

CREDIT OPINION

18 April 2024



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Delaware (State of)

Update to credit analysis

Summary

The [State of Delaware](#) (Aaa stable) maintains a strong credit position supported by healthy and stable finances, and strong management and governance. The state's well-established process for monitoring revenue and its statutory limits on annual spending growth are tools that aid financial management year after year. These tools and the state's continued growth in reserves provide a cushion should unforeseen fiscal challenges arise or persist.

Delaware's performance on job and income growth, both over the past couple years and over the past decade, has been just a bit behind that of the US. Over the longer term, the state should benefit from its attraction to new residents given its lower cost of living relative to nearby peers, and the state continues to enjoy stronger population growth than its regional neighbors. The state's economy has an above average concentration in financial services and the state is heavily reliant on business taxes, which can be volatile.

Delaware's leverage is high compared to most states, and consists mostly of post-employment benefits liabilities. The high leverage largely stems from the state reporting direct and total responsibility for funding post-employment benefits of local school districts, though school district property tax levies fund a portion of annual costs. Still, Delaware's leverage is far below that of the most heavily burdened states and its fixed costs are a manageable share of its budget.

Exhibit 1

Delaware's outstanding debt

Type of debt	Principal outstanding (\$m)	Moody's rating
General obligation	\$2,414	Aaa
Appropriation - sustainable energy	\$51	Aa1
Special tax - DTA transportation system	\$785	Aa1
Special tax - DTA US 301 revenue	\$198	Aa3
Special tax - DTA US 301 TIFIA loan	\$243	Aa3
Special tax - DTA GARVEEs	\$175	A1
Other debt	\$307	N/A

Principal shown as of June 30, 2023.

Source: State of Delaware and Moody's Ratings

Credit strengths

- » Healthy budget reserves, liquidity and GAAP-basis fund balance
- » Strong financial management and governance indicated by frequent revenue forecasting and statutory limit on spending
- » Solid population growth with lower business costs and cost of living relative to neighboring states continuing to attract new residents

Credit challenges

- » Low industrial diversity among US states given economic concentration in financial services
- » Heavy dependence on volatile business taxes

Rating outlook

The stable outlook is supported by the state's strong reserves and structural governance features, which will help preserve a sound financial position relative to peers.

Factors that could lead to an upgrade

- » Not applicable for the state's issuer rating

Factors that could lead to a downgrade

- » Deterioration of state finances, such that fund balance (on an audited, GAAP basis) falls below 15% of revenue
- » Substantial growth in leverage, such that the state's long-term liabilities burden rises above 250% of revenue

Key indicators

Exhibit 2

	2020	2021	2022	2023	State Medians (2022)
Economy					
Nominal GDP (\$billions)	77.6	83.0	90.2	93.6	264.2
Real GDP, annual growth	-2.7%	2.6%	1.0%	-1.2%	5.5%
RPP-adjusted per capita income as % of US	97.4%	93.8%	98.6%	98.6%	96.6%
Nonfarm employment, annual growth	-6.0%	2.9%	4.1%	2.5%	2.7%
Financial performance					
Available balance as % of own-source revenue	23.7%	26.5%	37.9%	47.3%	27.2%
Net unrestricted cash as % of own-source revenue	68.2%	74.4%	79.3%	86.6%	63.0%
Leverage					
Total long-term liabilities as % of own-source revenue	270.0%	274.0%	217.2%	189.5%	155.0%
Adjusted fixed costs as % of own-source revenue	11.5%	10.0%	7.4%	10.1%	6.6%

Source: Delaware's audited financial statements, US Bureau of Economic Analysis, US Bureau of Labor Statistics and Moody's Ratings

Profile

Delaware is the sixth-smallest state in the US, based on its estimated population of just over 1 million. The state's gross domestic product, as of the third quarter of 2023, was about \$94 billion.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody.com> for the most updated credit rating action information and rating history.

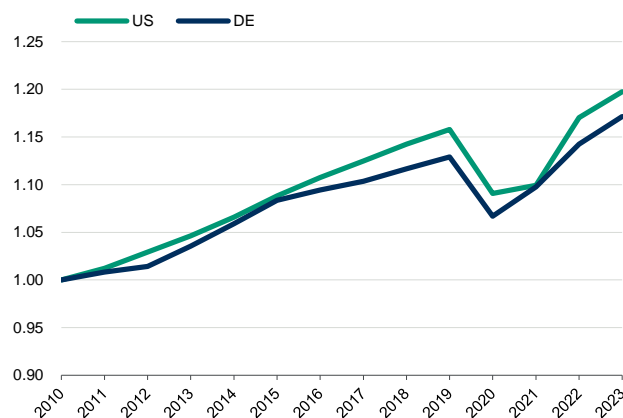
Detailed credit consideration

Economy

Employment and income in Delaware have tracked fairly close to the US, and Delaware's steady population growth will continue to support economic stability. The state stands out among its mid-Atlantic peers in terms of resident growth. It's true that a good portion of the state's growth represents retirees moving to the state to take advantage of a beneficial tax environment. But over the same period, the state has also seen above-state-average growth in its prime working age population.

Exhibit 3

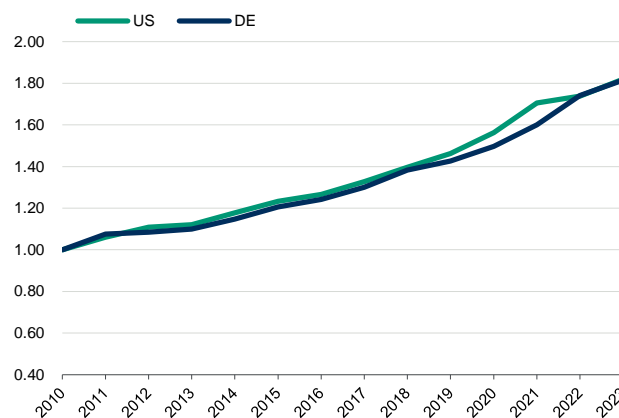
Annual nonfarm employment relative to 2010



Source: US Bureau of Labor Statistics

Exhibit 4

Annual personal income relative to 2010



Source: US Bureau of Economic Analysis

Exhibit 5

Population growth in select states

	Total population growth, 2010-22	Rank among states	Prime working age population growth, 2010-22	Rank among states
Delaware	13.2%	12th	1.7%	19th
North Carolina	11.8%	14th	4.7%	16th
District of Columbia	11.1%	16th	15.5%	4th
Virginia	8.2%	19th	0.0%	22nd
Maryland	6.4%	24th	-2.0%	30th
New Jersey	5.1%	30th	-3.2%	44th
Pennsylvania	2.0%	44th	-4.4%	38th

Source: US Census Bureau and Moody's Ratings

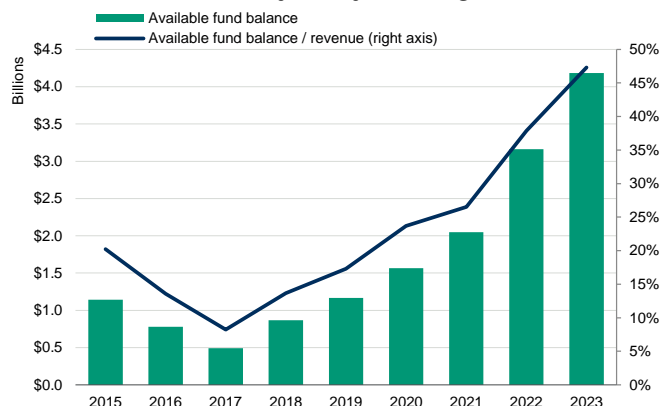
Delaware's business-friendly laws and regulations make it a haven for corporations looking to incorporate, and many large companies call the state home as a result. This comparative advantage relative to other states and the ability to tax these entities is one thing that helps keep Delaware's resident tax burden low relative to neighboring states. But it also injects some volatility in the state's economy. According to Moody's Analytics, financial company payrolls as a share of total payroll are the highest in Delaware among all states. Decreased demand for loans in the current higher interest rate environment has held employment in the state's banking sector back.

The state has seen strong employment gains in leisure and hospitality, another sector with outsize employment in Delaware given the state's coastal location. Other key drivers in the state's economy include chemical and pharmaceutical manufacturing.

Financial performance

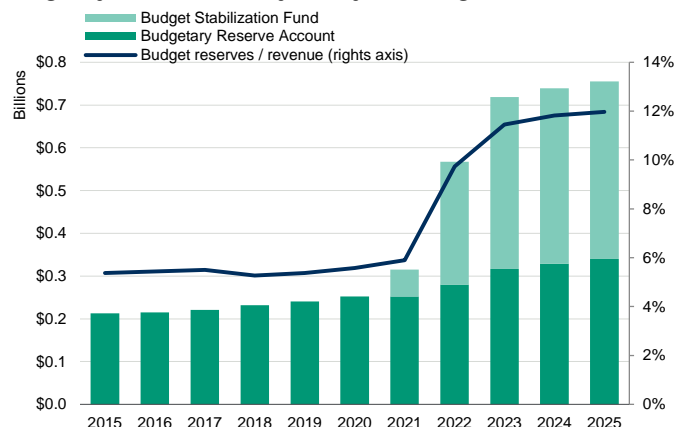
Delaware's finances will remain strong. On a GAAP basis, Delaware reported further growth in available fund balance in fiscal 2023 (the latest year of audited financial statements). The state also added to formal budget reserves in fiscal 2023. Those budget reserves comprise a portion of the state's larger GAAP-basis fund balance.

Exhibit 6

GAAP-basis fund balance, by fiscal year ending June 30

Source: Delaware's audited financial statements and Moody's Ratings

Exhibit 7

Budgetary-basis reserves, by fiscal year ending June 30

2024 figures projected by state; 2025 figures included in executive budget proposal
Source: State of Delaware and Moody's Ratings

The state is on pace to add to budgetary reserves in fiscal 2024, while potentially spending excess unencumbered cash on nonrecurring items, which was incorporated in the enacted budget. As with recent budgets, the governor's proposed fiscal 2025 budget keeps recurring spending below projected revenue, increases budgetary reserves in line with statutory limits, and allocates surplus funds to capital investments.

Delaware adheres to a strong limit on appropriations. The state can only appropriate 98% of estimated available funds (sum of general fund revenue and unencumbered cash outside of the budgetary reserve account), and this can only be waived with approval of three fifths of the legislature. This limit creates a buffer against revenue underperformance.

Strong reserves and budget planning mitigate potential volatility in state revenue. Delaware is the preferred legal home for publicly traded companies and is dependent on taxes it levies on businesses. The state derives more than 40% of its general fund revenue from potentially volatile taxes on businesses. The two largest components of business-related revenue are franchise taxes levied on corporations based in the state and abandoned property revenue.

Liquidity

Delaware's liquidity is very healthy (see Exhibit 2 above) and the state reports most of its pooled cash and investments in its general fund.

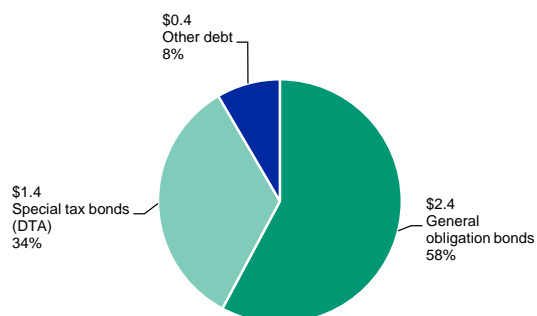
Leverage

Delaware's long-term liabilities, relative to revenue, will remain higher than the median for states going forward. However, the state's leverage remains well below that of the most heavily burdened states, and fixed costs remain manageable.

General obligation bonds account for nearly two-thirds of Delaware's outstanding debt, while unfunded post-employment benefits liabilities comprise a much larger share of total leverage. Delaware's pension and other post-employment benefits (OPEB) burdens account for all assets and liabilities of plans covering employees of local school districts, which is not the case for all states. We discuss in more detail below the state's recent approach of setting aside additional funds for its outstanding OPEB liabilities.

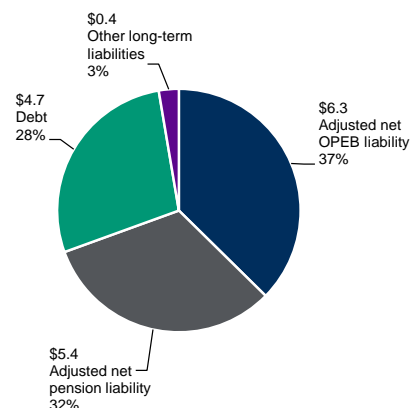
Aside from general obligation bonds, state debt mostly consists of bonds issued by the Delaware Transportation Authority, a component of the Delaware Department of Transportation. The state has a small amount of debt outstanding paid from annual appropriations of the legislature. The state's general obligation bonds include about \$500 million of bonds paid with school district property taxes. The state accounts for the property taxes in its audited financial statements and, because the taxes are part of the state's revenue base, we include these bonds in our calculation of state debt.

Exhibit 8
Composition of Delaware's debt
(\$billion)



Source: State of Delaware and Moody's Ratings

Exhibit 9
Composition of Delaware's long-term liabilities
(\$billion)



Source: State of Delaware and Moody's Ratings

Legal security

Exhibit 10 below details the legal security associated with each type of bond shown in Exhibit 1 above.

Exhibit 10

Security of Delaware's debt obligations

Type of debt	Legal security
General obligation	Full faith and credit obligations backed by the authority to levy taxes without limitation as to rate or amount
Appropriation - sustainable energy	Installment payments made by state agencies to the Delaware Sustainable Energy Utility, Inc., a nonprofit corporation created by the state. State agencies make payments from funds appropriated by the state
Special tax - DTA transportation system	Senior claim on Transportation Trust Fund into which the state deposits certain taxes, tolls and fees
Special tax - DTA US 301 revenue	Senior lien on US 301 tolls plus subordinated claim on the Transportation Trust Fund
Special tax - DTA US 301 TIFIA loan	Subordinated lien on US 301 tolls plus further subordinated claim on the Transportation Trust Fund
Special tax - DTA GARVEEs	Federal highway grants

Source: State of Delaware and Moody's Ratings

Debt structure

All of Delaware's debt is fixed rate.

Debt-related derivatives

The state is not party to any debt-related derivative agreements.

Pensions and OPEB

Delaware's fiscal 2023 fixed costs were close to 10% of its own-source revenue, which consists of all governmental revenue and transportation revenue less federal revenue. Fixed costs consist of debt service, pension contributions and payments of other postemployment benefits (OPEB). For the pension contribution, we calculate a pension "tread water" indicator, which is an estimate of the payment to a government's pension plans that keeps reported net pension liabilities from growing, assuming other actuarial assumptions hold. Delaware has historically contributed above the "tread water" level to its pension systems.

By executive order, the governor created a Delaware Retirement Benefit Study Committee in 2020 and tasked it with identifying options for reducing the state's unfunded OPEB liability. The committee issued its first report in November 2021, which, among other things, included a recommendation to pre-fund retirement healthcare benefits from available surplus revenue.

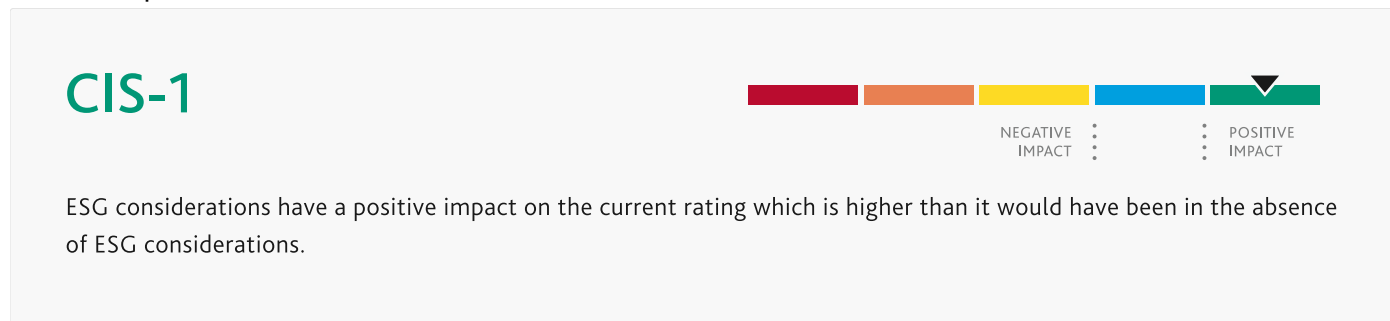
The state's fiscal 2023 and 2024 budgets included pre-funding contributions to the OPEB trust, and the governor's proposed fiscal 2025 budget does as well. Though the state's present approach to addressing this liability is to increase annual contributions to the trust, it is possible that future action could include revisions to benefits given the lack of constitutional protection of retiree healthcare benefits in the state.

ESG considerations

Delaware (State of)'s ESG credit impact score is CIS-1

Exhibit 11

ESG credit impact score



Source: Moody's Ratings

Delaware's ESG Credit Impact Score is positive (**CIS-1**) reflecting its moderately negative environmental risks, neutral-to-low social risks and a positive governance profile.

Exhibit 12

ESG issuer profile scores



Source: Moody's Ratings

Environmental

Delaware's E issuer profile is moderately negative. Delaware's small size and location on the Atlantic Ocean raises its exposure to flood and storm risk relative to many states. Delaware and its local governments are primarily exposed to cyclone risk. According to data of the US Bureau of Labor Statistics, close to 12% of statewide wages are earned in hurricane storm surge flood zones, though nearly 40% of this exposure is located in zones vulnerable only to the highest category of storm. Delaware is actively managing coastline development and we expect the state's significant credit strengths mitigate exposure to environmental risks.

Social

Delaware's S issuer profile is neutral-to-low. Delaware's population trends remain stable and employment and income are growing, albeit slightly more slowly than the US overall. Support for health services by the federal government, mainly through Medicaid grants, represents a vulnerability for states and Delaware is no exception. Delaware is no more vulnerable to federal funding decisions in this regard than most states.

Governance

Delaware's G issuer profile reflects legal and governance provisions that will encourage the state to maintain a strong financial profile over a long period. The DEFAC, a panel of 31 gubernatorial appointees, provides the state's revenue estimates and calculates its

spending authority. This panel, which includes officials from the public and private sector, meets five times each year and issues revenue and expenditure forecasts used by both the executive and legislative branches of government during the budget process.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

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 13

Delaware (State of)

	Measure	Weight	Score
Economy			
Resident Income (PCI Adjusted for RPP / US PCI)	98.6%	15%	Aa
Economic Growth (5-year CAGR real GDP - 5-year CAGR US real GDP)	-1.1%	15%	A
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)	189.5%	20%	Aa
Fixed-costs ratio (adjusted fixed costs / own-source revenue)	10.1%	10%	Aa
Notching factors			
Very limited and concentrated economy	-		
Scorecard-Indicated Outcome			Aa1
Assigned rating			Aaa

Source: Delaware's audited financial statements, US Bureau of Economic Analysis, US Bureau of Labor Statistics and Moody's Ratings

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