Commonwealth Debt Capacity

Presentation to Capital Outlay Subcommittee of the House Appropriations Committee

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January 21, 2010

Debt Capacity Advisory Committee

- Debt Capacity Advisory Committee (DCAC) was established in 1991 by Executive Order and codified in 1994.
- DCAC membership:
  - Secretary of Finance (Chairman), State Treasurer, Director of the Department of Planning and Budget
  - Auditor of Public Accounts
  - Director of the Joint Legislative Audit and Review Commission
  - Two citizen members who have expertise in financial matters appointed by the Governor
- Committee's mandate is to annually review the size and condition of the Commonwealth's tax-supported debt, and to annually submit to the Governor and the General Assembly an estimate of the maximum amount of additional tax-supported debt that prudently may be authorized and issued during the next two years.
- The estimate is advisory and in no way binds the Governor or the General Assembly.

Importance of Measuring Debt Affordability

- Debt affordability is one of four key factors assessed by rating agencies
- Attempts to correlate the borrowing for capital needs with the ability to repay
- Issuance above capacity can cause erosion in credit rating
- Capacity to issue debt is finite for a given credit quality

Debt Affordability Measure

- **Debt service on tax-supported debt is < 5% of blended revenues**
- Tax-supported debt includes:
  - Debt for which debt service payments are made or pledged to be made from funds derived from tax revenues
  - Bonded debt, capital leases, installment purchases, etc.
- Blended revenues include:
  - General Fund: Corporate/Individual/Sales, 2/3 Insurance Premium, Licenses & Permits, ABC/Beer Excise, Bank & Corporate Franchise, and Tobacco taxes
  - Transfers: ABC Profits
  - Transportation Trust Fund: Motor Fuels, Priority Transportation Fund, Vehicle Sales and Use, Aviation Fuels, Rental, Recordation (2 cents) and 1/3 Insurance Premium taxes
- Actual debt service on all outstanding tax-supported debt and long-term obligations
- Estimated debt service on authorized but unissued debt
  - Based on cash-flow estimates provided by agencies

Factors Affecting Debt Capacity

- Changes to revenue forecast
  - Driven by economy
  - Policy changes
    - Lottery segregated as special fund effective July 2008 - $450 million/year
    - Estate & Gift tax repealed effective July 2007 - $160 million/year
- Authorization of additional tax-supported debt
  - $3.3 billion authorized in 2007
  - $2.7 billion authorized in 2008
  - $0.7 billion authorized in 2009
- Issuance assumptions change
  - Spending needs – timing and sizing of new issues
  - Priorities
  - Interest rates, refinancing opportunities

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Debt Capacity Recommendations -- December 2009

No additional debt capacity for 2010 and 2011

(Dollars in Millions)

Fiscal Year	Blended Revenues	[A] Actual Outstanding Debt Service as a % of Revenues	[B] Actual & Projected Debt Service as a % of Revenues	[C] Amount of Additional Debt that may Be Issued December 2009	[C] Amount of Additional Debt that may Be Issued December 2008
Actual 2007	$17,282.60	2.79%	2.79%	N/A	N/A
Actual 2008	$17,534.60	3.04%	3.04%	**N/A**	N/A
Actual 2009	$15,671.80	3.75%	3.75%	**N/A**	$0.00
2010	$15,227.90	4.16%	4.50%	**$0.00**	$369.99
2011	$15,789.70	4.28%	4.98%	**$0.00**	$369.99
2012	$16,551.80	3.80%	**5.13%**	**$0.00**	$369.99
2013	$17,383.20	3.42%	**5.03%**	**$0.00**	$96.24
2014	$18,113.40	3.00%	4.77%	**$425.00**	$302.84
2015	$18,928.70	2.82%	4.64%	**$425.00**	$493.73
2016	$19,754.80	2.55%	4.40%	**$650.00**	$793.73
2017	$20,630.59	2.27%	4.14%	**$730.00**	$781.77
2018	$21,546.04	1.97%	3.80%	**$742.78**	$781.77
2019	$22,502.96	1.66%	3.44%	**$742.78**	-
			10 year Average	**$371.56**	**$406.01**

[A] Equals actual outstanding debt service as a percentage of blended revenues.
[B] Equals outstanding debt service and debt service on currently authorized but unissued debt as a percentage of blended revenues
[C] Equal to annual amount of additional principal that may be issued without violating the parameters of the model.

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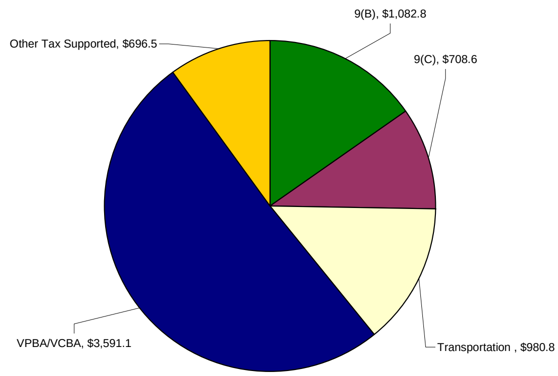
Outstanding Tax-Supported Debt As of December 2009

$7,059.8 Total

(Dollars in Millions)



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Model assumes bonds will continue to be issued for currently authorized projects

Authorized Tax-Supported Debt Issuance Assumptions

(Dollars in Millions)

	9(c) Higher Education	VPBA	VCBA 21st Century Equipment	VCBA 21st Century Projects	9(d) Transportation[2]	VPA	Total
Authorized & Unissued as of December 31, 2009	$443.0	$1,141.4	$58.8	$550.0	$3,180.0	$155.0	$5,528.2
Assumed Issued[1]:							
FY 2010	-	-	-		-	-	-
FY 2011	147.7	345.3	58.8	-	492.7	-	**1,044.5**
FY 2012	147.7	503.0	-	350.0	293.1	-	**1,293.8**
FY 2013	147.7	138.8	-	200.0	300.0	-	786.5
FY 2014-19		154.2	-	-	1,350.0	155.0	1,659.2
Total	$443.0	$1,141.3	$58.8	$550.0	$2,435.8	$155.0	$4,783.9

(1) Amounts issued are shown in the year of first debt service payment. Actual issuance occurs one-year prior (i.e. VPBA bonds shown in 2011, are issued in 2010).

(2) $744.2 million of remaining CTB revenue bonds to be issued beyond the 10-year model period. Plans are uncertain regarding $24.9 million of remaining NVTD bonds. May be issued beyond the 10-year model period.

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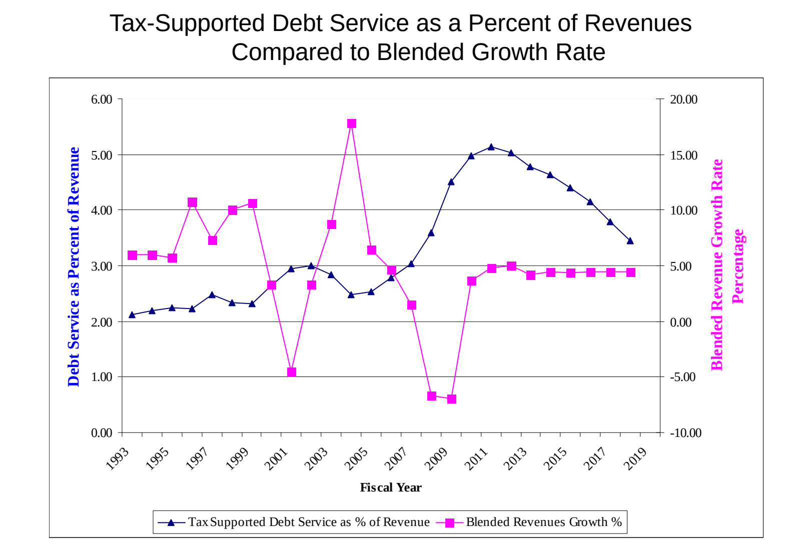
The dramatic and unprecedented decline in forecast revenues is the primary cause of diminished capacity



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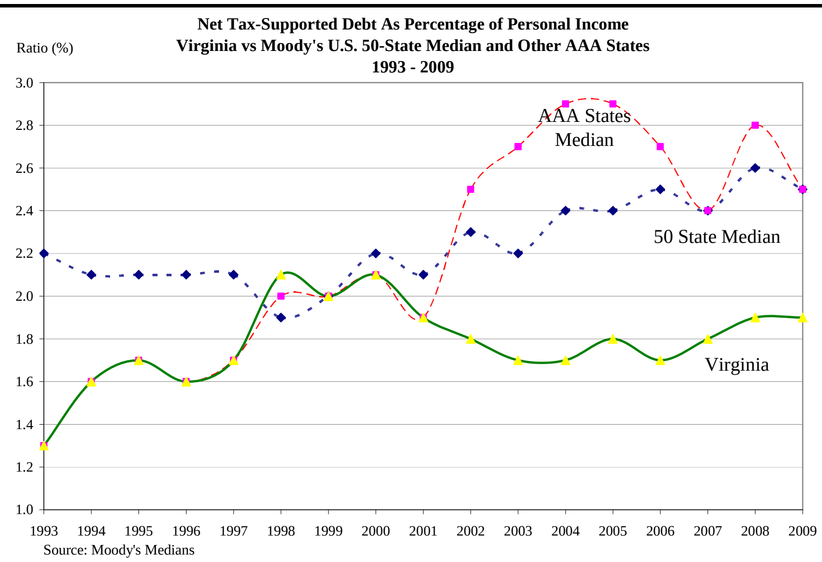
Virginia's debt position remains strong compared to peers



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Additional Recommendations of DCAC December 2009

- Prompted the DCAC to consider whether:
  - Current 5% measure is still an appropriate measure of Virginia's debt capacity
  - Reliance on a single measure tied to revenues is the best way to assess the Commonwealth's debt capacity
- Directed staff to conduct a study to be considered prior to the December 2010 meeting
- Requested participation from staff of House Appropriations and Senate Finance Committees

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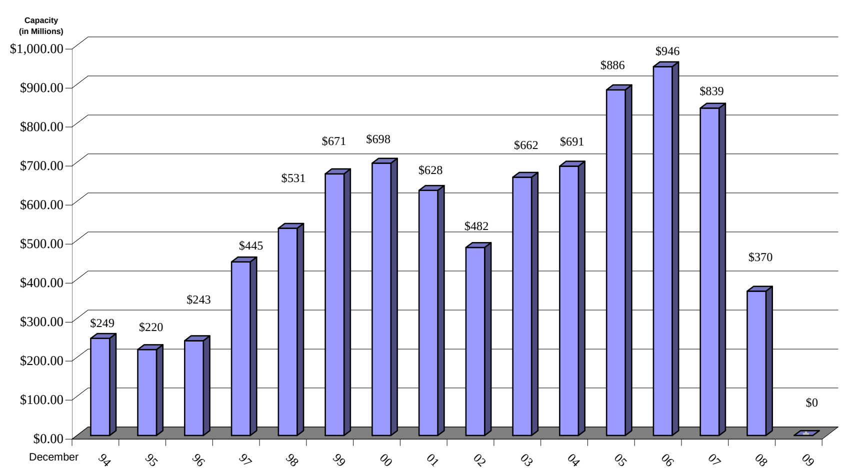
Debt Capacity 1994-2009



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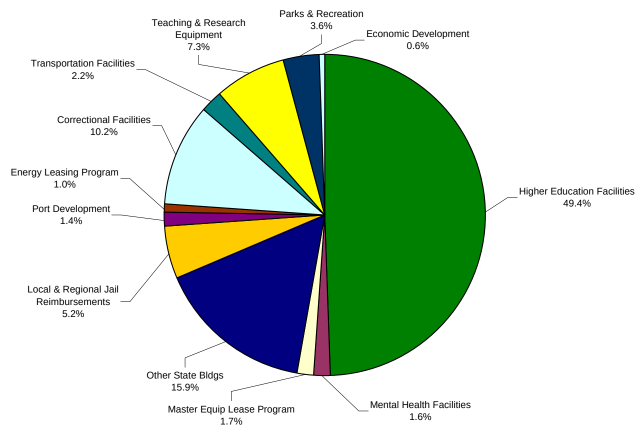
Uses of New Tax-Supported Debt Issued 2005 - 2009
$4.4 Billion Total



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Value of the AAA Bond Rating

- Commonwealth has held a AAA general obligation bond rating from Moody's since 1938
- Subject-to-appropriation bonds rated one notch below the state's GO rating at AA+ (Includes: VCBA 21st Century, VPBA, CTB)
- Low risk exposure means bond investors willing to accept lower rate of interest
- Demand for credit quality is high
  - 2008 financial melt-down and flight to quality
  - Exit of bond insurers make "natural" AAA's/AA's more valuable
  - Portfolio managers need highly-rated bonds to improve fund profile

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Financial benefit of "AAA" on $100 million in bonds

- If AAA became AA, expect to pay 25-35 basis points more
  - $200,000/year
  - $2.2 million over 20 years
- If AA became A, expect to pay 55-63 basis points more
  - $600,000/year
  - $6.4 million over 20 years
- Two years ago, the spread between AAA and AA was 5-7 basis points

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