FITCH RATES MARYLAND'S $1.3B GOS 'AAA'; OUTLOOK STABLE

Fitch Ratings-New York-03 August 2017: Fitch Ratings has assigned a 'AAA' rating to approximately $1.338 billion in State of Maryland general obligation (GO) bonds, state and local facilities loan of 2017, second series, consisting of:

--$550,000,000 second series A tax-exempt bonds (competitive);
--$787,630,000 second series B tax-exempt refunding bonds (competitive).

The par amount of the refunding series is subject to change pending final sale.

The bonds are expected to be offered by competitive sale on or about Aug. 16, 2017.

Additionally, Fitch affirms the long-term Issuer Default Rating (IDR) of the State of Maryland at 'AAA' and affirms the following ratings on securities with ratings linked to the IDR:

--$9.3 billion in outstanding state GO bonds at 'AAA';
--$211 million in outstanding bonds supported by annual general and transportation appropriations at 'AA+';
--$111 million in Maryland Stadium Authority lease revenue bonds at 'AA+'.

The Rating Outlook is Stable.

SECURITY
The bonds are general obligations to which the state's full faith and credit are pledged.

KEY RATING DRIVERS

Maryland's 'AAA' IDR reflects its broad, diverse and wealthy economy, extensive budget controls and sound financial operations, and strong management of debt. The state's economy has long benefited from proximity to the nation's capital, although exposure to federal budget cuts poses a greater uncertainty for Maryland given its large federal agency presence and associated private contracting. Fiscal management is very strong, with consensus-oriented long-term planning and multiple sources of flexibility including a consistently solid budgetary reserve and a demonstrated ability to adjust spending to address changing circumstances. Although liabilities are elevated for a state, they are moderate relative to resources and carefully managed.

Economic Resource Base
Maryland's economy is wealthy, diverse and service-oriented. The presence of the federal government in the neighboring District of Columbia has long served as an important anchor to Maryland's economy, with numerous federal agencies, military facilities and contractors supporting the state's solid economic performance. Trade and port activity are likewise significant given the prominence of Baltimore. Economic expansion continues and in fact accelerated in recent years, despite the earlier drag posed by federal sequestration.

Revenue Framework: 'aaa' factor assessment
Maryland's revenue growth is expected to be in line with or above the level of U.S. economic growth, given the state's solid economic base, service-oriented economy and broad tax resources. The state retains unlimited authority to raise operating revenues. Cyclical revenue performance is

a risk given both the prominence of personal income tax (PIT) in overall state revenues and the state's exposure to changes in federal spending. However, overall growth prospects for revenues remain strong.

Expenditure Framework: 'aaa' factor assessment
Maryland has a solid ability to change its spending commitments in response to shifting economic and revenue circumstances. Spending pressures from education and Medicaid, among other needs, have been notable in recent years. Carrying costs for liabilities are above the median for states, partly given the state's extensive role in funding education needs, including for capital and accrued pension liabilities.

Long-Term Liability Burden: 'aa' factor assessment
The burden of net tax-supported debt and unfunded pensions is elevated for a state, but only a moderate burden in relation to the state's resource base. Debt is comprehensively managed. Pensions have been a more significant burden, but the state has implemented multiple reforms to benefits and contribution policies to improve pension sustainability and accelerate funded ratio improvement over time.

Operating Performance: 'aaa' factor assessment
Financial resilience is very strong, with a well-funded budgetary reserve and a willingness to trim spending commitments and increase revenues in response to changing circumstances. Multi-year forecasting and planning are disciplined, including measuring actual performance against structural targets. Consensus-oriented practices ensure steady management of budgetary conditions and liabilities.

RATING SENSITIVITIES
CONTINUATION OF CURRENT PRACTICES: The rating is sensitive to continued sound fiscal management practices and maintenance of fiscal flexibility, providing the state with the ability to respond to near-term economic or fiscal uncertainties in a manner consistent with the 'AAA' rating.

CREDIT PROFILE

Maryland benefits from a diverse, wealthy economy centered on the Baltimore-Washington, D.C. metropolitan area. Services are the dominant sector, including professional and business services, education and health, and government. Trade and transportation are also significant, with notable port activity centered on Baltimore. The state's large federal workforce includes multiple agencies, research institutions and military facilities, and its importance has grown with several rounds of military consolidation undertaken in recent decades. Private-sector activity associated with federal contracting likewise augments the state's service-sector strength.

The state has generally enjoyed high personal income and solid labor market characteristics, including an unemployment rate consistently below the nation's. The state was not spared from the impact of the last recession; however, the drop-off was less severe and the initial recovery was faster in Maryland compared to the nation. State performance during much of the recovery, however, was slower than national averages, driven in part by federal sequestration and its impact on the federal workforce and on federal contracts. Recent economic gains continue, with personal income growth on a year-over-year basis in the first quarter of 2017 well ahead of the nation's and with job growth matching or exceeding national levels in recent months.

Revenue Framework
Maryland's revenue framework is very diverse. Personal income is the largest source of general revenues, with sales and corporate income taxes also significant. Transportation receipts are

similarly diverse and dedicated to transportation needs. The state also levies a statewide property tax to support general obligation debt.

The state's wealthy, service-oriented economy is the basis for a revenue growth profile that, while subject to economic cyclicality and federal policy actions, is likely to grow faster than state medians over time. Economic sensitivity is most notable in the component of personal income taxes linked to capital gains.

The state has an unlimited legal ability to raise revenues. It has shown a willingness to change tax policy, including implementing rate increases, in response to changing budgetary circumstances.

Expenditure Framework
Spending commitments are dominated by education and social services. Education spending for K-12, provided via transfers to counties, expanded significantly a decade ago as the state sought to address concerns regarding school funding adequacy. Education spending also includes amortization contributions for local teacher retirement liabilities, capital support, and a large and growing network of higher education institutions. Social services, including for Medicaid, are also a large and growing component of the state's budget.

Consistent with most states, spending is expected to be in line with to marginally above expected revenue growth, driven by social services spending needs.

Federal action to revise Medicaid's programmatic and financial structure remains a possibility given recent federal legislative and administrative efforts. Most proposals to date include a basic restructuring of federal Medicaid funding to a capped amount. Whether any future change in federal Medicaid funding has consequences for Fitch's assessment of a state's credit quality would depend on the state's fiscal response to those changes. Responses that create long-term structural deficits or increase liability burdens could negatively affect both the expenditure framework assessment and the IDR.

The state has demonstrated a solid ability to cut spending. Carrying costs for liabilities are higher than the median for states but remain manageable relative to resources. Debt service is elevated given a constitutional requirement to amortize most tax-supported borrowing within 15 years. Carrying costs also include those associated with accrued pension liabilities of local teachers although newly-earned benefits are the responsibility of local governments. The state has likewise established a practice of contributing additional resources to pensions to accelerate funding progress, most recently by establishing a mechanism to divert a portion of unappropriated surpluses to reduce the unfunded liability.

Long-Term Liability Burden
On a combined basis, net tax-supported debt and pension liabilities attributable to the state as of Fitch's 2016 state pension update are above average for a state, measuring 10.1% of personal income, compared to a statewide median of 5.1%. Tax-supported debt, which Fitch calculates at $13.1 billion, including new bond proceeds, measures 3.8% of 2016 personal income. Centralized debt planning and issuance are additional credit strengths. Debt affordability guidelines include holding tax-supported debt at or below 4% of personal income.

Pensions are a comparative credit weakness in Maryland, although the state has taken repeated action since 2011 to reform benefits and contribution practices. Reforms have included lower benefit accruals, higher service requirements, a phased-in decline in the discount rate, ending a contribution methodology that had consistently left actual contributions below actuarial calculations and replacing it with full actuarial contributions, and appropriating supplemental contributions. Given the changes implemented to date, Fitch views the prospects for funding improvement to be increased assuming investment performance matches expectations.

On an accounting basis, pension assets cover 67.7% of pension liabilities as of the state's fiscal 2016 financial statements, which were calculated assuming a 7.55% investment return assumption; since then, this rate has been lowered to 7.45%. Most of the state's net pension liability (NPL) consists of obligations for state employees and local teachers in the State Retirement and Pension System. As adjusted by Fitch to reflect a 6% return assumption (based on Fitch's U.S. Public Finance Tax-Supported Rating Criteria), pension assets would cover 57.8% of pension liabilities. When combined with net tax-supported debt, this would bring the state's long-term liability burden to 13.1% of personal income.

Changes in 2011 to other post-employment benefits are estimated to have reduced the state's OPEB liability by approximately 40% as measured at the time. The total unfunded OPEB liability as of June 30, 2016 was $11.8 billion.

Operating Performance
Maryland's financial resilience is exceptionally strong. Historically the state has relied on spending cuts, revenue increases and the use of non-recurring resources, including draws from the revenue stabilization account (RSA; the state's rainy day fund) when confronted with budgetary weakness.

The state has disciplined consensus revenue forecasting and monitoring that identify material changes in the direction of state economic and revenue performance. The Board of Public Works, which includes the Governor, Comptroller and Treasurer, has the power to trim spending during the year in response to budgetary weakness, and demonstrated this ability repeatedly during the last downturn.

The state routinely budgets to maintain flexibility both in the form of a general fund unencumbered balance and the separate RSA balance, the latter of which has been consistently funded at or near the statutory target of 5% of general fund revenues, including through most of the last downturn. The RSA balance has risen in step with the budget in recent years, and is forecast at $833 million (5% of general fund revenues) in fiscal 2017 and $859 million in fiscal 2018.

The state adopted further changes with its fiscal 2018 budget to manage revenue volatility, beginning in fiscal 2020. Under these changes, PIT revenues from non-withholding components that exceed a 10-year average will be diverted from routine spending and instead be directed to address general fund revenue shortfalls, build the RSA up to as high as 10% of general fund revenues, and ultimately cover one-time pay-go needs for K-12 and higher education.

Recent budgetary performance has been steady, although general fund revenues in fiscal 2017 slightly underperformed earlier estimates, driven primarily by sales tax weakness. Year-to-date collections through June, excluding the recognition of year-end accruals, are 2% above prior year levels and just below target. Fiscal 2017 revenues are forecast at $16.6 billion, 4% higher than fiscal 2016 actual revenues. Including reversions and deficiencies addressed in the legislative session, fiscal 2017 spending is forecast at $17.1 billion, 6% higher than fiscal 2016, with the state forecasting a general fund ending balance of $93.3 million (0.6% of general fund revenues), compared to $365 million in the adopted budget.

The adopted budget for fiscal 2018 anticipates that general fund revenues will rise 4% in fiscal 2018, to $17.1 billion. Total spending is forecast at $17.2 billion, an increase of 0.5%, as the state focuses on aligning structural spending with revenues. Although most program spending continues to rise, lower one-time appropriations for pay-go capital spending and reserve transfers and declining state employment, among other factors, restrain spending growth. Including adopted budget actions, the fiscal year is forecast to end with a general fund balance of $91.1 million (0.5% of general fund revenues).

Contact:

Primary Analyst
Douglas Offerman
Senior Director
+1-212-908-0889
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Eric Kim
Director
+1-212-908--0241

Committee Chairperson
Marcy Block
Senior Director
+1-212-908-0239

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available on www.fitchratings.com

Applicable Criteria
U.S. Public Finance Tax-Supported Rating Criteria (pub. 31 May 2017)
https://www.fitchratings.com/site/re/898466

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS. IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Copyright © 2017 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third- party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged

in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.
For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001