



# **State Bonding in Oregon**

## **Presentation to the 2007 Legislative Assembly**

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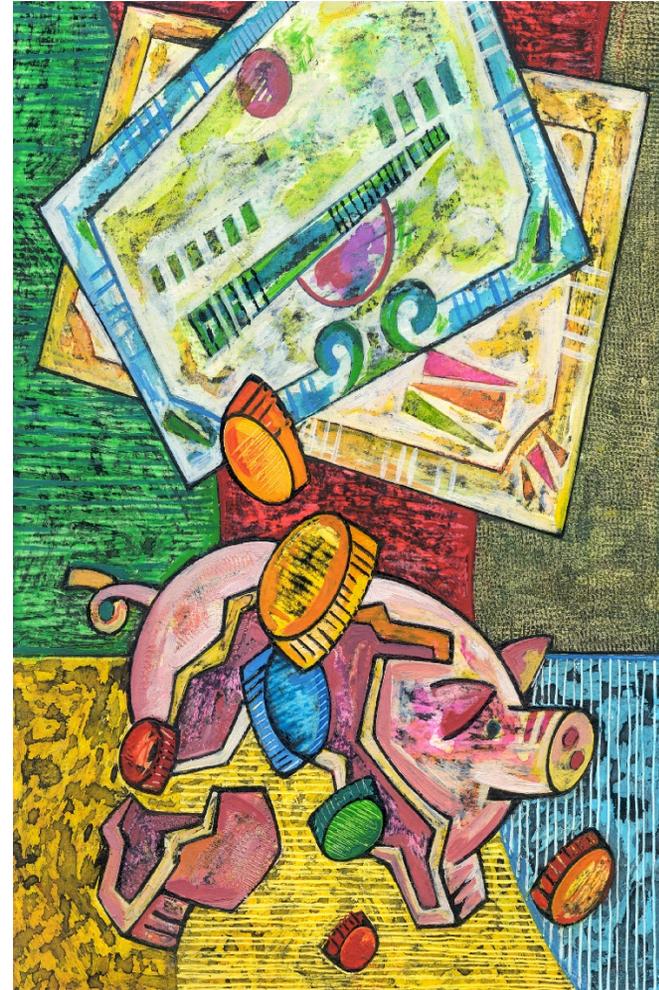
**Office of the State Treasurer**



- ❑ **Definitions**
- ❑ **U.S. Debt Market**
- ❑ **Municipal Bonds and Credit Ratings**
- ❑ **Oregon's Bonding Process**
- ❑ **Oregon's Long-term Debt Trends**
- ❑ **SDPAC's Debt Capacity Recommendations for 2007-09**
- ❑ **State Debt Ratio Comparisons**

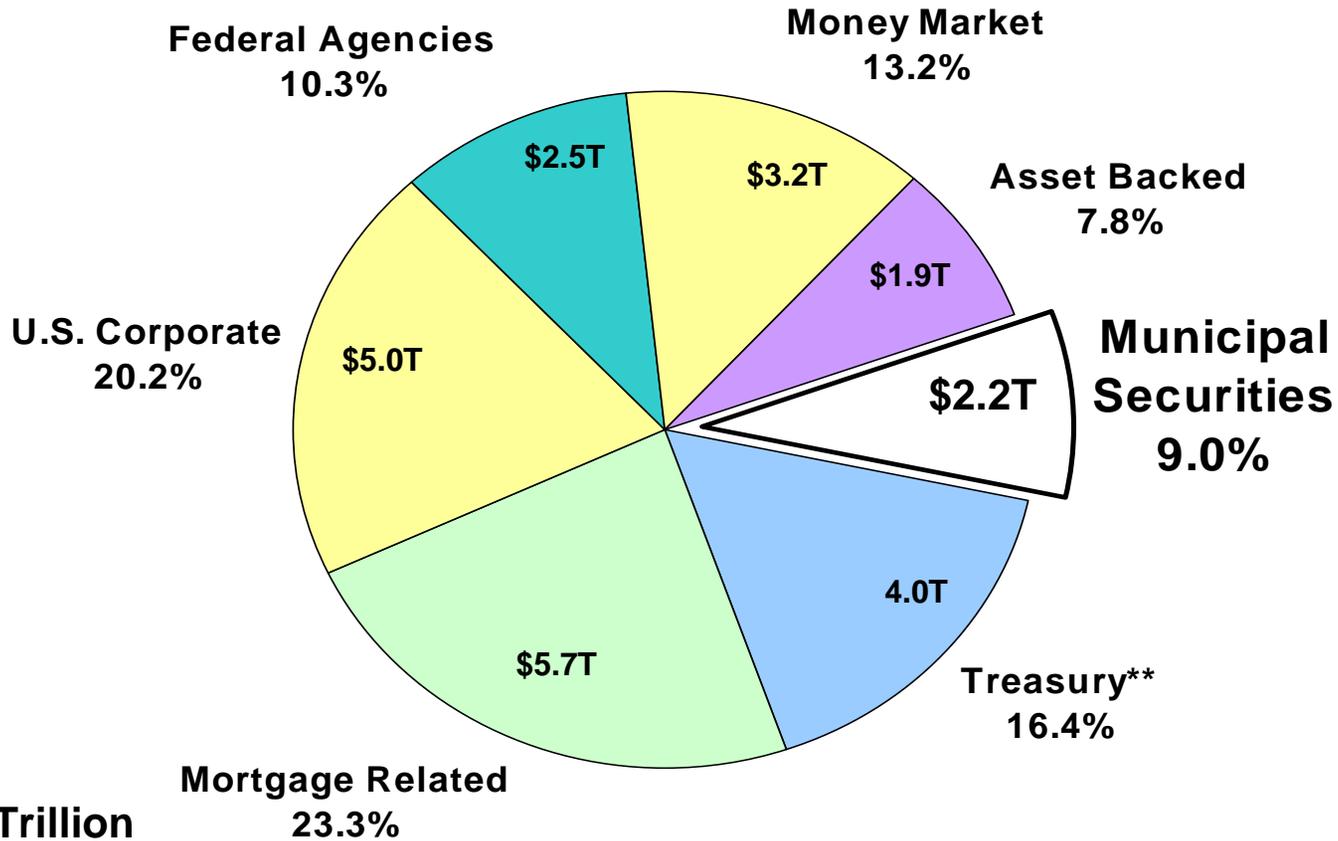
## What is a bond issue?

- ❑ The process of issuing bonds is the process of borrowing money
- ❑ A bond is a certificate that represents a promise to repay investors who loan money
- ❑ Specified schedule of principal and interest payments



## Outstanding Bond Market Debt

as of September 2005\* (\$Trillions)



Source: Bond Market Association

\* Figures may not add due to rounding

\*\* Includes interest bearing marketable public debt only

# Why does the State issue bonds?



- ❑ Major source of funding for the State's long-term infrastructure and capital needs
- ❑ Allows assets to be acquired as needed rather than when enough cash has been saved
- ❑ Spreads costs of capital assets over time to all those who benefit from it
- ❑ Interest on Oregon's state and local bonds issued for "governmental purpose" projects are exempt from both federal and state taxation
  - Investors are willing to accept a significantly lower interest rate due to the double tax-exemption offered

## What types of projects are financed with State bonds?

- ❑ **State infrastructure financed with bonds include:**
  - **Correctional facilities**
  - **Transportation improvements**
  - **Higher education and community colleges**
  
- ❑ **The State also issues debt to support local needs such as:**
  - **Economic and rural development**
  - **Single and multi-family housing loans**
  - **Veteran's home loans**
  - **Small scale energy loans**
  - **Drinking water and pollution control**





- ❑ Credit ratings provide investors with an easily identifiable way to assess the degree of risk in an issuer's securities
- ❑ Three major firms in municipal market
  - Standard and Poor's
  - Moody's Investors Service
  - Fitch Investors Service
- ❑ Different rating schemes, but same underlying theme:
  - AAA for highest rated securities
  - AA, A, BBB levels as perceived risk increases
  - BBB- is below investment grade
- ❑ Credit ratings impact:
  - Bond interest rates
  - State's overall borrowing costs of capital

### □ General Obligation Bonds

- Financial performance of jurisdiction
- Governance framework/management practices
- Debt burden
- Economic base

### □ Revenue Bonds

- All of the above, plus
- Strength of specific revenue streams pledged
- Legal, financial agreements
- Rate covenants





# Recent Oregon G.O. Bond Rating History

	<u>Moody's</u>		<u>S&amp;P</u>		<u>Fitch</u>	
1990	Aa	(January) ↑	AA-		AA	(September) ↑
1991	Aa		AA-		AA	
1992	Aa		AA-		AA	
1993	Aa		AA-		AA	
1994	Aa		AA-		AA	
1995	Aa		AA-		AA	
1996	Aa		AA	(September) ↑	AA	
1997	Aa2	(April) ↓	AA		AA	
1998	Aa2		AA		AA	
1999	Aa2		AA		AA	
2000	Aa2		AA		AA	
2001	Aa2		AA		AA	
2002	Aa2		AA		AA	
2003	Aa3	(February) ↓	AA-	(October) ↓	A+	(February) ↓
2004	Aa3		AA-		A+	
2005	Aa3		AA-		AA-	(April) ↑
2006	Aa3		AA-		AA-	



## Strengths

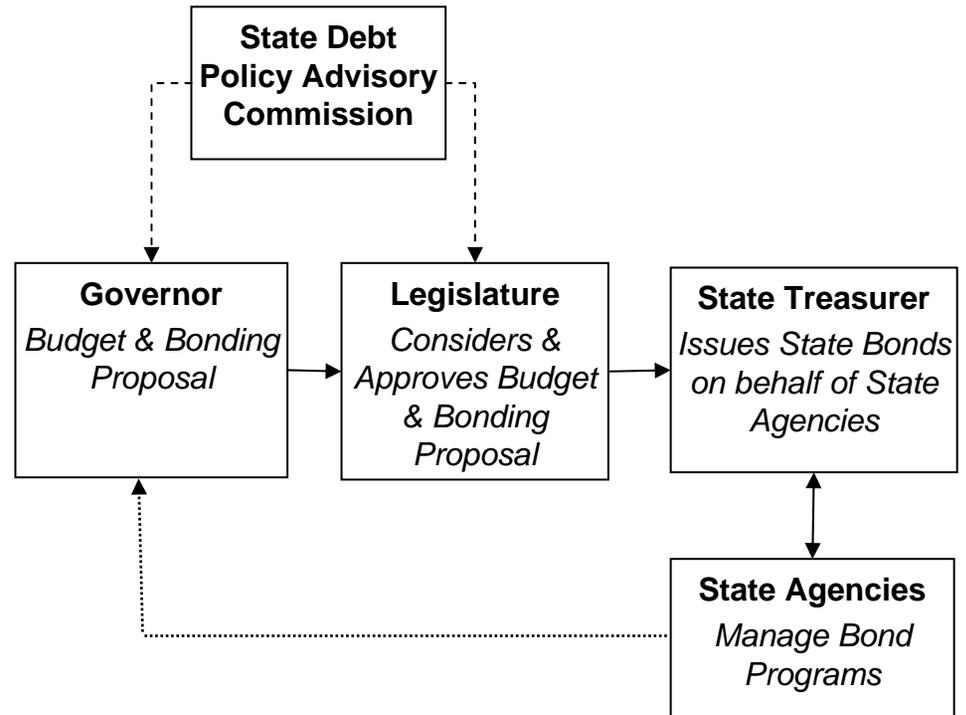
- Strong financial controls
- Conservative, consensus-based revenue forecasting process
- Constitutional balanced budget requirement
- Legislative budget oversight and willingness to adjust budget in response to changing revenue estimates
- Sound debt management and capital planning policies
- Growing economy with improving diversification of economic base
- Growing Education Stability Fund
- Comprehensive pension reform

## Weaknesses

- Low budget reserves
- Uncertainty associated with voter initiative activity
- 2% kicker law makes it difficult to build an adequate budgetary cushion
- Heavy reliance on cyclical income-tax for bulk of state general fund revenues
- Moderate but growing debt burden as state addresses critical infrastructure and capital needs
- Use of deficit financing and one-time revenues to address revenue shortfalls in 2002-03 biennium

# Oregon's Bond Authorization and Issuance Process

- ❑ Oregon has disciplined debt management policies and procedures
- ❑ State Debt Policy Advisory Commission (SDPAC) recommends prudent debt levels based on general fund and lottery revenue forecasts and State's existing debt position
- ❑ Governor presents bonding recommendations as part of proposed State capital construction budget
- ❑ Biennial budget process requires legislative authorization for all new bond issuances during a biennium ("bond bill")
- ❑ State Treasurer's office provides central debt management oversight and issues State bonds
- ❑ State agencies manage on-going bond programs



# Four Types of Long-term Debt

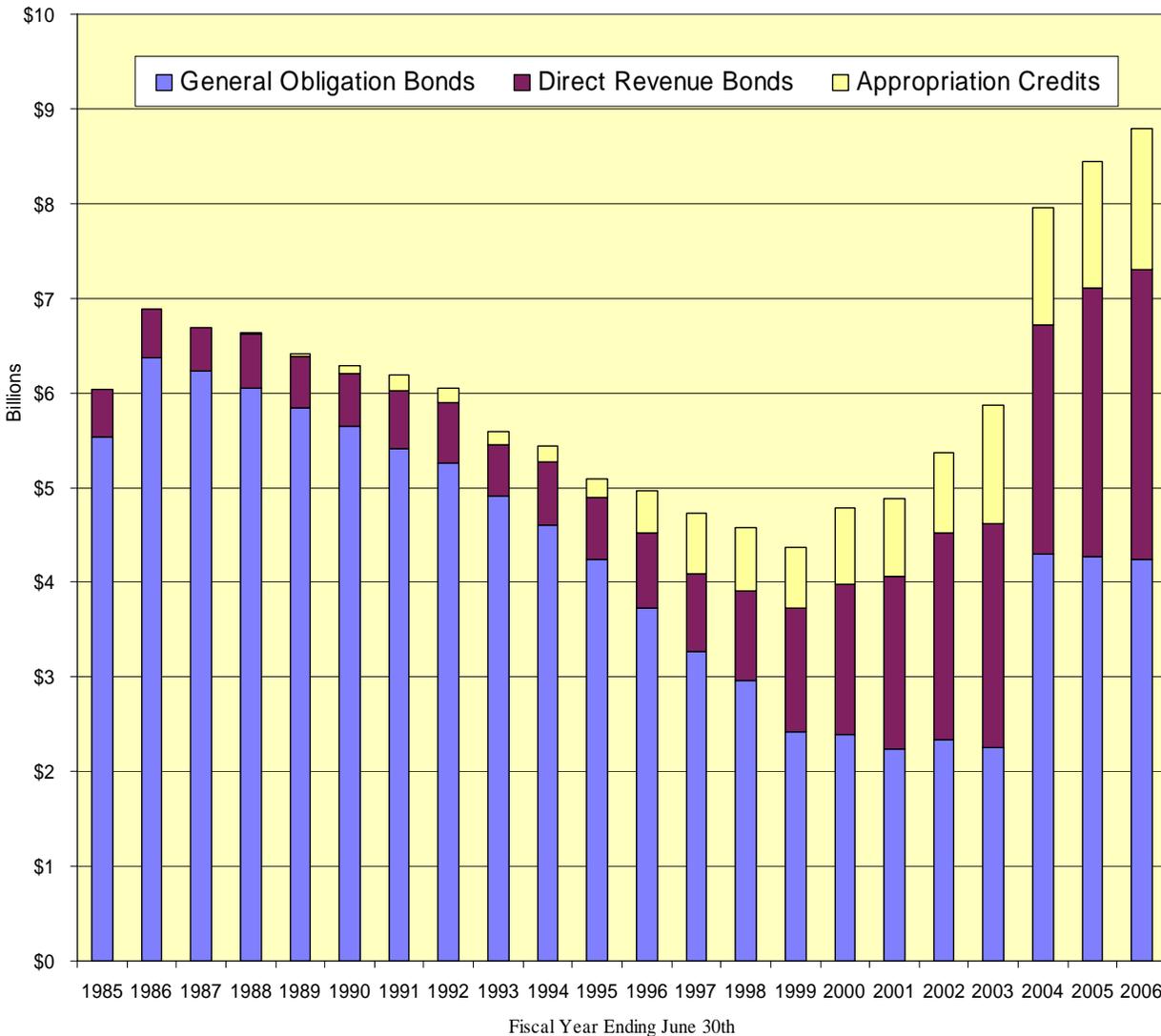
<b>1. General Obligation Bonds</b>	<ul style="list-style-type: none"><li><input type="checkbox"/> Requires voter approved constitutional amendment</li><li><input type="checkbox"/> Pledges the full faith &amp; credit of the state</li><li><input type="checkbox"/> General fund supported <u>or</u> non-general fund supported</li><li><input type="checkbox"/> Debt limits far exceed actual amounts issued in most cases</li></ul>
<b>2. Direct Revenue Bonds</b>	<ul style="list-style-type: none"><li><input type="checkbox"/> Established by the Legislature through statute</li><li><input type="checkbox"/> Not secured by the State's unconditional pledge to pay</li><li><input type="checkbox"/> Fully self-supporting through program revenues</li></ul>
<b>3. Appropriation Credits</b>	<ul style="list-style-type: none"><li><input type="checkbox"/> Appropriation Deficit Bonds issued to balance 2002-03 budget</li><li><input type="checkbox"/> Certificates of Participation (COPs) used to finance real or personal property</li><li><input type="checkbox"/> Generally payable by State agencies from general fund sources</li><li><input type="checkbox"/> Not secured by the full faith and credit of the State</li></ul>
<b>4. Conduit or "Pass Through" Revenue Bonds</b>	<ul style="list-style-type: none"><li><input type="checkbox"/> State is the issuer but has no obligation to pay debt service – no general fund or other state support.</li><li><input type="checkbox"/> Debt service paid by the entities on whose behalf the bonds are issued</li></ul>

## Constitutional & Statutory Provisions

Purpose	Constitutional or Statutory Provision	Constitutional Debt Limit (as % of RMV)	Constitutional Debt Limit (in Millions)	Statutory Debt Limit (in Millions)	Outstanding Debt at 6/30/06 (in Millions)
<b>General Obligation Bonds</b>					
State Highways	Article XI - Sec 7	1.00%	\$5,442.5		\$ 0.0
Higher Education & Comm Colleges	Article XI - Sec G	0.75%	2,721.3		196.8
Seismic Retrofit/ Public Educ Bldgs & Emerg Bldgs	Article XI - Sec M&N	0.20% (each)	725.7 (each)		0.0
<b>Direct Revenue Bonds</b>					
Lottery Bonds	ORS 286.563 - 585				593.6
Highway User Tax	ORS 367.620			\$2,228.0	921.3
Single & Multi Fam Housing Programs	ORS 456.661			2,500.0	1,423.7
<b>Appropriation Credits</b>					
Certificates of Participation	ORS 283 & 286				1,102.6
Appropriation Bonds	SB 856 - 2003 Leg			431.6	385.8

# Trends in overall state bond issuance

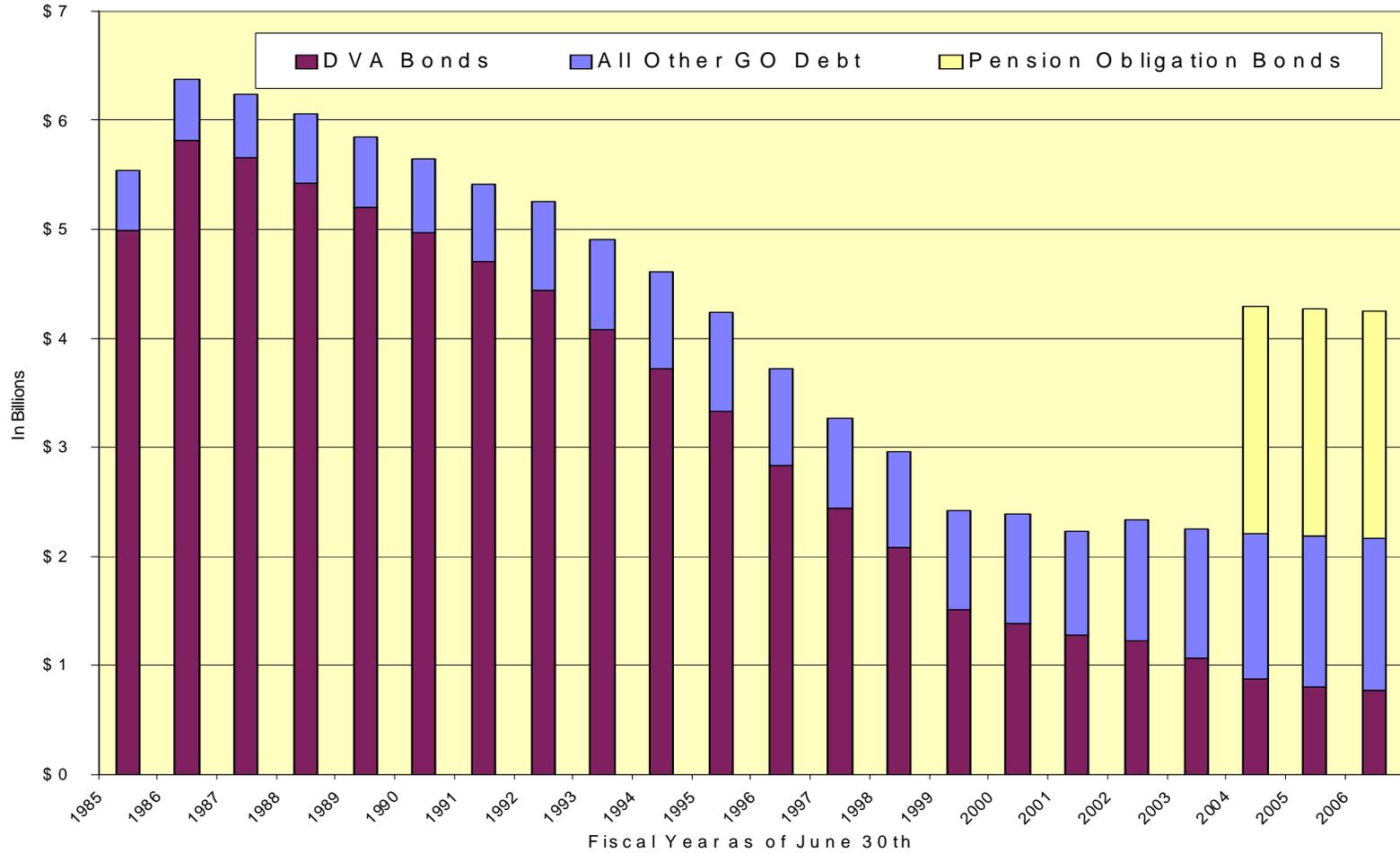
State Debt Outstanding



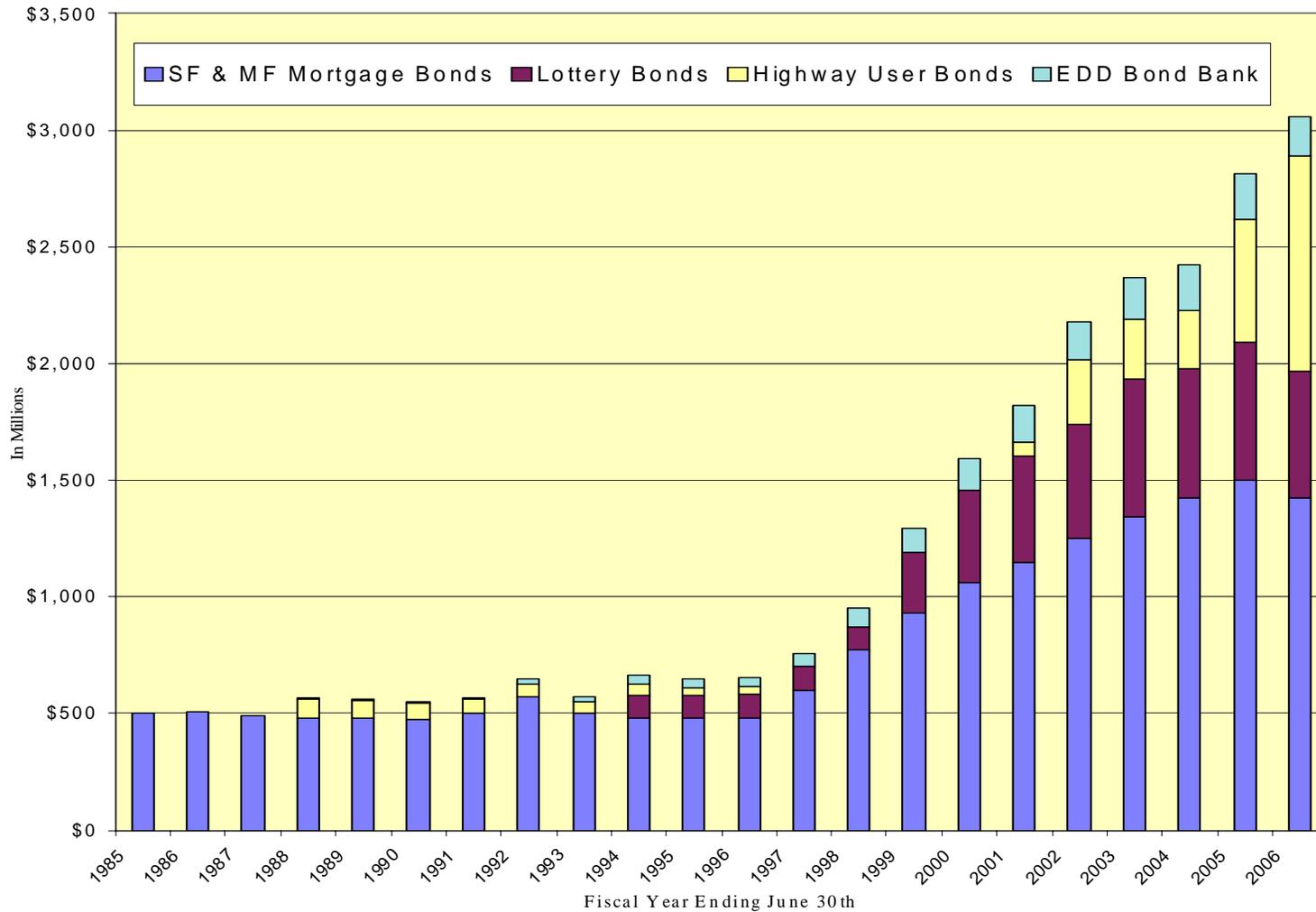
- Twenty years ago, most state bonds were issued for self-supporting Veteran's Mortgage program
- Since late 1990s's, growing use of revenue bonds and COPs by state agencies
- Budget shortfalls in 2003 led to issuance of \$432M in appropriation deficit bonds that will be paid off in 2014
- In 2003, State also issued \$2.0B in general obligation bonds to fund pension liabilities
- On the horizon -- \$1.4B remaining authorization for ODOT bridge and road improvements

# Trends in Issuance of General Obligation Bonds

## Outstanding General Obligation Debt

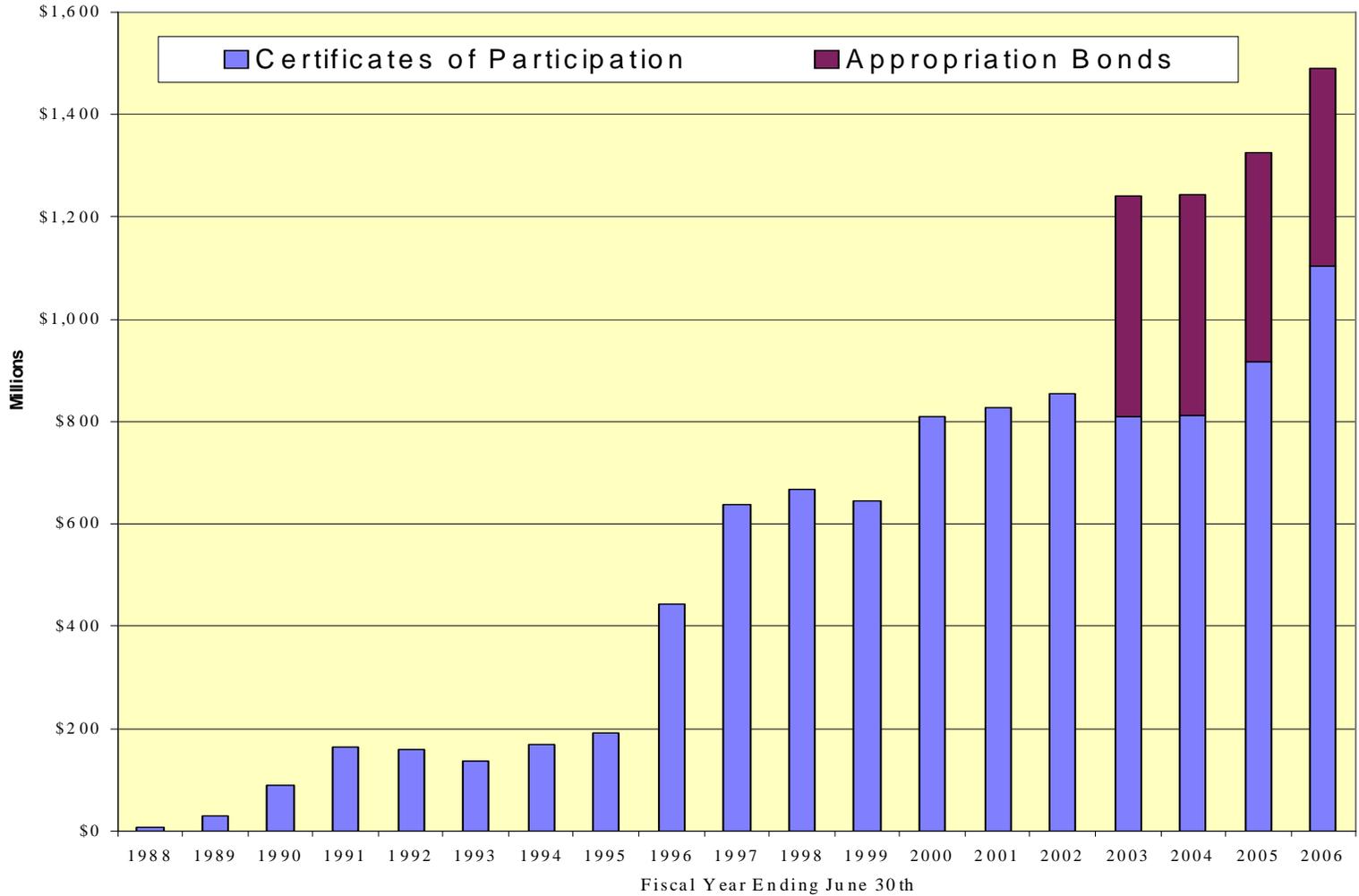


## Outstanding Direct Revenue Bonds



# Trends in Appropriation Credits Issuance

## Outstanding Appropriation Credit



## Four Debt Capacity Categories Considered by SDPAC

<p><b>1. General Fund Supported Debt</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Recommended maximum target:             <ul style="list-style-type: none"> <li>➤ General fund supported debt service not greater than <b>5.0%</b> of general fund revenues</li> <li>➤ As of 6/30/06, general fund debt service ratio was <b>3.7%</b></li> </ul> </li> <li><input type="checkbox"/> Maximum additional general fund debt capacity for 2007-09 biennium based on Dec 2006 revenue forecast -- <b>\$847 million</b></li> </ul>
<p><b>2. Lottery-Backed Debt</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Legal bond covenant - lottery revenue must be at least <b>4.0</b> times debt service on lottery bonds             <ul style="list-style-type: none"> <li>➤ Moral obligation pledge to replenish debt service reserve funds if necessary</li> <li>➤ As of 6/30/06, lottery debt service coverage was <b>7.4</b></li> </ul> </li> <li><input type="checkbox"/> Maximum additional lottery debt capacity for 2007-09 biennium based on Dec 2006 revenue forecast -- <b>\$978 million</b></li> </ul>
<p><b>3. Net Tax-Supported Debt</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> Includes all state indebtedness supported by taxes</li> <li><input type="checkbox"/> Allows national rating agencies to compare 50 states using “apples-to-apples” measurement approach</li> </ul>
<p><b>4. Non Tax-Supported Debt</b></p>	<ul style="list-style-type: none"> <li><input type="checkbox"/> No capacity limit or measurement. State programs in this category are self-supporting and managed by other means (available revenue, coverage tests, etc.)</li> </ul>

## General Obligation Bonds

- Higher Education Facility Bonds (XI-G)
- Community College Bonds (XI-G)
- Pollution Control Bonds (85% of total)
- Oregon Opportunity Bonds (OHSU)
- Water Resources Bonds
- Seismic Retrofit Public Education and Emergency Services Bldgs (XI-M & N)
- Pension Obligation Bonds (38% of total)

## Appropriation Credits

- Certificates of Participation
  - Funds state prisons, office buildings and other capital projects
- Appropriation “Deficit” Bonds

***As of 12/31/06 -- \$2.64 Billion Outstanding***

## General Obligation Bonds

- Higher Education Facility Bonds (XI-G)
- Community College Bonds (XI-G)
- Pollution Control Bonds (85% of total)
- Oregon Opportunity Bonds (OHSU)
- Water Resources Bonds
- Seismic Retrofit Public Education and Emergency Services Bldgs (XI-M & N)
- Pension Obligation Bonds (100% of total)

## Appropriation Credits

- Certificates of Participation
  - Funds state prisons, office buildings and other capital projects
- Appropriation “Deficit” Bonds

## Revenue Bonds

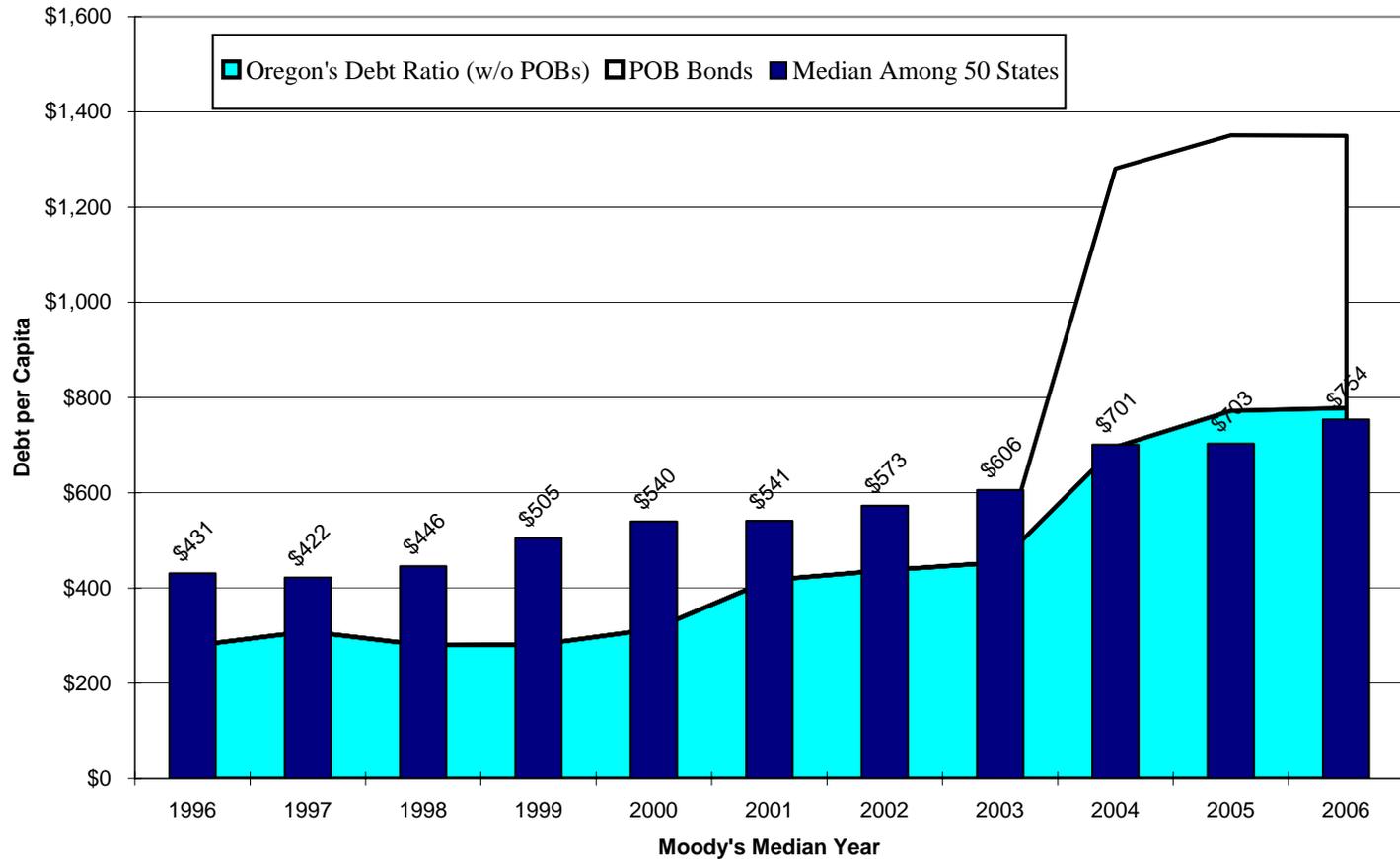
- Highway User Tax Revenue Bonds
- Lottery Revenue Bonds

***As of 12/31/06 -- \$5.41 Billion Outstanding***

# Calculation of Net Tax-Supported and General Fund Debt

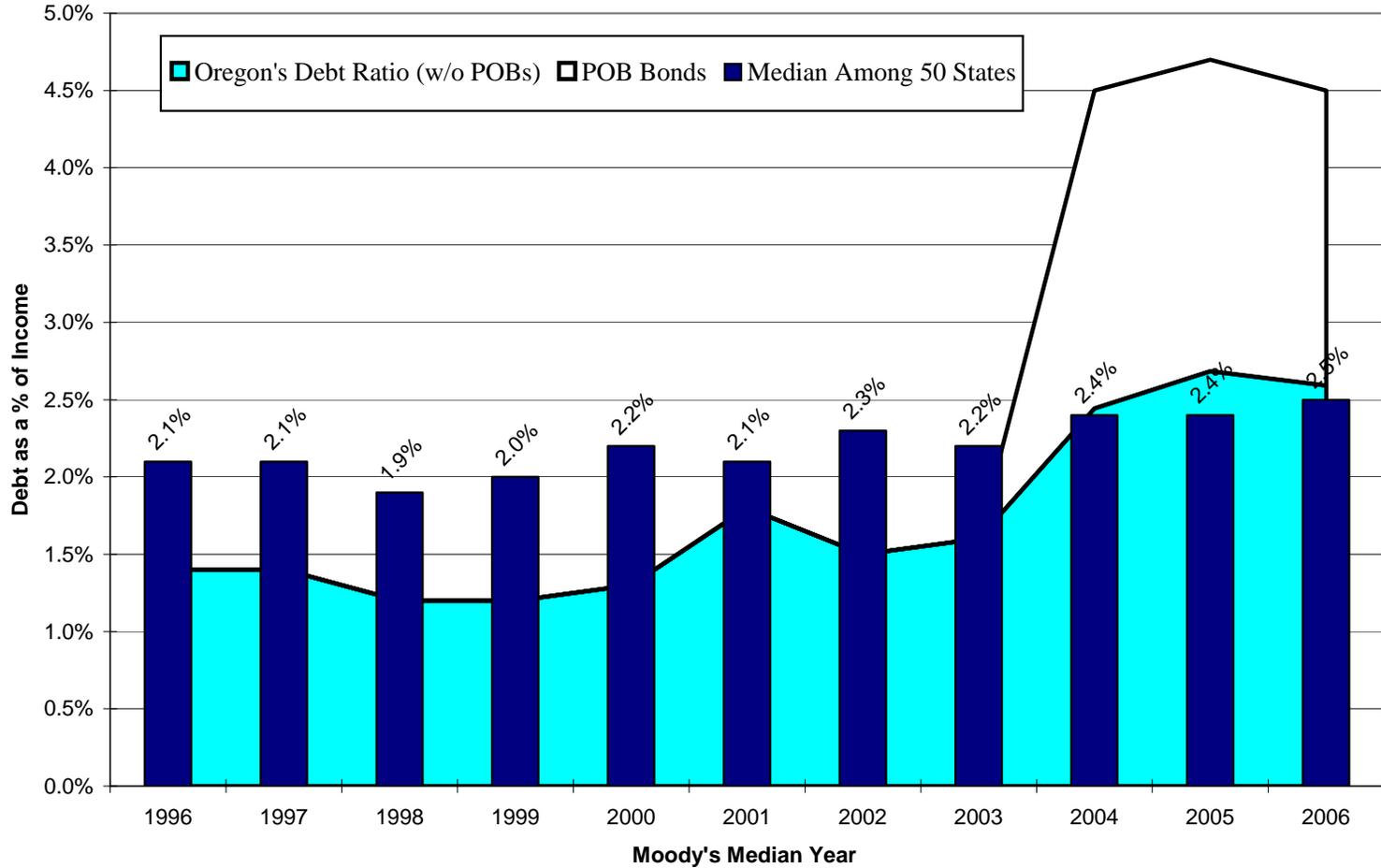
State of Oregon			
Comparison of Total Gross Debt, Net Tax-Supported Debt and General Fund Supported Debt			
as of December 31, 2006			
Type & Purpose	Total Gross Debt Outstanding	Net Tax-Supported Debt	General Fund Supported Debt
<b>General Obligation Bonds</b>			
<i>General Fund Supported</i>			
Community College Bonds	1,700,000	1,700,000	1,700,000
Higher Education Facility (XI-G) Bonds	189,396,367	189,396,367	189,396,367
Pollution Control Bonds (85% of Total)	31,671,000	31,671,000	31,671,000
DAS Oregon Opportunity Bonds	185,065,000	185,065,000	185,065,000
DAS Pension Obligation Bonds (38% of Total)	791,904,800	791,904,800	791,904,800
<b>Total General Fund Supported</b>	<b>\$1,199,737,167</b>	<b>\$1,199,737,167</b>	<b>\$1,199,737,167</b>
<i>Fully Self-Supporting</i>			
Veterans' Welfare Bonds	776,255,000	0	0
Higher Education Facility (XI-F) Bonds	612,913,822	0	0
Pollution Control Bonds (15% of Total)	5,589,000	0	0
Water Resources Bonds	0	0	0
Elderly & Disabled Housing Bonds	192,455,000	0	0
Alternate Energy Project Bonds	136,060,000	0	0
DAS Pension Obligation Bonds (62% of Total)	1,292,055,200	1,292,055,200	0
<b>Total Self-Supporting</b>	<b>\$3,015,328,022</b>	<b>\$1,292,055,200</b>	<b>\$0</b>
<b>Total General Obligation Bonds</b>	<b>\$4,215,065,189</b>	<b>\$2,491,792,367</b>	<b>\$1,199,737,167</b>
<b>Revenue Bonds</b>			
<i>Direct Revenue Bonds</i>			
Lottery Revenue Bond Program(s)	\$577,545,000	\$577,545,000	\$0
Highway User Tax I Revenue Bonds	167,130,000	167,130,000	0
Highway User Tax II Revenue Bonds	739,940,000	739,940,000	0
Economic Development - Bond Bank	159,995,000	0	0
Single-Family & Multi-Family Housing	1,503,855,301	0	0
<b>Total Direct Revenue Bonds</b>	<b>\$3,148,465,301</b>	<b>\$1,484,615,000</b>	<b>\$0</b>
<i>Conduit or Pass Through Revenue Bonds</i>			
Economic & Industrial Development	\$675,935,999	\$0	\$0
Oregon Facilities Authority	781,666,874	0	0
Multi-Family Housing Programs	130,530,480	0	0
<b>Total Conduit or "Pass Through" Revenue Bonds</b>	<b>\$1,588,133,353</b>	<b>\$0</b>	<b>\$0</b>
<b>Appropriation Credits</b>			
Certificates of Participation (COP's)	\$1,077,950,000	\$1,077,950,000	\$1,077,950,000
Oregon Appropriation Bonds	360,240,000	360,240,000	360,240,000
<b>Total Appropriation Credits</b>	<b>\$1,438,190,000</b>	<b>\$1,438,190,000</b>	<b>\$1,438,190,000</b>
<b>Total Gross Debt</b>	<b>\$10,389,853,843</b>		
<b>Total Debt - Less Conduit Revenue Bonds</b>	<b>\$8,801,720,490</b>	<b>\$5,414,597,367</b>	<b>\$2,637,927,167</b>

## Recent Trends in Oregon's Net Tax Supported Debt per Capita



Source: Moody's State Debt Medians Reports, 1996 - 2006

## Recent Trends in Oregon's Net Tax Supported Debt as a % of Personal Income



Source: Moody's State Debt Medians Reports, 1996 - 2006

# ***Conclusions***

- ❑ Oregon's debt programs continue to be prudently managed**
- ❑ While significant debt capacity remains to meet the State's most pressing capital and infrastructure needs, careful prioritization of projects is required to keep the State's debt ratios within SDPAC's target range**
- ❑ Oregon's net tax-supported debt burden has increased substantially since 2003 and this trend is expected to continue for several years as funding of the balance of the OTIA III program is completed**
- ❑ Building up the State's budget reserves will result in higher credit ratings and lower borrowing costs**