S&P Global Ratings

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Summary:

Virginia College Building Authority Virginia; Appropriations

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Credit Profile		
US$227.54 mil ed facs rev rfdg bnds (Virginia) (21st Century College And Equip Prog) ser 2019C due 02/01/2030		
Long Term Rating	AA+/Stable	New
US$125.22 mil ed facs rev bnds (Commonwealth of Virginia) (21st Century College And Equip Prog) ser 2019B due 02/01/2039		
Long Term Rating	AA+/Stable	New

Rationale

S&P Global Ratings has assigned its 'AA+' rating to the Virginia College Building Authority's series 2019B educational facilities revenue bonds and the series 2019C educational facilities revenue refunding bonds (the 21st century college and equipment programs), issued for the Commonwealth of Virginia. The outlook is stable.

The 'AA+' rating reflects our opinion of the commonwealth's:

- Obligation to annually appropriate sufficient amounts to pay debt service;
- General creditworthiness (AAA/Stable); and
- Demonstrated historical commitment within the administrative and legislative branches to repaying its appropriation-backed obligations.

Annual appropriations from the General Assembly secure the bonds. The bonds will finance certain capital projects for public institutions of higher education in the commonwealth and refund existing debt. The bonds represent the 46th and 47th series issued under the master indenture pursuant to the 46th and 47th supplemental indentures. The master indenture's financing structure uses a single-payment agreement between the authority and the treasury board to provide for debt service payments.

Under a payment agreement, the treasury board and authority will make their best efforts to request the governor to include an appropriation in his budget proposal that is sufficient to pay principal and interest on the bonds. The General Assembly is authorized, but not obligated, to make the appropriations. The current biennium budget provides sufficient appropriation to support debt service due. We rate these obligations one notch lower than the commonwealth'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. Virginia pledges to annually appropriate from its operating revenues, and has a long track record of appropriating for similar obligations. In our opinion, there is no unusual political, timing, or administrative risk related to the debt payment.

The Virginia College Building Authority Act of 1966 authorizes the authority to issue debt to finance capital projects at and acquire equipment for public higher education institutions in Virginia. The 1996 General Assembly created the 21st century college program, which authorizes the authority to issue bonds for capital projects and equipment for higher education institutions. All bonds under the master indenture are equally secured. The treasury board is the authority's fiscal agent, receives appropriations from the General Assembly, and makes debt service payments to the trustee when due. Debt service payments are due on Feb. 1, and Aug. 1, starting Feb. 1, 2021. Debt service payments, which occur well after the end of the fiscal year; the commonwealth's history of timely budget adoption; and the General Assembly's ability to make supplemental appropriations, if necessary, mitigate late budget adoption risk, in our opinion.

Fiscal 2020 revenue to date through the first quarter is up over 8% compared with the same period in the previous year, reflecting September collection of estimated quarterly income tax payments. Although estimated employment and personal income growth in 2019 fell below Virginia's forecast, the commonwealth still experienced strong fiscal 2019 general revenue growth of more than 7% compared with the previous year due mostly to the effects of the Federal Tax Cuts and Jobs Act, resulting in higher-than-forecasted net individual income tax collections. Sales and use tax collections were up 3.4% year-over-year, although just slightly under forecast. While the legislature directed approximately $450 million of the higher-than-expected revenue for taxpayer refunds, officials still expect growing reserve balances in the next couple of years including fiscal 2019 budget reserves of about $792 million, or 3.8% of expenditures, and $1.5 billion, or about 6.8% of annual budgeted appropriations in fiscal 2020. We believe that the commonwealth's legislative changes to direct deposits to a revenue reserve fund and continued focus on structural budget balance should also help to position Virginia for the next recession.

After Virginia expanded Medicaid in 2018 for adults with incomes up to 138% of the federal poverty level, more than 300,000 new individuals enrolled as of September 2019, which is still within original estimates of up to 400,000. The expansion also included new provider assessment fees to offset the commonwealth's share of expansion costs and matching funds. The Department of Medical Assistance Services submitted a program waiver with the Centers for Medicare and Medicaid Services and is in the process of negotiating some of the planned new features, including work requirements. Actual fiscal 2019 state Medicaid spending tracked just below budgeted estimates; officials expect the savings will be used to offset provider assessments in fiscal 2020.

Virginia's significant military and other federal presence buoyed the economy relative to that of the U.S. during the Great Recession, but the commonwealth's annual real GDP growth lagged that of the nation from 2010 to 2017. The economy has stabilized since 2013, when federal sequestration disproportionately affected the Northern Virginia and Hampton Roads regions of the commonwealth's overall economy, reflecting fewer federal contracts and lower defense spending. According to IHS Markit, the commonwealth's real gross state product (GSP) increased by a good 2.8% in 2018, above 2.7% for the nation. IHS Markit projects the GSP growth rate to increase by 2.40% in 2019, which is just under the forecast national rate of 2.45%; however, it projects the GSP growth rate to remain above that of the nation in the next few years, despite gradually slowing due to slackening global growth, the effect of new tariffs, and weaker fiscal stimulus for domestic spending. Virginia's projected 2019 employment growth of 0.9% is weaker than previously forecast and under the projected 1.44% national rate, reflecting slower growth in professional and business services jobs than the previous year and flat government payrolls. IHS Markit projects 0.9% employment growth in 2020, below the 1.04% forecast for the nation, but forecasts moderating annual growth rates of 0.9% and 0.6% in 2021 and 2022, respectively, led by professional and business service jobs will remain above projected national growth rates. While an increase in federal and defense spending is positive for Virginia's economy over the biennium, we believe political standoffs over the federal budget and future sequestration caps pose ongoing risks to the regional economic growth.

Virginia's debt burden across measures is moderate, in our opinion, representing about 2.5% of personal income. For the current biennium, the budget includes full funding of the Virginia Retirement System's (VRS) actuarially determined contribution (ADC). The commonwealth contributes directly to the VRS plan, the State Police Officers Retirement System, the Virginia Law Officers' Retirement System, and the Judicial Retirement System. It does not contribute directly to the VRS teacher plan; instead, as per the school funding formula, it distributes aid payments to school districts that cover approximately 40% of payroll, but we understand that state aid distributions are not based on ADC funding or pension liabilities. Including liabilities associated with the four VRS plans, the overall funded ratio is 74%, which is relatively low in our opinion. However, we consider Virginia's share of the net pension liability across funds also low at only 1.3% of personal income.

(For more information on the commonwealth's general credit characteristics, please see the most recent analysis on Virginia's GO debt, published Oct. 1, 2019, on RatingsDirect.)

Outlook

The stable outlook reflects our view that Virginia will experience continued positive revenue performance in the fiscal 2018-2020 biennium, remain committed to structural budget solutions, and rebuild reserve balances. We also anticipate that matching federal funding and a provider assessment fee will offset the costs of expanding Medicaid over the two-year outlook horizon. In addition, we expect that the commonwealth's economic growth pattern will more closely reflect U.S. trends, in part due to easing of the effects of federal sequestration. In the long term, we see the potential for slower revenue growth and rising Medicaid costs as posing credit risk across the state sector, including Virginia. However, we anticipate that the commonwealth's recent efforts to rebuild reserves and structurally align the budget will better prepare Virginia to weather these potential risks. If the commonwealth reverses recent efforts to rebuild its reserves, returns to structural imbalance, or if it experiences consistently weaker economic performance relative to that of the U.S., we could consider lowering the rating.