MOODY'S RATINGS

CREDIT OPINION
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Washington (State of)

Update to credit analysis

Summary

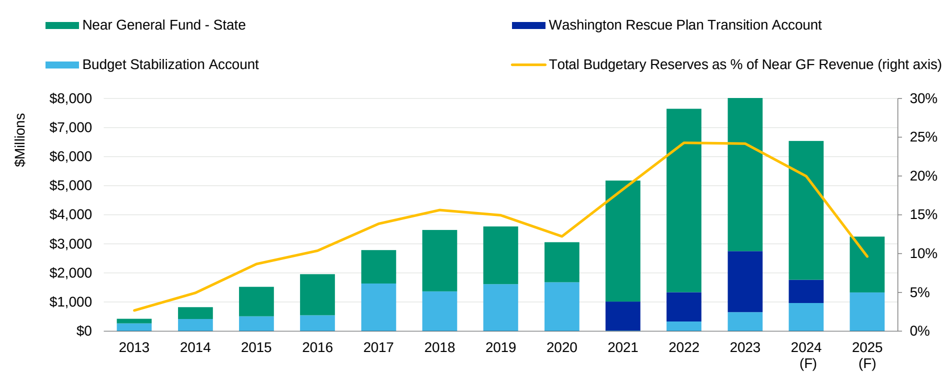
The State of Washington's (Aaa stable) credit profile is supported by its strong economic fundamentals, above-average demographic profile, sound financial position and prudent fiscal governance practices. Similar to other US states, Washington's reserve position is receding from record positions (see Exhibit 1) given softening revenue growth and continued spending increases under the 2025 biennium budget. While the state's total leverage (debt, pension, OPEB, other long-term liabilities) is moderately higher than the 50-state median, it has declined in recent years and the state's fixed costs are in-line with the sector median. Frequent voter initiative activity can add budget challenges, but the legislature has broad authority to suspend voter-enacted statutes and a history of responding effectively to maintain budget balance.

The State of Washington's low economic reliance on federal spending, sound finances, manageable leverage and fiscal autonomy support its ability to surpass the United States' rating (Aaa negative) in the event of a one-notch US downgrade.

Exhibit 1

Washington's strengthened reserves will help it weather rising costs amid slowing economic and revenue growth

Cash basis; fiscal year



The Washington Rescue Plan Transition Account was established during the pandemic for related expenditures and serves as a secondary rainy day fund, but with less restrictions.
(F) reflects the state's June 2024 quarterly revenue forecast and incorporates the 2024 supplemental budget to the 2023-2025 biennium budget. Near General Fund – State includes General Fund - State and certain funds that are statutorily designated as "related funds": the Opportunity Pathways Account ("OPA"), the Education Legacy Trust Account ("ELTA"), and the Workforce Education Investment Account ("WEIA")
Source: State of Washington; Moody's calculations

Credit strengths

» Strong economic and demographic fundamentals

» Sound financial reserves and liquidity

» Pension funding levels are strong and retiree health insurance liability is manageable

» Institutionalized governance practices are strong

Credit challenges

» Steep surge in costs of living could slow down population growth and drive continued spending pressure for social related services

» Exposure to cyclical commercial aerospace industry and commodity export markets, although reduced in recent years

» Debt burden is above average, but has been declining

Rating outlook

Washington's outlook is stable, reflecting the positive underlying fundamentals of its economy and the state's strong governance practices which will continue to support sound reserves. Long-term liabilities are expected to remain manageable.

Factors that could lead to an upgrade

» Not applicable

Factors that could lead to a downgrade

» A significant deterioration of the state's reserve and liquidity position, including a weakening of budgetary reserves

» Protracted structural budget imbalance and/or a shift to reliance on one-time budget solutions

» A sustained or structural weakening of the state's economy and demographic trends

» A material increase in leverage and fixed costs to levels well above sector medians

Key indicators

Exhibit 2

	2021	2022	2023	State Medians (2022)
Economy				
Nominal GDP ($billions)	688.6	738.1	801.5	288.7
Real GDP, annual growth	6.8%	1.6%	4.8%	1.7%
RPP-adjusted per capita income as % of US	105.8%	104.8%	105.8%	96.6%
Nonfarm employment, annual growth	2.7%	4.8%	2.8%	4.3%
Financial performance				
Available balance as % of own-source revenue	22.8%	40.5%	42.1%	38.6%
Net unrestricted cash as % of own-source revenue	35.4%	48.2%	46.1%	73.4%
Leverage				
Total long-term liabilities as % of own-source revenue	188.3%	150.7%	115.4%	127.0%
Adjusted fixed costs as % of own-source revenue	6.6%	4.9%	5.9%	4.7%

Source: State of Washington ACFRs with Moody's adjustments; US Bureau of Economic Analysis; US Bureau of Labor Statistics.

Profile

Washington is the thirteenth largest state by population, at 7.8 million. Its nominal gross domestic product (GDP) is the ninth largest, at $801.5 billion as of 2023. Resident income measures are above average, although Washington's cost of living has surged in recent years. Washington's per capita personal income is equal to 105.8% of the US after adjusting for regional cost of living.

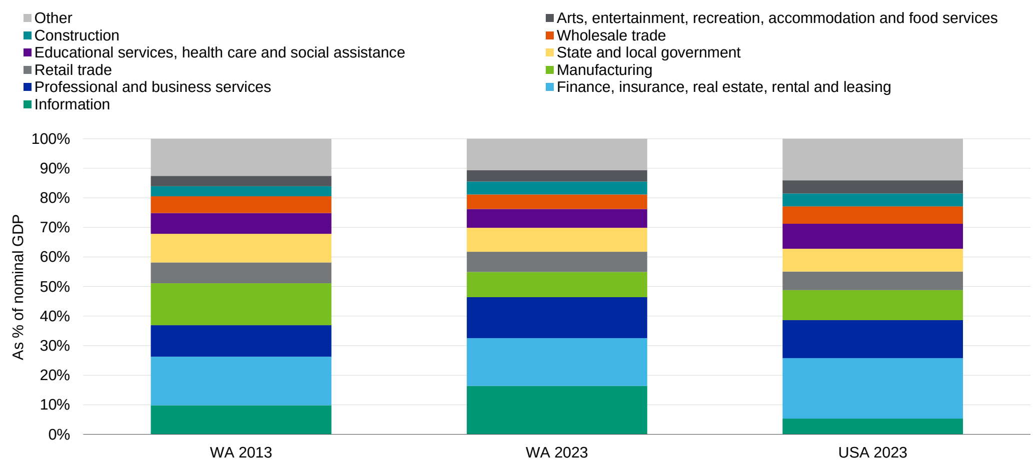
Detailed credit considerations

Economy

Washington's economy is demonstrating remarkable resilience amid higher interest rates, even as its crucial tech sector experiences some deceleration. Over the longer-term, Washington's economy will likely continue to outperform the nation's, supported by its favorable demographic trends and diverse industrial base (Exhibit 3). Still, the state's economic growth could slip closer to the national average as its population growth moderates given the state's weakened affordability (see ESG section). Competition from lower-cost hubs throughout the West could gradually chip away Washington's tech dominance and working-age demographic. Attracting international migrants is poised to play an increasingly important role in sustaining the state's working-age population growth over the next decade.

Exhibit 3

Washington's growing information technology industry has lessened the state's traditional dependence on aircraft manufacturing

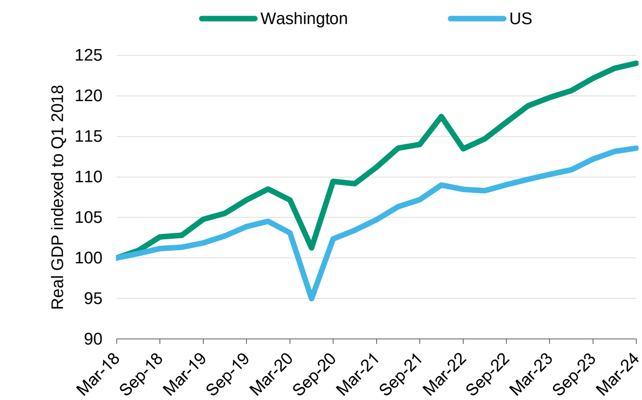


Source: US Bureau of Economic Analysis; Moody's Analytics

Washington has a much greater reliance on the information industry than the nation overall (Exhibit 3), and the state currently boasts the highest share of tech employment among all states. The technology sector centered in and around City of Seattle (Aaa stable) has expanded rapidly over the last decade and lessened the state's traditional dependence on aircraft manufacturing. Today, the Puget Sound region hosts the headquarters or major centers of operations for a dozen Fortune 500 companies, including Amazon.com (A1 stable), Microsoft (Aaa stable), Meta Platforms, Inc. (Aa3 stable), Costco Wholesale Corporation (Aa3 stable), The Boeing Company (Baa3 negative) and Starbucks (Baa1 stable), among others.

Exhibit 4

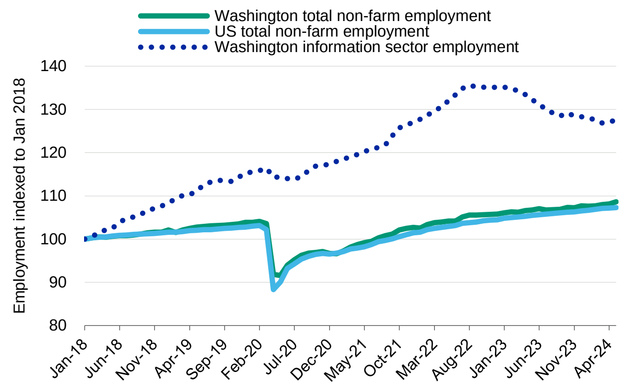
Washington's real GDP growth continues to outpace the US....



Source: U.S. Bureau of Economic Analysis; Moody's Investors Service

Exhibit 5

...despite slowing job growth overall, including contracting tech employment amid higher interest rates



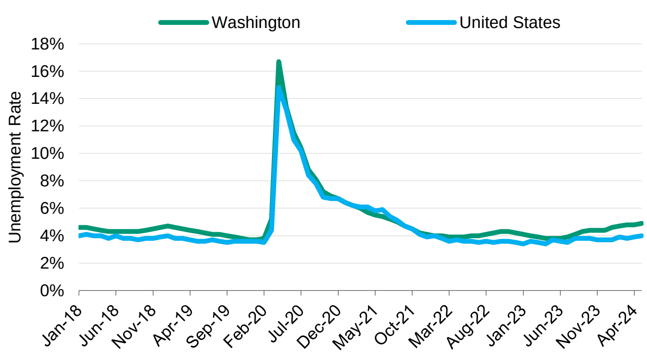
Source: U.S. Bureau of Economic Analysis; Moody's Investors Service

Similar to many peers, Washington's total employment growth is slowing amid higher interest rates; employment in its pivotal information industry has contracted the first time since the 2007-08 financial crisis. Washington's unemployment rate remains low but has ticked up recently (Exhibit 6) and the state's labor force participation rate has declined (Exhibit 7).

Despite some turbulence from the tech sector, Washington's economy is still expanding given continued recovery in other industries, including health services and manufacturing. Growth in government employment has also been a source of strength in recent months. The state's real GDP growth in the last few quarters continued to outpaced that of the nation's (Exhibit 4).

Exhibit 6

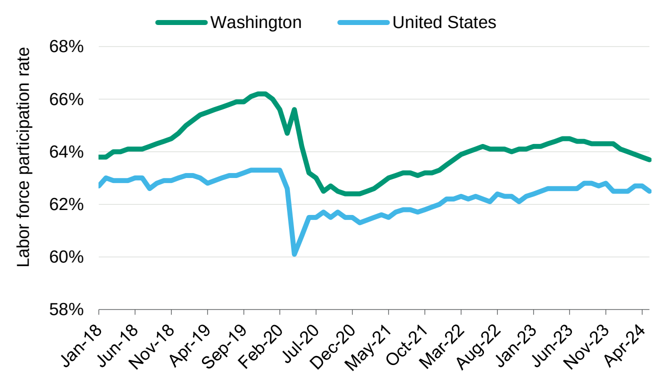
Washington's unemployment rate is slightly ticking up...



Source: US Bureau of Labor Statistics; Moody's Analytics.

Exhibit 7

...but Washington benefits from a higher labor force participation rate

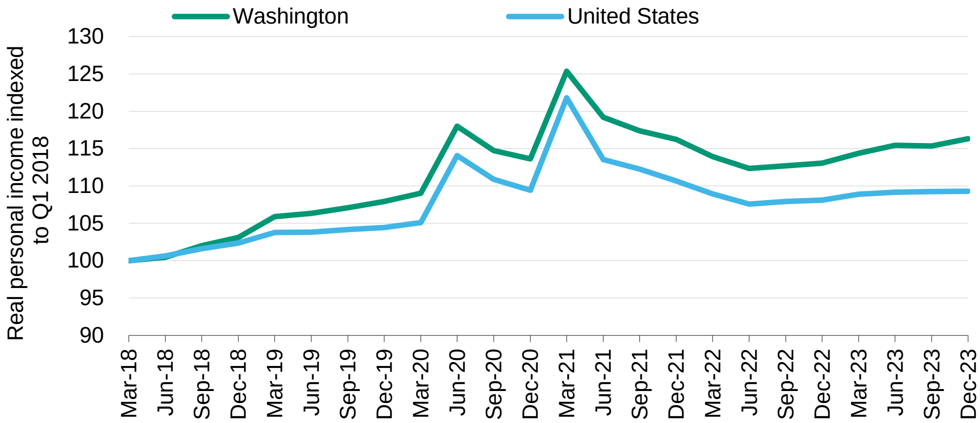


Source: US Bureau of Labor Statistics; Moody's Analytics.

Washington's per capita personal income is above average and personal income growth has exceeded that of the nation over the last few years (exhibit below); similar to the nation, Washington's real personal income growth has been hampered by high inflation in recent quarters.

Exhibit 8

Washington's personal income growth is above average, although somewhat hampered by high inflation in recent quarters



Note: real personal income is adjusted by quarter average consumer price index.
Source: US Bureau of Labor Statistics; Moody's Analytics.

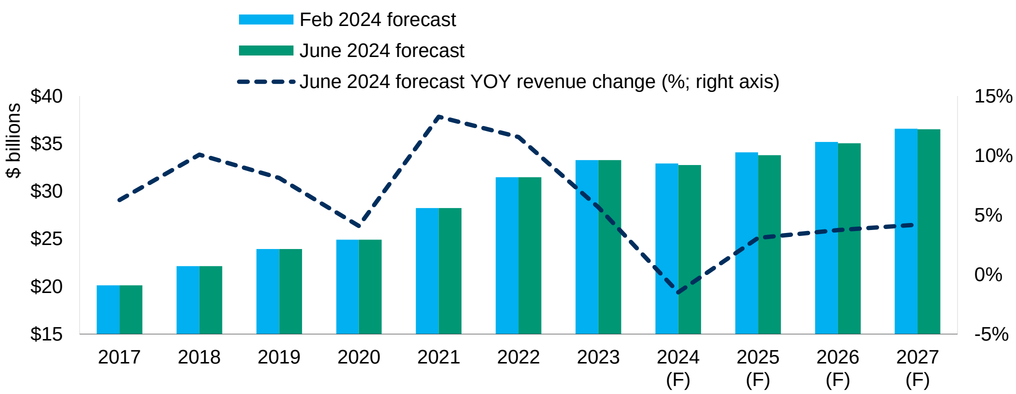
Finances and Liquidity

We expect Washington will maintain a sound financial position with fiscal prudence.

The state's revenue growth is moderating after strong double-digit percentage increases in fiscal 2021 and 2022 that benefited from taxpayers' income boost from federal stimulus aid, capital gains, and rising inflation rate. Washington's cash basis Near General Fund – State [1] revenues increased by 5.6% nominally in fiscal 2023, outperforming its forecast and benefitting from the addition of a capital gains tax. The state's latest June 2024 revenue forecast projects Near General Fund – State revenue to decline by 1.5% in fiscal 2024 before growing by 3.1% in fiscal 2025. The latest revenue forecast projects $470 million less Near General Fund - State revenue compared to the Feb 2024 forecast used to craft the 2024 supplemental budget, primarily because of weaker capital gains tax collections and weaker consumer spending.

Exhibit 9

Washington's Near General Fund - State revenue growth is moderating



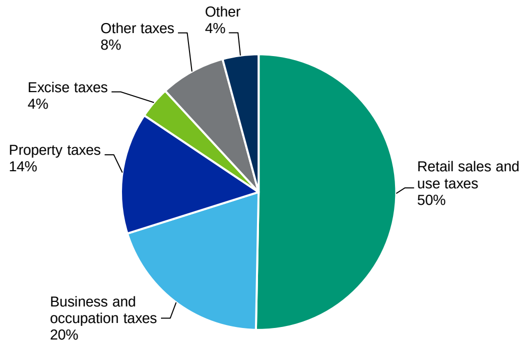
Source: State of Washington Economic and Revenue Forecast Council; Moody's Ratings

Sales tax and gross receipts tax (business and occupation tax) represent the largest sources of the state's general fund own source revenue. Historical US Census data shows that state sales taxes have generally been less volatile than income taxes, another major revenue source for the state sector. While Washington's real estate excise tax and the new capital gains tax are more volatile, they represent moderate shares of the state's Near General Fund - State operating revenue; volatility in the capital gains tax, an excise tax, is also somewhat insulated by the fact that only the first $500 million (indexed annually by inflation) becomes Near General Fund – State operating revenue; collections beyond $500 million (indexed annually) are deposited into the Common Schools Construction Fund for capital needs.

Exhibit 10

Sales and business tax represents the largest source of the state's general fund own source revenue

Fiscal 2023 GAAP basis



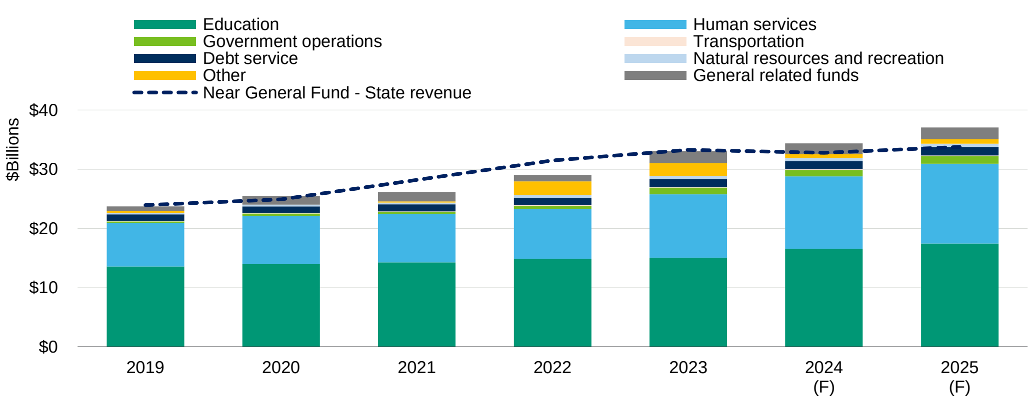
Source: State of Washington audited financial statement; Moody's Investors Service

The state's budgetary reserves will retreat from record positions under the 2025 biennium budget (see Exhibit 1), given continued spending increases and slower revenue growth. The 2023-2025 biennium budget tackles the state's pressing needs, including K-12 education (salary increases, special education enhancements etc.), housing affordability and homelessness, behavioral health services, opioid response, employee wage increases and climate-related investments. While education remains the largest component of Washington's Near General Fund - State expenditure, healthcare and social services related spending has been a major source of spending increase in recent years (Exhibit 11).

Around $1.7 billion of the 2025 biennium general fund operating budget are one-time spending, but we estimate that the budget includes a $3.2 billion (4.8%) structural deficit (ongoing expenditure exceeding ongoing revenue) based on the state's latest revenue forecast. The state has built up sizable reserves with prior surpluses that can bridge the continued spending increase and, typically, 0.5% - 1.8% of appropriations remain unspent by the end of each biennium, resulting in savings. Still, the state's ability to maintain structural balance over the longer-term and keeping its budgetary reserve at/ around the Treasurer's recommended 10% level will remain crucial for its credit quality.

Exhibit 11

Washington's fiscal 2025 biennium budget entails continued spending increases amid slower revenue growth



(F) reflects the state's June 2024 quarterly revenue forecast and incorporates the 2024 supplemental budget to 2023-2025 biennium budget.
Source: State of Washington Economic and Revenue Forecast Council; Moody's Ratings

Two citizen initiated measures on the November 2024 ballot could threaten the state's revenue flexibility: (1) an initiative to repeal the cap-and-trade program under the 2021 Climate Commitment Act and (2) an initiative to repeal the capital gains tax. The state has prudently taken action to mitigate the potential budgetary risks, by stopping or delaying some appropriations until January 2025 in case these measures pass. Washington's legislature has broad authority to amend or suspend voter-enacted statutes and a history of responding effectively to maintain budget balance.

Liquidity

The state's liquidity position will remain sound with conservative fiscal management.

Available operating reserves, which for the purpose of our analysis includes unassigned, committed and assigned general fund and non-major governmental fund balances and internal services fund balance, totaled $16.9 billion as of fiscal end 2023, representing a robust 42.1% of own-source revenue. Unrestricted operating cash totaled $18.5 billion or 46.1% of revenue as of fiscal end 2023. These balances will likely also retreat from record positions by the end of the 2025 biennium but remain sound. The state does not issue cash flow notes.

Washington's statute allows for the commingling of all balances in the State Treasury and in the custody of the State Treasurer for banking, cash management, and investment purposes. This allows the state to use non-general fund money to provide liquidity to the general fund, if needed.

Leverage and fixed costs

The state's overall leverage (total debt, pension, OPEB and other long-term liabilities) is moderately higher than the sector median, but has declined. Consistent with sector-wide trends, Washington's ability to service long-term liabilities improved in recent years as it saw strong revenue growth; also, its pension and OPEB burden declined in part because of higher interest rates we use to discount these liabilities.

As of fiscal year end 2023, the state's total leverage represented 115.4% of own source revenue, compared to a preliminary sector median[2] of 100.9%.

Washington's fixed costs, based on Moody's pension tread water metric, are moderate and represented 5.9% of own-source revenue in fiscal 2023, compared to a preliminary sector median of 5.1% of own source revenue. Washington's fixed costs generally tracks closely with the sector median.

Debt and debt structure

Debt currently represents the largest component of Washington's long-term liabilities, and Washington's debt burden is higher than the sector median.

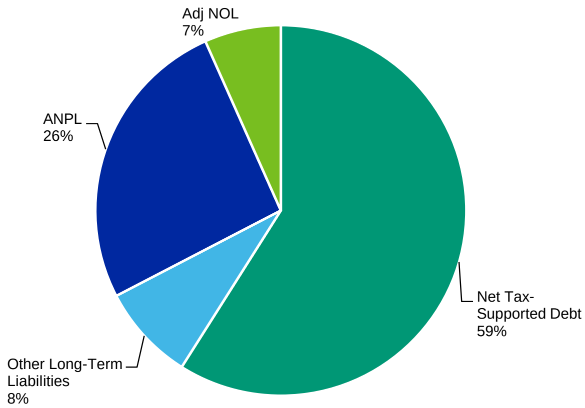
Washington's net tax-supported debt (NTSD) consists primarily of general obligation bonds, including those secured by and expected to be paid from transportation revenue. The state's bonds are long-term fixed rate bonds, mainly issued with a 25-year maturity and level debt service structure; on an aggregate basis, the state's debt has a declining debt service structure.

In the past, Motor Vehicle Fuel Tax (MVFT) GO bonds constituted the largest share of the state's transportation-related debt. To mitigate the risk of carbon transition and diminishing fuel consumptions in the future, the state passed Senate Bill 5898 (effective June 9, 2022) to prudently adapt its debt structure to changes in transportation revenue: new GO backed transportation-related bonds that remain unissued under previous authorizations are to be issued as Motor Vehicle Fuel Tax and Vehicle Related Fees (MVFT/VRF) GO bonds, including any bonds issued to refund outstanding MVFT GO Bonds. As such, the MVFT/VRF GO Bonds now constitutes the largest share of the state's transportation debt mix as of June 2024, and will become an increasing share as the MVFT GO bonds mature and are refunded.

Exhibit 12

Debt represents the largest component of Washington's long-term liabilities

Fiscal 2023 long term liability breakdown



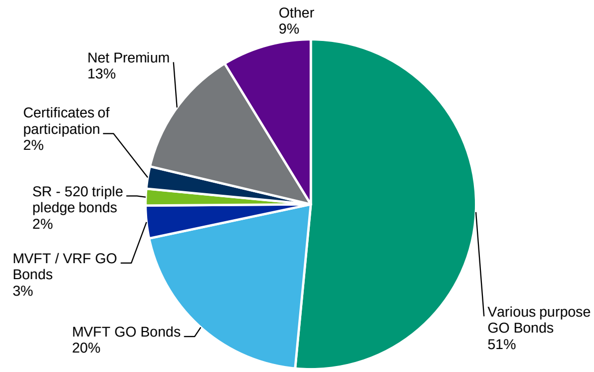
ANPL stands for adjusted net pension liability; Adj NOL stands for adjusted net OPEB liability

Source: State of Washington; Moody's Investors Service

Exhibit 13

Washington's net tax supported debt consists primarily of general obligation bonds

Fiscal 2023



Source: State of Washington; Moody's Investors Service

Debt legal security

The state has four classes of general obligation bonds: General Obligation Bonds or Various Purpose General Obligation Bonds, Motor Vehicle Fuel Tax (MVFT) General Obligation Bonds, Motor Vehicle Fuel Tax and Vehicle Related Fees (MVFT/VRF) General Obligation Bonds and Triple Pledge Bonds – all of which are general obligations of the state, to which the state has pledged its full faith, credit and taxing power. The MVFT bonds are additionally secured by and expected to be paid from motor vehicle fuel taxes. The MVFT/VRF bonds are additionally secured by and expected to be paid from motor vehicle fuel taxes and other vehicle-related fees. The Triple Pledge Bonds are additionally secured by motor vehicle fuel taxes and toll revenues and expected to be paid from toll revenues.

The state also issues certificates of participation, rated Aa1, to finance capital projects and equipment on behalf of state and local agencies. The COPs are secured by and expected to be paid from payments made by participating state and local agencies including: (1) lease payments for real property projects, and (2) installment purchase payments for personal property. Payments made by the state agencies are subject to appropriation by the legislature and executive order reduction by the governor. The state has never failed to make needed appropriations to meet the payment obligations for state agencies related to its COPs. Payments made by the local agencies are secured by the full faith and credit of the local agencies, effectively general obligation, limited tax obligations. In the event any local agency fails to make its scheduled payment, the state treasurer is obligated to make the payment on behalf of the local agency using state funds; such state payments, if necessary, are subject to appropriation by the legislature and executive order reduction by the governor. The treasurer is further obligated to withhold an amount equal to the payment advance from the local agency's share of state aid, to the extent legally permissible. No local agency has ever failed to make a payment obligation related to state-issued COPs.

Debt-related derivatives

The state has no variable rate debt and no debt-related derivatives.

Pensions and OPEB

Washington's pension liability will continue to remain moderate, supported by proactive management. Based on the state's fiscal 2022 reporting, Moody's has calculated that the state's adjusted net pension liability (ANPL) to be $20.2 billion or 54.8% of own-source governmental revenues, well below the latest 50-state median (79.8% of own source revenue). The state's fiscal 2023 ANPL was $12.0 billion or 29.9% of governmental revenue. Moody's adjustments are not intended to replace the state's reported liability information, but to improve comparability with other rated entities.

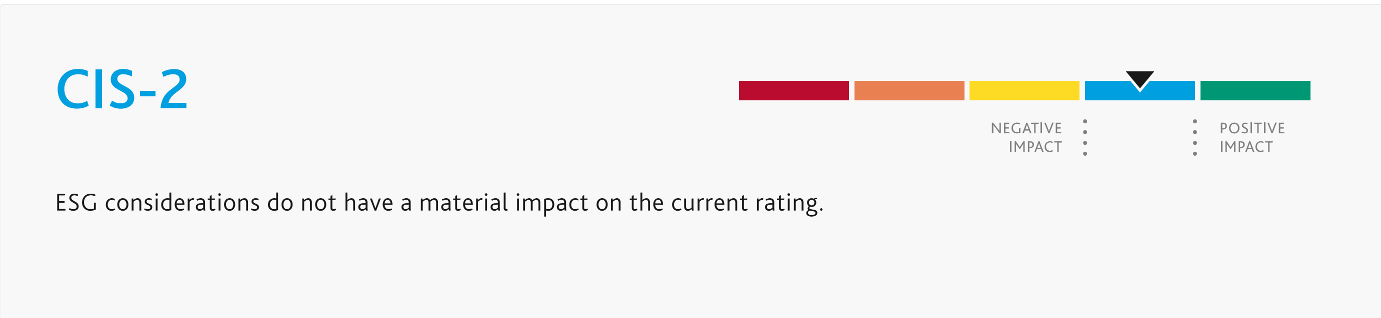
The state is committed to fully funding actuarially determined pension contributions. Notably, the state's pension contributions have consistently exceeded Moody's calculated tread water level, or the level of contribution that would prevent reported unfunded liabilities from growing under reported assumptions. Contributing at above the treadwater level signals that the state's reported pension burden will continue to decline if investment targets are achieved.

The state's other post-employment benefit (OPEB) liability is moderate. As of fiscal 2022 reporting, Moody's has calculated the state's adjusted net OPEB liability (ANOL) to be $4.8 billion, representing 13.1% of own source revenue, slightly above the 50-state median (8.8% of own source revenue). The state's fiscal 2023 adjusted net OPEB liability was $3.1 billion or 7.7% of own source revenue.

ESG considerations

Washington (State of)'s ESG credit impact score is CIS-2

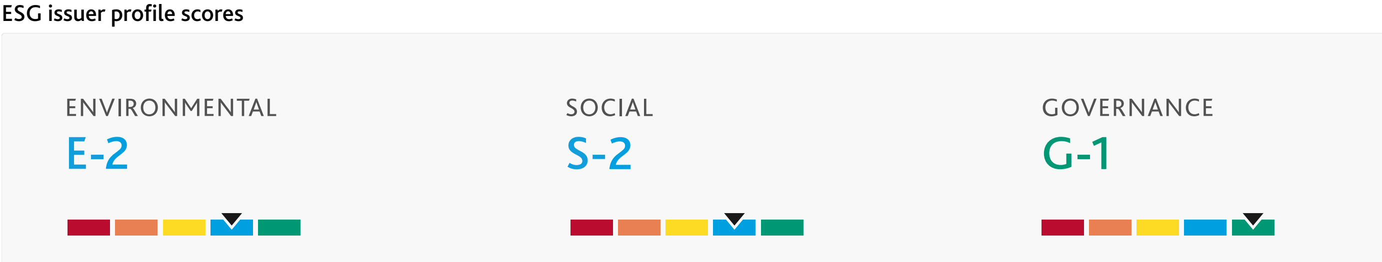
Exhibit 14
ESG credit impact score



Source: Moody's Ratings

Washington's ESG Credit Impact Score is neutral-to-low (**CIS-2**) reflecting its neutral-to-low exposure to environmental risks and social risks and positive governance profile.

Exhibit 15
ESG issuer profile scores



Source: Moody's Ratings

Environmental

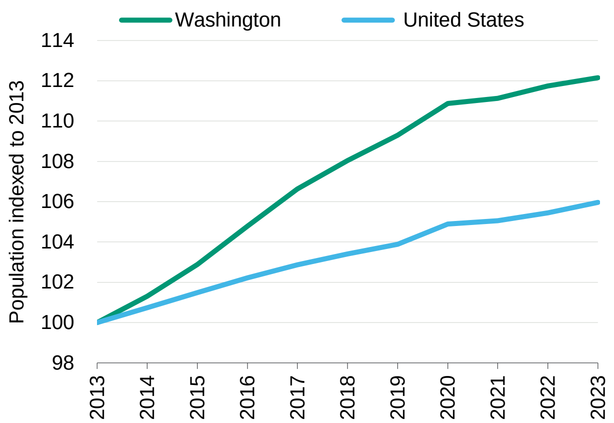
Washington's E issuer profile score is neutral-to-low (**E-2**). According to data from Moody's ESG Solutions, Washington counties average projected rate of change in five climate risk factors, when weighted by county GDP, is below average in the nation. King County, which accounts for nearly 50% of the state's GDP, is not projected to have high risk in any of the five climate factors according to Four Twenty Seven's assessment scale. The most significant impact of climate change for Washington may be an increase in the frequency and severity of wildfires. The state budgets a contingent amount for fires each year, but it will continue to depend upon the availability of federal aid through FEMA to mitigate the cost of the largest fires.

Social

Washington's S issuer profile is neutral-to-low (**S-2**). Demographic trends and income levels are generally positive and have contributed to its strong economic growth, particularly in the Seattle area, where there has been growth in the working-age population supporting growth in high-wage industries. Housing affordability, however, is a significant challenge. Residents have above average educational attainment and the state's labor force participation rate is above average. All of these factors contribute to the state's strong economic fundamentals.

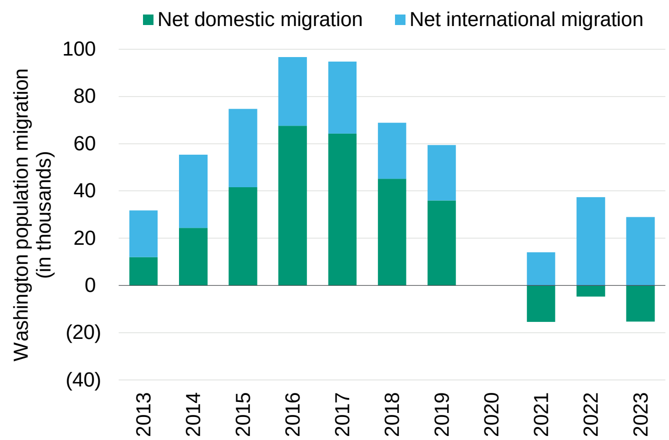
However, Washington's housing affordability has eroded and it is now one of the least affordable among 50 states. Weakened affordability will likely slow down migration, a main driver of the state's population growth. Washington also has one of the highest per capita homeless rates. The state has prioritized historic new investments in housing and homelessness in recent years.

Exhibit 16
Washington's population growth has favorably outpaced the nation's over the last decade, although growth has decelerated....



Source: U.S. Census Bureau; Moody's Investors Service

Exhibit 17
...as population in-migration into Washington has softened given weakening affordability



Migration data is not available during census year (2020)
Source: U.S. Census Bureau; Moody's Investors Service

Governance

Washington's G issuer profile score is **G-1**. Washington has strong governance practices including a quarterly consensus revenue forecasting process, multi-year revenue and expenditure projections, timely budget adoption and a demonstrated willingness to address budget shortfalls.

Since 2007, the State Constitution has required maintenance of a mandatory rainy day fund (Budget Stabilization Account), which requires the transfer, by the June 30 close of each fiscal year, of at least 1% of General State Revenues for that fiscal year. In addition, by June 30 of the second year of each Biennium, three-quarters of any "extraordinary revenue growth" must be transferred to the Budget Stabilization Account, unless the average state employment growth for the preceding biennium averaged less than 1% per fiscal year. "Extraordinary revenue growth" is defined as the amount by which the growth in General State Revenues exceeds the average biennial percentage growth in General State Revenues over the prior five biennia by more than one third. The state's constitutionally restricted Budget Stabilization Account may be spent only after appropriation and under specific circumstances: by legislation approved by a simple majority if the governor declares a state of emergency, or if employment growth is forecasted to be less than 1% for that fiscal year; or by legislation approved by at least 3/5 of the members of each house.

Although frequent voter initiative activity can create budget challenges, the state legislature has broad powers to amend or suspend voter-approved initiatives and a track record of doing so as needed to maintain budgetary balance.

Rating methodology and scorecard factors

The US States and Territories Rating Methodology includes a scorecard, which summarizes the rating factors generally most important to state and territory credit profiles. Because the scorecard is a summary, and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not map closely to the actual rating assigned.

Exhibit 18
US states and territories rating methodology scorecard
Washington (State of)

	Measure	Weight	Score
Economy			
Resident Income (PCI Adjusted for RPP / US PCI)	105.8%	15%	Aaa
Economic Growth (5-year CAGR real GDP - 5-year CAGR US real GDP)	1.6%	15%	Aaa
Financial performance			
Financial performance	Aaa	20%	Aaa
Governance/Institutional Framework			
Governance/Institutional Framework	Aaa	20%	Aaa
Leverage			
Long-term liabilities ratio (adjusted long-term liabilities / own-source revenue)	115.4%	20%	Aa
Fixed-costs ratio (adjusted fixed costs / own-source revenue)	5.9%	10%	Aaa
Notching factors			
Very limited and concentrated economy	NA		
Scorecard-Indicated Outcome			Aaa
Assigned rating			Aaa

Source: US Bureau of Economic Analysis, State of Washington, Moody's Investors Service

Endnotes

1 Near General Fund is the designation for the state's primary operating fund, which including General Fund and related funds (Education Legacy Trust Fund, Washington Opportunity Pathways Account and Workforce Education Investment Account)

2 Note: based on around 44 states with fiscal 2023 audit available as of Aug 2024

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