State of Ohio

General Government
Full Rating Report

Ratings

Issuer Default Rating	AA+
New Issue	
Capital Facilities Lease-Revenue Appropriation Bonds, Series 2016A (Cultural and Sports Facilities Building Fund Projects)	AA
Outstanding Debt	
General Obligation Bonds	AA+
Lease Appropriation Bonds	AA

Rating Outlook

Stable

Analysts

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New Issue Details

Sale Information: $40,000,000 Capital Facilities Lease-Revenue Appropriation Bonds, Series 2016A (Cultural Facilities and Sports Facilities Building Fund Projects), via negotiation on Aug. 16, 2016.

Security: Special obligation payable under a lease agreement between the Ohio Public Facilities Commission and the Ohio Facilities Construction Commission, subject to appropriation.

Purpose: To fund various capital facilities.

Final Maturity: Oct. 1, 2026.

Key Rating Drivers

The 'AA' appropriation bond rating is one notch below the state's Issuer Default Rating of 'AA+', reflecting the state's careful financial management, ongoing record of maintaining fiscal balance, and moderate, rapidly amortizing debt burden. Liabilities are supported by an economy that is slowly adding jobs lost during the most recent recession.

Economic Resource Base: Ohio's economy is large and diverse, with distinct economic regions centered on several large urban centers. Manufacturing remains a disproportionally large sector, with a concentration in more cyclically sensitive durable goods industries. Transportation equipment and related suppliers have had a strong presence. The state's economy is expanding but at a slower pace than immediately following the recession. Shale gas development along the Utica Shale formation is a potential stimulus in the eastern part of the state.

Revenue Framework ('aa' factor assessment): Like most states, Ohio maintains nearly unlimited ability to raise operating revenues. Its revenue base is diverse and relies on broad-based income and sales taxes. Tax policy changes implemented over the past several biennia have been manageable, aided by favorable economic and fiscal trends.

Expenditure Framework ('aaa' factor assessment): Ohio retains ample flexibility to cut spending throughout the economic cycle. Spending pressure in Medicaid and education appears to be well controlled.

Long-Term Liability Burden ('aaa' factor assessment): Debt is typically conservatively managed and primarily consists of GOs. On a combined basis, outstanding debt and pension obligations are manageable and a well below-average burden on the state.

Operating Performance ('aaa' factor assessment): The state generally has a careful approach to financial operations and has consistently managed to achieve budgetary balance. In recent years, the state has relied more on budget reductions than revenue enhancements to balance the budget and also utilized several one-time sources during the recession. The state's budget stabilization fund is fully funded, having been drawn down during the recession.

Rating Sensitivities

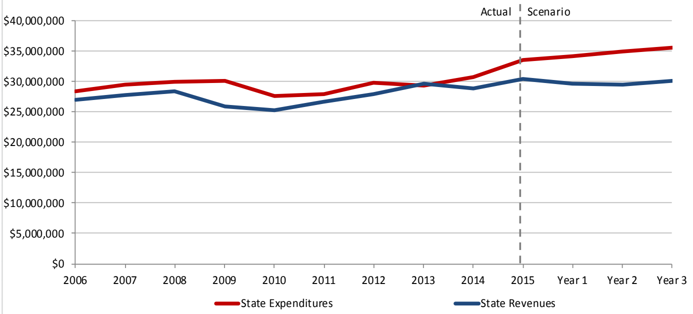
Fundamental Credit Characteristics: Ohio's rating is sensitive to shifts in its fundamental credit characteristics and to continued successful maintenance of fiscal balance in light of ongoing efforts to reduce the tax burden.

Ohio, State of (OH)

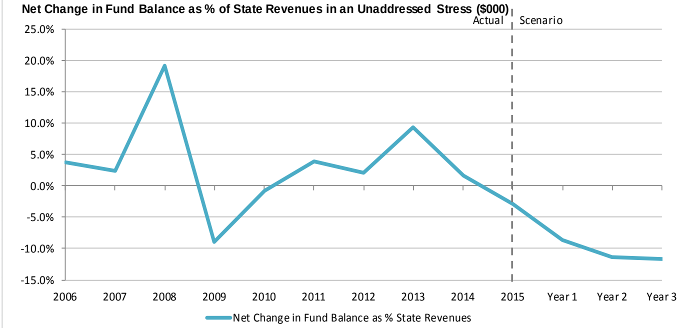
Scenario Analysis

v. 1.01 2016/05/04

State Revenues and Expenditures in an Unaddressed Stress ($000)



Net Change in Fund Balance as % of State Revenues in an Unaddressed Stress ($000)



Analyst Interpretation of Scenario Results:

Ohio's ability to respond to cyclical downturns reflects its ample budget flexibility and availability of reserves. During the most recent recession, Ohio's revenues suffered significant declines, exacerbated by ongoing tax reductions. The state closed the resulting budgetary gaps with both ongoing and one-time measures. Some of these measures include use of the rainy day fund, refunding debt for current year savings, asset sales including the liquor enterprise, changes in the education funding formula, and eliminating tax reimbursements for schools and local governments. It is Fitch's expectation that Ohio will continue to rely primarily on expense reductions to address a future downturn and would again draw upon its now restored rainy day fund.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(2.6%)	(0.3%)	2.1%

Revenues, Expenditures, and Net Change in Fund Balance	Actuals										Scenario Output		
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Year 1	Year 2	Year 3
Expenditures													
Total Expenditures	43,817,188	45,112,929	45,739,194	48,987,312	49,495,495	51,255,563	51,177,175	50,876,071	53,690,264	58,064,992	59,226,292	60,410,818	61,619,034
% Change in Total Expenditures	5.7%	3.0%	1.4%	7.1%	1.0%	3.6%	(0.2%)	(0.6%)	5.5%	8.1%	2.0%	2.0%	2.0%
State Expenditures	28,396,093	29,449,781	29,999,186	30,081,532	27,525,951	27,954,118	29,781,323	29,338,970	30,769,509	33,531,021	34,201,641	34,885,674	35,583,388
% Change in State Expenditures	5.9%	3.7%	1.9%	0.3%	(8.5%)	1.6%	6.5%	(1.5%)	4.9%	9.0%	2.0%	2.0%	2.0%
Revenues													
Total Revenues	42,434,128	43,344,713	44,132,302	44,734,526	47,301,545	49,977,434	49,297,817	51,164,075	51,738,478	54,880,042	54,583,323	55,004,873	56,122,836
% Change in Total Revenues	5.5%	2.1%	1.8%	1.4%	5.7%	5.7%	(1.4%)	3.8%	1.1%	6.1%	(0.5%)	0.8%	2.0%
Federal Revenues	15,421,095	15,663,148	15,740,008	18,905,780	21,969,544	23,301,445	21,395,852	21,537,101	22,920,755	24,533,971	25,024,650	25,525,143	26,035,646
% Change in Federal Revenues	5.3%	1.6%	0.5%	20.1%	16.2%	6.1%	(8.2%)	0.7%	6.4%	7.0%	2.0%	2.0%	2.0%
State Revenues	27,013,033	27,681,565	28,392,294	25,828,746	25,332,001	26,675,989	27,901,965	29,626,974	28,817,723	30,346,071	29,558,672	29,479,730	30,087,189
% Change in State Revenues	5.5%	2.5%	2.6%	(9.0%)	(1.9%)	5.3%	4.6%	6.2%	(2.7%)	5.3%	(2.6%)	(0.3%)	2.1%
Excess of Revenues Over Expenditures	(1,383,060)	(1,768,216)	(1,606,892)	(4,252,786)	(2,193,950)	(1,278,129)	(1,879,358)	288,004	(1,951,786)	(3,184,950)	(4,642,969)	(5,405,944)	(5,496,198)
Total Other Financing Sources	2,402,809	2,422,375	7,059,329	1,923,823	1,984,605	2,326,274	2,457,660	1,010,348	2,440,585	2,284,308	2,103,835	2,059,347	1,979,685
Net Change in Fund Balance	1,019,749	654,159	5,452,437	-2,328,963	-209,345	1,048,145	578,302	2,761,858	488,799	-900,642	-2,539,134	-3,346,597	-3,516,514
% Total Expenditures	2.3%	1.5%	11.9%	(4.8%)	(0.4%)	2.0%	1.1%	5.4%	0.9%	(1.6%)	(4.3%)	(5.5%)	(5.7%)
% State Expenditures	3.6%	2.2%	18.2%	(7.7%)	(0.8%)	3.7%	1.9%	9.4%	1.6%	(2.7%)	(7.4%)	(9.6%)	(9.9%)
% Total Revenues	2.4%	1.5%	12.4%	(5.2%)	(0.4%)	2.1%	1.2%	5.4%	0.9%	(1.6%)	(4.7%)	(6.1%)	(6.3%)
% State Revenues	3.8%	2.4%	19.2%	(9.0%)	(0.8%)	3.9%	2.1%	9.3%	1.7%	(3.0%)	(8.6%)	(11.4%)	(11.7%)

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. For further details, please see Fitch's US Tax-Supported Rating Criteria.

Credit Profile

The recession's impact on the Ohio economy accelerated a longstanding slump in manufacturing and weighed on the slowly growing service sector. Important employment sectors include transportation, distribution, and warehousing of manufactured goods, which is facilitated by an extensive system of ports on Lake Erie, barge service on the Ohio River, and advanced air-cargo and rail infrastructure. Healthcare and education are growing as employment and economic sectors and relatively low non-manufacturing wages in the state have been a magnet for back-office, banking, personnel, and trade operations. While there has been steady year-over-year job growth since July 2010, the state has yet to fully achieve the peak employment reached prior to the recession.

Rating History — GOs

Rating	Action	Outlook/ Watch	Date
AA+	Affirmed	Stable	5/17/16
AA+	Revised	Stable	4/5/10
AA	Downgraded	Stable	6/10/09
AA+	Affirmed	Negative	12/15/08
AA+	Assigned	—	8/14/96

Rating History — Appropriation Bonds

Rating	Action	Outlook/ Watch	Date
AA+	Affirmed	Stable	5/17/16
AA	Revised	Stable	4/5/10
AA–	Downgraded	Stable	6/10/09
AA	Affirmed	Negative	12/15/08
AA	Affirmed	Stable	2/13/07
AA	Upgraded	—	2/3/00
AA–	Assigned	—	8/14/96

Related Criteria
U.S. Tax-Supported Rating Criteria (April 2016)

Revenue Framework

Ohio relies on a diverse set of broad-based taxes to support operations, including income and sales and use taxes. These major tax revenues are collected in the general revenue fund (GRF) with constitutional exceptions for highway-related revenues that are directed to highway purposes and lottery proceeds that are directed to education.

In recent biennia, the state has pursued wide-ranging tax policy changes, shifting the source of GRF tax receipts and lowering overall receipts relative to baseline. To date, these tax policy changes have been manageable, aided by favorable economic and fiscal trends.

Ohio's historical revenue growth — adjusted for the estimated impact of policy changes — has lagged economic growth and has even declined on a real basis, with growth slightly below the inflation rate. Absent tax policy changes, recent performance has been a good deal stronger than is reflected in the historical trend. Fitch anticipates the long-term trend for revenue growth will be in line with historical performance.

Ohio has no legal limitations on its ability to raise revenues through base broadening, rate increases, or the assessment of new taxes or fees.

Expenditure Framework

Ohio has ample flexibility within its expenditure framework. The natural pace of spending growth is likely to be in line with or marginally above its somewhat slowly growing revenue stream. Carrying costs for debt and pensions are well below the median for states.

As with most states, Ohio's spending growth is expected to track future revenue growth. Primary cost drivers include Medicaid and education spending. With a shift to managed care, Medicaid spending growth is contained and with only modest population growth, education spending pressures should be manageable.

Ohio has solid expenditure flexibility. The state has had a budget-cutting bias rather than relying on revenue increases when necessary to maintain budgetary balance even in core spending areas. During the most recent recession, Ohio reduced distributions and phased out certain tax reimbursements to both local governments and school districts. The state's carrying costs for debt and pension obligations are well below the state median and are expected to remain low given the state's well-funded pensions and conservative debt management.

Long-Term Liability Burden

Ohio's liability position and structure are conservative and well below the median for U.S. states. The state carries a moderate amount of rapidly amortized net tax supported debt and debt ratios are expected to approximate current averages as GRF principal continues to roll off and personal income grows.

Funding of retirement benefits — both for pensions and healthcare — have historically been considered a credit strength, with pension systems generally well funded and a history of state full funding of annual contributions. Plans are cost-sharing, multi-employer with limited liabilities attributed to the state. However, funding for Ohio's five pension systems declined significantly with recessionary market losses and has only just begun to recover. Reform measures enacted in September 2012 have contributed to the improved financial sustainability of the Ohio Public Employees Retirement System and the state's other major systems.

The state has $463 million in outstanding general obligation variable-rate debt, with liquidity provided by the state (rated 'F1+'). Of that, $388 million is synthetically fixed through swap agreements. State policy is that all swap counterparties must be rated at least 'AA–'/'AA3' with progressive collateral requirements if the rating falls below this threshold.

Operating Performance

Ohio's ability to respond to cyclical downturns reflects its ample budget flexibility and availability of reserves. For details, see "Scenario Analysis" on page 2.

During times of economic recovery, Ohio rebuilds its financial flexibility including restoring draws on its rainy day fund and reducing the use of one-time budget items. In recent biennia, natural revenue growth has been met with tax reductions, which have, to some extent, absorbed tax revenue increases related to overall economic expansion. While it has been a concern that ongoing tax reductions could limit future flexibility, a statutory increase in the rainy day funding requirement from 5.0% to 8.5% of prior year revenue provides additional capacity to address future downturns and is emblematic of the state's approach during this period of expansion.

The state's cash position is sound. Ohio does not borrow for cash flow purposes and has ample liquidity to provide liquidity for its own variable-rate debt.

The budget for the 2016–2017 biennium was balanced as enacted, while incorporating further tax policy changes. Personal income tax (PIT) rates were lowered further across all brackets, with additional reductions for certain small businesses. Some offset to the reductions was provided by an increase in cigarette taxes, although the governor's proposed increase and expansion of the sales tax was not enacted. The net impact of tax policy changes was expected to reduce biennial revenues by $869 million in fiscal 2016 and $952 million in fiscal 2017, moderating what would otherwise have been strong revenue growth.

The enacted budget was based on an assumption of GRF tax revenue growth, while incorporating the tax reform and policy changes, of 3.3% in fiscal 2016, to $22.1 billion, and another 4.1% in fiscal 2017, to $23.0 billion. In fiscal 2016, tax revenues slightly underperformed forecast, increasing 1.9% year-over-year as compared to the 3.3% estimate. PIT revenues were 2.7% below budget and 8.3% below fiscal 2015. Overall financial performance remained stable with lower spending. The state made a $29.5 million deposit to the rainy day fund bringing its balance to just over $2 billion, or 6% of prior year revenues. The state revised its forecast for fiscal 2017, lowering expected tax receipts by 1.2% to $22.7 billion, to reflect the lower fiscal 2016 revenues.

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.