MOODY'S INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS Aaa RATING TO DELAWARE'S $275 MILLION GENERAL OBLIGATION BONDS

Global Credit Research - 20 Oct 2011

STABLE OUTLOOK APPLIES TO CURRENT ISSUE AND MORE THAN $2.2 BILLION IN NET TAX-SUPPORTED DEBT OUTSTANDING

State
DE

Moody's Rating

ISSUE		RATING
General Obligation Bonds, Series 2011A		Aaa
Sale Amount	$225,000,000	
Expected Sale Date	11/03/11	
Rating Description	General Obligation	
General Obligation Bonds, Series 2011B		Aaa
Sale Amount	$50,000,000	
Expected Sale Date	11/03/11	
Rating Description	General Obligation	

Opinion

NEW YORK, Oct 20, 2011 -- Moody's Investors Service has assigned Aaa ratings to the State of Delaware's General Obligation Bonds, Series 2011A and 2011B. The 2011A bonds are expected to have a par amount of approximately $225 million, and proceeds will fund various capital projects. The 2011B bonds are expected to have a par amount of approximately $50 million (preliminary and subject to change), and will refund other general obligation bonds for savings in each year. The bonds are expected to price the week of October 31.

SUMMARY RATING 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.

STRENGTHS

* Strong financial management and fiscal policies, including frequently updated revenue forecasts and conservative budgeting

* Healthy pension funded status

* Proactive management

CHALLENGES

* Economic recession caused declines in revenues and increasing expenditure needs

* Large debt burden relative to population and income

* Potential exposure to further consolidation or downsizing in the financial services industry

DETAILED CREDIT DISCUSSION

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.

FISCAL 2012 BUDGET REFLECTS INCREASED MEDICAID AND PENSION COSTS

The fiscal 2012 General Fund operating budget totals $3.5 billion, or 6.1% over the prior year. The budget reflects growing Medicaid costs and pension costs (pension expenditures grow by over 8% in 2012). These spending pressures were somewhat offset by the fact that the state preserved some federal assistance (approximately $82 million) received in fiscal year 2011 for use in 2012. General Fund revenues are expected to show a decline of approximately 4.3% in 2012, which includes certain tax cuts. The state lowered the top personal income tax rate effective January 2012, and also lowered the rate on the gross receipts tax, the public utility tax, and the bank franchise tax.

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 state's 8.1% unemployment rate for August 2011 was below the 9.1% national rate, and the state posted small employment declines of 1% in August compared to the prior August. Housing starts in August were up 14.8%, compared to a decline of 5.8% for the nation. Moody's Analytics 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 per capita of $2,676, compared to the national median net tax-supported debt per capita of $1,066. Delaware's debt amounts to about 6.8% of the state's personal income, based on the 2011 Debt Medians Report. This puts Delaware fifth 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). The state recently enacted pension reforms, including increasing the employee contribution for new hires and raising the retirement age.

To address other post-employment benefits (OPEB) liabilities (estimated at $5.6 billion), the state created a dedicated trust for OPEB-related payments. The fund had $130 million as of August 31, 2011. The state also has increased the time it takes to vest for retiree health care, which lowers the liability.

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 MAKE THE RATING GO DOWN

o Significant increase in debt levels

o Significant economic contraction that is worse than most states

o Erosion of trend of strong financial management

The principal methodology used in this rating was Moody's State Rating Methodology published in November 2004. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

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