

# RatingsDirect®

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## Summary:

# State of Washington; Appropriations; General Obligation

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### Credit Profile

US\$108.44 mil various purp GO rfdg bnds ser R-2021B due 01/01/2025

*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 \$108.44 million various purpose general obligation (GO) refunding bonds, series R-2021B. 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 projected revenue collections have been lowered due to the pandemic, 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. (BBB-/Negative), 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.

Officials estimate that revenues collected through Sept. 10, 2020, position the state to end the fiscal 2019-2021 biennium with a negative balance of \$1.16 billion (2.2% of biennial expenditures) to be solved for the general fund and

near general fund accounts including the education legacy trust account, opportunity pathways account, and workforce education investment account. If nearly \$2 billion of the beginning fund balance were excluded, the operating deficit would have been wider at approximately 5.0% of biennial expenditures, which is generally comparable to that of state peers. While Washington's Economic and Revenue Forecast Council (ERFC) had previously forecast in June that biennial revenues would decline by \$4.5 billion (9.1%), the council's updated September forecast reduced the shortfall by \$2.2 billion due to higher-than-expected federal stimulus payments and consumer retail spending, among other factors. We understand the state intends to use its budget stabilization account to resolve the gap. The current balance of this rainy-day fund is \$1.682 billion (or a good 6.5% of fiscal 2020 expenditures) and is projected to drop to \$768 million (or a reduced 2.97% of fiscal 2020 expenditures) by the end of the biennium.

The state's baseline projections, however, do not yet reflect Boeing's recent announcement that it is moving some aircraft production from Washington to South Carolina. The company recently confirmed that it will end production of the 787 Dreamliner in Everett, Wash., by mid-2021, while the Puget Sound area will continue to house production of several other aircrafts. It is unclear, at present, how many jobs will be affected by the move but the state estimates more than 1,000 residents work to build the 787 Dreamliner. Boeing, which employs about 70,000 in Washington (according to pre-pandemic data), has recently faced challenges including grounding of its 737 MAX fleet due to safety concerns and declining demand for air travel. Significant employment reductions had been expected and recent actions include the loss of about 10,000 of 30,000 jobs in Everett. In our view, the state's September 2020 forecast prudently included a Boeing production shift to South Carolina in its pessimistic scenario (the company had announced its intent to consolidate 787 Dreamliner production before determining location). The council's downside scenario simultaneously incorporates rising coronavirus infection rates with no additional fiscal stimulus and projects a nearly \$2 billion (4%) drop in revenues from the baseline forecast. Management expects the ERFC's next scheduled forecast in November will incorporate updated information on Boeing's production move into its baseline forecast--to the extent it is available. Although we view Washington's economy as sensitive to swings in the state's aerospace industry, we believe the state's economy is well-diversified.

We expect Washington'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.

Management reports that the average daily balance of the state treasury and treasurer's trust funds was \$9.4 billion in August 2020, which we consider a very strong 36.4% of fiscal 2020 expenditures or 17.6% of 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.

The state has taken action to help limit the effects of the COVID-19 pandemic 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

Washington's response to the outbreak by declaring a state of emergency issuing a stay-at-home order. Currently, Washington is operating a four-phased approach to reopening economic activity with progression varying by county. While recovery has begun, S&P Global Economics' latest forecast still anticipates that the resulting consequences from the pandemic-induced recession will be substantial for the nation, and estimates that U.S. real GDP will contract 4% this year (see "The U.S. Economy Reboots, With Obstacles Ahead," published Sept. 24, 2020, on RatingsDirect).

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 good reserve profile, will help insulate the state rating from pandemic- or employment-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.

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.

### **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, which if sustained could weaken the state's economy, liquidity, and budgetary performance. For more information on the potential effects of the pandemic on state credit conditions, see "The COVID-19 Outbreak Weakens U.S. State And Local Government Credit Conditions" (published April 2, 2020) and "U.S. States Mid-Year Sector View: States Will Continue To Be Tested In Unprecedented Ways" (July 13, 2020).

In our opinion, Washington's environmental risks are elevated given a combination of exposure to rising sea levels along the state's vast coastline and risk of wildfires in its expansive forests. Washington, which has more than 3,000 miles of coastline, derives much of its economic activity from 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. Other areas of the state have experienced drought conditions for a least part of the year over the past decade and officials expect dry conditions in summer months will likely persist in the decades ahead. 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 in the medium term from job losses in the state's aviation industry, 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 from voter-approved initiatives that, to a degree, limit the state's budgetary flexibility.

## Credit Opinion

For more information on our GO rating on the state, see the full analysis on the State of Washington (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 October 7, 2020)		
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed

Ratings Detail (As Of October 7, 2020) (cont.)		
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
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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

Ratings Detail (As Of October 7, 2020) (cont.)		
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>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
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Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

## Ratings Detail (As Of October 7, 2020) (cont.)

Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
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Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Washington GO (AMBAC)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO (MBIA)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO (MBIA) (National)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Washington GO (SYNCORA GTY)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
<b>FYI Properties, Washington</b>		
State of Washington, Washington		
FYI Properties (Washington) APPROP		
<i>Long Term Rating</i>	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](http://www.standardandpoors.com) for



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