State of Delaware

New Issue Summary

Sale Date: April 26, 2023 by competitive bid.

Series: $364,395,000 General Obligation Bonds, Series 2023A; $34,305,000 General Obligation Refunding Bonds Series, 2023B

Purpose: The bonds will fund the ongoing capital program and refund outstanding GO bonds for debt service savings.

Security: General obligation, full faith and credit of the state of Delaware

Delaware's 'AAA' IDR and GO bond rating are based on strong financial performance, supported by proactive management and institutionalized protections designed to ensure surplus operations. Long-term revenue growth has accelerated in recent years, and Fitch anticipates it will remain above the long-term level of inflation. Recent strong growth has allowed the state to fully fund two reserves to a combined 12% of revenues. The long-term liability burden is above the state median, reflecting in part debt issuance and recognition of obligations that are addressed at the local government level in most other states.

Economic Resource Base: Delaware's economy is largely based on service-providing enterprises, including financial activities, professional and business services, and education and health organizations. The state has implemented deliberate policies to maintain a climate attractive to banking and related entities. Population growth has trended above the U.S. per capita personal income growth and levels are slightly below the nation.

Key Rating Drivers

Revenue Framework: 'aa': Financial operations are supported by a diverse array of revenue sources with the personal income tax (PIT) accounting for the largest share at approximately one-third. Delaware also leverages its status as the legal home to over half of all publicly-traded corporations in the U.S., and assesses taxes on limited partnerships, franchises and other business entities. This structure results in a revenue framework that is somewhat more sensitive to national economic trends than most other states.

Expenditure Framework: 'aaa': While carrying costs are above the U.S. states median, Delaware has demonstrated the broad expense-cutting ability common to most U.S. states and benefits from the cushion provided by its statutory restriction to budget 98% of expected revenue. Education is a key cost driver, as the state is highly involved with funding local education, including capital projects and funding employer pension contributions for school district employees.

Long-Term Liability Burden: 'aa': The state's long-term liabilities are a moderate burden on resources. Debt levels are well above average for a U.S. state, in part due to the state's role in issuance for projects usually funded at the local level, and have recently ticked upward primarily due to transportation-related borrowing. Pension liabilities are also above the median and remain relatively stable. However, other post-employment benefit (OPEB) obligations are sizable, although reduced in fiscal 2022, which was largely attributable to the significant increase in the discount rate used to calculate the liability per the last valuation report issued in November 2022.

Operating Performance: 'aaa': The state has exceptional financial resilience from strong financial management that has contributed to the maintenance of an ample financial cushion through economic cycles. The relatively frequent monitoring of revenues and operating expenditures mitigates the effect of volatility in revenues and allows for rapid gap closing.

FACT Tools

Ratings

Long Term Issuer Default Rating	AAA

New Issue

$364,395,000 General Obligation Bonds, Series 2023A	AAA
$34,305,000 General Obligation Refunding Bonds, Series 2023B	AAA

Outstanding Debt

General Obligation Bonds	AAA

Rating Outlook

Stable

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (May 2021)

Related Research

Fitch Rates Delaware's $399 Million GO Bonds 'AAA'; Outlook Stable (April 2023)

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Rating Sensitivities

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

- Not applicable given the 'AAA' ratings.

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

- A sustained slowing of revenue growth to below the level of long-term inflation.
- A sustained increase in the long-term liability burden closer to 20% of personal income or an inability of the state to address its large net OPEB liability.

Rating History

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	4/13/23
AAA	Affirmed	Stable	4/13/06
AAA	Assigned		3/23/00

Current Developments

Delaware Economic Update

The pace of Delaware's labor market recovery has been mixed relative to the national pace through most of the post-pandemic recovery period. Nonfarm payrolls declined by about 15% at the pandemic's start (from February 2020 to April 2020), which matched the national decline. Delaware has regained 117% of the payroll employment declines versus 114% for the U.S. as of February 2023. Other indicators are not as strong. Headline unemployment in February of 4.6% exceeds the U.S. (3.6%) for that month. The state's employment to population ratio (EPOP, a measure of labor force utilization) as of February 2023 was 57%, below its pre-pandemic level and among the lowest of the states, with the national rate at 60.2%.

Delaware Budget Update

Delaware's revenues continue to outperform estimates, with the Delaware Economic and Financial Advisory Council (DEFAC) making frequent upward revenue revisions post-pandemic. The enacted fiscal 2022 general fund budget anticipated revenues would be relatively flat to fiscal 2021 at $5.4 billion. Actual fiscal 2022 general fund revenues of $5.8 billion were 14% above the June 2021 budget forecast, allowing the state to carry a $912 million operating balance into fiscal 2023, alongside $568 million in reserves. The forecast upon which the current fiscal 2023 budget was based assumed a modest 0.6% increase in revenues, to just over $5.8 billion. Through February, collections are 2.1% ahead of the prior year and as of its March 2023 meeting, DEFAC estimates fiscal 2023 revenues will be $6.2 billion, 6% above forecast.

Revenue over-performance has allowed the state to increase reserves, adding to both the budget reserve account (BRA, the state's rainy day fund), which contained $316.4 million as of December 2023, and to a second reserve, the budget stabilization fund (BSF), bringing its total to $402.6 million. These reserves combined provide a cushion of 12% of fiscal 2023 revenues.

The enacted budget for fiscal 2023 appropriated 98% of available revenues for an operating budget totaling $5.1 billion, a 7% increase as compared to fiscal 2022. The budget increased funding to schools and higher education, provided pay raises and bonuses to state employees, and funded a variety of increases to other program priorities.

The revenue estimate upon which the governor's budget proposal for fiscal 2024 is based again assumes revenues will be flat on a yoy basis at $6.1 billion. The proposal appropriates 98% of anticipated revenues, maintains a fully funded rainy day fund at 5% of estimated revenues and a fully funded BSA at $421.5 million, and controls ongoing spending by allocating funds to non-recurring expenditures including for capital.

The budget proposal would finance priorities in education, higher education, water resources and economic development, among others. It would provide significant pay increases to state employees and teachers to address workforce and recruiting and retention challenges. The budget includes modest tax policy changes - increasing the standard deduction and the earned income tax credit - at a cost of $25 million in fiscal 2024 and $50 million in fiscal 2025. The budget for fiscal 2024 is under consideration by the Delaware legislature.

Delaware has received $925 million under the American Rescue Plan Act (ARPA) and has allocated its share of ARPA funds to state-wide technology and capital upgrades, housing development and emergency housing, support for hospitals and healthcare facilities, and investments in non-profit entities in the state.

Credit Profile

Revenue Framework

General fund (GF) revenues are dependent on an unusual array of taxes related to business endeavors and financial institutions, linked to companies being legally domiciled in the state. Revenues include franchise and other fees levied on businesses and banks organized under state law as well as corporate income taxes and other fees. These combine to provide approximately one-third of general fund revenues. Abandoned property, which includes accounts and securities derived from the businesses domiciled in Delaware that revert to the state's general fund when left unclaimed for specific periods, typically accounts another 10% of GF revenues and is subject to significant volatility.

The state levies a personal income tax but not a general sales tax. The personal income tax provides about one-third of GF revenues and has recorded moderate growth over the past several years, offsetting more variable results in corporate-based taxes. Lottery revenues, which include gaming and account for just below 5% of revenues, have been pressured, reflecting growth and competition in nearby gaming venues outside the state.

Historical revenue growth, adjusted for the estimated effect of policy changes, has been above the rate of inflation over the past ten years. This reflects population growth that has been stronger than the U.S. average as well as reliance on higher growth areas of the economy, including in finance and other services. As a result, Fitch anticipates the long-term trend for revenue growth will remain above long-term inflation but trail the pace of national economic growth.

The state has no legal limitations on its ability to raise revenues through base broadenings, rate increases, or the assessment of new taxes or fees.

Expenditure Framework

As in most states, education and health and human services spending are Delaware's largest operating expenses. Education is the larger line item, as the state provides significant funding for local school districts and the public university and college system. The state's education commitment includes sharing the annual employer pension contribution for local school district employees with school districts. Health and human services spending is the second largest area of spending, with Medicaid being the primary driver.

Fitch expects that the pace of spending growth, absent policy actions, will be in line with to marginally above that of natural revenue growth, driven primarily by Medicaid, and require regular budget adjustments to ensure ongoing balance. Federal action to revise Medicaid's fundamental programmatic and financial structure does not appear to be a near-term priority of the current federal administration or Congressional Leadership. As with all federal initiatives, Medicaid remains subject to regulatory changes that could affect various aspects of the program. Delaware, like all other states, has begun the potentially complicated administrative task of resuming Medicaid redeterminations and disenrollment beginning April 1, 2023. In other major areas of spending such as education, Delaware is able to more easily adjust the trajectory of growth.

Overall, Delaware retains ample ability to adjust expenditures to meet changing fiscal circumstances. Spending requirements for debt service and retirement obligations are higher than for most states, but remain low at 7.2% of fiscal 2021 governmental funds expenditures.

Strong investment returns that have raised pension system funding levels have allowed the state to lower its contribution rate while still making full actuarial payments, creating additional flexibility within the budget.

Long-Term Liability Burden

As a small state with a minimal number of local governments, Delaware's service functions are highly centralized, leading to above average long-term liabilities for a U.S. state. Per Fitch's November 2022 State Liability Update ("Personal Income Surge Offsets Liability Increase", dated Nov. 15, 2022), the state's total debt and adjusted net pension liabilities equaled 12.8% of 2021 personal income, a level of long-term liabilities that is well above the state median (4.6%) but still considered moderate.

Delaware's Public Employees Retirement System includes nine plans, covering state and local employees, with most of the state's direct liabilities in the State Employees Plan. Exceptional investment returns in 2021 eliminated the net pension liability for the State Employees Plan on a market value basis and reduced the state's long-term liability metric calculated by Fitch based on the fiscal 2022 state audit to 8.2%. However, with investment losses in the subsequent year, the metric will again increase. Fitch anticipates that the metric will be somewhat volatile as investment returns return to more typical levels.

The net OPEB liability of over $9.3 billion equals 16% of 2021 state personal income, a sizeable increase as compared to the prior year that reflects a change in the discount rate used to calculate the liability. As is the case with pension system contributions, the state pays school district OPEB, contributing to the high liability. While Fitch views the OPEB liability as a more flexible obligation compared with pensions, and also more uncertain because of the complex assumptions used to calculate it, the magnitude of the liability given Delaware's already above-average long-term liabilities is a potential rating concern.

The extent to which OPEB liabilities will weigh Fitch's assessment of Delaware's long-term liability burden and its overall rating will depend on the state's ability to manage the liability going forward, including materially modifying benefits or contributions practices. The commission formed to develop options to address OPEB liabilities has issued initial reports that propose transitioning OPEB from pay-go to pre-funding to reduce the liability over time, as well as modifying the plan and benefits to reduce future liabilities. The recommendations have yet to be taken up by the Delaware legislature. Following an executive order, the state began to set aside 1% of prior year appropriations in the OPEB trust fund, beginning with a $48 million deposit in fiscal 2023, with $51 million proposed in the governor's budget for fiscal 2024.

Operating Performance

Delaware's ability to respond to cyclical downturns rests with its prudent budget practices, maintenance of reserves, and proactive approach to tracking and forecasting revenues and expenditures throughout the budget cycle. Structural balance is supported by a constitutional provision that limits appropriations to 98% of anticipated revenues in the subsequent fiscal year, plus the unencumbered prior year budgetary general fund balance.

In addition to the availability of unencumbered cash balances, the state maintains a fully funded budget reserve account at 5% of general fund revenue. The BRA may only be appropriated to fund an unexpected budgetary deficit and requires super-majority approval in both legislative bodies to access. In addition to the BRA, the state created and has funded an additional reserve, the Budget Stabilization Fund. The BSF, in conjunction with adherence to an appropriations benchmark that tempers spending growth, provides additional financial resilience.

The Fitch Analytical Stress Test scenario analysis tool, which relates historical tax revenue volatility to GDP, indicates the modestly higher level of volatility in Delaware's revenue structure relative to other states. Fitch believes the state's close tracking of both revenues and expenditures and frequent revenue forecast updates have historically allowed it to quickly respond to changing economic conditions.

The state closely tracks revenue collections and expenditures during the year and forecasts are updated at least five times each fiscal year through comprehensive reviews by DEFAC. The state proactively reviews its tax policies and makes adjustments to ensure its budgets are balanced on a structural basis, including full actuarial pension contributions. These practices have proven to be critical to sustaining financial balance and support the state's strong operating performance.

ESG Considerations

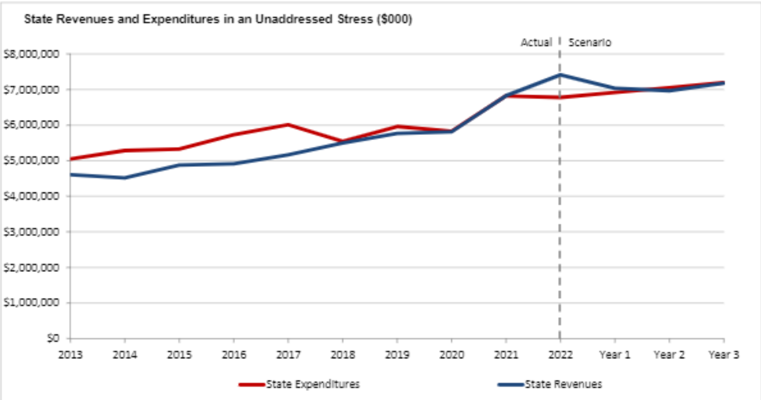
Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

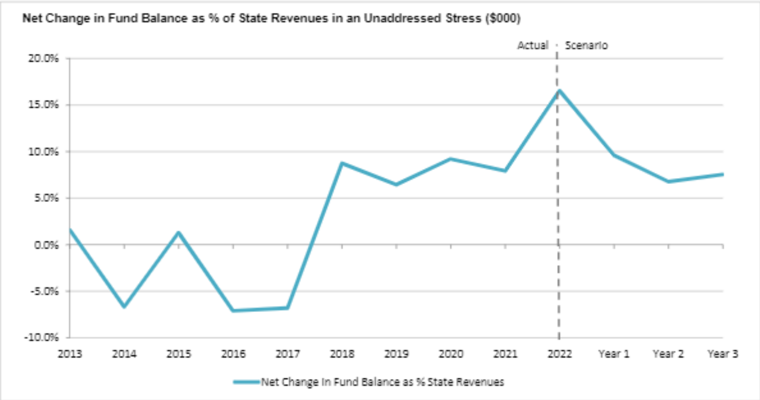
For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Delaware, State of (DE)

Scenario Analysis

Ver 36





Analyst Interpretation of Scenario Results

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Scenario Parameters:					Year 1	Year 2	Year 3
GDP Assumption (% Change)					(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)					2.0%	2.0%	2.0%
Revenue Output (% Change)	*Minimum Y1 Stress:*	-1%	*Case Used:*	Moderate	(5.1%)	(1.0%)	3.0%

Revenues, Expenditures, and Net Change in Fund Balance	Actuals										Scenario Output		
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Year 1	Year 2	Year 3
Expenditures													
Total Expenditures	6,577,485	7,222,687	7,403,424	7,928,772	8,214,973	7,918,111	8,313,932	8,533,918	10,958,389	10,641,945	10,854,784	11,071,880	11,293,317
% Change in Total Expenditures	2.6%	9.8%	2.5%	7.1%	3.6%	(3.6%)	5.0%	2.6%	28.4%	(2.9%)	2.0%	2.0%	2.0%
State Expenditures	5,047,564	5,286,190	5,326,981	5,732,338	6,011,766	5,542,502	5,959,056	5,829,702	6,824,221	6,779,933	6,915,532	7,053,842	7,194,919
% Change in State Expenditures	3.3%	4.7%	0.8%	7.6%	4.9%	(7.8%)	7.5%	(2.2%)	17.1%	(0.6%)	2.0%	2.0%	2.0%
Revenues													
Total Revenues	6,135,404	6,454,990	6,955,374	7,106,316	7,368,150	7,870,802	8,124,847	8,513,431	10,960,972	11,274,523	10,975,913	10,982,946	11,274,420
% Change in Total Revenues	4.9%	5.2%	7.8%	2.2%	3.7%	6.8%	3.2%	4.8%	28.7%	2.9%	(2.6%)	0.1%	2.7%
Federal Revenues	1,529,921	1,936,497	2,076,443	2,196,434	2,203,207	2,375,609	2,354,876	2,704,216	4,134,168	3,862,012	3,939,252	4,018,037	4,098,398
% Change in Federal Revenues	0.1%	26.6%	7.2%	5.8%	0.3%	7.8%	(0.9%)	14.8%	52.9%	(6.6%)	2.0%	2.0%	2.0%
State Revenues	4,605,483	4,518,493	4,878,931	4,909,882	5,164,943	5,495,193	5,769,971	5,809,215	6,826,804	7,412,511	7,036,661	6,964,908	7,176,022
% Change in State Revenues	6.6%	(1.9%)	8.0%	0.6%	5.2%	6.4%	5.0%	0.7%	17.5%	8.6%	(5.1%)	(1.0%)	3.0%
Excess of Revenues Over Expenditures	(442,081)	(767,697)	(448,050)	(822,456)	(846,823)	(47,309)	(189,085)	(20,487)	2,583	632,578	121,129	(88,934)	(18,897)
Total Other Financing Sources	516,165	466,286	511,010	474,569	495,030	528,199	560,943	555,885	537,340	593,703	555,214	560,617	560,552
Net Change in Fund Balance	74,084	(301,411)	62,960	(347,887)	(351,793)	480,890	371,858	535,398	539,923	1,226,281	676,343	471,683	541,655
% Total Expenditures	1.1%	(4.2%)	0.9%	(4.4%)	(4.3%)	6.1%	4.5%	6.3%	4.9%	11.5%	6.2%	4.3%	4.8%
% State Expenditures	1.5%	(5.7%)	1.2%	(6.1%)	(5.9%)	8.7%	6.2%	9.2%	7.9%	18.1%	9.8%	6.7%	7.5%
% Total Revenues	1.2%	(4.7%)	0.9%	(4.9%)	(4.8%)	6.1%	4.6%	6.3%	4.9%	10.9%	6.2%	4.3%	4.8%
% State Revenues	1.6%	(6.7%)	1.3%	(7.1%)	(6.8%)	8.8%	6.4%	9.2%	7.9%	16.5%	9.6%	6.8%	7.5%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's scenario analysis assumes the GDP and expenditure growth sequence shown in the 'Scenario Parameters' section. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.