the state general fund to retain for a longer period of time some sales and use tax receipts ultimately destined for local agencies. However, unlike some initial policy proposals that the legislature considered, the state did not defer state aid to school districts or pension contributions, both of which were funded at regular levels in the state budget.

Although the state ended fiscal year 2012 in a negative position on a budgetary basis, the result of the legislative session and the most current revenue forecasts suggest it may end fiscal year 2013 with a positive $289 million total reserve. This comprises $266 million in the state's budget stabilization account and a $23 million unrestricted ending fund balance. On a combined basis, the budget reserves are, thus, expected to equal a low 1.3% of fiscal year 2013 general fund expenditures. The balance could be somewhat higher, by up to $55 million, due to a recent downward revision to state caseloads, mostly in the Medicaid program. Partially offsetting this, however, could be a recent court decision against the state's ability to levy a tax on certain tobacco products. Depending on the final outcome, the ruling could reduce the state's ending balance by $28 million, still leaving the state with a $50 million ending unrestricted fund balance. Regardless, we view the state's ending reserve as low relative to its general fund budget.

If the state Supreme Court finds in favor of the state in the tobacco case, however, we believe there could be favorable fiscal implications. In effect, such a ruling would imply that the initiative requiring a two-thirds vote of the legislature (pursuant to Initiative 1053) to raise taxes is unconstitutional. We may consider revising upward our score of the state's governmental framework if the state were able to adjust tax rates with a simple majority legislative vote.

Other notable changes in the 2012 legislative session include a new statute requiring the legislature to balance its budget, not only in each biennium, but also for the two year period subsequent to the biennium. The basis of revenues for the longer-term forecast will continue to be a product of the state's independent Economic and Revenue Forecast Council, which will add the state treasurer as a voting member of the seven member council. In addition, the state legislature repealed Initiative 728, passed by voters in 1999, which provided funding for reduced class sizes in the state's public education system. It had already been suspended for the current biennium, saving $861 million, but its repeal removes $900 million of expense for the 2013-2015 biennium and forward. Also, the legislature approved putting a constitutional amendment related to the state debt limit before the voters in November 2012. The amendment would lower the limit on the state's annual debt service to 8% of a six-year moving average of general fund revenue from 9% of a three-year moving average. Finally, in 2012 the legislature approved reducing early retirement benefits for newly hired employees in three state pension plans and began phasing in a reduction of the assumed rate of return for its pensions.

As of its June forecast, the state's Economic and Revenue Forecast Council continues to anticipate a slow economic recovery and notes that material downside risks remain. The state's forecast for the U.S. economy is premised on that of the Blue Chip Consensus and, at 2.3% and 2.5% for 2012 and 2013, respectively, is somewhat more optimistic than Standard & Poor's forecast for U.S. economic growth of 2.0% and 2.1% for the same years. Most negative influences on the state's forecast relate to macroeconomic risk, such as the European sovereign debt crisis and a tightening of federal fiscal policy that is currently scheduled to take effect in January 2013. Washington state's economy, nonetheless, remains well-poised for recovery albeit at a slower pace than in recoveries from previous recessions. Total employment in Washington is expected to match the nation's growth rate in 2012, at 1.4%, before outpacing it in 2013 at 1.6% versus 1.3% for the U.S. Washington's real state gross domestic product has increased at an average (compound average annual growth) annual rate of 1.7% versus the nation's 1.4% since 2000. The forecast for real state GDP growth is 2.1% in 2012 and 2.16% in 2013. Strong performance in the high wage industries of aerospace and high technology suggest continued increases in total state personal income, which the state forecasts will grow by 1.5% in 2012 and 3.0% in 2013. These stronger parts of the economy are offset by flat performance in the state and local government and construction sectors.

Despite a cautious forecast, the state's actual general fund revenue experience during June came in at a solid 5.5% ($66.5 million) above the state's expectations. Following the June collections, however, the revenue forecast council underscored that revenue variability can be high on a monthly basis. Thus, it is too soon to determine if the recent collections represent the beginning of a trend or will be reversed in subsequent months.

As in other states, the housing sector has been a source of drag on the state's economy. Home construction troughed in 2009 and, according to the state's economist, is unlikely to rebound until home prices recover. Home prices in the Seattle metropolitan area increased 2.0% in April, according to the Standard & Poor's/Case-Shiller home price index; on a year-over-year basis, prices were down 1.0%, which is a marked improvement compared with several months ago and better than the 10- and 20-city national indices, which were down 2.2% and 1.9%, respectively. As they had forecasted in January 2012, downward pressure on the real estate market appears to be dissipating as there is a trend toward fewer newly delinquent mortgages in the state.

Washington's financial liquidity remains adequate despite its negative $467 million general fund cash balance at the end of June 2012. This is lower than the negative $70 million at the end of June 2011. The weaker general fund cash reflects that in September 2011, the state revenue forecast was reduced by $1.4 billion, with around $500 million of the deterioration anticipated to occur in fiscal year 2012, and the balance attributed to fiscal year 2013. The state has access to cash for liquidity in its treasury and treasury trust funds, the former of which is subject to legislative appropriation. This cash is held in the custody of and invested on a comingled basis by the state treasurer. As a result of its good access to internal liquidity, the state does not rely on external borrowing for cash flow management. As such, we continue to view the state's internal liquidity sources as sufficient to support its general fund budget operations.

For June 2012, the treasury and treasurer's trust fund's average cash balance was $4.34 billion, which is above the $3.54 billion balance at the same time in 2011. Investments are conservative in our view, with 53% of funds invested in U.S. Treasurys and agencies. Repurchase agreements, which are subject to a maximum term of 180 days, represent 28% of investments. In addition to the state's investment guidelines, state policies require that collateral in repurchase agreements 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.

Subsequent to the currently planned issuance, the state's direct tax supported debt burden (GO and appropriation-backed) is moderately high, in our opinion, at $2,776 per capita (based on U.S. Census 2011 state population), 6.3% of total personal income, and 5.3% of gross state product (GSP). Gross GO and lease appropriation backed debt service is moderate, at 4.5% of general government-wide (all funds) spending in fiscal year 2011 (audited). Gross GO and COP debt service as a portion of general fund expenditures is equal to 6.6% of fiscal year 2012 expenditures. Portions of the state's debt are funded from self-supporting or reimbursable sources, however. When adjusting for these offsetting revenues, we estimate that debt service is 4.36% of general fund expenditures, moderate in our view. We anticipate that continuing transportation needs, including two major urban highway projects, will likely translate into continuing GO issuance in the next two to three years. The state currently projects that it may issue up to approximately $502 million and $574 million in new GO and MVFT GO bonds, respectively, in early 2013. The state also estimates that it may issue around $300 million of additional GARVEE bonds in the spring of 2013 to finance a portion of its State Route-520 transportation projects.

Unlike 22 other states in the U.S., Washington maintains a positive balance in its unemployment insurance fund of $2.5 billion as of March 2012, sufficient to fund benefits for an estimated 13 months.

Based on the analytic factors we evaluate for states, on a scale of 1 (strongest) to 4, we have assigned Washington a composite score of '1.8'.

Outlook

The stable outlook reflects our view that the state's financial management is strong, as demonstrated by its continued willingness to make timely and proactive budget amendments as it deems necessary to maintain budgetary balance. The state's automatic budget stabilization fund deposits serve its credit well when the economy -- and revenues -- take a negative turn. At present, the state's reserves are low and, absent additional budget corrections, could deteriorate further despite its practice of making regular reserve contributions -- a reflection, we believe, of the halting economic recovery. The low reserves limit the state's rating from moving upward and, in fact, render its rating vulnerable to downward movement if revenues deteriorate further without very timely corrective budget action.

Related Criteria And Research

- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

Ratings Detail (As Of July 30, 2012)		
Washington adj rate GO bnds ser VR-96A&B due 06/01/2020		
Long Term Rating	AA+/A-1+/Stable	Affirmed
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 motor veh fuel tax GO rfdg bnds		
Long Term Rating	AA+/Stable	Affirmed
Washington mtr veh fuel tax go bnds ser 2004C dtd 08/06/2003 due 06/01/2009-2030		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington various purp gen oblig bnds		
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 Mtr Veh Fuel Tx		
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 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) spl rfdg rev bnds (Stafford Creek Corrections Ctr) ser 2009		
Long Term Rating	AA/Stable	Affirmed

Ratings Detail (As Of July 30, 2012) (cont.)		
FYI Properties, Washington		
Washington		
FYI Properties (Washington) Lease rev bnds (State Of Washington Dis Proj) ser 2009		
Long Term Rating	AA/Stable	Affirmed

Many issues are enhanced by bond insurance.

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