S&P Global
Ratings

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Summary:

Oregon; Appropriations; General Obligation

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Credit Profile		
US$309.075 mil GO bnds (Article Xi-q State Projs Tax-exempt) ser 2019A dtd 02/20/2019 due 06/30/2044		
Long Term Rating	AA+/Stable	New
US$149.365 mil GO bnds (Article Xi-m, Xi-n, And Xi-p State Grant Programs (tax-exempt)) ser 2019D due 06/30/2039		
Long Term Rating	AA+/Stable	New
US$40.22 mil GO bnds (Article Xi-q State Projs (federally Taxable) Sustainability Bnds) ser 2019B due 06/30/2039		
Long Term Rating	AA+/Stable	New
US$19.635 mil GO bnds (Article Xi-q State Projs (federally Taxable) ser 2019C due 06/30/2034		
Long Term Rating	AA+/Stable	New
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to the following bonds issued by the state of Oregon:

- Series 2019 A (Article XI-Q state projects bonds);
- Series 2019 B (Article XI-Q, federally taxable state projects bonds);
- Series 2019 C (Article XI-Q federally taxable state projects bonds); and
- Series 2019 D (Article XI-M, XI-N, and XI-P state grant programs bonds).

At the same time, we affirmed our 'AA+' rating on the state's general obligation (GO) bonds and our 'AA' rating on its appropriation-backed (certificates of participation [COPs]) debt outstanding. We rate the state's appropriation debt one notch lower than the state's general creditworthiness to reflect the appropriation risk associated with the annual payment. We view these bonds as having a strong relationship to the obligor. These obligations provide funding for projects we believe are significantly important to the obligor. The state also has an established track record of appropriating for resources necessary to satisfy debt service. In our opinion, there is no unusual political, timing, or administrative risk related to the debt payment. The outlook is stable.

The 'AA+' rating reflects our view of the state's:

- Demonstrated willingness to make revenue and expenditure adjustments to correct structural imbalances when they arise;
- Constitutional and statutory mechanisms to build rainy day funds and currently strong budget reserve levels;
- Strong financial policies and practices, including institutionalized quarterly reviews of financial performance and economic forecasts to guide budget assumptions; and

- Relatively good pension-funded ratio and other postemployment benefits (OPEBs) that represent a low risk, albeit with a growing pension liability, in our opinion.

Partly offsetting those strengths are what we consider:

- Oregon's propensity for revenue volatility given general fund dependence on personal income taxes (PIT), albeit with demonstrated stability in recent years; and
- An active citizen initiative process that can restrict budgetary flexibility, in particular the state's constitutional "kicker" provision, which generates rebates for taxpayers if PIT revenue growth exceeds the state's revenue forecasts by 2%. Most recently, the state's kicker was triggered for tax year 2017, resulting in estimated rebates of roughly $464 million. Estimates for the current biennium are for the PIT kicker to be $724 million.

The 2019 bonds are GOs of the state and are secured by its full faith and credit and taxing power. Proceeds will be used to fund capital projects.

Budgetary and economic update

According to Oregon's Office of Economic Analysis (OEA), which forecasts state revenues on a quarterly basis, the December 2018 revenue forecast reflects a minor bottom-line change in estimated revenues for the current biennium, relative to the September forecast. All told, the updated forecast reflects a $60.3 million (0.3%) upward bump from the previous forecast. Relative to the close-of-session forecast, gross general fund revenues have been revised up by $954 million (4.88%), largely reflecting strong personal and corporate income tax collections. Net general fund revenues for the biennium are now forecasted to be modestly higher than the close-of-session estimate by approximately $1.18 billion to $21.23 billion, reflecting changes to offsets and transfers, administrative actions, and legislative actions. Given current projections, the state's personal and corporate income tax kickers are anticipated to again be triggered by biennium's end. Personal income tax credits—estimated at $724 million--would be reflected in Oregonians' tax returns in 2020. The estimated $230 million corporate income tax kicker would be diverted to K-12 education spending. In our view, the changes in the forecast and actual collections are relatively modest compared to our last review, and remain credit neutral.

Based on Oregon's latest forecast and assuming no additional budget changes, the state projects reserve balances in the education stability and rainy day funds to total $1.2 billion, which, coupled with a general fund balance of approximately $1.3 billion, would give a combined $2.52 billion, or about 12.3% of two years' general fund appropriations or nearly 25% on an annualized basis, which we consider strong. Should the personal income tax kicker be triggered, as expected, effective total reserves would total roughly $1.8 billion, or 9% of biennial revenues—given that credits would be made in the subsequent biennium. The expected reserves and ending balances will be the highest levels in recent history and are up notably from fiscal 2011, when reserves represented about 0.5% of general fund expenditures.

Fueling the state's strong revenue growth has been the pace at which the economy has expanded, with employment gains continuing to grow at a faster clip than that of the nation. Additionally, OEA notes stronger-than-anticipated revenue growth reflects responses to tax law changes, although the stimulus effects are expected to fade within the medium term. Nevertheless, OEA's latest economic forecast continues to predict economic expansion, albeit at a more modest rate, reflecting a maturing economic cycle. The state's employment picture remains relatively unchanged and estimated unemployment is likely to settle at 3.8% in 2019 and 3.9% in 2020, near the expected national level. Personal incomes are estimated to grow 5.4% in 2019 and 2020, beating national estimates of 4.7% and 4.8% in 2019 and 2020, respectively. Due to a tightening labor market, OEA noted that population growth or higher labor participation rates will be necessary to maintain a strong labor market. Consistent with the OEA's previous forecasts, potential downside risks include a national recession or global economic weakness, heightened volatility in financial markets, diminished housing affordability in the state that could dampen relatively strong population growth, and potential voter initiatives.

2019-2021 biennium

In late November 2018, the 2019-2021 Governor's Budget proposal was released. Total combined general fund and lottery revenues came to $23.8 billion, roughly 5% greater than the current legislatively adopted budget supporting $21 billion of expenditures. Of the roughly 14% growth ($2.92 billion) in expenditures relative to the current biennium, roughly half reflects increases in health and human service. Reflecting a roughly 12% increase relative to the current biennium, Governor Brown's proposed budget totals $23.6 billion for the combined general and lottery fund for 2019-2020. The governor's proposal includes about $657 million in general fund offsets for the Oregon Health Authority generated largely by increases in health care system (insurers, hospitals, and employers) related assessments. These additional revenues effectively balance the state's budget by aligning combined revenues with current service-level estimates. Absent these primary revenue enhancers, current service-level expenditures would exceed revenues by slightly more than $600 million. Similar to the current biennium, the projected gap mainly reflects anticipated increases in general fund-supported health care expenditures for both traditional and expanded health care coverage under the current Affordable Care Act framework, principally the shift of federal resources to state resources. Among Governor Brown's legislative priorities is adding significantly more resources to support education programs. Notably, the governor is recommending a nearly 25% ($1.9 billion) increase in education programs above what is estimated to maintain current service-levels for the next biennium. Under the governor's proposed budget, the state's largest appropriations support K-12 education (50% of the budget), human services (27%), and public safety (15%).

Adjusted reserves forecasted for the fiscal 2019-2021 biennium, not including potential general fund available surplus, consist of the following:

- $884 million ending balance in the state rainy day fund; and
- $847.3 million ending balance in the education stability fund.

While both legislative chambers enjoy supermajorities, which reduces the potential for political roadblocks in moving revenue measures forward, the state's fiscal forecast is predicated on continued positive economic conditions, albeit at a slower clip than recent experience. While we do not anticipate it within the next 12 months, S&P Global Ratings, revised its recession probability up to 15%-20% in the next 12-months, from 10%-15%. Within the backdrop of less accommodative monetary policy, a deepening of international trade tensions, and fading federal fiscal stimulus, the outlook beyond the short term appears to have more friction than not, in our view. Therefore, while we have observed generally improving state credit conditions stemming in part from the infusion of late-cycle federal fiscal stimulus (tax cuts and deficit spending) for much of 2018, this may have been a peak in the economic cycle. Regardless, even absent a recession, we expect the pace of economic growth to decelerate in 2019 (see "U.S. State Sector 2019 Outlook: Caution – Slower Speeds Ahead," published Jan. 8, 2019, on RatingsDirect). OEA has also cautioned that economic growth will almost certainly slow going into the next biennium. Accordingly, as the legislature and governor work to develop the state's new biennial budget, we will continue to monitor whether measures to balance its budget are structural in nature with the long term in mind.

We view Oregon's debt burden as moderately high, but it has remained stable within the last couple of fiscal years. The state's tax-supported debt (less debt supported by other pledged nontax revenue) was slightly above $2,000 per capita and 3.7% of gross state product (GSP; for 2017, latest full year available), in our opinion. We consider the tax burden moderately high relative to personal income at slightly above 4%. Tax-supported debt service also represented a moderately high of nearly 5.4% of governmental expenditures in fiscal 2018. Debt amortization is rapid, in our view, with slightly more than 65% of principal amortized over 10 years. We don't expect recent and pro forma debt to change the state's overall credit profile given rapid retirement of existing debt.

Lower investment returns and lower discount rate assumptions resulted in the Oregon Public Employees Retirement System (OPERS) pension funded ratio declining to 82.07% in 2018 from 83.12% in 2017 (expressed as the plan fiduciary net position as a percentage of the total pension liability). The modest change partly reflected the system's reduced assumed investment rate of return to 7.2% from 7.5%, which is reflected in its 2017 valuation. OPERS reported a strong 9.7% money-weighted net return on investment at the end of June 2018. We estimate Oregon's share of the net pension liability for OPERS in fiscal 2018 totaled approximately $3.14 billion, or 1.6% of personal income, which we consider extremely low. The net pension liability was measured as of June 30, 2018, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of Dec. 31, 2016.

Based on the analytic factors described in our criteria, on a four-point scale, in which '1' is the strongest, S&P Global Ratings assigned a composite score of '1.6' to the state. The modest change in the overall composite score to 1.6 from 1.7 reflects an improvement in the state's age dependency ratio which now matches that of the U.S.

Outlook

The stable outlook reflects our view that Oregon's finances are poised to remain strong in the next two years and that currently strong reserves mitigate potential revenue cyclicality. While unlikely within our outlook period, we could raise the rating if there were a lower propensity for revenue volatility due to the state's dependence on income taxes and financial markets, as well as sustained improvement in demographic and income trends. A gradual strengthening of the state's pension discipline, evidenced by total plan contributions matching or exceeding actuarially determined levels as well as estimated annual amortization components. Downside credit risk would likely have economic origins and, in particular, could stem from a sustained downturn in the financial markets, changes in trade policy, or weaker-than-anticipated economies of some of Oregon's international trading partners. Such developments, particularly if they struck when the state already owed taxpayers the kicker-related refund, could strain its budget alignment. Growth in its pension liability and corresponding contribution increases could weigh on the state's budget, although they are currently manageable. A significant depletion of the state's budgetary reserves at a time of economic growth could further lead to downward rating pressure.

Ratings Detail (As Of January 28, 2019)		
Oregon GO bnds ser 2017R dtd 11/01/2017 due 11/01/2037		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds ser 2017T dtd 11/01/2017 due 11/01/2037		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (taxable) ser 2017S dtd 11/01/2017 due 11/01/2032		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (veterans		
Long Term Rating	AA+/A-1+/Stable	Affirmed
Oregon GO bnds (Article Xi-f(1) University Projs)		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (Article Xi-g Comnty Coll Proj) ser 2017K due 08/01/2027		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (Article Xi-g Univ Proj)		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (Article Xi-p Sch Dist Cap Proj)		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (Hgr Ed) ser 2016A due 08/01/2041		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (Hgr Ed) ser 2016B due 08/01/2022		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO bnds (ODOT projs) (Tax-Exempt)		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO VRDB (Veterans Welfare) 1985		
Long Term Rating	AA+/A-1+/Stable	Affirmed
Oregon GO VRDB (Veterans Welfare) 1986		
Long Term Rating	AA+/A-1+	Affirmed
Oregon GO VRDB (Veterans Welfare) 1987		
Long Term Rating	AA+/A-1+	Affirmed
Oregon GO VRDB (Veterans Welfare) 1988B		
Long Term Rating	AA+/A-1+/Stable	Affirmed
Oregon GO (Article Xi-g Comnty Coll Proj)		
Long Term Rating	AA+/Stable	Affirmed
Oregon APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon APPROP		
Long Term Rating	AA/Stable	Affirmed

Ratings Detail (As Of January 28, 2019) (cont.)		
Oregon APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon APPROP (AGM)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/A-1/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/A-1/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon GO (MBIA of Illinois)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Oregon Oregon GO (Vet Welfare)		
Long Term Rating	AA+/Stable	Affirmed
Oregon (Dept of Admin Svcs) certs of part 2003B		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Oregon (Dept of Admin Svcs) certs of part 2004B&C		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Oregon Dept of Admin Svcs, Oregon		
Oregon		
Oregon Dept of Admin Svcs (Oregon) APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon Dept of Admin Svcs (Oregon) APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon Dept of Admin Svcs (Oregon) APPROP		
Long Term Rating	AA/Stable	Affirmed
Oregon Dept of Admin Svcs (Oregon) GO bnds		
Long Term Rating	AA+/Stable	Affirmed
Oregon (Dept of Admin Svcs) certs of part ser 2003A		

Ratings Detail (As Of January 28, 2019) (cont.)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Oregon (Dept of Admin Svcs) certs of part ser 2004A		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Oregon Dept of Energy, Oregon		
Oregon		
Oregon Dept of Energy (Oregon) GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon Dept of Envir Qlty, Oregon		
Oregon		
Oregon Dept of Envir Qlty (Oregon) GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon Dept of Veterans Affairs, Oregon		
Oregon		
Oregon Dept of Veterans Affairs (Oregon) (Veterans Welfare) GO		
Long Term Rating	AA+/Stable	Affirmed
Oregon Dept of Veterans Affairs (Oregon) (Veterans Welfare) GO		
Long Term Rating	AA+/A-1+/Stable	Affirmed
Oregon St Brd of Hgr Ed, Oregon		
Oregon		
Oregon St Brd of Hgr Ed (Oregon) GO bnds		
Long Term Rating	AA+/Stable	Affirmed

Many issues are enhanced by bond insurance.

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