

## CREDIT OPINION

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### Contacts

William Oh +1.415.274.1739  
 AVP-Analyst  
 william.oh@moodys.com

Patrick Liberatore +1.415.274.1709  
 AVP-Analyst  
 patrick.liberatore@moodys.com

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Asia Pacific 852-3551-3077

Japan 81-3-5408-4100

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# City of Seattle, WA

## Update to credit analysis

### Summary

[Seattle](#) (Aaa stable) benefits from a strong economy and growing tax base with socioeconomic measures that are amongst the strongest in the country. The city also has solid finances that include healthy reserves and liquidity, a manageable debt profile that consists of fixed-rate debt, and moderate pension and OPEB liabilities.

### Credit strengths

- » A large and growing tax base and a regional economic center
- » Strong socioeconomic measures for an urban area including high median family income, full value per capita, and low unemployment
- » Healthy financial position that includes ample reserves and available liquidity
- » Favorable debt profile that includes only fixed-rate debt and relatively rapid amortization
- » Strong management team

### Credit challenges

- » Modest exposure to economically sensitive revenues
- » Somewhat dependent upon a small number of high profile private-sector firms for growth

### Rating outlook

The outlook is stable, reflecting our view that the city is well positioned financially and that the local economy will continue to be amongst the nation's strongest.

### Factors that could lead to an upgrade

- » Not applicable

### Factors that could lead to a downgrade

- » Material weakening in the city's finances
- » Prolonged deterioration in the economy and tax base
- » Substantial growth in debt and/or pension liabilities

### Key indicators

Exhibit 1

Seattle (City of) WA	2012	2013	2014	2015	2016
<b>Economy/ Tax Base</b>					
Total Full Value (\$000)	\$116,796,890	\$116,995,513	\$128,205,754	\$144,513,932	\$163,305,928
Population	612,916	624,681	637,850	653,017	668,849
Full Value Per Capita	\$190,559	\$187,288	\$200,997	\$221,302	\$244,160
Median Family Income (% of USMedian)	144.5%	149.5%	152.2%	155.8%	159.7%
<b>Finances</b>					
Operating Revenue (\$000)	\$1,080,845	\$1,138,767	\$1,180,513	\$1,257,992	\$1,361,066
Fund Balance (\$000)	\$202,583	\$220,184	\$232,287	\$258,373	\$297,852
Cash Balance (\$000)	\$205,669	\$253,283	\$232,318	\$312,039	\$370,777
Fund Balance as a % of Revenues	18.7%	19.3%	19.7%	20.5%	21.9%
Cash Balance as a % of Revenues	19.0%	22.2%	19.7%	24.8%	27.2%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$832,539	\$897,025	\$897,610	\$1,040,474	\$1,027,503
3-Year Average of Moody's ANPL (\$000)	\$1,420,096	\$1,648,620	\$1,880,940	\$2,177,634	\$2,272,141
Net Direct Debt / Operating Revenues (x)	0.8x	0.8x	0.8x	0.8x	0.8x
Net Direct Debt / Full Value (%)	0.7%	0.8%	0.7%	0.7%	0.6%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.3x	1.4x	1.6x	1.7x	1.7x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	1.2%	1.4%	1.5%	1.5%	1.4%

Source: Moody's Investors Service

## Profile

Seattle is the economic center for the Pacific Northwest. The full-service city has a relatively affluent population of nearly 714,000, a large and well-educated labor force, and ties to the broader metropolitan area including the cities of Bellevue and Everett.

## Detailed credit considerations

### Economy and tax base: Seattle is the economic center of the Pacific Northwest

The City of Seattle is the commercial and tourist hub of the Puget Sound region and the economic center of the State of Washington. Software development and aircraft manufacturing are key components of the local economy, and the area serves as the headquarters or major operating base to some of the world's most well-known international corporations, including Amazon, Boeing, Microsoft, and Starbucks. At just 3.3% as of December 2017 (according to data from the Bureau of Labor Statistics), the city's unemployment rate continues to outpace the state and the nation, even as the local labor force grew by 2.4%. Demand for Boeing aircraft remains high, with a sizeable order backlog that is estimated to take several years to fulfill. Online retailer Amazon continues to expand its footprint in Seattle, acquiring and developing substantial downtown office space to house its growing workforce. The city is forecasting continue economic growth into 2018, albeit at slower rates than in recent years.

Median family income in the city is amongst the highest among large urban areas in the United States at 159.7% of the national average. Full value per capita, a proxy measure of wealth, is robust at \$299,999. Price appreciation and new construction are continuing to drive the city's assessed value higher. In 2018, assessed value grew by 14.9%, the sixth consecutive year of growth and hit a new high of \$214.1 billion. Median home prices are up 17.0% year-over-year, and commercial office vacancy rates is low at 5.7%.

### Financial operations and reserves: structurally balanced with healthy reserves supported by diverse revenue streams

The city's finances are healthy and a credit strength, driven by strong growth amongst the city's diversified revenue streams. The city's General Fund is the city's principal operating fund, and is comprised principally of property taxes (20.6% in 2016), business taxes (20.7%), retail sales and use taxes (17.3%), and utility taxes (10.6%). Preliminary figures for 2017 indicate overall tax revenue growth of 4.0%. The city's property tax rate is subject to a \$3.60 per \$1,000 cap, not including the rate for voted bonds; the city's current rate

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(2018) subject to the rate limit is \$2.22. Outside of new growth and voter-approved levy lid lifts, operating property tax revenues are limited to 1% annual growth.

The city's more economically sensitive revenues were up strongly in 2017, with preliminary numbers showing sales tax revenues up 5.4% and business tax receipts up 7.5%. The city has forecasted sales tax and business tax growth of 4.1% and 7.1%, respectively, for 2018. The city updates its revenue projections three times a year.

The city's largest expense in 2016 was for public safety (43.9% of general fund revenues in 2016), followed by transfers out (23.8%) (principally for nonmajor special revenues funds including Park and Recreation and Human Services), and general government (17.3%). The city's 2018 budget continues to focus on public safety (including the addition of police officers), homelessness, and information technology. State law requires that the city balance its budget, and the city uses a quarterly supplemental budget process to consistently deliver structurally balanced financial operations.

Since 2011, the city's General Fund revenues have exceeded its expenditures, allowing the city to build up its total fund balance from \$204.8 million (20% of general fund revenues) in 2011 to \$442.4 million (32.1%) in 2016; available reserves (those not designated as nonspendable or restricted) increased from \$145.3 million (14.2%) to \$286.5 million (20.8%). Preliminary 2017 figures show total general fund reserves growing to \$476 million. City officials are projecting small increases in reserve levels in 2018, though Moody's notes that city projections have been conservative in recent years, with revenues outpacing expectations during the current portion of the economic cycle.

#### LIQUIDITY

The city's liquidity position is healthy. The city's General Fund cash and equity in pooled investments at the end of 2016 was \$359.5 million, or 26.1% of general fund revenues. Functionally, however, the city pools its cash and investments across funds. This consolidated pool held \$1.76 billion at the end of 2016 and an estimated \$2.4 billion at the end of 2017. City funds may withdraw cash out of the pool without prior notice or penalty.

#### Debt and pensions: modest debt and manageable pension liabilities

The city maintains a very moderate level of debt that amortizes quickly. Net direct debt is just 0.5% of full value and 0.76 times General Fund revenues. The ten-year amortization rate of the city's debt is average at 63.5%, with 78% of the city's limited tax general obligation bonds being retired within ten years. Potential future bond issuances include additional money for low income housing (\$10 million), continued improvements along the city's waterfront (up to \$200 million), as well as annual bond issuances of \$50-\$60 million annually for general government projects.

#### DEBT STRUCTURE

The city's governmental debt consists of fixed-rate unlimited tax and limited tax general obligation bonds. Peak debt service on the city's LTGO bonds is estimated at \$100.7 million in 2019, or 7.3% of General Fund revenues, and declines through final maturity in 2047.

#### DEBT-RELATED DERIVATIVES

The city has no debt-related derivatives.

#### PENSIONS AND OPEB

The city manages a single-employer and defined-benefit public employee retirement plan (Seattle City Employees' Retirement System), the Firefighter's Pension Fund, and the Police Relief and Pension Fund. The city's three-year adjusted net pension liability (ANPL) is modest at 1.06% of full value and 1.7 times operating revenues. ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities.

Based on our calculations, the city's 2016 pension contributions for its non-legacy plans public safety plans exceeded the amount necessary to "tread water"; that is, contributions were more than sufficient to prevent the city's net pension liability from growing under plan assumptions. In 2011, the city council passed legislation that commits the city to fully funding the actuarially determined contribution every year. Additionally, the city may, under state law, levy a \$0.225 per \$1,000 property tax levy to cover the Firefighter's fund; the city does not levy this additional tax.

On January 1, 2017, the city closed SCERS to new entrants, with new employees participating in a new system (SCERS 2). SCERS 2 has decreased benefit levels, increases the minimum retirement age, and defers retirement eligibility by increasing the age-plus-years-of-service requirement for retirement with full benefits. The city records an implicit subsidy for OPEB.

**Management and governance: strong management team with codified practices**

Moody's views the city's management team as strong. The strength of the management team is buttressed by codified practices that enhance the city's financial profile. Until 2017, the city appropriated sufficient money into the Emergency Subfund to the maximum amount allowed by state law (\$0.375 per \$1,000), but is now adding funds at a rate tied to inflation. Additionally, 0.5% of forecasted tax revenues are automatically contributed to the city's "Rainy Day Fund," also known as the Revenue Stabilization Account, as are 50% of any unanticipated excess General Subfund balances at year end. These contributions are suspended when forecasted nominal tax growth rate is negative or when the Rainy Day Fund exceeds 5% of total tax revenues.

Washington Cities have an Institutional Framework score of Aa, which is high. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenue sources are economically-sensitive sales taxes and property taxes. Cities can increase property tax collections 1% over the prior year, subject to state statutory limits on property tax rates. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed and mandated costs are generally greater than 25% of expenditures. Washington has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

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