FitchRatings

10 JAN 2023

Fitch Rates State of Washington's $726MM GOs 'AA+'; Outlook Stable

Fitch Ratings - San Francisco - 10 Jan 2023: Fitch Ratings has assigned a 'AA+' rating to the following State of Washington GO bonds:

--$631.935 million Various Purpose General Obligation Bonds, Series 2023B;

--$93.925 million Motor Vehicle Fuel Tax and Vehicle Related Fees General Obligation Bonds, Series 2023C.

In addition, Fitch has affirmed the state's 'AA+' Issuer Default Rating (IDR), and the 'AA+' rating on the state's outstanding GO bonds.

The Rating Outlook is Stable.

The bonds are expected to sell competitively on or about Jan. 18, 2023. The proceeds of the bonds will be used primarily to pay and reimburse state capex. Par amounts are subject to change.

SECURITY

All GO bonds are general obligations of the state to which the state has irrevocably pledged its full faith, credit and taxing power. The series 2023C bonds are further secured by motor vehicle fuel tax and vehicle related fees.

ANALYTICAL CONCLUSION

Washington's 'AA+' Issuer Default Rating (IDR) and GO bond rating reflect the state's broad and steadily growing economy, with solid long-term revenue growth prospects, a demonstrated commitment to fiscal balance and combined long-term liabilities that place a low burden on resources. The ratings also reflect the state's very strong financial resilience supported by a statutory requirement for a balanced multiyear budget and formulaic funding of the budget stabilization account (BSA) leading to solid reserves. Education poses a unique spending pressure for the state given both steady population growth and the state's role as the primary funder for K-12 schools across the state.

Economic Resource Base

Washington's fundamental economic profile remains strong, with long-term steady growth prospects, particularly in information technology, and a diverse employment base. Continued economic gains will be supported by high educational attainment and income levels above the national average.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

Revenue performance over time has generally been above long-term inflation, and Fitch expects this to continue to support solid growth prospects. The state has complete independent control over taxation, with an unlimited legal ability to raise operating revenues as needed.

Expenditure Framework: 'aa'

Washington benefits from solid expenditure flexibility, although its flexibility is somewhat more restricted than most states due to court mandates, statutory commitments and broad responsibility for education funding. Rapid demographic growth also exerts pressure on infrastructure spending. The state has a low burden of carrying costs, and benefits from broad expense-cutting authority common to most U.S. states.

Long-Term Liability Burden: 'aaa'

The combined burden of debt plus net pension liabilities is low as a percentage of personal income but above the median for U.S. states. Elevated debt ratios incorporate the funding of substantial capital needs, particularly for transportation, but are offset by a moderate net pension liability and an expanding economic resource base.

Operating Performance: 'aa'

Washington maintains very strong gap-closing capacity in the form of its superior budget flexibility and solid reserves. The state has prudently built up reserves in times of economic recovery and expansion, despite spending pressure for education and other pressing needs.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Strong economic and revenue growth that outpaces national GDP over time;

--Long-term management of higher spending for education and other overall growth pressures, while establishing superior gap-closing capacity, such as through maintaining reserves above the recent peak of 20% of spending.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A sustained increase in the long-term liability burden to 10% or more of personal income;

--Unanticipated shift in fiscal management that materially weakens fiscal resilience, such as sizable and continuing draws on reserves to support operations, particularly during times of economic expansion.

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CURRENT DEVELOPMENTS

Economic Recovery Picks Up Pace

Washington's recovery from the pandemic has been in line with national trends. As of October 2022, the state housed more jobs than before the pandemic (106% of pre-pandemic jobs), consistent with the 105% national recovery through that same month. October 2022 headline unemployment of 3.8% was slightly above the national 3.7% rate that month, consistent with the pattern heading into the pandemic.

Washington's labor force growth has been ahead of national trends, reflecting the state's ongoing economic expansion. The state's employment to population ratio (EPOP, a measure of labor force utilization) as of October 2022 was 62.1%, near full recovery to the February 2020 level of 62.8%. Nationally, EPOP of 60.0% lags the February 2020 level of 61.2%.

Washington Fiscal Update

Conservative revenue forecasting practices have allowed the state to prudently navigate challenging yet ultimately favorable economic conditions over the past years. The most recent update from the state's Economic and Revenue Forecast Council (ERFC) in November 2022 projected fiscal 2023 and 2024 revenues at levels 37% higher than fiscal 2019 revenues.

Upward revisions to the revenue forecast come despite mixed projections for key economic indicators such as personal income, state GDP and employment. Importantly, the state's economist notes that unexpectedly and persistently high inflation drives state sales tax growth, which is not inflation-adjusted. As prices rise, so have collections.

Following the February 2022 upwards forecast revision, the state enacted a supplemental 2022 budget bill in March that added approximately $5 billion in near general fund (NGF) appropriations for the current biennium. NGF is the designation for the state's primary operating funds. The additional appropriations were a mix of one-time allocations such as $2 billion transfer to the state's transportation fund and most of the $1.1 billion of allocated ARPA aid and recurring spending including $232 million for wage and compensation increases for state employees. Any additional revenues forecast in subsequent 2022 revisions and ERFC forecast adjustments are being incorporated into the legislature's 2023 session.

The state's budgetary reserves have shifted considerably through the pandemic and are now on a path towards exceeding pre-pandemic levels. Reduced balances in the constitutional BSA were followed by a sharp increase in ending balance in fiscal 2021, a steep decline in fiscal 2021, and moderate growth in fiscal 2022 and 2023. The legislature also established a new reserve fund, the Washington Rescue Plan Transition Account (WRPTA) and allocated $1 billion towards it in fiscal 2022 in the enacted biennial budget.

The supplemental 2022 budget bill brings the fiscal 2023 allocation to $2.1 billion. The WRPTA has statutory restrictions, but they are relatively broad and the fund provides an important source of future fiscal flexibility for Washington. Fitch anticipates future legislative sessions could provide further clarity on policymakers' long-term intentions regarding the WRPTA and its viability as a source of sustained fiscal resilience for the state.

In the current Four-Year Budget Outlook (a statutorily-required budget forecast that reflects the supplemental 2022 budget bill, but not the November 2022 revenue forecast update), the state anticipates another $500 million WRPTA deposit in fiscal 2025. By the end of the 2023-2025 biennium, the budget outlook forecasts combined reserves (ending balance plus BSA plus WRPTA) of $5.6. billion or nearly 19% of projected revenues and other resources. This compares to $3.6 billion in reserves at the end of fiscal 2019.

CREDIT PROFILE

Economic Resource Base Details

Boeing remains a large employer in Washington and an important contributor to its economy; however, the state's overall manufacturing sector is about the same proportion of GDP as the nation's manufacturing sector, while Washington's information technology sector generates over 2.5x the proportion of GDP as the nation. Microsoft and Amazon combined employ almost two times more individuals than Boeing, and several software and information companies continue to expand in the state. The workforce is highly educated, income levels are comparatively high and the state poverty rate is below the national average.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Washington, State of (WA) [General Government]	LT IDR	AA+	Affirmed		AA+
• Washington, State of (WA) /General Obligation -	LT	AA+	Affirmed		AA+

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Unlimited Tax/ 1 LT				

RATINGS KEY OUTLOOK WATCH

RATINGS KEY	OUTLOOK	WATCH
POSITIVE	⊕	⬘
NEGATIVE	⊖	⬙
EVOLVING	⊙	◆
STABLE	○	

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (pub.04 May 2021) (including rating assumption sensitivity)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

Washington, State of (WA)	EU Endorsed, UK Endorsed

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Endorsement policy

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