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Ratings

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Summary:

State of Washington; Appropriations; General Obligation

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Credit Profile		
US$573.625 mil var purpose GO bnds ser 2021A dtd 07/29/2020 due 08/01/2045		
Long Term Rating	AA+/Stable	New
US$119.57 mil MVFT/VRF GO bnds ser 2021B dtd 07/29/2020 due 06/01/2045		
Long Term Rating	AA+/Stable	New
US$36.56 mil GO bnds (taxable) ser 2021T dtd 07/29/2020 due 08/01/2023		
Long Term Rating	AA+/Stable	New
Washington GO		
Long Term Rating	AA+/Stable	Affirmed

Rating Action

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

- Series 2021A various purpose general obligation (GO) bonds;
- Series 2021B motor vehicle fuel tax and vehicle-related fees GO bonds; and
- Series 2021T (taxable) GO 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, and its 'AA' rating on the state's appropriation-backed debt outstanding. We rate these appropriation-backed debt obligations one notch lower than our rating on the state to reflect the service contract and lease payments appropriated by the state legislature for the bonds.

The outlook on all ratings is stable.

Our rating on the state's GO bonds reflects Washington's full faith, credit, and taxing powers. The motor vehicle fuel tax GO bonds are also secured and expected to be paid by motor vehicle fuel taxes. The motor vehicle fuel tax and vehicle-related fees GO bonds are also secured by, and expected to be paid from, motor vehicle fuel taxes and vehicle-related fees. The triple-pledge motor vehicle fuel tax GO bonds are additionally secured by and expected to be paid from certain toll revenues.

Credit overview

Heading into the COVID-19-pandemic-induced recession, Washington's credit profile benefited from an economy that had been among the strongest performing in the nation, often translating into better-than-forecast revenue growth. Although we expect revenue collections to materially deteriorate over the course of the pandemic compared to recent years, we believe Washington's strong fiscal management practices will help the state navigate through the recession.

We view the state's revenue forecasting practices as strong and note Washington has a history of making budget adjustments based on material changes to forecast. We expect that the importance of exports to the state's economy and the uncertainty plaguing Washington State's largest employer, The Boeing Co., could weigh on a meaningful recovery. In addition, we anticipate the debt profile will remain relatively high but relatively manageable given the state's comparatively low pension and other postemployment benefit (OPEB) liabilities.

Specifically, Washington's fiscal 2020 revenue collections through June 10, 2020, are below forecast by $452 million (5.6%) when adjusting for a large refund and deferred payments, which we view as comparable to that of many state peers. The state is anticipating a total near general fund ending fund balance of $893 million (3.5% of near general fund expenditures) for fiscal 2020 on a budgeted generally accepted accounting principles basis and a $3.372 billion (12.4% of near general fund expenditures) shortfall for fiscal 2021. While we understand a special session could be called for additional budget updates following the June 17, 2020, forecast update, it is unclear at present how Washington intends to resolve the budget gap. We expect the state's strong fiscal management will persist in the current recession. In addition to the state's history of making midbiennium budget updates based on updated economic and revenue forecasting, Washington convenes a Caseload Forecast Council that provides insight into expenditures by forecasting for various service requirements (such as public assistance, state corrections, medical assistance, and kindergarten to grade 12 education) three times per year. The executive and legislative branches use these forecasts, along with historical expenditures, to formulate midbiennium revisions.

The state has taken action to help limit the effects of the COVID-19 outbreak after becoming the first state in the U.S. to report a confirmed case of the coronavirus in January. In the subsequent weeks, the governor elevated the state's response to the outbreak by declaring a state of emergency on Feb. 29, 2020, and issuing a stay-at-home order effective March 23, 2020. Currently, Washington is in the process of implementing a four-phased approach to reopening economic activity. We expect restricted economic activities resulting from the pandemic will translate directly into contracted economic output and general revenue declines. S&P Global Economics forecasts that the resulting economic toll will be substantial globally (see "U.S. Faces A Longer And Slower Climb From The Bottom," published June 25, 2020, on RatingsDirect) with full year gross domestic product (GDP) contracting 5.0% for the U.S. Washington's Economic and Revenue Forecast Council (ERFC) predicts U.S. GDP will decline 6.1% for 2020 and acknowledges downside risk to the forecast include a second spike of coronavirus infections and depressed consumer confidence after business reopenings.

Management reports that the cash balance of the state treasury and treasurer's trust funds was $9.3 billion as of May 31, 2020, which we consider a strong 17.5% of near general fund expenditures enacted for the fiscal 2019-2021 biennium. The funds' average daily balance has significantly increased in recent years, but management reports that balances have varied widely, generally ranging from $3.0 billion-$8.5 billion.

In addition, the state's reserve levels are at what we consider good. The budget stabilization account (BSA) is currently forecast to total $1.693 billion for fiscal 2020 (6.6% of annual enacted fiscal 2020 expenditures) and $1.963 billion for fiscal 2021 (7.2% of annual enacted fiscal 2021 expenditures). Legislation passed on March 17, 2020, provided initial funding for the COVID-19 pandemic response and included appropriating $200 million from the BSA for disaster response and unemployment.

The ratings reflects our view of Washington's:

- Sales tax-based revenue structure that has demonstrated less sensitivity to economic cycles compared with income tax-reliant states;
- 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;
- High cost of housing, especially in key economic centers that could impede long-term growth prospects; and
- Moderately high debt burden across several measures, but relatively low unfunded pension and OPEB liability.

The stable outlook reflects our view of Washington's ability to maintain a strong financial position throughout changes in the business cycle, which we expect will persist through the pandemic-induced recession. We believe the state's strong budgetary management and forecasting practices, along with its good reserve profile, will help insulate the state rating from pandemic-related revenue deterioration and budgetary pressures.

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. While we expect that significant upward pressure on spending originating in legal- and voter-approved mandates over time will remain a soft point in the state's credit profile, we believe Washington's ability to enact budgets that not only balance for the current biennium but also project balance through the following biennium helps facilitate a structural approach.

Environmental, social, and governance factors

Absent the implications of COVID-19, we view Washington's social and governance risks as being in line with our view of the sector as a whole. We view the risks posed by the pandemic to public health and safety as a social risk that, if sustained, could weaken the state's economy, liquidity, and budget performance.

In our opinion, Washington's environmental risks are somewhat elevated given the state's exposure to rising sea levels along its vast coastline. Much of the state's economic activity takes place in the Puget Sound region, which includes Seattle, Olympia, Tacoma, and Bremerton. Specifically, IHS Markit estimates half of the state's population and jobs are based in the area. Washington reports it has begun preparing for a changing climate by integrating consideration of such changes into decision making; multiple state agencies have been tasked with studying the impacts of climate change on their areas of focus and the ERFC prepares a climate study on an annual basis.

Stable Outlook

Downward scenario

We believe the COVID-19 pandemic will pose severe stresses to Washington's economy, especially given the state's exposure to international trade activity and relations. Additional budgetary pressure could arise over the medium term if maintenance of various voter-approved spending initiatives (such as increases to education funding following the resolution of the McCleary decision) diminished the state's budgetary flexibility or if various emergency federal funding (for example, enhanced Medicaid matching) were to end abruptly. State policymakers' response--whether it's timely and structurally oriented--will likely dictate any effect on our rating on Washington. We could lower the rating if lawmakers delayed taking corrective action in addressing revenue shortfalls or relied extensively on one-time solutions to remediate budget gaps. We could also lower the rating if Washington's reserve balances were to decline precipitously and the state lacked sufficient plans for timely replenishment.

Upward scenario

While unlikely based on current economic conditions and forecasts, we could raise the rating if growth in Washington's debt levels were to moderate alongside sustainable growth in revenue that keeps pace with both the state's underlying economic growth rates and mandated costs originating voter-approved mandates that, to a degree, limit the state's budgetary flexibility.

Credit Opinion

Updated forecasting projects severe revenue declines through the fiscal 2021-2023 biennium

Washington's most recent forecasting has lowered the state's revenue estimates substantially compared with its previous forecast conducted in February 2020 (that did not yet incorporate the effects of the pandemic). The ERFC's projections for the near general fund (general fund-state, education legacy trust account, and opportunity pathways account) as of June 17, 2020, lowered expected collections by $4.5 billion (8.6%) for the fiscal 2019-2021 biennium and $4.3 billion (7.7%) for the fiscal 2021-2023 biennium. The council notes this baseline forecast includes a substantial level of uncertainty; an alternative optimistic scenario incorporates low infection numbers and additional federal stimulus while an alternative pessimistic scenario includes a second spike in infections and depressed consumer confidence after business reopenings.

Reported collections as of June 10, 2020, underperformed the council's February forecast by $464.8 million (14.8%) for the month and $893.3 million (11.1%) for the fiscal year-to-date. The council reports that about half of the monthly shortfall was due to deferrals of property tax payments that were granted by several large counties. The payments are expected to be collected before the end of June. Historically, the state's revenue collections have exhibited less cyclicality than that of its peers due in part to the lack of a personal income tax.

The forecast notes Washington's employment declined by an unprecedented level in April--with the steepest job loss in the private services sector--before rebounding slightly in May. Currently, the state's unemployment rate is 15.1% and ranks 42nd in the country, according to the U.S. Bureau of Labor Statistics May 2020 reporting. Management reports that as of June 24, 2020, the state's unemployment insurance trust fund balance was $2.87 billion and approximately equal to 9.2 months of benefits under current economic conditions. The Employment Security Department expects to update projections to incorporate the ERFC's June 17, 2020, forecast; the state is required to have three-months' worth of the fund balance in the account and would likely seek a loan from the federal government if that threshold was not met.

We expect that the state will remain committed to timely budget adjustments as it has in years past. Currently, Washington is operating off a supplemental operating budget for the 2019-2021 biennium that was adopted in March 2020. It increased appropriations by $805 million to bring total biennium spending to $53.3 billion. However, the governor issued several line-item vetoes of new appropriations that reduce spending through the next biennium. Specifically, the fiscal 2020 supplemental operating budget was reduced by $235 million (0.4%) for the fiscal 2019-2021 biennium and by an additional $210 million for the 2021-2023 biennium. We understand a special session could be called again for further budget updates. Washington's constitution allows a special session to be convened by either a proclamation from the governor or by resolution of the legislature on a two-thirds affirmative vote in each house of elected members.

Increased Medicaid costs spurred by enrollment uptick tempered by additional federal funding

While Washington has already experienced a substantial increase in enrollment during the COVID-19 pandemic, the federal government's temporarily increased funding for state Medicaid expenses is expected to help manage these additional costs. The Families First Coronavirus Response Act increases the state's base reimbursement of its Federal Medical Assistance Percentage (FMAP) for Medicaid by 6.2 percentage points every quarter that the federal national emergency declaration remains in place (beginning March 13). State officials preliminarily estimate the FMAP increase will generate about $131 million per quarter of additional funding to Washington.

Federal aid provides some relief to state budgets

Outside of the changes to FMAP reimbursement, the federal government has taken additional measures to address the economic and fiscal effects of the COVID-19 pandemic. The U.S. federal government approved the Coronavirus Aid Relief and Economic Security Act, which provides an estimated $2 trillion stimulus package to combat the economic and health risks posed by the COVID-19 pandemic. The law creates a $150 billion Coronavirus Relief Fund for state, local, and tribal governments. Washington's allocation of this funding resulted in $2.2 billion to the state. We expect that the state will continue to use the funding to alleviate some direct fiscal strain brought on by the pandemic. Whether this funding is enough to offset any revenue declines and increasing expenditures is unclear at this time.

The Federal Reserve has also created a municipal lending facility to directly purchase up to $500 billion in short-term debt based on issuers in the municipal market by population. It is uncertain if Washington will use the facility at any point, but we expect it to have very strong market access to private lenders if needed. Officials report there is currently no plan for Washington to partake in cash-flow borrowing.

For more information on the potential effects of the COVID-19 pandemic on state credit conditions, please see "The COVID-19 Outbreak Weakens U.S. State And Local Government Credit Conditions" (published on April 2, 2020), and "All U.S. Public Finance Sector Outlooks Are Now Negative" (published on April 1, 2020).

Based on the analytic factors we evaluate for states, we have assigned a composite score for Washington of '1.6' on a four-point scale whereby '1.0' is the strongest and '4.0' is the weakest.

For more information on our GO rating on the state, see the full analysis on Washington (published Jan. 27, 2020).

Related Research

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of June 29, 2020)

Ratings Detail (As Of June 29, 2020) (cont.)		
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO		
Unenhanced Rating	AA+(SPUR)/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		
Long Term Rating	AA+/Stable	Affirmed
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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 GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Ratings Detail (As Of June 29, 2020) (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		
Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
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Long Term Rating	AA+/Stable	Affirmed

Ratings Detail (As Of June 29, 2020) (cont.)		
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
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Long Term Rating	AA+/Stable	Affirmed
Washington GO		
Long Term Rating	AA+/Stable	Affirmed
Washington GO (AMBAC)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (MBIA)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (MBIA) (National)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Washington GO (SYNCORA GTY)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Ratings Detail (As Of June 29, 2020) (cont.)		
FYI Properties, Washington		
State of Washington, Washington		
FYI Properties (Washington) APPROP		
Long Term Rating	AA/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.