S&P Global
Ratings

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Summary:

Seattle; General Obligation; General Obligation Equivalent Security

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Credit Profile		
US$80.93 mil ltd tax GO imp and rfdg bnds ser 2017A due 11/01/2047		
Long Term Rating	AAA/Stable	New
US$15.01 mil unltd tax GO imp bnds ser 2017 due 12/01/2018		
Long Term Rating	AAA/Stable	New
US$8.15 mil ltd tax GO imp bnds ser 2017B due 11/01/2037		
Long Term Rating	AAA/Stable	New

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to Seattle's series 2017A limited-tax general obligation (GO) improvement and refunding bonds, 2017B taxable limited-tax GO improvement bonds, and 2017 unlimited-tax GO refunding bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the city's previously issued GO bonds and GO-equivalent obligations. The outlook is stable.

The city's full faith and credit, including the obligation to levy ad valorem property taxes without limitation as to rate or amount, secure the city's unlimited-tax GO bonds. The city's limited-tax GO bonds are subject to statutory limitations that include a limit on annual property tax revenue growth without a voter override and a limit on the city's levy rate of $3.60 per $1,000 of assessed value (AV). The city's 2017 levy rate is $2.46. The GO-equivalent obligations have a contingent limited-tax GO pledge of the city; this pledge has been invoked for debt instruments representing $2.9 million in principal as of the end of 2016.

Proceeds of the series 2017A and 2017B will pay for various capital projects, including a downtown seawall, fire facilities, and information technology. Management estimates that about 32% of debt service on these series will be supported by designated revenue with the balance by general revenue. Proceeds of the series 2017 will refund unlimited-tax GO debt outstanding to achieve interest expense savings, including $4.7 million International District Preservation and Development Authority debt for which the city has contingent exposure; hereafter the authority will pay the city for the authority's share of the series 2017 debt service.

Our issue ratings are based on our view that the city's general creditworthiness is above that of the U.S. sovereign rating. This reflects our view that the city would not default in a stress scenario likely to accompany a sovereign default given autonomy from sovereign intervention. We view the city as exhibiting relatively low funding interdependency with the federal government, as local taxes represent the vast majority of total governmental funds revenue. However, consistent with our view that U.S. state and local governments are moderately sensitive to country risk, should our view of the city's general creditworthiness deteriorate we would be unlikely to set GO issue ratings more than two notches above the U.S. sovereign rating.

The city's exposure to sovereign intervention could be tested in the medium term as part of a national debate on "sanctuary cities," a term generally used to refer to cities and other local governments that have policies that limit cooperation with federal immigration enforcement. On Jan. 25, 2017, the White House issued an executive order ("Enhancing Public Safety in the Interior of the United States") to eliminate federal funding for local governments that do not comply with federal immigration enforcement requests. We recently concluded that there was not an immediate credit risk to Seattle and other local governments with sanctuary cities policies because federal revenue generally represents a small proportion of their revenue structures and because federal law may limit the White House's ability to impose cuts without Congressional action. (See "Federal Cuts To Sanctuary Jurisdictions Are Not An Immediate Credit Risk," published March 30, 2017 on RatingsDirect.) We calculate, based on the city's 2015 federal single audit, that Seattle's potential exposure to federal cuts is roughly $85 million, or the equivalent of 4% of the city's unaudited 2016 total governmental funds revenue, and the city estimates approximately $51 million in federal governmental revenue for operations and $99 million in capital grants in its 2017 budget. In March 2017, Seattle announced it had filed suit against the federal government regarding the executive actions; we understand that part of its challenge focuses on the lack of full alignment between the justice or public safety activities that are the focus of sanctuary city policies and a much broader array of city services supported by federal dollars. In our view, the revenue effects of Seattle's strong economic growth are likely to offset any potential federal revenue losses, with the city's proposed 2017 budget estimating a $43.4 million increase in general subfund tax revenue. This, combined with our view that the city's management and budgetary flexibility are strong to very strong, leads us to doubt that federal actions will materially affect Seattle's credit quality.

The ratings reflect our assessment of the following factors for the city:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with an operating surplus in the general fund but an operating deficit at the total governmental fund level in fiscal 2016;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 21% of operating expenditures;
- Very strong liquidity, with total government available cash at 64.4% of total governmental fund expenditures and 15.4x governmental debt service, and access to external liquidity we consider exceptional;
- Very strong debt and contingent liability position, with debt service carrying charges at 4.2% of expenditures and net direct debt that is 56.8% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Adequate institutional framework score.

Very strong economy

We consider Seattle's economy very strong. The city, with an estimated population of 686,800, is located in King County in the Seattle-Tacoma-Bellevue MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 160% of the national level and per capita market value of $271,295. Overall, the city's market value grew by 14.1% over the past year to $186.3 billion in 2017. The county unemployment rate was 4.4% in 2015.

Seattle's economy is running hot, with multiple metrics showing strong growth on an already ample base that benefits from a deep reservoir of human capital, exposure to export markets, and large regional employers that are major players in their respective markets. Chief among them has been assessed value (AV), the growth rate of which has been improving for six consecutive years. This is comparable to the prior two economic expansions by our calculation, with the peak (so far) three-year average growth rate at 13.3% for the current expansion, compared with 12.9% for the three years through 2009 and 13.8% for the three years ending 2002. The employment growth rate in the city's overlapping county also is significant for its acceleration, with year-over-year growth by month slowing to 1.6% in 2015 but preliminarily up to 2.7% for 2016. We anticipate that growth will continue in some form, consistent with our projection of real GDP growth in the Western U.S. states through 2018.

We understand that Boeing and Microsoft have kept regional employment largely stable in recent years, but Seattle-focused Amazon.com's headquarters growth continues to make waves within the city's office and housing markets. Real estate services firm Cushman and Wakefield's central business district first-quarter 2017 report estimates Amazon.com's office occupancy at 7.3 million square feet relative to a total office market size of 48.4 million square feet, with 1.7 million absorbed by the online retailer in 2016 alone. The firm projects that Amazon.com will add another 4.7 million through 2022. Other major local investments include online travel agency Expedia's renovation of a vacant biotechnology facility northwest of the city's downtown to add 3,500 employees by 2020 and a $1.6 billion renovation of the state convention center located downtown. Housing developers appear to be responding to strong employment growth, with multifamily projects visible throughout the city. Marcus and Millichap, another real estate services firm, reports that regional multifamily housing development has been vigorous in response to employment growth and that vacancy rates could rise to 4% after multiyear declines to 3% in 2016, although it estimates that effective rents will rise by about 6% in 2017. The Seattle Times, citing Dupre and Scott data, reports that multifamily housing construction within the city exceeded 3,000 units in only a single year during the previous economic expansion but has exceeded this threshold annually since 2012 and is slated to add 9,900 units in 2017 and 12,500 in 2018.

Employment and population growth have intensified a public debate about strains on the city's transportation infrastructure and housing affordability. Partly mitigating these concerns is progress in transit capacity, with the region's light rail operator, Sound Transit, opening the first two stations of its northern spur in March 2016 and continuing construction that is slated to extend the line almost to the city's northern city limits by the end of the decade. Voters approved a tax increase in November 2016 that authorized Sound Transit's next generation of rail and other infrastructure, which we believe will further support the city's regional accessibility, although the legislature is debating a proposal to force the agency to use a different vehicle valuation methodology that we think could require Sound Transit to slightly modify its capital plan. City voters recently have supported infrastructure improvements in the form of a 10-year property tax increase that the city projects will total $930 million during 2016 to 2024 and low-income housing development with a projected total of $290 million during 2017 to 2023.

Very strong management

We view the city's management as very strong, with strong financial policies and practices under our FMA methodology, indicating our view that financial practices are strong, well embedded, and likely sustainable.

Elements of the city's financial policies and practices include:

- What we view as a consistent approach to budgeting, with the use of detailed, empirically based revenue and expenditure forecasts to build budgets;
- Management's provision of budget-to-actual updates to the council in May, September, and November and the council's practice of making quarterly expenditure amendments;
- The use of a detailed financial forecasting model covering the current and subsequent three years to consider the long-term effects of current-year budgeting decisions;
- An annually updated rolling six-year capital improvement plan with funding sources identified;
- Quarterly reporting on investment holdings and returns under an internally guided investment policy;
- Formal and well-embedded comprehensive debt management policy; and
- Compliance with automatic formula contributions to designated reserves, although the city does not set reserve policy minimums.

Adequate budgetary performance

Seattle's budgetary performance is adequate, in our opinion. The city had surplus operating results in the general fund of 2.8% of expenditures in fiscal 2016, but a deficit result across all governmental funds of 2.3%.

The city's general fund operations have been balanced-to-positive in the context of strong economic growth and upward pressure on salaries and benefits. General fund results for 2016 (unaudited), including our adjustments to treat recurring transfers-out as expenditures, stepped down from a robust 4.1% in 2015, but this is higher than we anticipated at this time last year based on the risk that new labor contracts would cause employee expenditures to more strongly offset tax revenue growth. Based on the city's projections, discussions with management, and the city's record of past conservative assumptions, we anticipate that the general fund's performance will likely weaken from 2015 and 2016 results but come in stronger than the negative 1% result in 2017 suggested by the city's proposed budget for its budgetary basis general subfund, which, we understand, mostly overlaps with its general fund on a Generally Accepted Accounting Principles basis.

A continuing strength of the city's general fund revenue structure, in our view, is the diversity of its tax sources, with taxes representing 86% of the general subfund's budgeted 2017 revenue, led by property taxes (25%) and followed closely by gross receipts taxes (21%), sales taxes (21%), and utility taxes (17%). The city estimates that its general subfund will see 4.5% tax revenue growth overall for 2017, which is slightly slower than the estimated 5.6% increase in 2016. We understand that the city plans to continue a pattern of using core revenue, the revenue or rates of which are restricted under state law, for basic services and to request that voters approve property tax increases for specific policy initiatives. Examples include a November 2015 approval for transportation capital improvements and an August 2016 approval for affordable housing programs totaling $290 million over seven years. The mayor proposed a property tax increase to address homelessness earlier this year, but has since rescinded the proposal in favor of a possible joint effort with the city's overlapping county. We understand that the city is likely to place on the ballot renewal requests in some form for its families and education levy expiring in 2018 that encompasses $232 million over seven years and a pre-kindergarten learning levy also expiring in 2018 ($58 million over four years).

Very strong budgetary flexibility

Seattle's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 21% of operating expenditures, or $267.5 million.

Our calculation of the city's budgetary flexibility includes analytic adjustments that treat recurring transfers-out as expenditures given their recurring nature. Based on the city's 2017 proposed budget and projections through 2020, we anticipate that the city's financial flexibility will remain very strong and possibly grow.

Very strong liquidity

In our opinion, Seattle's liquidity is very strong, with total government available cash at 64.4% of total governmental fund expenditures and 15.4x governmental debt service in 2015. In our view, the city has exceptional access to external liquidity if necessary, with approximately annual issuances of GO bonds in recent years and frequent issuances of various security types during the past 15 years. We do not consider the city's investments to be aggressive, with U.S. agency, government-sponsored enterprise, and U.S. Treasury obligations making up 55% of the city's portfolio and repurchase agreements and commercial paper making up 14% as of January 2017.

The city has agreed to loan, on a contingent basis, sufficient and timely resources to enable three obligors to meet their debt service obligations. One obligor, representing $441,700 in annual debt service in 2017, is not fully paying debt service. Should the risk of the city making payments under the other contingent agreements become nonremote, we would consider the city's liquidity exposure modest, with $3.9 million, or about 0.2% of total governmental funds expenditures, in remaining annual payments after excluding debt the city currently supports and those to be removed as part of the series 2017.

Management has confirmed that the city has no private placement obligations outstanding.

Very strong debt and contingent liability profile

In our view, Seattle's debt and contingent liability profile is very strong. Total governmental fund debt service is 4.2% of total governmental fund expenditures, and net direct debt is 56.8% of total governmental fund revenue. Overall net debt is low at 0.9% of market value, which is in our view a positive credit factor.

We anticipate that the city will continue a pattern of annual limited-tax GO issuances in the spring of each year, with management estimating about $50 million to $60 million for 2018, and additional debt depending on decisions regarding larger projects such as waterfront improvements ($100 million to $200 million), arena improvements ($150 million) and low-income housing ($29 million). We do not anticipate that the city's net direct debt will rise materially in the coming years, as the city continues to secure voter authorization for property tax increases for pay-as-you-go capital needs.

The city has agreed to loan, on a contingent basis, sufficient and timely resources to enable three obligors to meet their debt service obligations. The principal of these loans totaled $49 million at the end of 2016. Our calculation of the city's debt profile excludes these obligations, with the exception of $2.9 million for loans associated with the Indian Services Commission, the debt service for which the city is supporting.

Seattle's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 6.7% of total governmental fund expenditures in 2015, with 5.4% representing required contributions to pension obligations and 1.3% representing OPEB payments. The city made 95% of its annual required pension contribution in 2015.

The city independently manages two defined benefit pension plans for most of its nonsworn employees (SCERS 1 and SCERS 2) and two small closed plans for public safety employees. Other public safety employees participate in the state-managed Law Enforcement Officers' and Firefighters' Retirement System. The city's required pension contribution is its actuarially determined contribution (ADC), which is calculated based on an actuary study. We view the largest plan's (SCERS 1) funded ratio, which we estimate as the plan fiduciary net position as a percentage of the total pension liability, as low at 66.5%. In August 2016, the city and its bargaining groups agreed to create a new, lower-cost tier (SCERS 2) into which employees hired starting in 2017 will enroll.

In 2012, the city shifted its valuation of its pension assets to a five-year smoothing approach and formally declared its intention to fund its actuarially calculated annually required contribution (ARC) for the city-managed pension system based on a 30-year amortization. It has consistently met the ARC under its definition, although its payments fall slightly below the ARC under Governmental Accounting Standards Board guidelines because, as we understand, the guidelines do not allow an entity to assume growth in the number of employees.

The city's OPEB liability consists of an implicit subsidy and, for certain public safety employees under a now closed plan, a direct subsidy. The city manages this cost on a pay-as-you-go basis.

Adequate institutional framework

The institutional framework score for Washington municipalities is adequate.

Outlook

The stable outlook reflects our view that Seattle's strong economic performance will likely continue during our two-year outlook horizon, consistent with our expectation of GDP growth in the region, and that financial performance is likely to remain adequate, with continuing negative total governmental funds results offsetting balanced-to-positive general fund performance. We view the chance of lowering the rating during the next two years as less than one in three.

Downside scenario

We do not anticipate lowering the rating during the outlook horizon unless the city experiences deterioration in multiple factors that we view as important to credit quality, such as a major economic reversal and rising costs that create a significant operating deficit that substantially erodes the city's liquidity position and available reserves.

Related Research

- U.S. State And Local Government Credit Conditions Forecast, July 27, 2016
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- 2016 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of April 25, 2017)		
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed

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Ratings Detail (As Of April 25, 2017) (cont.)		
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
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Seattle GO		
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Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle Chinatown Intl Dist Pres & Dev Auth, Washington		
Seattle, Washington		
Seattle Chinatown Intl Dist Pres & Dev Auth (Seattle) GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle Chinatown Intl Dist Pres & Dev Auth (Seattle) GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle Indian Svcs Comm, Washington		
Seattle, Washington		
Seattle Indian Svcs Comm (Seattle) GO		
Long Term Rating	AAA/Stable	Affirmed
Seattle Museum Dev Auth, Washington		
Seattle, Washington		
Seattle Museum Dev Auth (Seattle) GO equiv		
Long Term Rating	AAA/Stable	Affirmed
Washington St Hsg Fin Comm, Washington		
Seattle, Washington		
Washington St Hsg Fin Comm (Seattle) (Lowman Bldg) GO		
Long Term Rating	AAA/Stable	Affirmed

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria.

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