FitchRatings

FITCH AFFIRMS DISTRICT OF COLUMBIA'S GOS AT 'AA-'; OUTLOOK STABLE

Fitch Ratings-New York-05 December 2012: Fitch Ratings has affirmed the 'AA-' rating on approximately $2.8 billion in general obligation bonds of the District of Columbia (DC, or the District).

Fitch has also affirmed the 'A+' rating on the following certificates of participation (COPs) of the District:

--$7.7 million COPS series 2002;
--$48.9 million COPs series 2003;
--$170.1 million COP s series 2006.

The Rating Outlook is Stable.

SECURITY

The bonds are general obligations of the District, with its full faith and credit pledged. Also pledged is revenue from a special real property tax, unlimited as to rate or amount and levied in an amount to pay debt service on GO and parity bonds.
The certificates evidence proportionate interests in lease payments from the District to the trustee as lessor for various essential facilities. The payments, equal to annual debt service, are subject to inclusion in the District's annual budget and annual appropriation by the United States Congress.

KEY RATING DRIVERS

SOUND FINANCIAL MANAGEMENT: The District's financial management practices are sound. Recession-driven revenue weakness led to drawdowns of the sizable general fund balance, but the District has begun to restore those losses and reserve levels remain solid. Prudently, the District's current-year budget assumes revenues losses due to possible federal sequestration.

ELEVATED DEBT BURDEN: The District's debt levels are high and expected to remain so, partially due to its unique position in serving as both sole funder and provider of government services for its residents. Pension and OPEB obligations are limited and well managed.

RELIANCE ON FEDERAL GOVERNMENT: Government employees comprise a very high approximately one-third of the District's total employment and an even higher percentage of personal income, with the vast majority from the federal government. While historically this has been an important source of stability, potential sequestration and other expected federal deficit reduction in the coming years could weaken the District's economy.

CREDIT PROFILE

The 'AA-' GO rating reflects the District's strong financial management practices, including consistently sound reserves levels and timely actions to maintain budgetary balance, a broad and diverse array of tax revenues, and high resident wealth levels. The District regularly delivers below budget expenditures, which allowed it to restore general fund reserves in recent years after several years of drawdowns. The recent gains in operating performance are especially impressive in light of the District's continued full funding of its actuarially required contributions (ARC) for pensions and other post-employment benefits (OPEB) obligations. The rating also incorporates the District's high debt ratios, which are expected to remain high, as well as possible economic and revenue weakness due to reliance on the federal government at a time of federal deficit reduction.

FINANCES

District financial operations have begun rebounding from recession-driven pressures. The general fund total balance declined for three consecutive years between fiscal 2008 to fiscal 2010 (years ending Sept. 30). In fiscal 2011, tax revenue growth of 2.8% on a GAAP basis and tight expenditure control (1% growth) resulted in an increase in fund balance. The general fund balance at fiscal year-end 2011 totaled $1.1
billion, or 18.9% of general fund expenditures.

Budgeted general fund expenditures and transfers out, and general fund resources for fiscal 2012 were both 3.6% below the prior year's revised budget. Tax revenues were budgeted to decline 5.9% (including dedicated and non-dedicated). The District's June 2012 revenue estimate substantially improved the forecast, projecting a 6.2% increase in general fund local revenues, and the September 2012 monthly cash report showed a robust 10% gain in general fund taxes (gross basis) from fiscal 2011.

For the current fiscal year (2013), the District's balanced budget conservatively forecasts a 1.2% decline in general expenditures and transfers out versus the revised fiscal 2012 budget estimate, and a 0.4% decline in general fund resources (including a modest $31.2 million use of fund balance). The long-range financial plan through fiscal 2016 projects balanced operations in fiscal years 2014 through 2016, with no use of the fund balance. Pay-go capital contributions, mainly for school modernization are contemplated later in the plan while additional OPEB trust contributions remain budgeted.

ECONOMY

District economic indicators, which grew strongly earlier this decade and significantly outperformed the U.S. in the recession, moderated more recently with just 0.6% year-over-year employment growth in October 2012 versus 1.4% nationally. As the nation's capital, government employment constitutes a substantial nearly one-third of District employment, with the majority made up of federal employees. Federal employment contracted year over year for 13 consecutive months. In October, federal employment declined 1.1% from the prior year. Fitch expects the trend to continue, whether or not federal sequestration is implemented as federal deficit reduction is likely in the coming year. Growth in the services sector, namely education and health, helped offset the government employment contraction. The District's unemployment rate in October reached 8.5%, down substantially from 10.3% in the prior year but still above the national rate of 7.9%.

Income levels remain very high for the district, but growth is slowing relative to the national rate, and an income inequity gap remains. Personal income per capita (PIPC) is by far the strongest in the nation at nearly $74,000 (178% of the U.S. average) in 2011. But the poverty rate was a high 18.7% versus a national 13.2% for the same year. PIPC grew 3.6% in 2011, but that was slower than the national growth rate of 4.4%. That was the first time since 1999 that the District's annual PIPC growth rate fell below the national rate. Federal budget cuts would likely accelerate this trend, though continued growth in the services sectors could provide a partial offset.

DEBT AND OTHER LONG-TERM LIABILITIES

Debt levels are high and are projected to increase moderately given the backlog of deferred capital needs (most importantly for school modernization) and other borrowing plans. Direct tax-supported debt represents a high 18.7% of personal income, 6.1% of 2011 market value, and is $13,826 on a per capita basis. The District's locally funded six-year capital improvement plan (CIP) for fiscal years 2013-2018 totals $5.0 billion (excluding the Local Highway Trust Fund) and is expected to be primarily debt financed, though the District plans to maintain compliance with the Debt Ceiling Act that statutorily limits tax-supported debt service to 12% of expenditures. District debt amortization, when considering GO and income tax secured revenue bonds, is below average, with approximately one-third amortized in 10 years, which Fitch attributes to adherence to the Debt Ceiling Act cap. The 'A+' rating on the District's COPs reflects the District's long-term credit characteristics, satisfactory legal provisions, and the essentiality of the assets financed.

The District's pension and other post-employment benefits (OPEB) obligations are well-managed, partially due to significant support from the federal government. The District's Retirement Board estimates its pension plans for teachers and police/fire employees were over 100% since fiscal 2007. Regarding OPEB, the District makes full ARC payments and reduced its unfunded liability to $784 million at the end of fiscal 2011, or a low 1.7% of the District's personal income.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. State Government Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015
U.S. State Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686033
U.S. Local Government Tax-Supported Rating Criteria
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