

**New Issue: MOODY'S ASSIGNS Aaa RATING TO DELAWARE'S \$255 MILLION GENERAL OBLIGATION BONDS**

Global Credit Research - 08 Oct 2010

**STABLE OUTLOOK APPLIES TO CURRENT ISSUE AND MORE THAN \$2.28 BILLION IN NET TAX-SUPPORTED DEBT OUTSTANDING**

State  
DE

**Moody's Rating**

<b>ISSUE</b>	<b>RATING</b>
General Obligation Bonds, Series 2010B	Aaa
<b>Sale Amount</b>	\$100,000,000
<b>Expected Sale Date</b>	10/18/10
<b>Rating Description</b>	General Obligation
General Obligation Bonds, Series 2010C (Federally Taxable - Build America Bonds)	Aaa
<b>Sale Amount</b>	\$100,000,000
<b>Expected Sale Date</b>	10/18/10
<b>Rating Description</b>	General Obligation
General Obligation Bonds, Series 2010D (Federally Taxable- Qualified School Construction Bonds)	Aaa
<b>Sale Amount</b>	\$55,000,000
<b>Expected Sale Date</b>	10/18/10
<b>Rating Description</b>	General Obligation

**Opinion**

NEW YORK, Oct 8, 2010 -- Moody's Investors Service has assigned Aaa ratings to the State of Delaware's \$100 million General Obligation Bonds, Series 2010B, \$100 million General Obligation Bonds, Series 2010C (Federally Taxable - Build America Bonds) and \$55 million General Obligation Bonds, Series 2010D (Federally Taxable - Qualified School Construction Bonds). The tax exempt bonds (Series 2010A) are expected to price the week of October 18, with the taxable series expected to sell immediately thereafter. Proceeds of all three series will fund various capital projects; a refunding component may be added to the tax-exempt series pending market conditions.

**RATINGS RATIONALE**

The highest rating assigned to the state's general obligation debt is based on strong financial management characteristics and a history of maintaining ample budgetary reserves throughout recent economic cycles.

**CREDIT STRENGTHS**

- \* Strong financial management and fiscal policies, including frequently updated revenue forecasts and conservative budgeting
- \* Healthy pension funded status
- \* Proactive management of declining revenues

**CREDIT CHALLENGES**

- \* Economic recession leading to declines in revenues and increasing expenditure needs
- \* Large debt burden relative to population and income
- \* Exposure to further consolidation or downsizing in the financial services industry

**HIGHEST RATING REFLECTS FINANCIAL MANAGEMENT STRENGTHS**

The highest rating level assigned to Delaware's general obligation bonds is based in large part on legal provisions that Moody's believes will lead the state to maintain a strong financial profile over a long period. Delaware's constitution requires the state to budget expenditures at 98% of available resources, which helps maintain budgetary balance. There is also a constitutional mandate that unencumbered budgetary general fund resources, as much as 5% of general fund revenue in any fiscal year, be transferred to a budget reserve (Rainy Day Fund). This funding may be accessed only by a three-fifths vote of the members of each house and may be used only to close a general fund deficit or to provide funds needed as a result of the enactment of legislation reducing revenue. The Rainy Day Fund is currently fully funded, at over \$186 million. It has never been used, and the state at this time does not plan to use it.

Revenue estimates are made by a 34-member panel appointed by the governor, known as the Delaware Economic and Financial Advisory Council (DEFAC). This panel, which includes officials from the public and private sectors, meets six times per year and issues revenue and

expenditure forecasts that are used by both the executive and legislative branches of government during the budget process. These provisions for consensus forecasts, well-managed expenditure growth, and a limit on appropriations have led to the state's long-term prospects for sustained financial strength. Delaware's otherwise strong management profile is tempered by a constitutional requirement that tax increases be approved by a three-fifths majority in the legislature.

#### 2011 REVENUES SLIGHTLY AHEAD OF BUDGET TO DATE

The fiscal 2011 operating budget totals \$3.3 billion, representing 6.9% growth over the prior year (budget to budget). The budget reflects growing Medicaid costs (approximately \$100 million) and a \$110 million decline in federal stimulus funding (to \$123.5 million). These pressures were offset with nearly \$50 million in budget cuts. Additionally, the budget assumed modest revenue growth (2% overall) driven by projected 14% growth in personal income tax collections, offset by flat to declining projected receipts on other revenue sources. Favorably, the budget did not anticipate extension of enhanced FMAP funding from the federal government. The state received nearly \$75 million from the stimulus extension, which is expected to be rolled forward to fiscal 2012.

The state's current revenue forecast (September) projects revenues in excess of budget estimates by 2% (\$63 million), reflecting continued weak personal income tax collections (12%, or \$14.8 million below budget estimate), offset by over-performance of business-related receipts and other revenue lines.

#### 2010 BUDGET SOLVED GAP WITH RECURRING SOLUTIONS

For fiscal year 2010, the state had to find solutions for a gap of \$800 million, which represents 25% of General Fund revenues. Measures taken to close the gap included spending cuts (over \$300 million), federal stimulus funds (over \$233 million), and almost \$200 million in new revenues. Of the new revenues, the state enacted tax increases and changes through a broad spectrum of taxes and sectors, including personal income taxes, cigarette taxes, public utility taxes, and the sports lottery. Unaudited results for fiscal 2010 indicate revenues in line with budget overall. The state did not need to utilize its Rainy Day Fund in 2010. The fund is projected to be fully funded at \$186.4 million as of year-end fiscal 2010.

The Professional and Amateur Sports Protection Act of 1992 exempts Delaware (as well as Nevada, Montana, and Oregon) from the ban of organized betting on sporting events; accordingly, Delaware planned to implement a sports lottery to increase revenues. The National Football League (NFL) sued the state on the grounds that the sports lottery wasn't constitutional; an appellate court decided to limit Delaware's sports lottery to parlay betting (a single bet that links several individual bets and is dependent on all bets winning together) on NFL games, which is operated out of the state's three racino locations. Additionally, in January 2010, the state passed legislation to allow table games at its racinos, which were operational at all three locations by May 31, 2010.

#### ECONOMY SEEING EFFECT OF NATIONAL DOWNTURN

Delaware recovered more quickly from the 2001 recession than many other states. When the national economy returned to a job-creation mode in 2004, Delaware's non-farm employment growth rate was significantly faster, at 2.2% versus a 1.1% national pace. The rebound was enough for Delaware to surpass its pre-recession peak total non-farm employment level.

The Delaware labor market has performed better than the nation in recent months. The state's 8.4% unemployment rate for August 2010 was below the 9.6% national rate, and the state posted modest 1% year over year employment growth in both July and August. Housing indicators are down, however, with July and August year over year declines in housing starts and housing permits exceeding national averages. Moody's Economy.com, however, is expecting that the state's economic recovery will modestly outperform the nation.

#### DEBT BURDEN HAS GROWN AT PACE BELOW 50-STATE MEDIAN

Delaware's debt burden is high relative to other states, with net tax-supported debt of \$2,489, a 17% increase compared with \$2,128 one year earlier. In comparison, the national median net tax-supported debt per capita increased by 8% during this period. Delaware's debt amounts to about 6.2% of the state's personal income, based on the 2010 Debt Medians Report. This puts Delaware sixth in the ranking of the states for this measure. The state's relatively high debt burden reflects its role in financing facilities, such as schools and prisons, which in other states would receive capital through local entities. A 1991 state law imposes several constraints on Delaware's debt, including a requirement that in any fiscal year the state can only authorize new debt equal to as much as 5% of budgetary general fund revenue projected for the year. Although these limits appear fairly generous, the state's debt burden has decreased since they were enacted. The state has no outstanding variable rate debt.

#### HEALTHY FUNDING LEVELS FOR MAIN PENSION PLAN

Delaware benefits from a well-funded pension system. The Delaware Employees Pension Plan is 96% funded (as of the end of fiscal year 2010). To address other post-employment benefits (OPEB) liabilities (estimated at \$5.6 billion), the state created a dedicated trust for OPEB-related payments. \$95 million had accumulated in the fund as of August 31, 2010.

#### Outlook

The outlook for Delaware is stable. The combination of the state's strong structural governance features (including frequent revenue forecast revisions), speedy actions to deal with downward revenue revisions, the use of recurring solutions to solve gaps, a low-risk debt profile and high pension funding ratio will result in the state coming out of this recession in a strong position relative to its peers.

What could move the rating--DOWN:

- o Significant increase in debt levels relative to the economy
- o Significant economic contraction that is worse than most states
- o Erosion of trend of strong financial management

The last rating action with regard to the State of Delaware was on April 30, 2010 when a Aaa rating was assigned to the state's General Obligation Bonds, Series 2010A.

The principal methodology used in rating the State of Delaware was Moody's State Rating Methodology, rating methodology published in November 2004. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found on

Moody's website.

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