S&P Global Ratings

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Delaware; Appropriations; General Obligation

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Credit Profile		
US$286.77 mil GO bnds ser 2024A due 05/01/2044		
Long Term Rating	AAA/Stable	New
US$68.505 mil GO rfdg bnds ser 2024B due 07/01/2034		
Long Term Rating	AAA/Stable	New
Delaware GO		
Long Term Rating	AAA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AAA' long-term rating to the State of Delaware's approximately $286.8 million general obligation (GO) bonds, series 2024A, and approximately $68.5 million GO refunding bonds, series 2024B.
- At the same time, we affirmed our 'AAA' long-term rating on the state's GO debt outstanding and our 'AA+' long-term rating on the state's appropriation debt outstanding.
- The outlook on all ratings is stable.

Security

Delaware's full faith and credit pledge secures the series 2024 bonds as well as the state's GO debt outstanding. Proceeds will be used to finance various projects in the state's capital program and to refund portions of the series 2014B bonds.

Credit overview

Delaware's demonstrated history of proactive fiscal management and well-embedded strong financial policies underpin the rating. The long-standing practice of at least five Delaware Economic and Financial Advisory Council (DEFAC) meetings per year has allowed the state to remain fiscally strong and build reserves post-pandemic. DEFAC's regular reporting allows the state to adjust revenue expectations and expenditure allocations as needed, resulting in regular general fund surpluses. The state has been able to maintain a high level of liquidity, and it expects to close fiscal 2024 with another surplus. Through December 2023, these positive fiscal outcomes have also allowed the state to build a $410.1 million budget stabilization fund (BSF) and maintain a fully funded $328.7 million "rainy day" fund, or a very strong 11% of fiscal 2024 expenditures.

The governor's presented $6.1 billion fiscal 2025 general fund budget continues to build on these strengths, appropriating less than 98% of DEFAC-determined available revenues, continuing to fully fund the rainy day fund at 5.0% of general fund operating expenditures, and keeping the BSF at more than 5% of gross revenues while maintaining the fund at $410.1 million. These reserve balances remain at an all-time high nominal level, and the state does not expect to draw upon them in fiscal 2025.

The 'AAA' rating on Delaware's GO bonds also reflects our view of the state's:

- Strong economy that continues to diversify,

- Strong and resilient budgetary performance, and
- Moderate debt with rapid amortization and overall strong funding and governance of pension liabilities.

We believe these strengths are partially offset by credit pressure stemming from the state's unfunded other postemployment benefits (OPEB) liabilities, which we consider significant. As of June 30, 2023, the state's $8.04 billion share of the net OPEB liability is among the largest in the nation on a per capita basis, at $7,192, though less than the near $9,500 per capita in fiscal 2020. The state has been looking at ways to manage this liability and in fiscal 2023 and fiscal 2024 allocated 1% of the previous year's extraordinary revenues into the OPEB trust fund. This 1% carveout is again included in the governor's fiscal 2025 budget proposal and would contribute an additional $56 million to the fund, which the state estimates would increase the OPEB funded ratio to around 9%. The implementation of these and other pension and OPEB reforms over the past two decades demonstrates the state's efforts to address long-term liabilities through legislative actions. We believe the state's history and ability to pass and implement retirement reforms positions Delaware well, compared with many other states without such flexibility.

The governor's fiscal 2025 budget proposal represents 8.3% growth over the adopted fiscal 2024 budget, reflecting both inflationary costs and continued revenue collection surpluses. The proposed budget complies with all state budget stabilization requirements and is balanced. DEFAC's estimates as of March 2024 show slightly higher fiscal 2025 revenue compared with estimated fiscal 2024. The DEFAC forecast for fiscal 2026 continues a recent trend of growth, with revenues now expected to increase 2.0% compared with fiscal 2025 projected revenues. We expect the budget will be adopted before the start of the fiscal year, but the May DEFAC meeting could influence this, should estimates change.

Delaware faces several lawsuits about its claim to certain unclaimed properties. In February 2023, the U.S. Supreme Court decided in favor of litigants regarding an unclaimed property case surrounding check products. A special master has been remanded by the court to determine damages, and the state is working through the court system to resolve the claims. The state's potential exposure could exceed $300 million. The state reports it has considered this potential exposure in its revenue forecasts and reserve levels, and should it be made to pay the full amount, current liquidity would not be meaningfully limited.

Based on the analytic factors that we evaluate for states, we assigned a total score of '1.5' to Delaware under our state ratings methodology, in which '1.0' is the strongest score and '4.0' the weakest. This score corresponds to a 'AAA' GO rating.

Environmental, social, and governance

We believe the state's physical risks have an overall neutral influence on our credit ratings but, given its geographical exposure to ocean storms and river flooding, could increase infrastructure costs and potentially disrupt tourism. Delaware has a climate action plan focusing on reducing greenhouse gases and maximizing resilience to climate change and considers these risks within the capital plan. We consider Delaware's social and governance risks to be generally neutral to our credit rating analysis. Despite having a higher-than-average age dependency ratio, Delaware is managing any associated cost risk and is benefiting from population growth.

Outlook

The stable outlook reflects our view of Delaware's strong fiscal management that has allowed the state to proactively manage its budgets through various economic cycles and has been key to the state's long-term credit stability, and our anticipation that this will continue during the two-year outlook time frame.

Downside scenario

We could lower the rating if the state's budget or reserve profile were to be challenged, or if worsening trends in retiree health care liabilities increase its OPEB liabilities to a level that is not commensurate with the rating.

Credit Opinion

Debt and liability profile

The state limits tax-supported debt authorized in any given year to no more than 5% of estimated general fund revenue. This, coupled with clearly defined debt affordability parameters, rapid amortization (more than 80% within 10 years), and a commitment to cash-funding capital projects, when available, will contribute to a stable debt profile. Total tax-supported debt in fiscal 2023, including GO, transportation, and appropriation obligations, is moderately high compared with that of state peers, at $2,717 per capita and 4.2% of personal income. Factoring in this issuance, debt per capita increases slightly to $3,061. Delaware pays 60%-80% of the cost of capital improvements for public school districts on approval of such costs; the school districts pay the remaining portions supported by local property taxes. State-supported GO debt was $1.7 billion as of June 30, 2023, excluding $660.8 million that the local school districts support. Delaware has no variable-rate debt outstanding, and it has not entered into any interest-rate swap agreements or related derivative transactions.

Strong pensions offset by weak OPEB funding

Delaware's pensions are well funded compared with those of other states, with what we consider a strong funded ratio. As of June 30, 2023, the combined funded ratio across the five pension plans for which the state reports liability has declined to 94% from 108% in 2021 but improved from 87% in 2022. State contributions to four of its five pension plans are determined on an actuarial basis, with contributions historically meeting 100%, which we view positively. The closed state police plan is funded on a pay-as-you-go basis. We also note that aggregate annual plan contributions for the pension system exceeded our calculation of minimum funding progress or amounts necessary for the plans to cover a portion of the amortization in unfunded liability, as well as certain cost drivers of the annual change in the liability.

Credit risks reside in the future treatment of funding OPEB obligations, as this liability is larger than that of peers. We believe Delaware's ability to pass and implement reforms will remain important in supporting the state's credit profile. The state offers retiree health care benefits through a cost-sharing, multiple-employer, defined-benefit plan administered by the Delaware Public Employees' Retirement System. Coverage is available to retirees and eligible dependents covered under the state employees', new state police, judiciary, and closed state police pension plans.

On a four-point scale, where '1.0' is the strongest, S&P Global Ratings assigned an overall score of '2.1' to Delaware's debt and liability profile.

Economic stability through the forecast

Overall economic performance has been stable historically, in our view, and this will likely continue. Personal income, employment gains, and economic growth are forecast to be approximately in line with national rates through 2027, according to S&P Global Market Intelligence. There has been diversification within the state's economic sectors in recent years. High tech, chemical, and distribution companies are expanding in the state, with multiple companies expecting to increase employees by 400-500. For 2023, Delaware's unemployment rate was 4.0%, slightly higher than the 3.6% national average, and we expect the state's unemployment will be in line with the national average over the next couple of years.

Currently, S&P Global Ratings' economists are forecasting steady U.S. real GDP growth of 2.5% in 2024, based on the sturdy labor market, and still expecting the economy to transition to slightly below-potential growth in the next couple of years. Overall, we expect inflation will remain above the Fed's 2% target through 2024, primarily reflecting persistently higher service price inflation. We expect the real GDP growth to be 1.5% in 2025 and 1.7% in 2026. For more information, see "Economic Outlook U.S. Q2 2024: Heading For An Encore," published March 26, 2024, on RatingsDirect. On a four-point scale, where '1.0' is the strongest, S&P Global Ratings assigned an overall score of '1.9' to the state's economic factors.

Strong financial management a hallmark of the 'AAA' rating

The state's financial management highlights include regular general fund revenue and expenditure reports, multiyear revenue forecasting, a formal general fund reserve policy, and formal statutory debt affordability issuance guidelines. The state has implemented various debt management policies to decrease its debt burden and limit bond issuance. These measures have reduced Delaware's debt, despite the broad role the state maintains in funding capital requirements for education, transportation, and corrections.

On a four-point scale, where '1.0' is the strongest, S&P Global Ratings assigned an overall score of '1.0' to Delaware's financial management.

Fiscal performance shows increasing flexibility

Delaware posted a record $941 million general fund operating surplus (14.3% of general fund expenditures) as of June 30, 2023, following a $1.2 billion surplus (20.4% of expenditures) on June 30, 2022. This is the sixth consecutive net general fund result above 7.0% of expenditures. When incorporating other sources and uses of financial resources, the state's general fund finished fiscal 2023 with a total fund balance of $4.3 billion, a 28% increase from $3.3 billion in fiscal 2022. Within this total, Delaware's unassigned fund balance was $2.7 billion.

On a four-point scale, where '1.0' is the strongest, S&P Global Ratings assigned an overall score of '1.2' to Delaware's budgetary performance.

Government framework

In our opinion, Delaware has a strong government framework. Due to well-established policies, the state has maintained what we view as a solid financial position, especially during recessionary periods, including the recent recession.

On a four-point scale, where '1.0' is the strongest, S&P Global Ratings assigned an overall score of '1.4' to Delaware's government framework.

Delaware's varied credit strengths and independent treasury function allow a rating above the U.S. sovereign

Delaware's bonds are eligible to be rated above the sovereign because we believe the state can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, "Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions" (published Nov. 19, 2013), U.S. states are considered to have moderate sensitivity to country risk. State-derived revenues are the sole source of security on the bonds, and the institutional framework in the U.S. is predictable, with significant state autonomy and flexibility.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of April 19, 2024)		
Delaware GO		
Long Term Rating	AAA/Stable	Affirmed
Delaware GO		
Long Term Rating	AAA/Stable	Affirmed
Delaware GO		
Long Term Rating	AAA/Stable	Affirmed
Sustainable Energy Utility Inc., Delaware		
Delaware		
Sustainable Energy Util, Inc. (Delaware) APPROP		
Long Term Rating	AA+/Stable	Affirmed