

RatingsDirect®

Summary:

State of Washington; Appropriations; General Obligation

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Credit Profile

US\$457.86 mil various purp GO bnds ser 2020A due 08/01/2044		
<i>Long Term Rating</i>	AA+/Stable	New
US\$222.5 mil motor veh fuel tax & veh related fees GO bnds ser 2020B due 06/01/2044		
<i>Long Term Rating</i>	AA+/Stable	New
US\$91.785 mil GO rfdg bnds ser R-2020A due 01/01/2026		
<i>Long Term Rating</i>	AA+/Stable	New
US\$53.065 mil motor veh fuel tax ser R-2020B due 01/01/2026		
<i>Long Term Rating</i>	AA+/Stable	New
US\$38.435 mil GO bnds ser 2020T due 08/01/2023		
<i>Long Term Rating</i>	AA+/Stable	New
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to the State of Washington's:

- Series 2020A various purpose general obligation (GO) bonds;
- Series 2020B motor vehicle fuel tax and vehicle related fees GO bonds;
- Series 2020T GO bonds;
- Series R-2020A various purpose GO refunding bonds; and
- Series R-2020B motor vehicle fuel tax GO refunding bonds.

At the same time, S&P Global Ratings affirmed its 'AA+' long-term and underlying ratings on Washington's GO and motor vehicle fuel tax GO debt outstanding.

Finally, we affirmed our 'AA' rating on the state's appropriation-backed debt outstanding based on the application of our "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" criteria (published Jan. 22, 2018). We rate these appropriation-backed debt obligations one notch lower than our rating on the state based on our view of Washington's general creditworthiness and to reflect the service contract and lease payments appropriated by the state legislature for the bonds. We view these bonds as having a strong relationship to the obligor since they provide funding for projects we believe are significantly important to Washington. In our opinion, there is no unusual political, timing, or administrative risk related to the debt payment.

The outlook on all ratings is stable.

Our rating on the state's GO bonds reflects its full faith, credit, and taxing powers. The motor vehicle fuel tax GO bonds are also secured by motor vehicle fuel taxes.

The ratings reflect our view of Washington's:

- Relatively well-educated workforce and good income indicators;
- Good recent economic growth relative to that of the nation and a sales tax-based revenue structure that has demonstrated less sensitivity to economic cycles than income tax-reliant states;
- High cost of housing, especially in key economic centers that could impede long-term growth prospects, although officials have begun to forecast a cool down in the housing sector throughout the next five years as the state's economy is projected to moderate;
- 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, which is key given increasing expenditure pressures; and
- Moderately high debt burden across several measures, but relatively low unfunded pension and other postemployment benefit (OPEB) liability.

Washington's credit profile has benefited from a state economy that has been among the strongest performing in the nation in recent years. This economic strength has often translated into better-than-forecast revenue growth. While Washington's revenues have historically exhibited less cyclical than others (due in part to the lack of a personal income tax), the economy is somewhat concentrated, in our view. Exports comprise over 15% of gross state product (GSP), creating a unique sensitivity to international trade activity and policy. Specifically, we expect trade tariff discussions with China (Washington's top export destination) to continue to affect state exports. Concentration also stems from the importance of Seattle (over 60% of the state's jobs are located within the metro area) and the presence of three large corporations (employing over 160,000 in total) whose decisions and performance have far-reaching economic implications for the state. The state's economic and revenue forecasting practices are well established and in tune with worldwide economic activity, in our view. Both IHS Markit and the state expect Washington's economy will moderate over the next five years. An active voter initiative process which has reduced the state's revenue and spending autonomy over the years, although it is possible for the legislature to amend or repeal an initiative. The McCleary decision, which has since been resolved, pressured state spending over multiple biennia by requiring higher state funding for kindergarten to grade 12 (K-12) school districts. While unfunded retirement liabilities are relatively low, we expect the state's debt levels to remain moderately high given anticipated future issuance.

Several of the nation's largest companies are headquartered or operate in Washington, including The Boeing Co. The state estimates that Boeing is their largest employer as of June 2018, employing 65,000 state residents full time. In March 2019, aviation regulators and airlines across the globe grounded Boeing's 737 MAX fleet in response to two accidents involving the model. The primary assembly plant for the grounded planes is in Renton, Wash.; the factory employs about 12,000 workers. Following the grounding, Boeing is reportedly considering production cuts or

suspension of production altogether, likely dependent on how long the aircraft remains grounded. Washington's exports in second-quarter 2019 dropped by a substantial 27.6% compared to second-quarter 2018. The state reports the decrease is primarily due to a 41.9% drop in transportation equipment exports, mostly Boeing planes; the company suspended deliveries of the 737 MAX model in March. While we believe the decline in exports is evidence of the state's exposure to international trade, we do not expect these developments to affect Washington's credit profile at this present, given our opinion, based on currently available information, that the issue is a short-term disruption. The state has not yet forecast the potential related job loss and officials report they are monitoring developments as they occur.

Washington's enacted budget for the 2019-2021 biennium maintains McCleary funding and allocates approximately 52% of expenditures for K-12 schools. Overall, the budget totals \$52.1 billion for the state general fund, education legacy trust account, and opportunity pathways account. The budget significantly increases both revenues and expenditures, in our view, with sources 13.1% and expenditures 16.7% above levels enacted for the state's 2017-2019 biennium budget. Spending priorities for items other than education include initiatives for behavioral health and state employee compensation changes (including higher education). Other notable legislation passed during the session include the establishment of a graduated real estate excise tax (a \$244.5 million increase to current biennium revenue), facilitating the collection of new sales tax revenues following *South Dakota v. Wayfair Inc.* (a \$115.9 million increase to current biennium revenue), and an additional business and occupation tax on certain financial institutions (a \$133.2 million increase to current biennium revenue).

While the state's reliance on retail sales tax, and business and occupation taxes typically affords Washington more revenue stability than other states that rely on personal income tax revenues, economic cyclicity could pressure 2019-2021 general fund revenue. The Economic Revenue and Forecast Council's (ERFC) pessimistic economic scenario in the June 2019 forecast reflects 4.6% lower general fund revenue than currently estimated for the next biennium due to downside risks from international trade concerns, geopolitical risks, and a maturing economic expansion.

Furthermore, S&P Global Ratings expects the pace of economic growth for states and local governments to slow for the rest of 2019. For more information, please see "Credit Conditions: U.S. State And Local Governments Will Need To Keep Their Hands On The Wheel," published July 31, 2019, on RatingsDirect.

Washington does not levy a personal income tax and is one of nine states that does not currently impose a capital gains tax. Together, retail sales, and business and occupation taxes, account for a combined 71% of general fund tax revenues in fiscal 2018 and typically afford more revenue stability than other states, many of which rely on personal income tax revenues. We believe Washington's economy has gradually become more service-oriented over time; however, the goods and services subject to the state's retail sales and use taxes have not evolved alongside this shift. Nevertheless, legislation passed in the 2019 session makes it easier for the state to collect certain sales taxes following the Supreme Court decision in *South Dakota v. Wayfair Inc.* In addition, we have observed that capital gains-related tax revenues are among the most cyclical and difficult to forecast revenues in numerous other states. In our view, how a state manages through this volatility is an important credit factor. Previous attempts to implement a capital gains tax were included in the governor's 2019-2021 biennium, 2015-2017 biennium budget proposal and the house's 2018

supplemental budget.

Washington's economy is among the highest performing in the country: In 2018, real GDP growth outpaced every state in the nation at 5.7% and was 1.4% above the state with the second-highest growth (Utah at 4.3%). Washington is the fourth-largest exporter in the country with a large presence in transportation exports. Specifically, more than 55% of the state's exports are transportation equipment (valued at approximately \$42.8 billion). IHS Markit reports that despite Washington's exports as a percentage of GSP dropping to 15.3%, this remains the third-highest proportion in the country behind Louisiana and Texas. Other large employers such as Microsoft Inc. and Amazon continue to support the state's low unemployment rate (4.6% as of July 2019) and high per capita incomes (113 in 2018% of the national average). However, as we discussed in "Credit Conditions: U.S. State And Local Governments Will Need To Keep Their Hands On The Wheel" (July 31, 2019), the region faces challenges in housing affordability and trade. As of the June 2019 ERFC, officials forecast a 2.4% reduction in housing permits over the next five years. Management reports this decline mostly reflects a slowdown in multifamily housing permits for which construction has boomed in recent years. Washington's economy could be particularly vulnerable to escalating trade tensions. The state remains an important gateway for trade with Asia and Canada, and ranks fourth in the nation in annual export value and first in export value per capita. The state's ERFC, in its June 2019 revenue forecast, projects slower growth in Washington's major export markets including China, South Korea, Canada, and Japan.

The state's strong economy has translated into better-than-forecast revenue growth. For the two months from June 11, through Aug. 10, 2019, revenues were tracking \$108 million (3.1%) above the latest quarterly forecast from June. We expect the next quarterly revenue forecast to be submitted to the governor and legislature in late September 2019.

Three initiatives will appear on the ballot in Washington in November 2019. Initiative 976 would limit certain motor vehicle taxes and fees. Officials expect that if the measure is passed it would have no impact on support for transportation debt issued before the creation of the state's Connecting Washington program due to the composition of pledged revenues and only a minor impact on debt issued thereafter. Other measures on the ballot concerning affirmative action policies and succession of public offices in the event of a catastrophic incident are expected to have minimal fiscal impact.

In general, we consider Washington's approach to financial management strong, as reflected in our Financial Management Assessment (FMA) 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.

As of Aug. 30, 2019, Washington is expected to have about \$19.4 billion in GO bonds outstanding. Of this, about \$6.1 billion of the state's net GO debt is payable first from excise taxes on motor vehicles and special fuels. The state is also expected to have about \$870 million of certificates of participation (COPs) outstanding including COPs for state and local agencies. Tax-supported debt was moderately high, in our opinion, at about \$2,512 per capita and 4.1% of total personal income at the end of fiscal 2018. Debt paydown remained average, in our view, with about 56% of principal outstanding amortized over 10 years. We expect debt levels to remain moderately high given anticipated future issuance, particularly for Washington's transportation capital program.

Long-term liabilities include those related to the state's pension system and retiree health care. Based on June 30, 2018, comprehensive annual financial reports for the cost-sharing plans, we calculate Washington's share of the net pension liability across 12 pension plans (not including a share of the school employees retirement system liability) totaled about \$1.3 billion as of June 30, 2018, or about \$168 per capita and 0.3% of personal income, which is very low, in our view. The aggregate funded ratio across plans, including cost-sharing plans in which the state participates as of June 30, 2018, is what we consider good at almost 89%. We note the plan adopted a 7.5% rate of return assumption in fiscal 2017, down from 7.7%, which is more conservative. We understand the assumed rate of rate could be reduced further following a preliminary recommendation from the state actuary to drop the assumption to 7.4% from 7.5%. A determination is expected by Oct. 31, 2019.

We consider Washington's unfunded OPEB liability, representing about \$773 per capita, below average. OPEBs are funded on a pay-as-you-go basis.

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

Outlook

The stable outlook reflects our view of Washington's ability to maintain a strong financial position throughout changes in the business cycle. In addition, the state's legal requirements to enact budgets that are not only balanced for the current biennium but subsequent biennia help provide a sustainable framework to facilitate structural balance throughout economic cycles.

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. Coupled with Washington's ongoing discipline vis-a-vis funding the state's budget reserves, should help insulate the state rating from unexpected economic or revenue weakening within the outlook period. Potential for upward movement would likely entail moderation of growth in debt levels and sustainable growth in revenue that keeps pace with the state's underlying economic growth rates and mandated costs originating voter-approved mandates that limit the state's budgetary flexibility to a degree.

Downside pressure on the state rating would likely have economic origins. A sharp falloff in the housing market or sustained weak demand for key state exports, fueled in part by a strong U.S. dollar, changes in trade policy, or slower-than-expected growth from China, 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 effect on our rating on Washington. If lawmakers delayed taking corrective action or relied extensively on one-time solutions to budget gaps, allowing the state's reserve balances to decline precipitously, this could result in downward pressure on the rating.

Ratings Detail (As Of August 28, 2019)

Ratings Detail (As Of August 28, 2019) (cont.)

State of Washington motor vehicle fuel tax GO bnds		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor vehicle fuel tax GO bnds ser 2018B due 08/01/2042		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor vehicle fuel tax GO rfdg bnds ser R-2016C dtd 02/16/2016 due 07/01/2016 2019-2033		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor vehicle fuel tax GO rfdg bnds ser R-2017B due 07/01/2034		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor vehicle fuel tax GO rfdg bnds ser R-2018B due 08/01/2023		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax go bnds ser 2016B dtd 09/20/2016 due 08/01/2017-2041		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax go bnds (SR 520 Corridor Prog-toll Rev) ser 2016C dtd 09/20/2016 due 06/01/2017-2041		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax GO bnds		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax GO bnds (Competitive & Negotiated Sale) ser 2012B-1&2 dtd 08/03/2011 due 08/01/2012-2041		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax GO rfdg bnds ser R-2011C dtd 09/28/2010 due 01/01/2011 & 07/01/2012-2027		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington motor veh fuel tax GO rfdg bnds ser R-2015B due 07/01/2026		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr vehicle fuel tax GO bnds ser 2017E dtd 01/24/2017 due 02/01/2018-2042		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO bnds ser 2009F dtd 04/21/2009 due 02/01/2010-2030 2034		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO bnds ser 2012E due 02/01/2042		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO bnds ser 2013E dtd 02/05/2013 due 02/01/2014-2039 2043		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO bnds ser 2014B dtd 08/21/2013 due 08/01/2038		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO bnds ser 2016B dtd 10/08/2015 due 08/01/2016-2040		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO rfdg bnds ser R-2017D dtd 01/24/2017 due 08/01/2017-2025		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington mtr veh fuel tax GO rfdg bnds ser R-2012-B dtd 11/09/2011 due 01/01/2012 & 07/01/2014-2024		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

Ratings Detail (As Of August 28, 2019) (cont.)

State of Washington var purp go bnds & mtr veh fuel tax (ferry vessel) dtd 06/01/1991 due 06/01/1992		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington GO bnds (Motor Vehicle Fuel Tax) ser 2009B dtd 07/23/2008 due 07/01/2009-2033		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington GO bnds (Motor Vehicle Fuel Tax) ser 2009D dtd 01/22/2009 due 02/01/2010-2034		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
State of Washington Motor Vehicle Fuel Tax GO bnds (Taxable BABs) ser 2010F dtd 06/01/2010 due 08/01/2015-2024 2031 2033 2040		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

Ratings Detail (As Of August 28, 2019) (cont.)

Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
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<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		

Ratings Detail (As Of August 28, 2019) (cont.)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
FYI Properties, Washington		
State of Washington, Washington		
FYI Properties (State of Washington) lse rev rfdg bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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