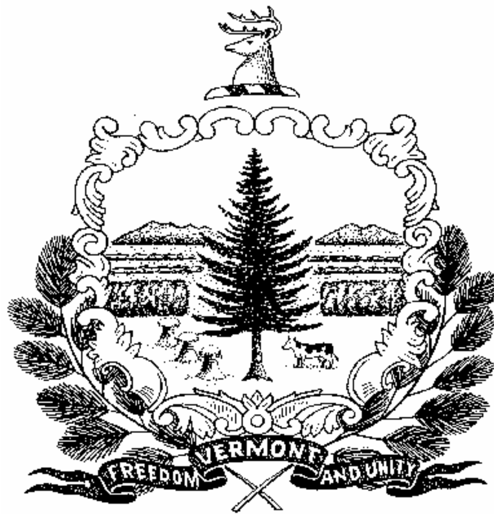
Government Finance Associates, Inc.

590 Madison Avenue, 21st Floor
New York, New York 10022
(212) 521-4090/4091
Fax (212) 521-4092

CAPITAL DEBT AFFORDABILITY ADVISORY COMMITTEE

State of



Vermont

RECOMMENDED ANNUAL GENERAL OBLIGATION DEBT AUTHORIZATION

September 2007

TABLE OF CONTENTS

Introduction....1

1. Debt Statistics....6
2. Economic and Financial Forecasts....10
3. Debt Authorizations and Projection Scenarios....13
4. Debt Ratios....16
5. Summary....22
6. Provisions of Enabling Legislation and Methodology....23
7. Appendices....27

INTRODUCTION

We are pleased to present this report to the Capital Debt Affordability Advisory Committee of the State of Vermont (the "Committee" or "CDAAC"). As in prior years, this analysis is intended to assist the Committee in determining the maximum amount of long-term, general obligation debt ("G.O. debt") that the State should authorize for the upcoming fiscal year (ending June 30, 2009).

The Committee's enabling legislation requires the Committee to present to the Governor and the General Assembly each year, no later than September 30, a recommendation as to the maximum amount of G.O. debt the State should authorize for the forthcoming fiscal year, consistent with certain guidelines enumerated in the statute. This report provides the supporting analysis and documentation necessary for the Committee to comply with the legislative requirements. As required by the enabling legislation, this analysis extends through fiscal year 2018.

In fiscal year 2007, $44.5 million of G.O. debt was issued (representing all but $500,000 of the full amount of that year's authorization) while $46.1 million of G.O. debt was retired. It is expected that during FY 2008, a total of $49.2 million of general obligation bonds will be issued, representing the full amount of the year's authorization. This year's report presents an analysis of the recommended level of G.O. debt issuance for FY 2009 of $54.65 million. The reasons for CDAAC's recommendation of $54.65 million are set forth below under "Reasons for Fiscal 2009 Recommended Authorization."

According to Moody's Investors Service's most recent information, the State's relative position, among states, changed during the past year with respect to both net tax-supported debt as a percent of personal income (improving from 28th in 2006 to 30th in 2007) and net tax-supported debt per capita (declining from 29th in 2006 to 28th in 2007).

In September 2004, the Committee adopted new debt guidelines, reflecting the State's comparative current and prospective performance in terms of debt load measures (i.e., debt per capita and debt as a percent of personal income) against triple-A rated states. This new set of guidelines reflected, among other things, the commitment of the State to work toward the achievement of a triple-A investment grade rating from all three major rating agencies.

Moody's Triple-A Rating

The State of Vermont achieved a very significant milestone in February when it was raised to the coveted triple-A category by Moody's Investors Service. Not since the early 1970s has Vermont been rated Aaa by Moody's. There are cost of capital and economic development reasons, among others, that the triple-A rating is a very worthy goal to be achieved. Among the reasons Moody's cited for the increased rating was the State's "steady progress in reducing previously high debt ratios and maintaining an affordable debt profile." Based on numerous communications with Moody's, it has also become

clear that the role of the CDAAC and the credibility that CDAAC has brought to the debt authorization process were factors in the rating agency's decision to take this important move. Over time, we expect that Fitch and Standard & Poor’s will duplicate Moody's action and increase the State's rating to triple-A. The State's adherence to the debt guidelines, as previously indicated, will improve the prospects for that eventuality.

Moody's Credit Scorecard

In August 2007, Moody's Investors Service issued its annual report entitled, "U.S. States Credit Scorecard." This report has been included as an appendix to this document. It is being included for the reason that Moody's has identified the scorecard "as an additional analytic tool to enhance the consistency of our state general obligation (G.O.) credit analysis." As part of the Moody's report, the rating agency places each of the 50 states within one of five tiers for the four major rating categories germane to a Moody's rating: finance, economy, debt, and governance.

For the most recent scorecard, Vermont was dropped from the first tier to the second tier in finance and economy but was raised in governance. It is our understanding that for the governance factor, the State was improved, largely as a result of the advances the State has made in recent years in financial reporting. At the same time, Moody's has indicated that the State's decline in the finance ranking is, in part, a result of Vermont expenditures being a little higher, on a percentage basis, than in previous years. Apparently, the decrease in the economy ranking occurred from Vermont's job and income growth being at a slower pace than for the nation as a whole.

In terms of a general explanation, Moody's has stated that even though there was a deterioration for the State in the scorecard in two categories, Vermont's general obligation rating was increased to Aaa over the last year. The agency indicates that the scorecard is backward looking, while ratings are forward looking, so that adjustments in tier classification does not have a direct bearing on the State's rating. It is also relevant, according to Moody's, to note that since only ten states fall into each tier, Vermont, as a result of its being toward the end of the alphabet, would be one of the first states to fall from one tier to the next if another state were moved into the same tier in which Vermont appeared.

Approach To State Moral Obligation Indebtedness

As the State’s rating improves, the value of its moral obligation also grows. It is therefore likely that there will be greater pressure on the State to raise the size of its existing moral obligation commitments and/or to assign the moral obligation pledges to new State borrowers. In this context, it is relevant for CDAAC to consider a policy approach toward quantifying and limiting the State’s exposure to this type of debt. Indeed, without some form of containment, it is possible that an ever-increasing moral obligation debt load could, over time, erode the State’s debt position.

In accordance with the appropriate provisions from the enabling statute that created CDAAC, the Committee has already been authorized to consider "any other long-term debt of instrumentalities of the state not secured by the full faith and credit of the state, or for which the state legislature is permitted to replenish reserve funds." Therefore, it is not inconsistent for CDAAC to develop guidelines for Vermont regarding the size and use of the State's moral obligation debt.

In recent years, CDAAC has adjusted its debt load guidelines to take into account the comparative debt load statistics for triple-A rated states throughout the country. Unfortunately, none of the rating agencies prepare comparative data on the respective triple-A rated states on moral obligation or contingent debt. Moreover, there is little consistency among the triple-A rated states regarding the size, nature and role of such debt; for example, the moral obligation component in Virginia represents less than 20% of the Commonwealth's tax-supported debt, while the contingent-type debt in Delaware is approximately the same size as Delaware's tax-supported debt. Also, the types of contingent debt are quite varied among the states, including state guarantees of local school debt, back-up support for revenue obligations, etc. Because of the mixture of contingent debt applied by triple-A states, it would not be possible to employ guidelines that are similar to the general obligation guidelines that have been utilized by CDAAC in connection with its annual recommendation of long-term general obligation debt to be authorized by the State legislature.

Therefore, it is our recommendation that CDAAC develop an approach toward moral obligation debt that is consistent with the State's conservative debt management and that is acceptable to the nationally recognized credit rating agencies. Toward this end, we propose consideration of the following approach.

Amount of MO/Contingent Debt As Of 6/30/07*: $745 million

Amount of State General Obligation Debt As Of 6/30/07: $438 million

* Includes $52,450,000 of Vermont Municipal Bond Bank debt sold on July 11, 2007.

Using a multiple of 225% of GO debt, the State could have outstanding (using current computations) as much as $985 million of MO/contingent. This approach would give the State enough flexibility to deal with any foreseeable (and even unforeseen) needs, but it would also establish some discipline in addressing future moral obligation commitment requests in the context of the increased the value of the State's MO pledge.

There have been some preliminary discussions with the rating agencies regarding this approach. As a general matter, the agencies are pleased that Vermont is attempting to restrain the potential growth in this area. For example, the State of Maine has adversely affected its debt position by supplying over the years too much moral obligation commitment. At the same time, it would not appear that the rating agencies will give the State an approval of the precise percentage that would be employed; indeed, the level of

potential exposure will likely have to become a decision that the State will need to make, in consultation with its financial advisor.

Incipient Lease Transactions

For the first time in a number of years, the State is expecting to incur lease indebtedness. First, Vermont anticipates the purchase of rail cars in the approximate amount of $17.5 million as a demonstration project, utilizing a Federal loan assistance program. Under a "buy-back" provision from the supplier of the rail cars, the State will be allowed, after making an initial down payment of approximately $1.7 million, to put back the cars to the supplier over the initial three-year period after delivery of the cars if the project proves unsatisfactory. The credit of the supplier to actually take back the cars is an outstanding issue at the present time. As a result of this "buy-back" structure (if the credit issue with the supplier can be satisfactorily resolved), we would not plan to put this debt on the State's debt statement until after the three-year period has ended. This structure has been veted with the rating agencies, and they generally concur with the approach.

Second, the State is also considering a lease financing for energy savings in the amount of approximately $4.5 million. It is hoped that the operating savings from greater energy efficiencies through improved facilities will more than cover the debt service costs; from this perspective, the State will argue that this lease should be self-supporting. At this point, the rating agencies have not been briefed on the project. The briefings will occur after receipt of financing proposals from a request for proposals that has only been recently distributed.

CDAAC has taken the appropriate position that in the absence of special security provisions, such as those outlined above, lease (capital/finance) obligations must be taken into account as part of the authorization recommendation process. For example, for the 2001 recommendations, the amount to be recommended was reduced from $39 million to $34 million when it was discovered that there was an outstanding capital lease in the amount of $5.0 million then being carried in the Department of Transportation.

Reasons For Fiscal 2009 Recommended Authorization

As stated above, CDAAC is proposing that the maximum amount of long-term G.O. debt authorized for the State in fiscal 2009 be $54.65 million. The rationale for this recommendation is presented below:

1. The fiscal 2005 recommended authorization rose by over 5% from $39 million to $41 million, and the fiscal 2006 recommended authorization increased the 2005 authorization by nearly 10% to $45 million for an increase of over 15% in two years. The FY 2007 recommended authorization remained at the 2006 level. In addition, there was an additional $4.2 million increase for fiscal 2008, reflecting a 26% increase over the period 2004-2008. The CDAAC is proposing a further increase to $54.65 million, or over 40% for the 2004-2009 period.

2. Nonetheless, CDAAC believes that the fiscal 2009 recommended authorization is consistent with its policy of trying to provide important capital contributions to the State's physical infrastructure requirements within a framework of acceptable debt affordability. Over the last five years, including fiscal 2009, CDAAC has recommended a sizeable amount of new capital funding for Vermont – that is, approximately $40 million of additional proceeds in aggregate from the sale of general obligation debt toward the State's capital improvement program.

3. At present, the State is in compliance with all of its guidelines with the exception of the 5-year median debt per capita for triple A-rated states. However, based on current projections, the $54.65 million debt authorization amount is expected to allow the State to be in line with all debt guidelines within the near future without any deterioration in meeting our schedule for compliance, possibly as early as 2008. Any higher amounts would delay this occurrence.

4. CDAAC also has some concerns about the economic and financial uncertainties affecting the country near-term. With volatile oil prices, significant market volatility, Federal deficits, mortgage defaults and uneven economic trends, the economic and financial outlook of the State and the country is now more unsure; as a result, CDAAC believes it is a more prudent course of action for the State at present to continue to be modest with respect to new authorizations of future State indebtedness.

This year's report is organized into seven sections. **Section 1** presents the State's key existing debt statistics. **Section 2** consists of economic and financial forecasts. **Section 3** discusses the State's recent authorization history and sets forth the effect of the issuance of $49.2 million in fiscal year 2008 and $54.65 million annually thereafter on future outstanding debt and debt service requirements. **Section 4** includes a history of the State's debt ratios and shows the projected effect of the Section 2 and 3 forecasts on the State's future debt ratios. **Section 5** summarizes the findings of the previous sections and offers considerations for the Committee in its determination of whether to revise the planned future fiscal year debt authorizations. **Section 6** documents relevant provisions of the enabling legislation and explains the methodology and assumptions behind certain projections included in this report. **Section 7** is composed of appendices, including rating agency reports and the "Vermont Economic Outlook" dated May 2007 published by the New England Economic Partnership ("NEEP").

We would like to express our gratitude to the State Treasurer's Office, the Department of Finance and Management, Economic and Policy Resources, Inc. ("EPR"), NEEP, and various officers and staff members of the State, whose assistance has been invaluable in completing this report. Certain computations and projections were made based on population, personal income, and revenue projections provided by EPR. The numbers presented herein have not been audited and are, therefore, subject to change, possibly in a substantial manner.

DEBT STATISTICS

Net Tax-Supported Debt Outstanding

The State's aggregate net tax-supported principal amount of debt decreased from $440.0 million as of June 30, 2006 to $438.4 million as of June 30, 2007, a decrease of 0.36%. Except for the fiscal year 2002, when a carry-forward amount of authorization was included in the debt issue, for each of the years during the period 1999-2006, the State retired more G.O. bonds than it sold, including the issuance of refunding debt.

The table below sets forth the sources of the change in net tax-supported debt outstanding from 2006 to 2007 (in thousands):

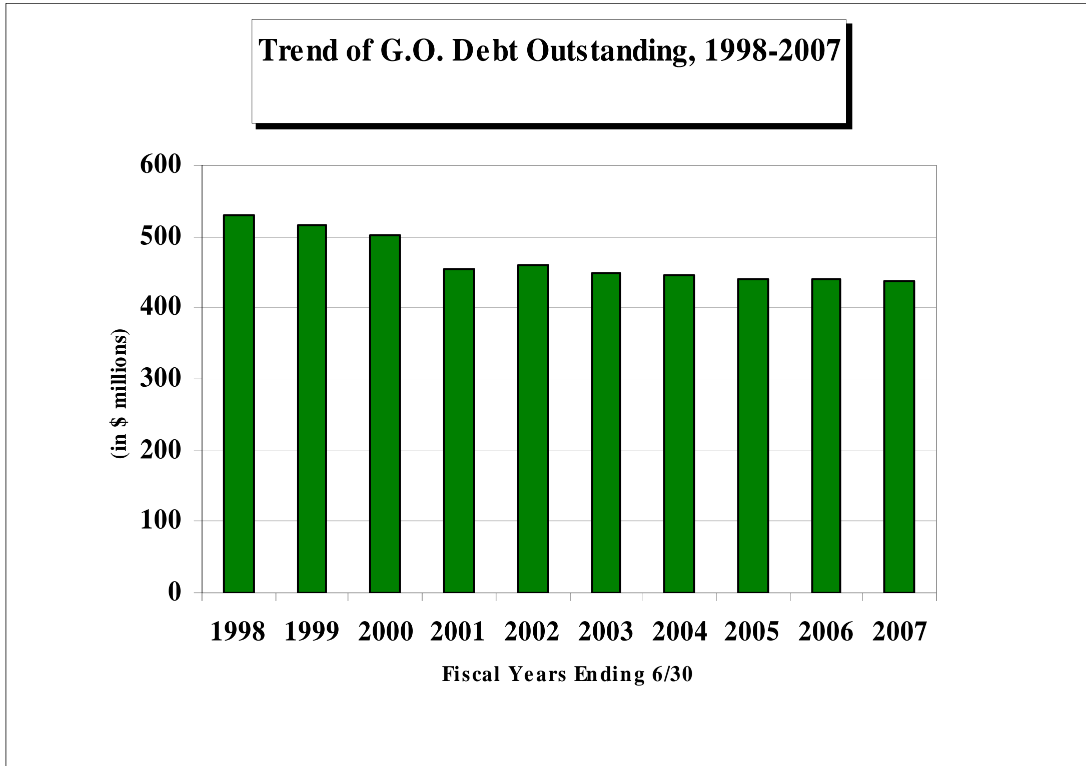
Net Tax-Supported Debt as of 6/30/06	$439,994
G.O. New Money Bonds Issued	44,500
Less: Retired G.O. Bonds	(46,097)
Net Tax-Supported Debt as of 6/30/07	$438,397

Debt Statement

As of June 30, 2007 ($ Thousands)

General Obligation Bonds*:	
General Fund	417,698
Transportation Fund	10,594
Special Fund	10,105
Contingent Liabilities:	
VEDA Mortgage Insurance Program	9,068
VEDA Financial Access Program	896
Reserve Fund Commitments:	
Vermont Municipal Bond Bank	479,950
Vermont Housing Finance Agency	92,605
VEDA Indebtedness	70,000
Vermont Telecom Authority	40,000
Gross Direct and Contingent Debt	1,130,916
Less:	
Contingent Liabilities	(9,964)
Reserve Fund Commitments	(682,555)
Net Tax-Supported Debt	**438,397**

* Includes original principal amounts of Capital Appreciation Bonds.



G.O. DEBT OUTSTANDING, 1998-2007
(As of June 30, in $ millions)

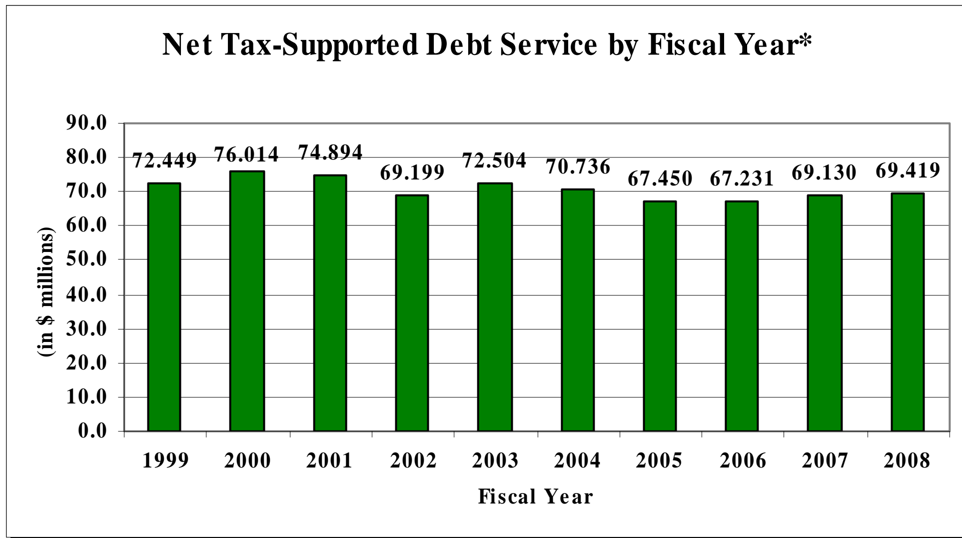
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
TOTAL	528.6	517.3	503.9	454.9	460.5	448.2	444.7	440.3	440.0	438.4

(THIS SPACE INTENTIONALLY LEFT BLANK)

Net Tax-Supported Debt Service by Fiscal Year

- The State's net tax-supported fiscal year debt service requirement for fiscal year 2008 will be $69.42 million, 0.42% more than the $69.13 million paid in fiscal year 2007. This increase comes after annual decreases ranging from 0.3% to 7.6% over the period 2000-2007, except for an anomaly of a 4.8% increase in 2003.

Net Tax-Supported Debt Service Paid in FY 2007	$69,130
Decrease in Annual D/S Requirement FY 2007-2008	(2,588)
D/S Increase Due to G.O. Debt Issued in FY 2007	2,887
Net Tax-Supported Debt Service Due in FY 2008	$69,419



**Consists of General Obligation Bonds.*

(THIS SPACE INTENTIONALLY LEFT BLANK)

The table below sets forth the State's existing principal amounts outstanding and annual debt service requirements as of June 30, 2007 without the issuance of any additional G.O. debt. Please refer to the table on page 14 for the State's projected principal amounts outstanding and annual debt service requirements assuming the issuance of $49.2 million G.O. debt during FY 2008 and $54.65 million annually thereafter through and including FY 2018.

PROJECTED GENERAL OBLIGATION NET TAX-SUPPORTED DEBT
As of June 30, 2007
(in $ thousands)

	GENERAL OBLIGATION BONDS							
	GENERAL FUND		TRANSP. FUND		SPECIAL FUND		STATE DIRECT DEBT	
Fiscal Year	Beginning Principal Outstanding	Debt Service	Beginning Principal Outstanding	Debt Service	Beginning Principal Outstanding	Debt Service	Beginning Principal Outstanding	Debt Service
2008	417,698	64,926	10,594	1,997	10,105	2,496	438,397	69,419
2009	374,574	62,827	9,088	1,912	8,120	2,496	391,782	67,235
2010	332,249	58,133	7,594	1,795	6,030	2,500	345,873	62,428
2011	292,925	54,054	6,146	1,728	3,825	1,026	302,896	56,809
2012	256,238	48,063	4,695	1,642	2,985	626	263,918	50,331
2013	221,001	41,885	3,259	790	2,505	628	226,765	43,303
2014	189,610	40,659	2,605	760	2,000	629	194,215	42,048
2015	158,352	30,579	1,953	472	1,470	633	161,775	31,684
2016	134,442	26,437	1,563	356	910	636	136,915	27,428
2017	113,638	22,691	1,272	343	320	336	115,230	23,370
2018	95,714	19,805	981	232	0	0	96,695	20,037

(THIS SPACE INTENTIONALLY LEFT BLANK)

2. ECONOMIC AND FINANCIAL FORECASTS

This section of the report is based on the economic analysis provided by NEEP for the State of Vermont. NEEP's report, "Vermont Economic Outlook," dated May 2007 (a copy of which is included in the appendices), states that "the overall tone to the Vermont outlook is positive, but the pace of economic and labor market activity is expected to remain restrained throughout the 2007-11 forecast time horizon."

According to the May 2007 NEEP Report, "growth in the Vermont economy will slow in 2007 followed by healthier rates of growth throughout the remainder of the forecast period. Job growth will remain sluggish throughout the forecast period with an improving tone to the rate of job growth in the later years of the forecast period. Output growth, with the exception [of 2007], is expected to grow at a slightly higher pace than New England as a whole [and the] unemployment rate will continue to remain among the lowest in New England region – if not among states in the entire country."

"The housing market correction in Vermont remains as the most significant unknown and the largest source of downside forecast risk – given the current shakeout in subprime lending and the higher than average contribution that home construction (particularly second home construction) made to Vermont's recent job and economic growth." Declines in housing prices "are not expected to be of the magnitude or persist for the length of time necessary to derail the current economic upturn either nationally or in the state. However, it is unmistakable that the housing market correction has and will continue to be a drag on the pace of the state's economic progress over at least the next 6 quarters."

Another major factor in the NEEP outlook "concerns the resumption of the upward creep in energy prices, just as the summer driving season is about to begin," affecting Vermont's tourism economy since money that is spent on higher gas prices will take money away from expenditures by visitors on "entertainment-recreational activities and on other goods and services that drives Vermont's tourism sector."

"On the upside, the fundamentals of the U.S. economy and the Vermont economy overall remain sound, and the global economy is experiencing strong, broad based growth creating healthy demand for American goods and services (including Vermont goods and services). The weak dollar is reinforcing the demand created by a healthy global economy, and is being particularly helpful in northern Vermont where Canadian activity is boosting activity."

The NEEP report states that "growth overall in the Vermont economy is expected to remain positive but restrained. Payroll job growth is expected to remain between 0.50% and 1.0% throughout the forecast period, while personal income is expected to grow at relatively healthy rates of between 2.3% and just under 3.5%. Manufacturing employment is expected to remain slightly positive for the next two years but will be

offset by declining construction employment over the same period. Output growth is expected to have its second weak year in a row in calendar 2007, followed by rates of growth ranging between 2.5% and 3.0% over the rest of the forecast period."

As shown below, the EPR forecasts for Vermont indicate growth in revenues, population, personal income and estimated full valuation.

As shown in the table below, EPR's population estimate for 2007 is about 0.35% greater than its forecast for 2006, and its estimates of future population growth average about 0.38% annually from 2008 through 2018. Personal income increased 5.7% from 2006 to 2007 and is projected to achieve an average annual growth rate of 4.9% from 2008 through 2018. Estimated full valuation increased 1.3% from 2006 to 2007 and is projected to achieve an average annual growth rate of 2.3% from 2008 through 2018. EPR's current and projected General Fund and Transportation Fund revenues are shown in the table on the following page.

Current and Projected Economic Data [1]

Year	Population (in thousands)	Personal Income (in $ billions)	E.F.V. (in $ millions)
2005	622.6	20.36	56,404
2006	624.1	21.32	57,959
2007	626.3	22.54	58,721
2008	629.1	23.71	60,266
2009	631.9	24.94	61,934
2010	634.0	26.17	63,502
2011	636.4	27.50	65,073
2012	639.7	28.89	66,685
2013	642.6	30.28	68,243
2014	645.0	31.70	69,749
2015	647.2	33.18	71,201
2016	649.1	34.70	72,603
2017	650.9	36.30	74,047
2018	652.8	37.98	75,484

(1) These figures were prepared by EPR, except Effective Full Valuation. We projected Effective Full Valuation based on Real Vermont Gross State Product annual growth rates provided by EPR.

As shown in the table below, total revenue for fiscal year 2007 is $49.6 million more than in 2006, an increase of 3.8%. Fiscal year 2008 revenue growth is forecast at 2.1%, and the average annual revenue growth rate during the period 2008 through 2018 is expected to be approximately 3.3%.

Current and Projected Revenues [2]

Fiscal Year	General Fund (in $ millions)	Transportation Fund (in $ millions)	Total Revenue (in $ millions)
2006	1,111.9	209.9	1,321.8
2007	1,151.5	219.9	1,371.4
2008	1,170.2	229.4	1,399.6
2009	1,198.8	234.4	1,433.2
2010	1,249.0	241.5	1,490.5
2011	1,302.2	247.2	1,549.4
2012	1,352.2	255.6	1,607.8
2013	1,399.5	262.1	1,661.6
2014	1,442.9	271.3	1,714.2
2015	1,492.0	278.1	1,770.1
2016	1,538.2	286.8	1,825.0
2017	1,593.6	294.2	1,887.8
2018	1,647.8	302.9	1,950.7

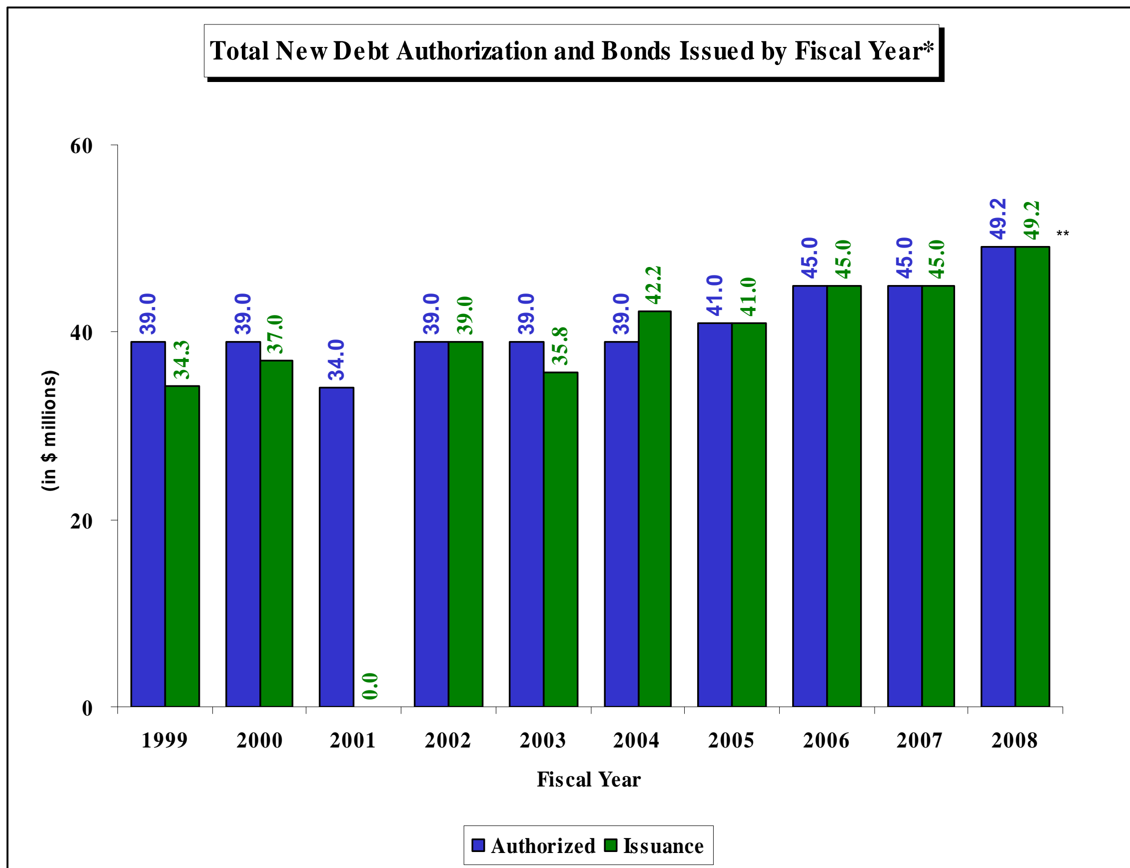
(2) Amounts for FY 2007-2018 are "current law" revenue forecasts based on a consensus between the State's administration and legislature.

(THIS SPACE INTENTIONALLY LEFT BLANK)

3. DEBT AUTHORIZATIONS AND PROJECTION SCENARIOS

Recent Debt Authorizations

During fiscal year 2004, $42.2 million of debt was sold, representing the full amount of that year's authorization ($39 million) plus the carry forward of the authorized but unissued amount from fiscal year 2003 ($3.2 million). During fiscal years 2005 and 2006, $41 million and $45 million of debt, respectively, were sold, representing the full amount of those years' authorizations. During fiscal year 2007, $44.5 million of debt was issued, representing all but $500,000 of the $45 million authorized for that year. During fiscal year 2008, $49.2 million of debt is expected to be sold, the total amount of the 2008 authorization. We believe this trend in which the State has annually extinguished all or nearly all of the authorized amount of debt so that there doesn't exist a rising residual amount of authorized but unissued debt has enhanced the State's credit position with favorable responses from the rating agencies. The following chart presents the amounts of G.O. debt that have been authorized and issued by the State since 1999.



** Authorized but unissued debt has been carried forward and employed in subsequent years' bond issuances. Note: It should be emphasized that a sizeable amount of the $34 million authorization in 2001 was paid down through pay-as-you-go funding and the use of surplus funds.*
*** Anticipated to be issued.*
Note: Annual issuances do not include refunding bonds.

General Obligation and General Fund Supported Bond Debt Service Projections

The State's projected annual G.O. debt service and debt outstanding are presented on the following page and summarized below. The projected debt service (at 6% interest rate) assumes the issuance of $49.2 million in G.O. debt during fiscal year 2008 and $54.65 million annually thereafter through fiscal year 2018.

TOTAL PROJECTED GENERAL OBLIGATION DEBT SERVICE AND DEBT OUTSTANDING (In Thousands of Dollars)

Fiscal Year	G.O. Debt Service
2007	69,130
2008	69,419
2009	72,777
2010	73,973
2011	74,185
2012	73,366
2013	71,823
2014	75,880
2015	70,651
2016	71,357
2017	72,088
2018	73,372

Fiscal Year Ending	G.O. Bonds Outstanding
6/30/2007	438,397
6/30/2008	440,982
6/30/2009	447,133
6/30/2010	453,336
6/30/2011	460,658
6/30/2012	466,925
6/30/2013	474,915
6/30/2014	480,135
6/30/2015	490,060
6/30/2016	500,285
6/30/2017	510,785
6/30/2018	521,065

(THIS SPACE INTENTIONALLY LEFT BLANK)

EXISTING AND PROJECTED NET TAX-SUPPORTED G.O. DEBT SERVICE ($000)													
		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total
	Current	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Est.
FY	D/S	49.2MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	D/S
2008	69,419												69,419
2009	67,235	5,542											72,777
2010	62,428	5,387	6,159										73,973
2011	56,809	5,231	5,986	6,159									74,185
2012	50,331	5,076	5,813	5,986	6,159								73,366
2013	43,303	4,920	5,641	5,813	5,986	6,159							71,823
2014	42,048	4,765	5,468	5,641	5,813	5,986	6,159						75,880
2015	31,684	4,610	5,290	5,468	5,641	5,813	5,986	6,159					70,651
2016	27,428	4,454	5,118	5,290	5,468	5,641	5,813	5,986	6,159				71,357
2017	23,370	4,299	4,945	5,118	5,290	5,468	5,641	5,813	5,986	6,159			72,088
2018	20,037	4,143	4,773	4,945	5,118	5,290	5,468	5,641	5,813	5,986	6,159		73,372

EXISTING AND PROJECTED NET TAX-SUPPORTED G.O. BOND PRINCIPAL PAYMENTS ($000)													
		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total
	Current	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Est.
FY	Principal	49.2MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	Principal
2008	46,615												46,615
2009	45,909	2,590											48,499
2010	42,977	2,590	2,880										48,447
2011	38,978	2,590	2,880	2,880									47,328
2012	37,153	2,590	2,880	2,880	2,880								48,383
2013	32,550	2,590	2,880	2,880	2,880	2,880							46,660
2014	32,440	2,590	2,880	2,880	2,880	2,880	2,880						49,430
2015	24,860	2,590	2,875	2,880	2,880	2,880	2,880	2,880					44,725
2016	21,685	2,590	2,875	2,875	2,880	2,880	2,880	2,880	2,880				44,425
2017	18,535	2,590	2,875	2,875	2,875	2,880	2,880	2,880	2,880	2,880			44,150
2018	15,880	2,590	2,875	2,875	2,875	2,875	2,880	2,880	2,880	2,880	2,880		44,370

EXISTING AND PROJECTED NET TAX-SUPPORTED G.O. BONDS OUTSTANDING ($000)													
		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total
	Current	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Issue	Est.
FY	Debt	49.2MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	54.65MM	Debt
2007	438,397												438,397
2008	391,782	49,200											440,982
2009	345,873	46,610	54,650										447,133
2010	302,896	44,020	51,770	54,650									453,336
2011	263,918	41,430	48,890	51,770	54,650								460,658
2012	226,765	38,840	46,010	48,890	51,770	54,650							466,925
2013	194,215	36,250	43,130	46,010	48,890	51,770	54,650						474,915
2014	161,775	33,660	40,250	43,130	46,010	48,890	51,770	54,650					480,135
2015	136,915	31,070	37,375	40,250	43,130	46,010	48,890	51,770	54,650				490,060
2016	115,230	28,480	34,500	37,375	40,250	43,130	46,010	48,890	51,770	54,650			500,285
2017	96,695	25,890	31,625	34,500	37,375	40,250	43,130	46,010	48,890	51,770	54,650		510,785
2018	80,815	23,300	28,750	31,625	34,500	37,375	40,250	43,130	46,010	48,890	51,770	54,650	521,065

4. DEBT RATIOS

G.O. Debt Guidelines

In the last several years, the State's investment grade ratings have significantly improved. Even before the State's rating was increased to Aaa by Moody's, the State had been the highest rated state in New England for several years. The State also enjoys high double-A ratings from the two other nationally recognized credit rating agencies. The State is currently pursuing a strategy to achieve a triple-A rating in the near future from all three nationally recognized credit rating agencies and has employed its debt load guidelines to assist the State achieve this goal.

CDAAC has adopted guidelines that are consistent with a triple-A rated state. As such, there are four guidelines that are followed by CDAAC in the development of the annual proposed general obligation bond authorization. First, the State will be guided annually by its ability to meet the 5-year average for the mean in per capita debt load for triple-A states. Second, the State should be able annually to meet the 5-year median of triple-A states in per capita debt load. Third, the State should be able to meet annually the 5-year average for the mean of debt as a percent of personal income for triple-A states. Fourth, the state will be guided annually by its ability to meet the 5-year median for triple-A states of debt as a percent of personal income. At present, the State is able to meet three of the four standards for both debt per capita and debt as a percent of personal income. Vermont, at present, is not able to meet the 5-year median debt per capita for triple-A rated states. It is our expectation that the spread between the triple-A 5-year median and Vermont's performance with respect to debt per capita should close over time; until such time as that happens, the median related to debt per capita will remain a goal.

In addition, CDAAC has adopted the guideline of limiting annual general obligation debt service to no more than 6% of operating revenues, consisting of the annual aggregate of General and Transportation Funds. At present and based on the 2009 proposed general obligation authorization amount, the State will be in compliance with the 6% guideline for the foreseeable future. Please see the accompanying charts to evaluate the State's current and anticipated position with respect to the CDAAC guidelines.

This section discusses the impact of the proposed issuance of $49.2 million of G.O. debt during FY 2008 and $54.65 million of G.O. debt annually during FY 2009-2018 on the State's key debt ratios. Please refer to the "Historical and Projected Debt Ratios" on page 21 for the statistical detail described below.

Debt Per Capita

The Committee has adopted a guideline for the State to equal or perform better than the 5-year average for the mean and 5-year median of triple-A rated states on the basis of debt per capita. At present, the targets are $838 for the mean and $691 for the median. Based on data from Moody's Investors Service, Vermont's 2007 debt per capita figure of

$706 is better than the 5-year average mean for triple-A rated states but is above the median. However, looking at 2007 figures alone for triple-A rated states, Vermont's relative comparison improves, although the State is still not able to match the median. Using the 5-year Moody's median for triple-A rated states ($691) and increasing it by 2.70% annually, combined with an assumption that the State will issue $54.65 million through 2018, it appears that Vermont will match the 5-year Moody's median for triple-A rated states in the near future, possibly as early as 2008 (see "Historical and Projected Debt Ratios"). It should be emphasized that the debt numbers for Vermont have been falling and stabilizing while those of the triple-A rated states, on a composite basis, have been rising – this factor explains the reason that the State should incrementally improve its relative position regarding debt per capita over time.

Debt as a Percent of Personal Income

The Committee has adopted a guideline for the State to equal or perform better than the 5-year average for the mean and 5-year median of triple-A rated states on the basis of debt as a percent of personal income. At present, the targets are 2.7% for the mean and 2.4% for the median. Based on data from Moody's Investors Service, Vermont's debt as a percent of personal income figure is better than the 5-year average mean and 5-year median for triple-A rated states. Moreover, considering the 2007 figures alone, Vermont's relative comparison improves even more, with a widening gap between Vermont's figure and those of the triple-A rated states. Assuming that the State will issue $49.2 million in FY 2008 and $54.65 million annually thereafter through 2018, Vermont should continue to improve relative to the 5-year average of mean and 5-year median for triple-A rated states (see "Historical and Projected Debt Ratios").

Debt Service as a Percentage of Revenues[1]

This ratio, reflecting annual general obligation debt service as a percent of the annual aggregate General and Transportation Funds, is currently 5.1%. With the projected issuance of G.O. debt, this ratio is expected to decrease to 5.0% for the fiscal year ending June 30, 2008, increase to 5.1% during the next fiscal year, and drop 0.01%-0.05% annually thereafter until 2018, at which time it is estimated to be 3.8%. As noted elsewhere herein, the State's newly adopted standard for this category is 6% of annual general obligation debt service as a percent of the annual aggregate General and Transportation Funds. At present and for the foreseeable future, it is anticipated that the State will satisfy this standard by a considerable margin.

[1] *In this discussion, "Revenues" does not include any revenues associated with Act 60.*

STATE OF VERMONT

APPROACH TOWARD ESTABLISHING DEBT RATIO GOALS

Comparative Mean Debt Ratios*

Per Capita	2003	2004	2005	2006	2007
All States	$ 838	$ 944	$ 999	$1,060	$1,101
Triple-A**	735	823	831	879	922
VERMONT	**861**	**724**	**716**	**707**	**706**
% of Pers. Inc.	**2003**	**2004**	**2005**	**2006**	**2007**
All States	2.7%	3.1%	3.2%	3.2%	3.2%
Triple-A**	2.5	2.7	2.7	2.8	2.7
VERMONT	**3.0**	**2.5**	**2.3**	**2.2**	**2.1**

* Based on data provided by Moody's Investors Service and excluding Florida prior to 2006 and Vermont.

** See chart on "Debt Per Capita" for complete listing of triple-A states and respective ratings. Eleven states currently rated triple-A by one or more of the nationally recognized rating agencies: Delaware, Florida (in 2005), Georgia, Maryland, Minnesota, Missouri, North Carolina, South Carolina, Utah, Virginia and Vermont (in 2007).

Listing of Triple-A Rated States By Rating Agency

2007 Triple-A Rated States	Fitch	Moody's	S&P
Delaware	Yes	Yes	Yes
Florida	No	No	Yes
Georgia	Yes	Yes	Yes
Maryland	Yes	Yes	Yes
Minnesota	Yes	No	Yes
Missouri	Yes	Yes	Yes
North Carolina	Yes	Yes	Yes
South Carolina	Yes	Yes	No
Utah	Yes	Yes	Yes
Virginia	Yes	Yes	Yes
VERMONT	No	Yes	No

(THIS SPACE INTENTIONALLY LEFT BLANK)

STATE OF VERMONT

MOODY'S INVESTORS SERVICE
DEBT PER CAPITA

Triple-A Rated States	July, 2007 Ratings							
	Moody's	S&P	Fitch	2003	2004	2005	2006	2007
Delaware	Aaa/Stable	AAA/Stable	AAA/Stable	$1,599	$1,800	$1,865	$1,845	$1,998
Florida*	Aa1/Stable	AAA/Stable	AA+/Stable	985	1,023	1,008	976	1,020
Georgia	Aaa/Stable	AAA/Stable	AAA/Stable	802	827	803	784	916
Maryland	Aaa/Stable	AAA/Stable	AAA/Stable	977	1,077	1,064	1,169	1,171
Minnesota	Aa1/Stable	AAA/Stable	AAA/Stable	625	691	679	746	827
Missouri	Aaa/Stable	AAA/Stable	AAA/Stable	368	461	449	496	613
North Carolina	Aaa/Stable	AAA/Stable	AAA/Stable	429	556	682	804	728
South Carolina	Aaa/Negative	AA+/Stable	AAA/Stable	587	599	558	661	630
Utah	Aaa/Stable	AAA/Stable	AAA/Stable	682	846	792	707	621
Virginia	Aaa/Stable	AAA/Stable	AAA/Stable	546	546	589	601	692
MEAN**	___________	___________	__________	**735**	**823**	**831**	**879**	**922**
MEDIAN**	___________	___________	__________	**625**	**691**	**682**	**765**	**778**
VERMONT*	Aaa/Stable	AA+/Stable	AA+/Stable	861	724	716	707	706

* Florida raised to triple-A in 2005 and first reflected in 2006 numbers; Vermont raised to triple-A in 2007.
** These calculations include Florida for the years 2006 and 2007, and exclude Vermont numbers.

Triple-A Rated States
5-Year Mean and Median Including Florida and Excluding Vermont:
MEAN: $838 Vermont: $743
MEDIAN: $691 Vermont: $716

(THIS SPACE INTENTIONALLY LEFT BLANK)

STATE OF VERMONT

MOODY'S INVESTORS SERVICE
DEBT AS % OF PERSONAL INCOME

Triple-A Rated States	2003	2004	2005	2006	2007
Delaware	5.0%	5.6%	5.5%	5.3%	5.5%
Florida*	3.5	3.5	3.4	3.2	3.1
Georgia	2.9	2.9	2.8	2.7	3.0
Maryland	2.8	3.0	2.9	3.0	2.8
Minnesota	1.9	2.0	2.0	2.1	2.2
Missouri	1.3	1.6	1.5	1.6	1.9
North Carolina	1.6	2.0	2.5	2.8	2.4
South Carolina	2.4	2.4	2.2	2.5	2.3
Utah	2.9	3.5	3.2	2.7	2.3
Virginia	1.7	1.7	1.8	1.7	1.8
MEAN**	**2.5**	**2.7**	**2.7**	**2.8**	**2.7**
MEDIAN**	**2.4**	**2.4**	**2.5**	**2.7**	**2.3**
VERMONT*	3.0	2.5	2.3	2.2	2.1

* Florida raised to triple-A in 2005 and first reflected in 2006 numbers; Vermont raised to triple-A in 2007.
** These calculations include Florida for the years 2006 and 2007, and exclude Vermont numbers.

Triple-A Rated States

5-Year Mean and Median Including Florida and Excluding Vermont:
MEAN: 2.7% Vermont: 2.4%
MEDIAN: 2.4% Vermont: 2.3%

(THIS SPACE INTENTIONALLY LEFT BLANK)

Government Finance Associates, Inc.

Historical and Projected Debt Ratios

Fiscal Year (ending 6/30)	Net Tax-Supported Debt Per Capita (in $): State of Vermont	Moody's Median	State's Rank [4]	Net Tax-Supported Debt as Percent of Personal Income: State of Vermont	Moody's Median	State's Rank [4]	Net Tax-Supported Debt Service as Percent of Revenues [5]: State of Vermont [2]	Moody's Median	State's Rank [4]
Actual [1]									
1996	984	431	9	4.9	2.1	8	7.2	3.5	8
1997	992	422	9	4.7	2.1	8	6.9	n.a.	n.a
1998	946	446	9	4.2	1.9	9	7.6	n.a.	n.a
1999	953	505	10	4.2	2.0	10	7.2	n.a.	n.a
2000	925	540	9	3.8	2.2	10	7.0	n.a.	n.a
2001	828	541	15	3.3	2.1	14	6.8	n.a.	n.a.
2002	813	573	18	3.0	2.3	14	6.5	n.a.	n.a.
2003	861	606	16	3.0	2.2	17	6.7	n.a.	n.a.
2004	724	701	24	2.5	2.4	25	6.0	n.a.	n.a.
2005	716	703	25	2.3	2.4	27	5.4	n.a.	n.a.
2006	707	754	29	2.2	2.5	28	5.1	n.a.	n.a.
2007	706	787	28	2.1	2.4	30	5.1	n.a.	n.a.
Current [2]	700	n.a.	n.a.	1.9	n.a.	n.a.	5.1	n.a.	n.a.
Projected (FYE 6/30) [3]		State Guideline [6]			State Guideline [7]			State Guideline	
2008	701	710		1.9	2.4		5.0	6.0	
2009	708	729		1.8	2.4		5.1	6.0	
2010	715	748		1.7	2.4		5.0	6.0	
2011	724	769		1.7	2.4		4.8	6.0	
2012	730	789		1.6	2.4		4.6	6.0	
2013	739	811		1.6	2.4		4.3	6.0	
2014	744	833		1.5	2.4		4.4	6.0	
2015	757	855		1.5	2.4		4.0	6.0	
2016	771	878		1.4	2.4		3.9	6.0	
2017	785	902		1.4	2.4		3.8	6.0	
2018	798	926		1.4	2.4		3.8	6.0	
5-Year Moody's Mean for Triple-A States		838			2.7			n.a.	
5-Year Moody's Median for Triple-A States		691			2.4			n.a.	

(1) Actual data for 1996 to 2007 were compiled by Moody's Investors Service, reflective of all 50 states.
(2) For years 1997-2007, calculated by Government Finance Associates, Inc.; for year 1996, calculated by Moody's.
(3) Projections assume the issuance of $49.2 million of G.O. debt during FY 2008 and $54.65 million annually thereafter through 2018.
(4) Rankings are in numerically descending order (i.e., from high to low debt).
(5) Revenues are adjusted beginning in fiscal year 1998 reflecting "current law" revenue forecasts based on a consensus between the State's administration and legislature.
(6) State Guideline equals the 2007 5-year Moody's median for triple-A states of $691 increasing annually at 2.7%.
(7) The 5-year Moody's median for triple-A States (2.4%) has not been increased for the period 2008-2018 since the annual number is quite volatile, ranging from 2.3% to 2.7% over the last five years.

5. SUMMARY

The State's positive debt trends are highlighted as follows:

- The Committee adopted new debt authorization guidelines in order to compare Vermont's debt load performance against triple-A states. As a general matter the State's recent debt position is more positive than the composite results for triple-A states, except for one standard. It is expected that the State will be able to comply with every one of its standards in the near future, possibly as early as 2008.

- The State's revenue surpluses in many previous years, resulting in the funding (often at full funding) of the State's budgetary stabilization funds for the General, Transportation, and Education Funds, contributed to significant pay-as-you-go and budgetary surplus amounts being employed for funding capital improvements.

- The State's practice of issuing debt with level annual principal installments has resulted in a favorable amortization rate. At roughly 81% within ten years, the State's bond payout ratio (rapidity of debt repayment) has been favorably received by the rating agencies and represents a debt management characteristic to be continued.

These developments have helped Vermont attain a series of incremental upgrades from Moody's Investors Service, Fitch Ratings, and Standard & Poor's, which currently rate the State Aaa, AA+ and AA+, respectively. Vermont continues to be the highest rated state in New England. The State must maintain the stabilization of its debt position in order to preserve and, hopefully, further enhance its current ratings from Fitch Ratings and Standard & Poor's into the coveted triple-A category.

The State of Vermont experienced a slight decrease (i.e., improvement) in its relative debt position among all states for 2007, as determined by Moody's Investors Service, on the basis of net tax-supported debt as a percent of personal income (i.e., from 28th in 2006 to 30th in 2007). Vermont's position declined slightly, as determined by Moody's, with respect to net tax-supported debt per capita (i.e., from 29th in 2006 to 28th in 2007).

(THIS SPACE INTENTIONALLY LEFT BLANK)

6. PROVISIONS OF ENABLING LEGISLATION AND METHODOLOGY

The Committee is responsible for the submission of a recommendation to the Governor and the General Assembly of the maximum amount of new long-term, general obligation debt that the State may prudently issue for the ensuing fiscal year. At the discretion of the Committee, such recommendation may include guidelines and other matters that may be relevant to the additional debt to be authorized. The deadline for the Committee's annual recommendation is September 30th. In making its recommendation, it is the Committee's responsibility to consider the following provisions of the enabling legislation:

SUBPARAGRAPH (1):

The amount of state general obligation bonds that, during the next fiscal year, and annually for the following nine fiscal years:

(A) will be outstanding; and

(B) have been authorized but not yet issued.

SUBPARAGRAPH (2):

A projected schedule of affordable state general obligation bond authorizations for the next fiscal year and annually for the following nine fiscal years. The assessment of the affordability of the projected authorizations shall be based on all of the remaining considerations specified in this section.

SUBPARAGRAPH (3)

Projected debt service requirements during the next fiscal year, and annually for the following nine fiscal years, based upon:

(A) existing outstanding debt;

(B) previously authorized but unissued debt; and

(C) projected bond authorizations.

SUBPARAGRAPH (4)

The criteria that recognized bond rating agencies use to judge the quality of issues of state bonds, including but not limited to:

(A) existing and projected total debt service on general obligation debt as a percentage of combined general and transportation fund revenues, excluding surpluses in these revenues which may occur in an individual fiscal year; and

(B) existing and projected total general obligation debt outstanding as a percentage of total state personal income.

SUBPARAGRAPH (5)

The principal amounts currently outstanding, and balances for the next fiscal year, and annually for the following nine fiscal years, of existing:

(A) obligations of instrumentalities of the state for which the state has a contingent or limited liability;

(B) any other long-term debt of instrumentalities of the state not secured by the full faith and credit of the state, or for which the state legislature is permitted to replenish reserve funds; and

(C) to the maximum extent obtainable, all long-term debt of municipal governments in Vermont which is secured by general tax or user fee revenues.

The effect of the above items, 5(A), 5(B) and 5(C), on State debt affordability is a function of the level of dependency for the repayment of debt on the State's general operating revenues. With respect to this matter, the principle that the rating agencies follow should give us relevant guidance: Until such time that the State's guarantee or contingent obligation becomes real (through a payment or a replenishment obligation being made), then such debt or guarantee is not included in the State's debt statement. Similarly, to the extent that the State has not been called upon to pay for the debt components, as envisioned in Subparagraph (5), then those items should not become quantifiable factors included in the affordability analysis.

- Contingent or Limited Liability Obligations (all figures as of June 30, 2007):

1. VEDA Mortgage Insurance Program: The State had a contingent liability of $9.07 million with respect to this Program.

2. VEDA Financial Access Program: The State had a contingent liability of $0.9 million with respect to this Program.

- Reserve Fund Commitments (all figures as of June 30, 2007):

1. Vermont Municipal Bond Bank: The Bank had $479.95 million of debt outstanding secured by reserve fund commitments from the State. The General Assembly is legally authorized, but not legally obligated, to appropriate money to maintain the reserve funds at their required levels. Since participating borrowers have always met

their obligations on bonds, the State has not been required to appropriate money to the reserve fund for this program.

2. Vermont Housing Finance Agency ("HFA"): The State HFA had $92.6 million of debt outstanding secured by reserve fund commitments from the State. It has not been necessary for the State to appropriate money for the reserve fund.

3. It should also be noted that the State has authorized the VEDA to incur indebtedness in an amount of $70 million secured by the State's reserve fund commitment. Based upon VEDA's historical performance and the quality of the loans it has provided and expects to provide, it is not anticipated that it will be necessary for the State to appropriate money for the reserve fund.

4. Recently, legislation was passed to create the Vermont Telecom Authority to facilitate broadband and related access to an increased number of Vermonters. In this connection, the State has authorized $40 million of debt that will have a moral obligation pledge from the State. The legislation requires that projects must be self-supporting in order to utilize the moral obligation support. Accordingly, combined with the fact that no debt has yet been issued by the Authority, the report has not included any portion of such debt in the State's net tax-supported debt computations.

- Municipal Debt:

In conformance with the standards followed by the rating agencies, this evaluation does not set forth or incorporate any debt obligations of Vermont municipalities. Should any such obligations be required to be payable by the State (e.g., through assumption or support of local debt as part of a financial emergency), a corresponding and appropriate amount related to the State's contribution would then be required to be included in the analysis. At present, no such liability has occurred and, therefore, none has been included in this review.

SUBPARAGRAPH (6):

The economic conditions and outlook for the state.

SUBPARAGRAPH (7):

Any other factor that is relevant to:

(A) the ability of the state to meet its projected debt service requirements for the next five fiscal years; or

(B) the interest rate to be borne by, the credit rating on, or other factors affecting the marketability of state bonds.

There are numerous factors that can affect the State's affordability to incur future indebtedness, including the prospective State economy and the availability of adequate financial resources. Of course, it should be recognized that even though the debt load indices employed in this report are also used by the rating agencies for determining the amount of debt that the State can effectively support, these indices do not take into consideration the possibility for deterioration in the State's financial results. For example, if the State were to confront a significantly increased or new financial liability that was not contemplated in the context of this analysis, the predictability of these indices would become less certain. Similarly, if the State were to incur serious deficits or face a significantly eroding economy, the ability of the State to incur debt in the future could be affected. These managerial and unpredictable aspects of debt affordability have not been considered in this analysis. It should be emphasized that the rating agencies, in the development of the various comparative debt ratios that are applied and reviewed in the rating of State debt obligations, also do not predict the impact of unexpected financial fortunes that can befall governmental borrowers. It will be important for State officials to monitor Vermont's annual financial condition and results, together with the State's economic trends, in order to continue to evaluate the State's credit position to determine whether annual issuance of debt should be adjusted to reflect a changing financial outlook and credit condition for the State under altered circumstances.

With respect to the interest rate and credit ratings assumed in the evaluation, we have made realistic and conservative assumptions, consistent with the past. For example, for anticipated debt issuances, we have assumed that future interest rates on State G.O. indebtedness will average approximately 6.00%; while the 11-bond Index has risen about 25 basis points over the last year, we do not believe the State would pay in excess of 4.50% true interest cost for a long-term borrowing at present.

At the same time, we have assumed that the State will maintain its current ratings: "Aaa" from Moody's, "AA+" from S&P, and "AA+" from Fitch. Of course, a negative change in the State's ratings in the future would adversely affect the comparative interest rates that Vermont pays on its bond issues, thereby increasing the amount of the State's annual fixed costs for debt service. This effect could reduce the amount of long-term, general obligation debt that the State can annually afford to issue.

(THIS SPACE INTENTIONALLY LEFT BLANK)

7. APPENDICES

A. 2007 State Debt Medians (Moody's Investors Service)

B. Fitch Ratings Credit Report

C. Moody's Investors Service Credit Report

D. Moody's U.S. States Credit Scorecard 2007

E Standard & Poor's Credit Report

F Vermont Economic Outlook (New England Economic Partnership)

April 2007

Contact	Phone
New York	
Nicole Johnson	1.212.553.4573
Maria Coritsidis	1.212.553.4173
Ted Hampton	1.212.553.2741
Robert Kurtter	1.212.553.4453
Kimberly Lyons	1.212.553.4673
Emily Raimes	1.212.553.7203
Nick Samuels	1.212.553.7121
Mark Tenenhaus	1.212.553.0849

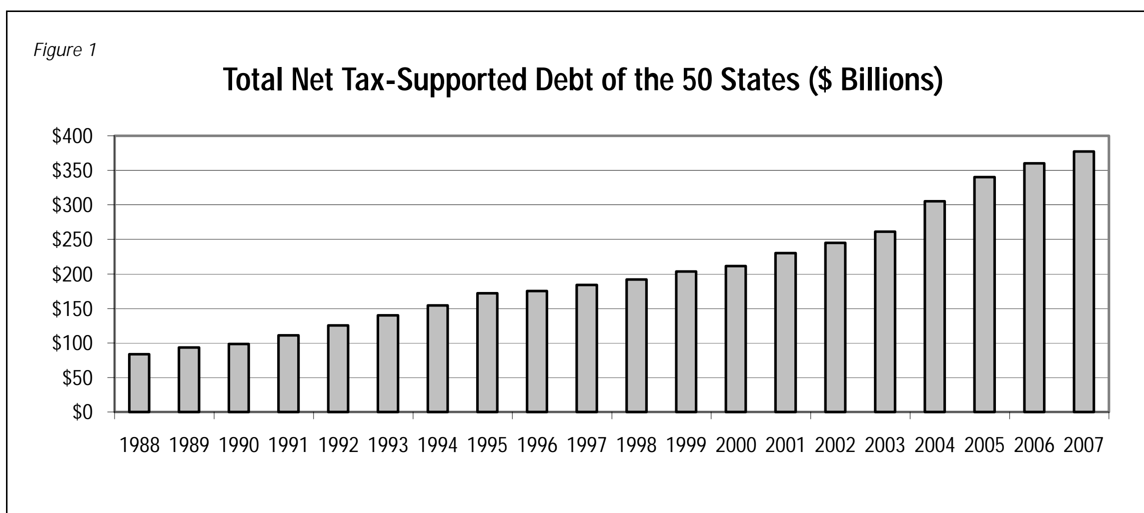
2007 State Debt Medians

Summary Opinion

State net-tax supported debt increased by 5.0% in 2006, the lowest growth since 2000 and the flush period before the state fiscal downturn. Slower than the previous year (5.9% in 2005), the lower growth continues to reflect stronger state revenue and the use of pay-as-you-go financing, following substantial increases in state borrowing during the lowest points of the fiscal downturn. In 2003 and 2004—years when almost all states made cuts to their enacted budgets—net tax-supported debt increased by 16.8% and 11.5%, respectively. Net tax-supported debt outstanding in 2006 totaled $378.4 billion (see Figure 1). Going forward, states may face both revenue and spending pressure that will lead to increased debt issuance, particularly for under-funded pensions and post-retirement benefits.

Figure 1

Total Net Tax-Supported Debt of the 50 States ($ Billions)



Moody's annual analysis of state debt medians examines the condition of net state tax-supported debt. Two measures of state debt burden—debt per capita and debt as a percentage of personal income—are used to gauge the long-term obligations supported by state tax bases. Debt burden is one of many factors that Moody's uses to determine state credit quality. We also consider gross debt, which includes contingent debt liabilities that may not have direct tax support but are included in state audited financial statements.

Moody's Investors Service
Global Credit Research

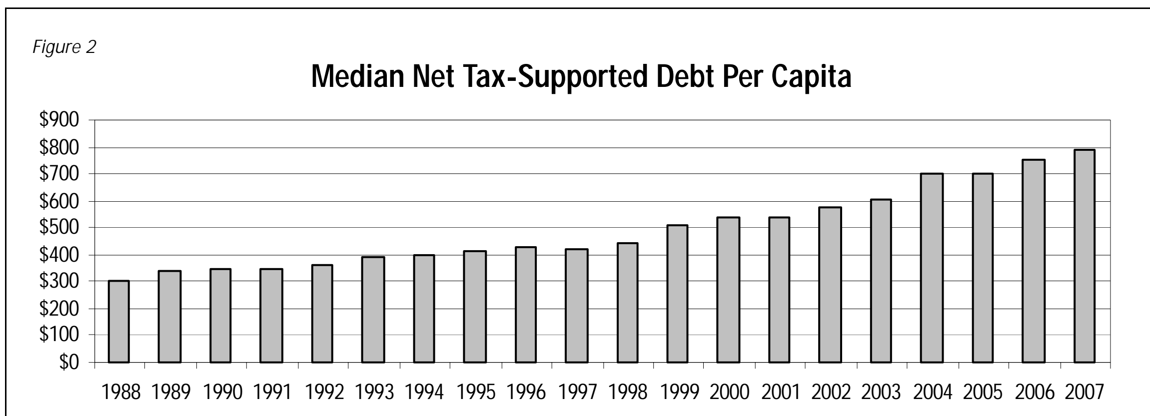
Slower Growth in Net-Tax Supported Debt Reflects Improved State Finances in 2006

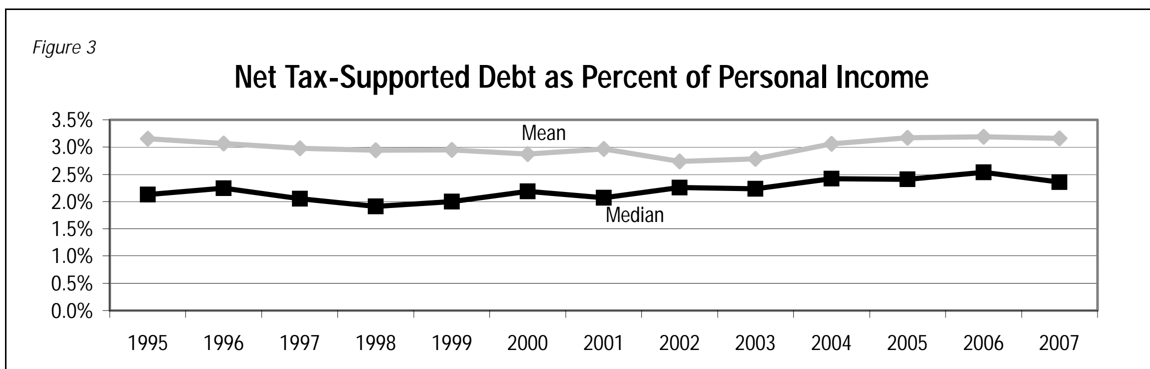
Several factors contributed to the comparatively low 5.0% growth of net tax-supported debt in 2006. Outstanding tax-supported debt increased substantially earlier in the decade as cash-strapped states borrowed heavily. Amid an improved economy, robust revenue growth in fiscal 2005 and fiscal 2006 allowed states to replace some debt issuance with pay-as-you-go financing and to limit cash flow borrowing. (Short-term cash flow borrowing such as tax and revenue anticipation notes are not included in Moody's calculations of tax-supported debt.) Low interest rates also have allowed states to issue new debt for capital projects and to refinance existing debt at comparatively reduced costs; refinancing volume was particularly heavy during the fourth quarter of 2006. Since 1988, the long-term average annual growth rate of net tax-supported debt is 8.3%.

Notable bond transactions in 2006 included $3 billion of highway bonds issued by the Texas Transportation Commission in several sales, including $2 billion backed by the state's general obligation pledge; $900 million of general obligation new money and refunding bonds issued by the Commonwealth of Pennsylvania; $400 million of Louisiana Gulf Opportunity Zone bonds, $200 million of which are state general obligations with two-year maturities and interest payments subsidized by federal tax credits, and $200 million of which are 20-year, interest-bearing general obligations; $1 billion of State Payment Acceleration Notes (SPANs) issued by California's Bay Area Infrastructure Financing Authority and backed by state appropriations; and $1.2 billion of new money and refunding highway revenue bonds issues by the Missouri Highways and Transportation Commission.

State Debt Burdens Also Continue to Increase

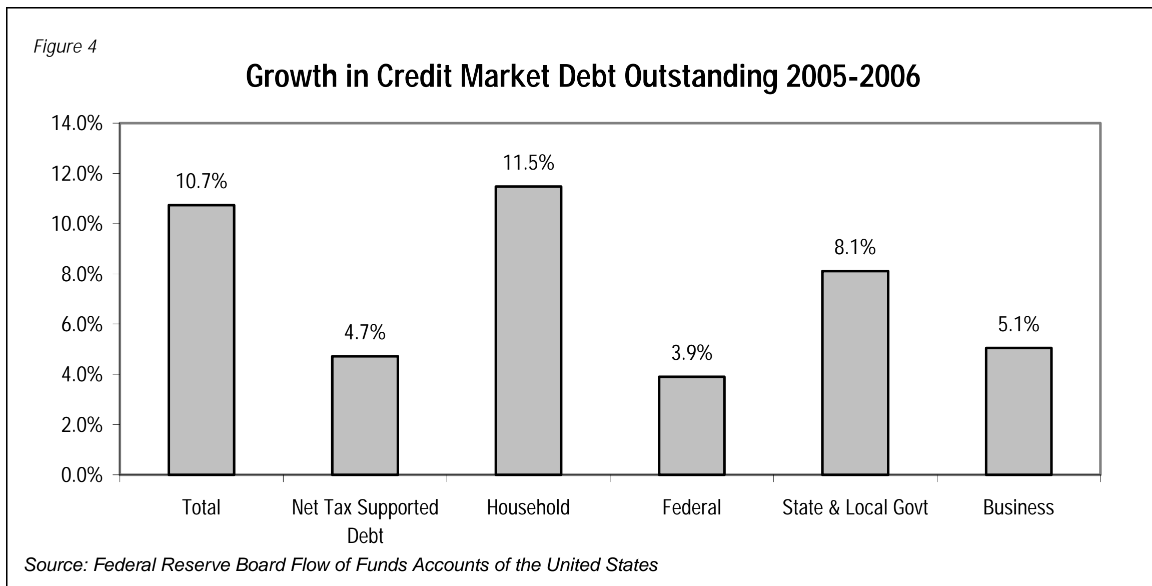
State debt burdens continued to rise in 2006, although at a lower pace than recent years, and have declined slightly relative to personal income. Median net tax-supported debt per capita increased by 4.4% in 2006 to $787, while the median ratio of debt to personal income decreased to 2.4% (see Figure 2). By comparison, median net tax-supported debt per capita was $754 in 2005 (a 7.2% increase compared to 2004) and median debt to personal income was 2.5% (see Figure 3). Mean debt per capita in 2006 increased by 3.9%, to $1,101, the smallest increase since 2003, when it increased by 3.6%. Mean net tax-supported debt as a percentage of personal income in 2006 was 3.2% and reflects personal income growth among the largest state issuers at rates closer to the U.S. average (5.2% in 2005 and, on a preliminary basis, 6.3% in 2006).



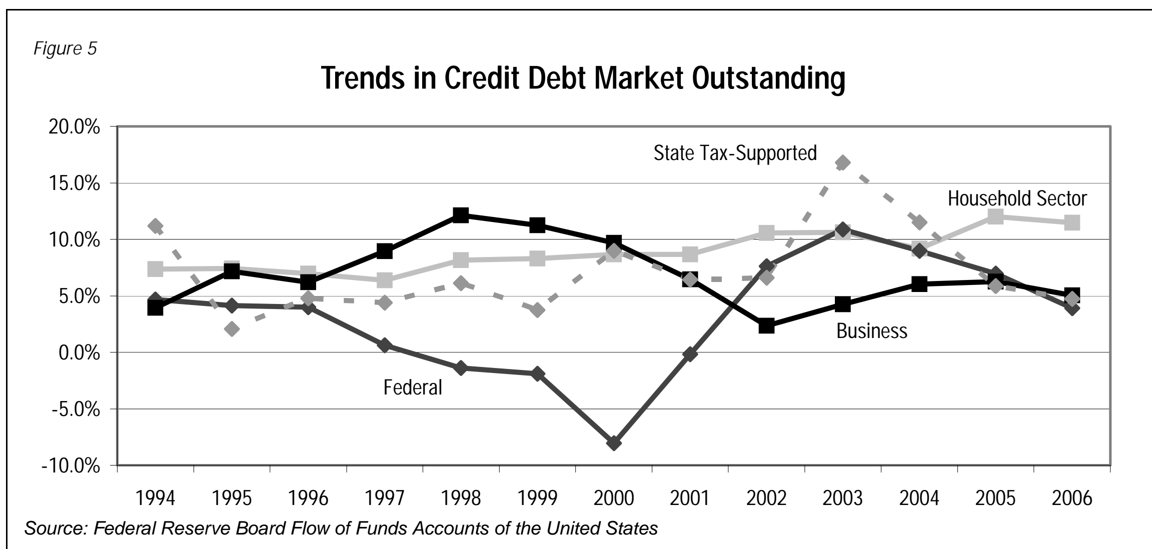


U.S. Credit Markets Expand Significantly in 2006, Led By Household Sector

Debt outstanding in the U.S. credit markets increased by 10.7% in 2006 (see Figure 4). Household sector debt continues to grow the fastest, by 11.5%, and now reflects 29% of the total (see Figure 5 and Figure 6). Driven upwards by the booming home mortgage market and growth in revolving consumer credit during the past five years, household debt has increased annually by an average 10.8%.



Source: Federal Reserve Board Flow of Funds Accounts of the United States

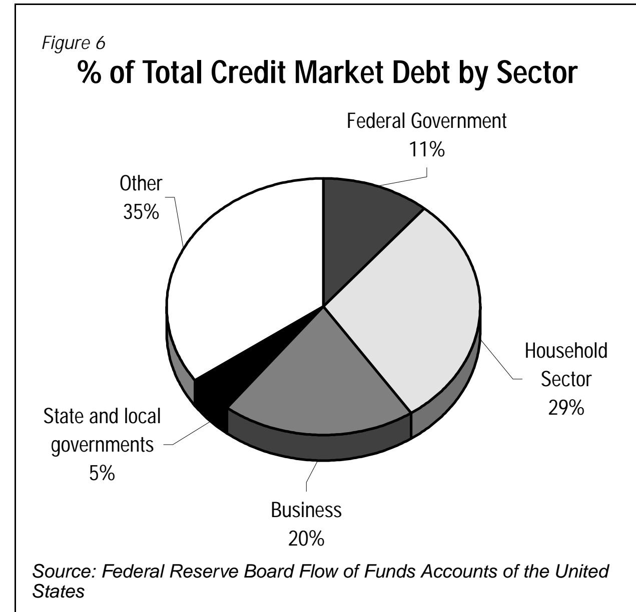


Source: Federal Reserve Board Flow of Funds Accounts of the United States

Following several years of substantial spending increases primarily for national security and healthcare, federal government borrowing slowed significantly in 2006, increasing by 3.9% compared to the previous year, after 9% and 7% growth in 2004 and 2005, respectively; it accounts for 11% of total debt outstanding. Business sector debt, 20% of total debt, grew by 5.1% in 2006 (see Figure 6).

Figure 6

% of Total Credit Market Debt by Sector



Source: Federal Reserve Board Flow of Funds Accounts of the United States

2007 State Debt Outlook: Continued Spending Pressure, More Moderate Revenue Growth May Boost Issuance

Going forward, states face both revenue and spending challenges that may lead to higher debt issuance. Pent-up demand for spending deferred during the downturn remains strong, particularly for K-12 and higher education. The costs of Medicaid and other state-supported public health programs continue to grow at the same time that supporting federal grants-in-aid are proposed to be reduced. State-employee healthcare costs also are rising dramatically, particularly for prescription drugs. Infrastructure needs continue to grow, including for highway construction and maintenance. States also face under-funded employee pension plans and the need to begin to fund other post-employment benefits, problems that some states may finance through debt issuance in coming years. At the same time, although state revenue continues to grow, and states likely will record strong personal income tax collections this month, some risks exist: the effects of the housing market slowdown on employment and consumer confidence have not yet been fully realized.

Related Research

Special Comments:

Stable Outlook for State Ratings in 2007 Reflects More Moderate Economic and Revenue Environment, March 2007 (102355)

Moody's Municipal Rating Revisions — Fourth Quarter 2006, January 2007 (101928)

Rating Changes for the 50 States from 1973 to Date, February 2007 (102238)

U.S. States Credit Scorecard, August 2006 (98088)

Rating Methodology:

Moody's State Rating Methodology, November 2004 (89335)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Table 1

Net Tax-Supported Debt Per Capita

			Rating
1	Massachusetts	$4,153	Aa2
2	Connecticut	$3,713	Aa3
3	Hawaii	$3,630	Aa2
4	New Jersey	$3,317	Aa3
5	New York	$2,694	Aa3
6	Delaware	$1,998	Aaa
7	Illinois	$1,976	Aa3
8	Washington	$1,765	Aa1
9	Rhode Island	$1,687	Aa3
10	California	$1,623	A1
11	Oregon	$1,464	Aa3
12	New Mexico	$1,435	Aa1
13	Wisconsin	$1,405	Aa3
14	Louisiana	$1,294	A2
15	Mississippi	$1,247	Aa3*
16	Kansas	$1,218	Aa1
17	Kentucky	$1,204	Aa2*
18	Maryland	$1,171	Aaa
19	West Virginia	$1,071	Aa3
20	Florida	$1,020	Aa1
21	Ohio	$974	Aa1
22	Alaska	$939	Aa2
23	Georgia	$916	Aaa
24	Pennsylvania	$852	Aa2
25	Minnesota	$827	Aa1
26	Michigan	$747	Aa2
27	North Carolina	$728	Aaa
28	Vermont	$706	Aaa
29	Virginia	$692	Aaa
30	Indiana	$657	Aa1*
31	South Carolina	$630	Aaa
32	Utah	$621	Aaa
33	Missouri	$613	Aaa
34	Maine	$603	Aa3
35	Arizona	$594	Aa3
36	Nevada	$591	Aa1
37	Alabama	$590	Aa2
38	New Hampshire	$492	Aa2
39	Oklahoma	$450	Aa2
40	Montana	$439	Aa2
41	Texas	$415	Aa1
42	Arkansas	$370	Aa2
43	Colorado	$343	NGO**
44	North Dakota	$322	Aa2*
45	South Dakota	$261	NGO**
46	Tennessee	$213	Aa2
47	Idaho	$157	Aa2*
48	Iowa	$104	Aa1*
49	Wyoming	$97	NGO**
50	Nebraska	$24	NGO**
	MEAN:	***$1,101***	
	MEDIAN:	***$787***	
	Puerto Rico	$8,322***	Baa3

** Issuer Rating (No G.O. Debt)*
*** No General Obligation Debt*
**** This figure is not included in any totals, averages, or median calculations but is provided for comparison purposes only.*

Table 2

Net Tax-Supported Debt as a % of 2005 Personal Income

1	Hawaii	10.6%
2	Massachusetts	9.4%
3	Connecticut	7.8%
4	New Jersey	7.6%
5	New York	6.7%
6	Illinois	5.5%
7	Delaware	5.5%
8	New Mexico	5.3%
9	Washington	5.1%
10	Louisiana	4.9%
11	Mississippi	4.9%
12	Oregon	4.6%
13	Rhode Island	4.6%
14	California	4.4%
15	Kentucky	4.3%
16	Wisconsin	4.2%
17	West Virginia	3.9%
18	Kansas	3.7%
19	Florida	3.1%
20	Georgia	3.0%
21	Ohio	3.0%
22	Maryland	2.8%
23	Alaska	2.7%
24	Pennsylvania	2.4%
25	North Carolina	2.4%
26	Utah	2.3%
27	South Carolina	2.3%
28	Michigan	2.2%
29	Minnesota	2.2%
30	Vermont	2.1%
31	Indiana	2.1%
32	Alabama	2.0%
33	Arizona	2.0%
34	Missouri	1.9%
35	Maine	1.9%
36	Virginia	1.8%
37	Nevada	1.7%
38	Oklahoma	1.5%
39	Montana	1.5%
40	Arkansas	1.4%
41	Texas	1.3%
42	New Hampshire	1.3%
43	North Dakota	1.0%
44	Colorado	0.9%
45	South Dakota	0.8%
46	Tennessee	0.7%
47	Idaho	0.6%
48	Iowa	0.3%
49	Wyoming	0.3%
50	Nebraska	0.1%
	MEAN:	***3.2%***
	MEDIAN:	***2.4%***
	Puerto Rico	66.3%**

*** This figure is based on 2005 Personal Income. It is not included in any totals, averages, or median calculations but is provided for comparison purposes only.*

Table 3

Total Net Tax Supported Debt (000's)

			Rating
1	California	$59,171,200	A1
2	New York	$52,014,000	Aa3
3	New Jersey	$28,935,074	Aa3
4	Massachusetts	$26,735,227	Aa2
5	Illinois	$25,359,214	Aa3
6	Florida	$18,454,123	Aa1
7	Connecticut	$13,013,222	Aa3
8	Washington	$11,290,608	Aa1
9	Ohio	$11,176,473	Aa1
10	Pennsylvania	$10,604,000	Aa2
11	Texas	$9,756,427	Aa1
12	Georgia	$8,577,760	Aaa
13	Wisconsin	$7,806,409	Aa3
14	Michigan	$7,538,800	Aa2
15	Maryland	$6,573,900	Aaa
16	North Carolina	$6,447,199	Aaa
17	Louisiana	$5,549,156	A2
18	Oregon	$5,418,714	Aa3
19	Virginia	$5,285,480	Aaa
20	Kentucky	$5,064,823	Aa2*
21	Hawaii	$4,666,432	Aa2
22	Minnesota	$4,274,574	Aa1
23	Indiana	$4,147,983	Aa1*
24	Arizona	$3,664,752	Aa3
25	Mississippi	$3,628,815	Aa3*
26	Missouri	$3,583,258	Aaa
27	Kansas	$3,368,025	Aa1
28	New Mexico	$2,803,880	Aa1
29	South Carolina	$2,724,402	Aaa
30	Alabama	$2,713,198	Aa2
31	West Virginia	$1,947,646	Aa3
32	Rhode Island	$1,801,344	Aa3
33	Delaware	$1,705,328	Aaa
34	Colorado	$1,632,403	NGO**
35	Oklahoma	$1,608,998	Aa2
36	Utah	$1,583,029	Aaa
37	Nevada	$1,476,024	Aa1
38	Tennessee	$1,286,373	Aa2
39	Arkansas	$1,039,494	Aa2
40	Maine	$797,180	Aa3
41	New Hampshire	$647,412	Aa2
42	Alaska	$629,100	Aa2
43	Vermont	$440,735	Aaa
44	Montana	$414,294	Aa2
45	Iowa	$310,061	Aa1*
46	Idaho	$230,764	Aa2*
47	North Dakota	$204,725	Aa2*
48	South Dakota	$204,171	NGO**
49	Wyoming	$49,834	NGO**
50	Nebraska	$42,400	NGO**
	Totals	***$378,398,441***	
	Puerto Rico	$32,557,100***	Baa3

** Issuer Rating (No G.O. Debt)*
*** No General Obligation Debt*
**** This figure is not included in any totals, averages, or median calculations but is provided for comparison purposes only.*

Table 4

Gross Tax Supported Debt (000's)

			Gross to Net Ratio
1	California	$66,664,200	1.13
2	New York	$52,014,000	1.00
3	Massachusetts	$34,203,405	1.28
4	New Jersey	$33,740,775	1.17
5	Illinois	$25,717,314	1.01
6	Florida	$22,594,723	1.22
7	Michigan	$21,929,300	2.91
8	Connecticut	$20,952,322	1.61
9	Washington	$17,090,608	1.51
10	Pennsylvania	$14,051,000	1.33
11	Texas	$13,099,845	1.34
12	Oregon	$11,992,195	2.21
13	Ohio	$11,259,233	1.01
14	Minnesota	$11,156,199	2.61
15	Wisconsin	$10,020,527	1.28
16	Virginia	$9,614,993	1.82
17	Georgia	$8,577,760	1.00
18	Colorado	$8,492,403	5.20
19	Kentucky	$7,224,467	1.43
20	Maryland	$6,573,900	1.00
21	North Carolina	$6,447,199	1.00
22	Louisiana	$6,373,287	1.15
23	Alabama	$6,301,950	2.32
24	Hawaii	$6,079,265	1.30
25	Utah	$5,811,454	3.67
26	Indiana	$5,760,898	1.39
27	South Carolina	$5,252,412	1.93
28	Maine	$4,808,836	6.03
29	Arkansas	$4,483,923	4.31
30	Tennessee	$4,003,348	3.11
31	Arizona	$3,884,172	1.06
32	Missouri	$3,649,623	1.02
33	Mississippi	$3,628,815	1.00
34	Kansas	$3,595,773	1.07
35	Alaska	$3,494,800	5.56
36	New Mexico	$3,466,256	1.24
37	West Virginia	$3,029,310	1.56
38	Delaware	$2,757,585	1.62
39	Nevada	$2,682,984	1.82
40	Iowa	$2,679,697	8.64
41	Rhode Island	$2,178,044	1.21
42	New Hampshire	$1,979,637	3.06
43	Oklahoma	$1,657,735	1.03
44	Idaho	$1,101,199	4.77
45	Vermont	$1,092,976	2.48
46	North Dakota	$953,117	4.66
47	Montana	$560,632	1.35
48	South Dakota	$459,380	2.25
49	Wyoming	$49,834	1.00
50	Nebraska	$44,085	1.04
	Totals	***$505,237,394***	***1.34***
	Puerto Rico	$35,494,100**	1.09

*** This figure is not included in any totals, averages, or median calculations but is provided for comparison purposes only.*

Table 5
Net Tax-Supported Debt as a Percentage of Personal Income

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Alabama	2.4	2.2	2.0	2.0	1.8	1.9	1.7	1.5	2.3	2.2	2.2	2.2	2.0	2.0	2.2	2.0
Alaska	2.5	2.6	2.4	1.2	0.9	0.9	0.5	0.0	1.0	0.4	0.4	0.3	3.0	2.8	2.6	2.7
Arizona	1.6	1.8	1.6	2.7	2.4	2.1	1.9	1.9	1.6	1.6	1.9	2.1	2.3	2.6	2.2	2.0
Arkansas	0.7	0.7	0.7	0.6	0.7	0.6	0.8	0.6	0.9	1.2	1.2	1.4	1.8	1.6	1.6	1.4
California	2.0	2.5	3.0	3.5	2.8	2.6	2.6	2.6	2.4	2.5	2.5	2.5	3.2	4.7	4.6	4.4
Colorado	0.3	0.3	0.2	0.2	0.1	0.1	0.1	0.0	0.03	0.4	0.7	0.9	0.9	1.0	0.9	0.9
Connecticut	8.7	8.9	9.1	9.6	9.7	9.4	8.7	8.7	8.1	8.0	8.0	8.2	8.4	8.5	8.0	7.8
Delaware	8.1	7.5	8.0	8.0	7.6	6.4	5.9	5.7	5.2	5.5	5.3	5.0	5.6	5.5	5.3	5.5
Florida	2.2	2.3	2.9	3.0	2.9	3.0	3.4	3.5	3.4	3.3	3.4	3.5	3.5	3.4	3.2	3.1
Georgia	2.5	2.9	3.0	3.1	3.3	3.1	2.9	2.9	2.8	2.6	2.9	2.9	2.9	2.8	2.7	3.0
Hawaii	10.2	10.4	12.1	10.5	10.3	10.9	10.7	11.2	11.6	11.0	10.4	10.9	10.4	11.1	12.1	10.6
Idaho	0.3	0.4	0.3	0.3	0.3	0.3	0.2	0.4	0.4	0.3	0.4	0.3	0.5	0.6	0.6	0.6
Illinois	2.7	2.7	3.0	3.2	3.2	2.9	2.7	2.6	2.6	2.7	2.8	3.2	5.8	6.2	5.9	5.5
Indiana	0.7	1.0	1.0	1.0	0.9	0.9	0.8	0.9	0.9	1.1	1.1	1.1	1.3	1.4	1.6	2.1
Iowa	0.2	0.4	0.4	0.6	0.6	0.6	0.5	0.5	0.4	0.4	0.6	0.6	0.5	0.5	0.4	0.3
Kansas	0.5	1.3	2.0	2.1	2.0	1.9	1.7	2.0	2.4	3.1	3.0	3.0	3.3	4.0	3.8	3.7
Kentucky	4.7	5.1	5.0	4.7	5.1	4.1	3.9	3.7	3.5	4.4	4.3	4.4	4.4	4.0	4.5	4.3
Louisiana	6.5	6.3	5.9	5.4	4.9	4.4	2.6	2.6	2.4	2.5	2.4	2.7	2.6	2.4	3.1	4.9
Maine	2.2	2.7	2.6	2.7	2.7	2.6	1.9	1.9	2.1	2.0	1.9	1.8	1.8	2.2	2.0	1.9
Maryland	3.4	3.3	3.3	3.5	3.4	3.3	3.1	3.3	3.0	2.6	2.6	2.8	3.0	2.9	3.0	2.8
Massachusetts	8.0	8.5	8.2	8.4	8.3	8.1	7.8	7.8	8.0	8.5	8.5	8.5	8.5	8.5	9.8	9.4
Michigan	1.2	1.6	1.5	1.5	1.5	1.5	1.6	1.7	1.5	1.6	1.5	1.8	2.2	2.2	2.1	2.2
Minnesota	2.2	2.2	2.0	1.9	1.9	2.2	1.9	2.0	1.9	1.8	1.8	1.9	2.0	2.0	2.1	2.2
Mississippi	1.8	1.8	2.1	2.0	3.0	2.9	3.5	4.4	4.7	4.6	4.7	5.6	5.2	4.8	4.8	4.9
Missouri	1.3	1.3	1.2	1.2	1.3	1.3	1.0	1.0	1.0	1.1	1.3	1.3	1.6	1.5	1.6	1.9
Montana	2.2	2.1	1.9	3.2	2.4	1.4	1.4	1.7	1.7	1.7	1.6	1.4	1.3	1.1	1.4	1.5
Nebraska	0.2	0.2	0.2	0.3	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Nevada	2.9	2.7	2.2	2.1	2.0	1.8	1.6	1.8	1.8	1.8	1.7	1.4	2.0	2.0	2.2	1.7
New Hampshire	2.5	2.7	2.9	2.9	2.9	2.5	2.4	2.3	2.0	1.5	1.5	1.4	1.5	1.3	1.4	1.3
New Jersey	2.2	3.0	2.9	3.7	3.6	3.8	5.1	5.2	5.3	5.5	5.6	5.5	5.9	7.4	7.9	7.6
New Mexico	1.8	1.7	2.1	2.1	2.1	2.0	1.9	2.6	3.1	4.0	4.0	3.7	4.1	5.3	4.7	5.3
New York	5.6	6.1	6.4	6.6	6.9	6.7	6.5	6.6	6.4	6.2	5.9	5.9	6.7	7.2	6.7	6.7
North Carolina	0.6	0.6	0.6	0.8	0.7	0.7	1.0	1.2	1.4	1.4	1.4	1.6	2.0	2.5	2.8	2.4
North Dakota	1.2	1.2	1.1	1.1	1.1	1.0	0.8	0.6	0.7	0.9	0.9	0.9	0.9	0.6	1.2	1.0
Ohio	2.4	2.5	2.5	2.4	2.5	2.5	2.5	2.7	2.7	2.6	2.6	2.6	2.7	2.9	2.9	3.0
Oklahoma	0.4	0.4	1.0	1.0	0.8	0.9	0.8	1.2	1.3	1.4	1.3	1.2	1.2	1.2	1.4	1.5
Oregon	1.5	1.1	1.2	1.2	1.4	1.9	1.2	1.2	1.3	1.6	1.5	1.6	4.5	4.7	4.5	4.6
Pennsylvania	2.7	2.6	2.7	2.6	2.4	2.2	2.0	2.3	2.2	2.2	2.3	2.3	2.2	2.3	2.3	2.4
Rhode Island	6.1	8.8	8.9	8.7	8.5	8.7	6.6	6.5	6.2	5.3	5.2	5.0	4.4	4.3	4.1	4.6
South Carolina	1.8	1.9	1.6	1.7	1.6	1.6	1.6	1.6	1.6	1.8	2.5	2.4	2.4	2.2	2.5	2.3
South Dakota	2.2	2.3	2.3	2.1	1.8	1.8	1.5	1.5	1.5	1.2	0.9	0.7	0.9	0.9	0.7	0.8
Tennessee	1.0	0.8	0.8	0.9	0.9	0.9	0.9	1.0	1.0	1.2	0.9	0.8	0.8	0.7	0.8	0.7
Texas	1.2	1.1	1.2	1.6	1.7	1.5	1.4	1.3	1.2	1.0	0.9	0.9	0.8	1.0	1.0	1.3
Utah	1.6	1.7	1.6	1.7	1.8	1.7	3.1	3.6	3.3	2.8	3.0	2.9	3.5	3.2	2.7	2.3
Vermont	4.5	4.6	4.5	4.7	4.9	4.7	4.2	4.2	3.8	3.3	3.0	3.0	2.5	2.3	2.2	2.1
Virginia	1.2	1.3	1.6	1.7	1.6	1.7	2.1	2.0	2.1	1.9	1.8	1.7	1.7	1.8	1.7	1.8
Washington	4.4	5.0	5.0	5.0	4.8	5.0	4.8	4.6	4.6	4.4	4.4	4.8	4.9	4.9	4.9	5.1
West Virginia	4.7	3.4	3.1	2.5	2.6	2.7	2.8	3.4	3.3	4.2	4.0	4.1	3.6	4.6	4.4	3.9
Wisconsin	2.7	3.1	3.0	3.0	2.9	3.2	2.8	2.8	2.7	3.2	3.0	3.3	4.5	4.7	4.3	4.2
Wyoming	0.0	0.0	0.5	0.4	0.4	0.7	0.7	1.0	1.0	1.0	1.4	0.9	0.8	0.7	0.3	0.3
Median	**2.2**	**2.2**	**2.1**	**2.1**	**2.1**	**2.1**	**1.9**	**2.0**	**2.2**	**2.1**	**2.3**	**2.2**	**2.4**	**2.4**	**2.5**	**2.4**

To order reprints of this report (100 copies minimum), please call 1.212.553.1658.
Report Number: 102778

Author

Nicholas Samuels

Production Specialist

Yung Louie

© Copyright 2007, Moody's Investors Service, Inc. and/or its licensors and affiliates including Moody's Assurance Company, Inc. (together, "**MOODY'S**"). All rights reserved. **ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY COPYRIGHT LAW AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT**. All information contained herein is obtained by **MOODY'S** from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind and **MOODY'S**, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. Under no circumstances shall **MOODY'S** have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of **MOODY'S** or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if **MOODY'S** is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The credit ratings and financial reporting analysis observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. **NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.** Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling.

MOODY'S hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by **MOODY'S** have, prior to assignment of any rating, agreed to pay to **MOODY'S** for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,400,000. Moody's Corporation (MCO) and its wholly-owned credit rating agency subsidiary, Moody's Investors Service (MIS), also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually on Moody's website at www.moodys.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Tax Supported
New Issue

State of Vermont

Rating

General Obligation Bonds .... AA+
Rating Outlook .... Stable

Analyst

Richard J. Raphael
+1 212 908-0506
richard.raphael@fitchratings.com

Issuer Contact

Jeb Spaulding
State Treasurer
+1 802 828-2301

New Issue Details

$30,000,000 General Obligation Refunding Bonds, 2007 Series A, are scheduled to sell competitively on Feb 13. The bonds will be due July 15, 2007–2026 and are callable on or after July 15, 2016 at par.

Security: The bonds are general obligations of the state of Vermont, with its full faith and credit pledged.

■ Outlook

Vermont's continued conservative debt planning and budgeting and steady economy are reflected in its Stable Rating Outlook and 'AA+' general obligation (GO) bond rating. Challenges include the need to address continued education and Medicaid spending pressures, as well as attract jobs and a younger work force. Debt is almost entirely GO and matures rapidly, and net tax-supported debt has declined to reach lower moderate levels. Pension systems are well funded. Reserves in each major operating fund are at or near full funding at 5% of prior-year appropriations. The state budgets conservatively and responds rapidly to changing conditions to maintain balances. The state has a diverse revenue stream, including a state property tax for education. Reflecting its older and well-educated population, Vermont has a relatively small income base; its economy is supported by larger than average manufacturing, tourism, and health and educational services sectors.

■ Rating Considerations

Vermont's demonstrated willingness to keep debt within manageable parameters is important to its long-term credit assessment. The state has long been faithful to a simple debt structure; direct debt is exclusively GO, and amortization is very rapid, with obligations stretching to only 20 years. In line with affordability recommendations, annual borrowing has been reduced, and some planned bond issuance was completed with pay-as-you-go financing instead. Net tax-supported debt has declined 23% since 1997, and debt ratios are moderate.

Financial operations were successful for the six years through fiscal 2001. After elimination of the deficit in fiscal 1996, the rebuilding of the budget stabilization reserve commenced, followed by the establishment of further reserves for education and welfare, as well as the use of current surplus for capital purposes. Reserves became fully funded at 5% of revenues. Revenues, driven by the personal income tax, consistently exceeded estimates until weakness surfaced in fiscal 2001, forcing use of more than one-half of the reserves by fiscal 2002. In fiscal 2003, revenues recovered to meet estimates, and in fiscal years 2004–2006, surging revenues allowed for sizable surpluses and full replenishment of reserves. Through December 2006, fiscal 2007 revenues were on track with estimates that projected slower growth.

Vermont lost nearly 5% of employment in the early 1990s recession, but by 1994, employment exceeded the pre-recession level. However, manufacturing employment, higher paying than the services sector, was slower to recover. Manufacturing again suffered from 2000–2003, falling 19% before stabilizing in 2004. This loss was offset by resilience in other sectors, and total employment was virtually unchanged from 2000–2003 before resuming growth during 2004 with a 1.3% job gain.

February 9, 2007

Jobs grew 0.8% in 2005 and retained that pace through much of 2006, with manufacturing losses offset by service growth. Income growth has generally lagged U.S. levels, in part due to slower population growth. Per capita personal income growth exceeded the U.S. levels for six consecutive years before falling short in 2004 and 2005. Vermont's revised 2005 personal income was $32,731, 95% of the U.S. level, ranking it 25th among the states.

Strengths

- Virtually exclusive use of GO debt.
- Moderate and declining debt ratios, with affordability planning.
- Generally conservative financial policies.
- Fully funded reserves.

Risks

- Some vulnerability due to the importance of the manufacturing sector.
- Growing Medicaid and education expenditures constrain future budgets.

Debt Position

Vermont has an increasingly favorable debt position, and debt levels have consistently declined, with reduced issuance recommendations from the debt affordability advisory committee. As of June 30, 2006, net tax-supported debt of $440 million was 23% below that of 1997, which has driven ratios down to $705 per capita and 2.2% of personal income, well below the 1997 levels of $991 and 4.5%, respectively.

There are no constitutional or statutory restrictions on debt in Vermont. All direct debt is now GO, as a minor amount of leases and certificates of participation was refunded in fiscal 1998. General purpose bonds are serviced from the general fund and highway debt from the transportation fund. Not included in the GO debt is debt issued by the Education and Health Building Finance Agency for the benefit of developmental and mental health services providers, although much support for the programs comes from state appropriations.

There is considerable exposure through credit extension, although it was significantly reduced with the sale of the portfolio of the Vermont Home Mortgage Board in 1998. The state's full faith and credit back up certain programs of the Vermont Economic Development Authority (VEDA, or the authority), including the authority to insure up to $15 million in mortgages. As of June 30, 2006, the authority had $9.05 million in mortgage contracts outstanding. The authority also is authorized to reimburse lenders participating in the Financial Access Program to a maximum of $2 million. As of June 30, 2006, the reimbursement liability was $917,276. VEDA has also issued commercial paper ($64.7 million outstanding) for financing new loans; the commercial paper program has a reserve deficiency makeup provision with the state, not to exceed $70 million. Calls on the various guarantees have been minor.

Debt Statistics

($000, As of June 30, 2006)

General Fund	415,861
Special Fund	12,005
Transportation Fund	12,128
Total General Obligation Debt	439,994
Contingent Liabilities:	
VEDA Mortgage Insurance Program	9,049
VEDA Financial Access Program	917
Reserve Fund Commitments:	
Bond Bank	477,070
Housing Finance Agency	95,205
VEDA	70,000
Gross Tax-Supported Debt	1,092,235
Less: Contingent Liabilities	9,966
Less: Reserve Fund Commitments	642,275
Net Tax-Supported Debt	439,994
Net Tax-Supported Debt	
Per Capita ($)	705
As % of Personal Income	2.2
As % of Estimated Property Value	0.7
Amortization – General Obligation Debt (%)	
Due in Five Years	48
Due in 10 Years	79

VEDA – Vermont Economic Development Authority.

In addition to VEDA commitments, the state has reserve fund deficiency makeup provisions with the municipal bond bank and the housing finance agency, with the latter limited to $125 million in bonds; no calls have been employed.

The state has issued short-term debt, both for operating and capital purposes. In fiscal years 1993–1997, it was entirely in the form of commercial paper. Subsequently, there was no need for operating borrowing until fiscal 2003, when $75 million was issued. In fiscal 2004, $48 million was issued, but the state's finances have improved since then, with no short-term borrowing needed.

Vermont has a capital debt affordability advisory committee that will recommend prudent debt authorizations, taking into account, among other things, debt in relation to personal income and debt service in relation to revenues. Annual amounts declined from $64 million in fiscal 1994 to $43 million in fiscal years 1997 and 1998 and less than $40 million from 1999–2004. The recommendation rose to $41 million in fiscal 2005, $45 million in fiscal years 2006 and 2007, and $49.2 million for fiscal 2008. Authorizations have approximately matched recommendations, although surpluses were used to reduce bond issuance in fiscal years 2000 and 2001.

The state will follow the current issuance with $15 million of GO Vermont citizen bonds next month. The state now makes annual bond authorizations, eliminating any overhang of authorized but unissued debt. The governor has proposed one extension of debt in his fiscal 2007 budget to create a Vermont Telecom Authority to facilitate broadband access to residents. Direct debt is not expected, although contingent debt of $40 million is proposed.

Pensions/Other Post-Employment Benefits

Vermont's pension systems are comparatively strong. The Vermont State Employees Retirement System (VSERS) was 99.3% funded at the last actuarial valuation on June 30, 2006. The Vermont State Teacher's Retirement System (VSTRS) was 84.6% funded. The state has funded the teachers' system below the actuarially recommended contribution (ARC); however, following a change in some actuarial calculations, it fully funded the ARC in fiscal 2007.

Vermont completed actuarial studies for its other post-employment benefits liability earlier than most states. For VSERS, assuming a trust is established and prefunding is assumed, the liability is $303.5 million, and the ARC is calculated at $25.3 million for fiscal 2007. For VSTRS, with the same assumptions, the liability is $414.3 million, with an ARC of $35.4 million for fiscal 2007. The state has statutorily established an irrevocable trust, but it has not decided on how to fund the ARC.

■ Financial Operations

The general fund is the basic operating account. Accounting has been done on a cash basis, but the conversion to generally accepted accounting principles (GAAP) was completed for fiscal 1996. Vermont's comprehensive annual financial reports (CAFRs) for fiscal years 2002, 2003, and 2004 were each delayed due to complications of a new financial system, conversion to GAAP Statement No. 34, and a delay in auditing capital assets. The problems have been remedied, and the fiscal 2006 CAFR was issued promptly.

Vermont has a relatively high tax burden, and the state has a diverse revenue stream that includes a personal income tax, which provided 28% of combined audited fiscal 2006 general and education fund own-source revenues. The income tax was decoupled from the federal income tax in tax year 2001. Vermont's 6% sales tax — which yields 16% of revenues — exempts food, medicine, clothing, and supplies and energy for manufacturing and agricultural uses. Vermont also has a corporate income tax, an insurance tax, a property transfer tax, an estate tax, liquor and cigarette taxes, and a statewide property tax for education, which was 39% of revenues.

The state maintains three major funds: general; transportation; and education. Transportation revenues have been sluggish over the past few years, requiring some general fund support and reductions to programs. The education fund relies on the allocation of the sales tax, the statewide property tax, lottery proceeds, and motor vehicle purchase and use tax receipts. Each fund maintains its own reserve.

After a lengthy difficult period, Vermont returned to surplus operations in fiscal 1996, which, when combined with a transfer from the transportation fund, eliminated the general fund deficit from the previous year. By fiscal 1997, major deposits to reserve funds had been made. Financial operations in the following years, through fiscal 2001, were favorable, with revenues generally ahead of estimates, operating surpluses achieved, and reserves fully funded at 5% of revenues.

Fiscal 2002 represented the state's poorest financial performance since the early 1990s. Revenues, projected to hold steady, fell by 7% over 2001 levels, with personal income tax receipts off 11%. The state responded throughout the year by lowering estimates twice, reducing appropriations, and using portions of the reserves. On a GAAP basis, the general fund ran a $23 million operating deficit, to close with a $149.6 million total fund balance.

The state expected fiscal 2003 revenues to also decline and lowered revenue estimates and made cuts. However, following late-year strength, revenues

Financial Summary — GAAP Basis

($000, Fiscal Years Ended June 30)

	General Fund					Education Fund				
	2002	2003	2004	2005	2006	2002	2003	2004	2005	2006
Personal Income Tax	443,453	369,498	434,395	499,007	575,710	0	0	0	0	0
Sales Tax	215,503	217,984	254,107	207,630	218,227	0	0	10,884	103,786	109,112
Property Tax	0	0	0	0	0	424,198	453,914	487,536	732,331	813,588
Total Revenue	875,775	821,510	967,977	1,049,325	1,122,681	519,770	558,960	612,107	865,631	951,632
Education	118,167	118,056	121,775	128,356	137,093	818,330	838,313	874,787	1,159,872	1,239,072
Public Safety	55,572	64,382	69,148	75,347	81,477	0	0	0	0	0
Human Services	310,435	270,664	233,961	326,496	272,633	0	0	0	0	0
Debt Service	63,899	67,903	66,044	62,609	62,702	0	0	0	0	0
Total Expenditures	628,098	588,205	560,795	672,817	636,751	818,330	838,313	874,787	1,159,872	1,239,072
Transfers In and Other Sources	20,380	34,015	162,435	19,831	11,044	280,439	270,211	296,609	279,275	289,476
Transfers Out and Other Uses	(291,141)	(317,160)	(514,643)	(387,397)	(499,192)	0	(1,071)	0	0	(932)
Net Surplus/(Deficit)	(23,084)	(49,840)	54,974	8,942	(2,218)	(18,121)	(10,213)	33,929	(14,966)	1,104
Balance Sheet										
Cash and Investments	33,948	22,805	78,070	106,427	100,436	19,880	11,315	39,568	29,075	29,556
Less: Current Liabilities/Encumbrances	22,771	19,789	26,804	53,215	54,946	9,744	10,226	9,271	13,538	25,386
Current Position	11,177	3,016	51,266	53,212	45,490	10,136	1,089	30,297	15,537	4,170
Taxes Receivable	172,121	121,537	147,440	160,883	165,686	9,564	6,467	13,750	13,840	13,352
Deferred Revenues	(79,107)	(66,160)	(80,519)	(93,140)	(102,629)	(4,069)	(1,343)	(3,089)	(3,407)	(2,500)
Total Fund Balance	149,593	99,753	154,726	163,668	161,450	17,256	7,042	40,971	26,005	27,109
As % of Revenues	17.1	12.1	16.0	15.6	14.4	3.3	1.3	6.7	3.0	2.8
Reserved for Budget Stabilization	9,442	23,565	44,486	45,771	51,808	14,244	11,076	22,763	22,901	24,324
As % of Revenues	1.1	2.9	4.6	4.4	4.6	2.7	2.0	3.7	2.6	2.6
Unreserved, Undesignated Fund Balance	97,898	47,062	61,974	68,610	68,317	3,012	(4,068)	18,209	3,104	2,785
As % of Revenues	11.2	5.7	6.4	6.5	6.1	0.6	(0.7)	3.0	0.4	0.3

GAAP – Generally accepted accounting principles.

actually matched the originally budgeted level, allowing for modest reserve replenishment at a much earlier stage in the cycle than was possible for most other states. Tax revenues for the year rose 3.1%. At the close of the year, the general fund stabilization reserve was about one-half funded at $23.6 million. On a GAAP basis, the general fund ran a $49.8 million operating deficit and closed with a $99.8 million total fund balance.

Fiscal years 2004 and 2005 were both characterized by good revenue growth leading to surplus, full reserve funding, and balance carry-forward. As in most states, fiscal 2004 operations were also assisted by federal aid, which helped offset rapid growth in Medicaid spending. The state closed fiscal 2004 with a $57 million general fund surplus, which allowed full funding of all reserves at fiscal year end. On a GAAP basis, the general fund incurred a $55.0 million operating surplus and a total fund balance of $154.7 million. Fiscal 2005 revenue estimates were raised several times to reflect strong income tax growth. General fund revenues ended nearly 9% over fiscal 2004 levels, with income tax receipts up more than 16%. On a GAAP basis, the state ran an $8.9 million surplus in fiscal 2005 and closed with a $163.7 million total fund balance.

Fiscal 2006 was the third consecutive strong year for the state. General fund revenues of $1.11 billion were up 7.3% over the fiscal 2005 level, with receipts for the income tax up 8.4%, sales tax up 4.2%, and business taxes surging 26%. On an operating basis, the state closed with a $43 million surplus, which was transferred in part to the transportation fund ($10 million) and the budget stabilization reserve ($6 million); $29.4 million was carried forward to fiscal 2007. Fiscal 2006 expenditures rose 7.2%, about the same as revenues. On a GAAP basis, the state finished with a $2.2 million general fund deficit, to close with a $161.5 million total fund balance, or 14.4% of revenues.

Reserves at the end of fiscal 2006 were nearly fully funded. The general fund stabilization reserve, required to hold 5% of prior-year expenditures, was fully funded at $51.2 million. The transportation fund stabilization

reserve, also required to hold 5%, was fully funded at $11.04 million. The education fund stabilization reserve, required to hold between 3% and 5% of fund spending, was 90.8% of the maximum level at $24.3 million. The state also maintains a human services caseload reserve within the general fund, which totaled $8.5 million at the close of fiscal 2006.

Education fund spending was up sharply in fiscal 2005 as the result of Act 68, which increased the state's share of kindergarten through grade 12 (K–12) education spending and lowered local property taxes. The sales tax was raised to 6% from 5% on Oct. 1, 2003, and effective July 1, 2004, one-third of all sales tax receipts are allocated to the education fund, with the remainder retained in the general fund. The act also splits the statewide property tax rate, with homestead property taxed at a rate equal to about two-thirds of the nonresidential rate, which takes advantage of the significant and increasing number of out-of-state second-home owners in Vermont.

Spending pressures include K–12 public education, where expenditures have grown significantly despite declining enrollment statewide. Medicaid spending has also been a pressure, although the state has used some cost-control methods and taken advantage of national easing of medical inflation to reduce projected outyear funding gaps.

Economic Base

Vermont has a relatively small but stable economy that includes manufacturing, tourism, agriculture, and health and educational services. Health and educational services now account for nearly 18% of employment, and leisure and hospitality make up nearly 11%, both well above national averages. Educational services alone make up more than 4% of Vermont's jobs, nearly twice the national share, and Fletcher Allen Health Care is reportedly the state's second largest employer. The business and professional services sector is small in Vermont, making up just 7.2% of state jobs, compared with 12.5% for the nation.

Manufacturing, mostly durables, is still important at 11.7% of jobs, above the nation's 10.9%. Manufacturing declined in the 1990s recession, with employment dropping from more than 50,000 in 1985 to 43,000 in the early 1990s. There was recovery, with 2000 manufacturing employment at 46,400, but it slipped by 2003 to 37,600 and has stabilized near that level. The state's largest private employer continues to be IBM, which reduced its work force, primarily in the Burlington area, by some 1,800 employees during the recession, although it has added back some employees. General Electric also has a significant manufacturing facility in Rutland. Tourism is broad based, including several ski areas for winter attraction, while the scenic beauty and countryside encourage summer and fall visitors. Several ski areas have undergone improvements, including a continuation of year-round use. Increasing second-home and condominium usage provides some stability and has driven a surge in housing prices. Canadian tourism and shopping are an economic factor.

Employment in Vermont peaked in 1989 after a period of rapid growth. Nearly 5% of employment was lost, only about half as severe as the losses in most New England states. By the end of 1994, the loss had been regained, and 2001 employment was more than 15% over the earlier peak.

Vermont's employment growth outperformed the nation's annually from 2000–2004. Year-over-year job losses began in December 2001 and persisted through July 2003. On an annual basis, recessionary losses were about a combined 1% during 2002 and 2003, well below the national loss. Job growth returned to Vermont in 2004, with a 1.3% increase. Growth since has been tepid, with 0.8% in 2005 and 0.7% year-over-year for December 2006. Growth has been strongest in business and professional services, education and health services, and construction, which was up 4.2% in December. Manufacturing jobs performed weakly throughout 2006 and were down 0.5% in December. Vermont's unemployment is consistently among the lowest in the nation.

Vermont's personal income per capita has lagged the U.S. rate since World War II, falling to as low as 77% of the U.S.'s in 1950, and it hovered at only 83% as recently as 1977. More recently, per capita personal income hovered around 90% of the U.S. average until 1998. Since then, a strong growth period has brought per capita personal income to 95% of the U.S. level, ranking it 25th among the states. Vermont remains less wealthy than neighboring New Hampshire, where a faster growing economy and the influence of the Boston metropolitan region drove per capita personal income to nearly 110% of the U.S. rate in 2005.

Vermont's population grew 8.2% during the 1990s, faster than the New England region, yet slower than the U.S. The census bureau estimates Vermont has grown about 2.5% during this decade, slightly faster than New England but slower than the U.S. Vermont's population

is well educated, with nearly one-third of adult Vermonters holding college degrees, ranking it seventh of the states. Vermont also has the nation's largest share of population — nearly three-quarters — living outside the state's primary metropolitan area.

Economic Trends

Nonfarm Employment
(000, Not Seasonally Adjusted)

	VT	% Change	U.S.	% Change
1990	258	—	109,487	—
1995	270	4.9	117,298	7.1
1996	275	1.8	119,708	2.1
1997	279	1.6	122,776	2.6
1998	285	2.0	125,930	2.6
1999	292	2.3	128,993	2.4
2000	299	2.4	131,785	2.2
2001	302	1.1	131,826	0.0
2002	299	(0.9)	130,341	(1.1)
2003	299	0.0	129,999	(0.3)
2004	303	1.3	131,435	1.1
2005	305	0.8	133,463	1.5
December 2005	313	—	135,041	—
December2006p	315	0.7	136,935	1.4

Unemployment Rates
(%, Not Seasonally Adjusted Annual Rates)

	VT	U.S.	VT as % of U.S.
1990	4.9	5.6	88
1995	4.3	5.6	77
1996	4.4	5.4	81
1997	4.0	4.9	82
1998	3.1	4.5	69
1999	2.9	4.2	69
2000	2.6	4.0	65
2001	3.3	4.7	70
2002	4.0	5.8	69
2003	4.5	6.0	75
2004	3.7	5.5	67
2005	3.5	5.1	69
December 2005	3.6	4.9	73
December2006p	3.8	4.5	84

Personal Income
(Change from Prior Year)

	% Change		VT as % of
	VT	U.S.	U.S. Growth
1995	4.8	5.3	89
1996	5.4	6.0	90
1997	6.9	6.1	114
1998	6.1	7.4	83
1999	5.8	5.1	114
2000	7.9	8.0	98
2001	5.1	3.5	145
2002	1.7	1.8	97
2003	3.9	3.1	124
2004	4.3	6.2	70
2005	4.2	5.2	81

Personal Income per Capita
(Change from Prior Year)

	% Change		VT as % of
	VT	U.S.	U.S. Growth
1995	3.8	4.1	94
1996	4.6	4.8	96
1997	4.7	4.8	99
1998	7.1	6.1	116
1999	5.1	3.9	129
2000	7.0	6.8	102
2001	4.6	2.4	187
2002	1.2	0.8	156
2003	3.4	2.1	160
2004	4.0	5.2	77
2005	3.9	4.2	93

Components of Personal Income: Earnings
(%)

	VT		% Change	U.S.		% Change
	2002	2005	2002–2005	2002	2005	2002–2005
Construction	7	8	30	6	6	23
Manufacturing	18	16	4	14	13	9
Durable Goods Manufacturing	13	12	2	9	8	8
Computer and Electronic Manufacturing	6	5	(10)	2	2	5
Trade, Transportation, and Utilities	17	16	12	16	16	13
Financial Activities	6	6	17	10	10	19
Professional and Business Services	9	10	22	13	15	20
Education and Health Services	15	15	20	15	11	20
Government and Government Enterprises	17	18	23	16	17	18
Total Nonfarm Earnings	—	—	16	—	—	16

State Population: 608,827 (2000 census), 623,908 (2006 census estimate)
Population Change: 1990–2000: U.S. 13.1%, Vermont 8.2%; 2000–2006: U.S. 6.4%, Vermont 2.5%
Personal Income per Capita 2005: $32,731 = 94.9% of U.S., rank 25th

p – Preliminary. Note: Monthly unemployment rates are seasonally adjusted.

Copyright © 2007 by Fitch, Inc., Fitch Ratings Ltd. and its subsidiaries. One State Street Plaza, 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. All of the information contained herein is based on information obtained from issuers, other obligors, underwriters, and other sources which Fitch believes to be reliable. Fitch does not audit or verify the truth or accuracy of any such information. As a result, the information in this report is provided "as is" without any representation or warranty of any kind. A Fitch rating is an opinion as to the creditworthiness of a security. 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. 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, suspended, or withdrawn at anytime 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 USD1,000 to USD750,000 (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 USD10,000 to USD1,500,000 (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 Great Britain, 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.

Global Credit Research
New Issue
5 FEB 2007

New Issue: Vermont (State of)

MOODY'S UPGRADES STATE OF VERMONT GENERAL OBLIGATION BONDS TO Aaa FROM Aa1

Aaa RATING AND STABLE OUTLOOK APPLIES TO SERIES 2007 A BONDS AND APPROXIMATELY $440 MILLION IN OUTSTANDING GENERAL OBLIGATION BONDS

State
VT

Moody's Rating

ISSUE		RATING
General Obligation Bonds 2007A		Aaa
Sale Amount	$30,000,000	
Expected Sale Date	02/13/07	
Rating Description	General Obligation	

Opinion

NEW YORK, Feb 5, 2007 -- Moody's Investors Service has upgraded the rating on the State of Vermont's general obligation bonds to Aaa from Aa1. The upgrade to Moody's highest rating level incorporates Vermont's strong history of financial management, evident in the state's maintenance of healthy reserve levels through the recent recession; manageable debt profile that reflects the state's focused efforts to reduce its debt ratios and maintain well-funded pension systems; and a stable, diversifying economy that lacks the kind of volatility that can make revenues swing dramatically up or down and increase financial uncertainty. The outlook on Vermont's general obligation bond rating is stable reflecting Moody's expectations for sustainable growth in the state's revenue sources, maintenance of solid operating reserve balances, and manageable debt levels. We expect that Vermont will continue to demonstrate the willingness and ability to respond with budget adjustments as needed to maintain budget balance.

Vermont plans to sell $30 million General Obligation Series 2007A the week of February 12th. Proceeds will be used for a variety of capital projects of the state.

Credit strengths are:

*Sound financial management and fiscal policies indicated by conservative budgeting practices.

*Prompt action and bipartisan willingness to reduce spending following revenue weakening during recession.

*Relatively rapid restoration of reserves used during period of revenue weakness.

*Steady progress in reducing previously high debt ratios and maintaining an affordable debt profile.

*Low unemployment and poverty rates.

Credit Challenges are:

*Slower job growth moderates revenue performance.

*Still prominent manufacturing sector that has not recovered jobs lost during recession.

*Despite gains, Vermont's per capita income levels remain below the national average. *Potential service pressures due to a population that is aging at a relatively rapid pace.

SOUND FINANCIAL MANAGEMENT REFLECTED IN MAINTENANCE OF HEALTHY RESERVE LEVEL AND PROMPT ACTION TO RESTORE BUDGET BALANCE

Vermont is not immune to economic cycles although it weathered the recent recession relatively well as a result of its established conservative budgeting practices and available reserves. In fiscal years 2002 and 2003 Vermont's economy and revenues weakened along with those of the nation. On a GAAP basis the state's General Fund revenues dropped 3% in fiscal year 2003 and 6% the following year, driven largely by a precipitous decline in personal income taxes. Sales and use tax revenues were essentially flat during the recession but growth in a variety of smaller state tax resources, such as the room and meal tax, helped Vermont offset, to some extent, the substantial 16.7% personal income tax decline. Vermont's General Fund revenues recovered relatively quickly from the recession, aided by prompt bipartisan willingness to restore budget balance. Expenditures were realigned downward, and in fiscal 2004 revenues received a boost from a 1% increase in the state's general sales and use tax rate from 5% to 6% effective October 1, 2003. The telecommunications sales tax rate was also increased to the same rate of 6%. Income taxes also rebounded with GAAP basis gains of nearly 17% and 15%, respectively, in fiscal years 2004 and 2005. The federal government provided relief funds to all states in fiscal years 2003 and 2004, and Vermont prudently applied its allocation for one-time uses rather than base-building, a pattern it continues to maintain with other one-time revenues.

Combining Vermont's major operating funds, General and Education, GAAP results showed much more modest revenue declines of 0.3% and 1.1% in fiscal years 2002 and 2003. This reflects the offsetting impact of statewide education property taxes that did reasonably well in Vermont and across the nation during the recession due to the robust housing market.

Vermont began early restoration of its reserves in fiscal 2003, bringing its General Fund BSR to the full statutorily required level of 5% of prior year budgetary appropriations by year-end fiscal 2004, a level that has been maintained since then as indicated in audited results through fiscal year 2006. Vermont also maintains a fully funded Transportation Fund BSR, also at 5% of prior year appropriations, and one in its Education Fund at the statutory required level of 3.5% to 5% of prior year expenditures, excluding General Fund transfers. A Human Services Caseload Reserve, which is available for unexpected caseload growth due to the economy, adds another layer of flexibility in the event of revenue fluctuation. Vermont used a portion of this reserve to fund its Medicare Part D expenses and repaid the amount with a subsequent federal reimbursement. Combined available operating reserves have averaged about 7% of operating revenues over the past five years, excluding the caseload reserve, and remained at or above 5.8% over that period.

Vermont's management strength has improved with the now timely publication of its financial audits. In earlier years financial reporting was delayed during the extended implementation of a new software system.

HEALTHY REVENUE GROWTH CONTINUED IN FISCAL 2006, SLOWING IN FISCAL 2007 AS EXPECTED

Revenue growth moderated in fiscal year 2006 but maintained a healthy pace of about 7% in its three operating funds combined - General, Transportation, and Education Funds. Income tax growth increased about 8% in fiscal year 2006. Along with personal income taxes, sales tax growth also moderated in fiscal year 2006, increasing by 5% after two very strong years of growth at 21% and 18% in fiscal years 2004 and 2005, respectively, aided by the 1 cent tax increase. As of the beginning of fiscal year 2005, one-third of the state's sales and use taxes are dedicated to the Education Fund, pursuant to Act 68 which changed the state's education funding formula.

Personal income taxes are one of the state's largest revenue sources, accounting for about one-fourth of total operating revenues in fiscal 2006, and the largest source of General Fund revenues at nearly one-half. Other taxes make up about one-fourth of the state's General Fund revenues, with the room and meal tax alone bringing in about 10% in fiscal year 2006.

Vermont publishes a consensus revenue forecast twice a year and the most recent forecast (January 2007) indicates modest General Fund revenue growth of 1% for fiscal year 2007, in line with net positive but slower expected job gains. The initial fiscal 2007 revenue forecast was modest to begin with at 2% above fiscal 2006 forecasted results. Higher than expected personal income, corporate, and estate taxes have helped offset slightly lower sales and other tourism-related taxes that have been negatively affected by high fuel prices and a slow start to the state's winter tourist season. Going forward, the revenue forecast for the next biennium is about 3%, in line with expectations of continued moderate economic expansion and job growth.

For the fourth consecutive year in a row, Vermont expects its Budget Stabilization Reserves (BSR) in the General and Transportation Funds to remain fully funded at statutory levels at the end of fiscal 2007. The Education Fund BSR is also expected to end at the statutorily required level.

FISCAL 2008 BUDGET PROPOSAL INCORPORATES MODEST SPENDING GROWTH; GLOBAL HEALTHCARE INITIATIVE TO BE IMPLEMENTED IN COMING YEAR

The governor's budget plan for the upcoming fiscal year 2008 budget reflects modest General Fund baseline spending growth of 3.16% resulting in a small operating surplus and all BSR's funded at required levels. The budget increase is in line with projected job growth that is slower than the national pace, as it has been over the past year, but sustainable. The governor also proposed two caps: 1) a limit on General Fund spending growth tied to inflation plus population growth, and 2) limiting education spending growth to establish a soft cap on property taxes. The latter cap would sunset after five years and could be overridden by a 60% local vote.

Vermont is one of three states, along with Maine and Massachusetts, which has taken steps to provide broad access to health care. Last year Vermont passed the 2006 Health Care Affordability Act to control costs and make health care affordable and accessible for all state residents. Funding for the program is expected to come from: 1) individuals, who will pay sliding scale premiums; 2) employers, including an employer-sponsored insurance initiative that will use Medicaid to cover some of the costs of lower-income individuals; and 3) a portion of the state's tobacco tax which was increased last year. Enrollment caps are expected to help limit the state's fiscal obligation.

Vermont also obtained two major Medicaid waivers that are intended to increase the state's management flexibility and fiscal control of publicly supported health care programs. The arrangement limits federal spending for certain Medicaid services in Vermont for five years. The state is responsible for managing with the funding limits and stands to benefit from any savings from efficiencies. Given the state's manageable size and recent progress with Medicaid cost containment, Vermont appears to be well-positioned to launch its healthcare initiative in October 2007. However analysis of the plan's effectiveness will be evaluated over time.

CONTINUED ECONOMIC IMPROVEMENT; JOBS EXPECTED TO GROW AT SUSTAINABLE PACE

Vermont's economy held up relatively well in the recent recession. Total non-farm jobs lost were recovered by 2004, earlier than most states. Continuous job growth in education and health services, Vermont's largest employment sector, along with healthy job gains in the professional and business services sector have helped offset persistent weakness in manufacturing. For 2006, Vermont's average annual year-over-year job growth has been positive for almost all employment sectors. Manufacturing, still one of the core industries of Vermont's economy, is finally experiencing job growth although the sector is still down about 9,700 (20%) from peak levels six years ago. The state's unemployment level has remained among the lowest in the New England region 3.8% in December 2006, also below the national average of 4.5% the same month. Vermont's job growth will likely maintain a below average but sustainable pace reflecting modest net in-migration and slow population growth. As a result, unemployment levels should remain low.

Employment is stable at IBM, the Vermont's largest employer with over 6,000 employees. The company has succeeded in securing several long-term supply contracts with the US Department of Defense and Eastman Kodak, although IBM does not expect significant additions to its employment base. Fletcher Allen Health Care, a private company that is Vermont's second largest employer, has recently completed a major expansion of its facilities.

DEBT RATIOS REMAIN MANAGEABLE; MODEST ISSUANCE PLANNED

Vermont's debt levels have declined considerably over the past decade and are now about average relative to Moody's 50-state median, on both a per capita and personal income basis. Debt per capita of $707, compared to the state median of $754 ranked Vermont 29th among the fifty states in Moody's 2006 state debt medians. Debt to total personal income of 2.2%, compared to the 2.5% state median, ranked Vermont 29th. Both ratios represent steady improvement in Vermont's debt profile, reflecting efforts by the state's Capital Debt Affordability Advisory Committee which oversees long-term capital planning for the state. The state's debt authorization levels have dropped steadily over the past decade. The fiscal 2008 amount recommended by the advisory committee for legislative authorization is 20% lower than the level authorized in 1995.

Vermont's overall pension funding levels are strong relative to other states. The state employees system has

a funding level of 99%. While the teachers' system is lower, at about 85%, the level reflects a recent revision to the state's funding method that brings it in line with other state systems. The method change in 2006 had the effect of reducing the teachers' system pension funding from the prior level about 95%. At the same time, the state committed to full annual funding requirements which had previously been low due to the appearance of higher funded levels. Vermont recently completed its assessment of its other post employment benefit (OPEB) liability which totaled about $1.5 billion. Under a pre-funding assumption, the liability drops to about $718 million.

Outlook

The stable outlook on Vermont's general obligation bond rating incorporates Moody's expectations for continued growth in the state's primary revenue sources and maintenance of strong reserve balances and manageable debt levels. We believe that Vermont will continue to demonstrate the willingness and ability to respond with budget adjustments as needed to maintain budget balance.

What could make the rating go - DOWN

*Deterioration in the state's financial performance.

*Weakened reserve levels.

*Increasing debt ratios relative to Moody's 50-state median.

*Economic weakness resulting in persistent revenue underperformance.

Analysts

Nicole Johnson
Analyst
Public Finance Group
Moody's Investors Service

Emily Raimes
Backup Analyst
Public Finance Group
Moody's Investors Service

Robert A. Kurtter
Senior Credit Officer
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

© Copyright 2007, Moody's Investors Service, Inc. and/or its licensors including Moody's Assurance Company, Inc. (together, "MOODY'S"). All rights reserved.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY COPYRIGHT LAW AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind and MOODY'S, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The credit ratings

and financial reporting analysis observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER. Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling.

MOODY'S hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MOODY'S have, prior to assignment of any rating, agreed to pay to MOODY'S for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,400,000. Moody's Corporation (MCO) and its wholly-owned credit rating agency subsidiary, Moody's Investors Service (MIS), also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually on Moody's website at www.moodys.com under the heading "Shareholder Relations - Corporate Governance - Director and Shareholder Affiliation Policy."

Special Comment

August 2007

Contact	Phone
New York	
Nicole Johnson	1.212.553.4573
Maria Coritsidis	1.212.553.4173
Ted Hampton	1.212.553.2741
Whitney Jones	1.212.553.7488
Kimberly Lyons	1.212.553.4673
Emily Raimes	1.212.553.7203
Nicholas Samuels	1.212.553.7121
Mark Tenenhaus	1.212.553.0849
Robert Kurtter	1.212.553.4453

U.S. STATES CREDIT SCORECARD 2007

Quantitative Results Presented for 2007 With Comparisons to 2006

Summary

The 2007 Moody's U.S. States Credit Scorecard is the second publication of a quantitative analytic tool that enhances the consistency of our state general obligation (G.O.) credit analysis. As noted in our initial scorecard report last year, the fundamental approach to rating state debt, outlined in Moody's State Rating Methodology (November 2004) remains unchanged. The updated scorecard reflects and supports the fundamental methodology, by comparing select data points and other variables for the four main factors in our state credit analysis: economy, debt, finances, and governance framework. Use of the scorecard aids in the identification of important statistical trends within the state sector and also helps preserve consistency regarding the statistical aspects of our analysis.

- The scorecard provides clear relative rankings of the 50 states on the most important statistical variables included in Moody's credit analysis of state governments.
- The quantitative data and rankings are used in the rating process to enhance state comparative analysis and identify sector trends.
- Variables related to states' financial best practices and measures of institutional financial flexibility are incorporated in the scorecard. These have been updated to reflect any changes in governance framework since our last report.
- The scorecard results have limitations in that they are backward-looking, using only historical data. The results are used to inform the rating process but not to determine Moody's G.O. rating assignments.

This report provides the 2007 scorecard results, repeats the 2006 results and reviews the scorecard description, including the individual variables. The 2007 scorecard results reflect data from the most recent fiscal year (FY06, ended 6/30/06 for most states) in which consistent data for all states are available. In the appendices, we present the 2006 and 2007 ranking results, as well as median and range information for the underlying statistical data in both years.

The scorecard is not meant to be a substitute for rating committee judgments regarding ultimate credit quality and G.O. bond ratings for the individual states, nor is it meant to be a matrix for automatically assigning or changing ratings. Moody's state ratings are forward-looking opinions of relative financial strength, with an emphasis on the management of financial results within the constraints of a state's governance framework. Included in the rating is our assessment of the expected willingness of state leadership to preserve a strong financial profile in the future, recognizing that all states face inevitable cyclical economic downturns as well as persistent constituent demands in excess of available fiscal resources. The willingness to make these difficult decisions is ultimately a matter of judgment, which we believe transcends the output or results of any strictly quantitative tool or approach. Moreover, the limited number of variables included in the scorecard cannot fully capture the breadth and depth of our fundamental credit analysis. Nevertheless, the historical performance statistics captured in the scorecard are important, and in general higher ratings can be expected among the states with the highest statistical scores and rankings from the scorecard.

The 2007 Scorecard Results: 14 States Change Tiers; State Economic and Finanical Data Show Overall Improvement

Since the publication of the 2006 scorecard most states have experienced economic growth leading to stronger tax revenue collections and, in turn, improved financial operations and higher reserve positions. Given the overall improvement of state credits as a class and the relative nature of the set of measures used in the scorecard, tier movement similiar to 2006 is not unexpected in the 2007 scorecard. The results bear this out, with 7 states showing tier movement up and 7 moving down compared with the prior 2006 scorecard in which 14 states had tier movements relative to 2005. Appendix B shows a comparison of overall tier rankings in 2006 and 2007 and highlights the states that had tier movement. Appendix C further breaks out the tier changes by category - i.e. Finances, Economy, Debt, and Governance Framework. Appendix D provides median data for each of the variables as reported in the 2006 and 2007 scorecards, primarily reflecting 2005 and 2006 data.

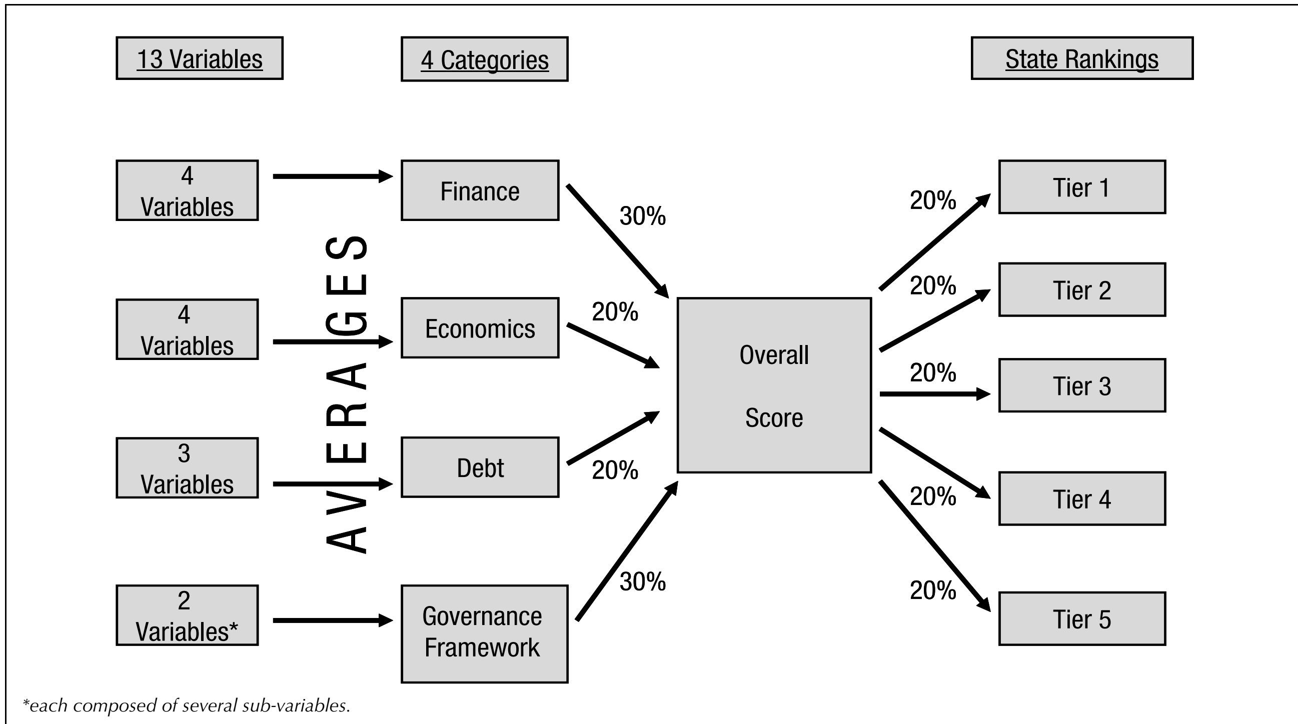
State	2007 Scorecard Tier	2006 to 2007 Scorecard Tier Change
Alabama	2	Improved from tier 4
Alaska	3	Improved from tier 4
Arkansas	3	Declined from tier 2
Connecticut	3	Improved from tier 4
Idaho	1	Improved from tier 2
Louisiana	5	Declined from tier 4
Minnesota	2	Declined from tier 1
New Hampshire	3	Declined from tier 2
North Carolina [1]	2	Improved from tier 3
Oklahoma	4	Declined from tier 3
Oregon [2]	4	Improved from tier 5
Pennsylvania	4	Declined from tier 3
Washington	2	Improved from tier 3
West Virginia	4	Declined from tier 2

[1] Rating upgraded to Aaa from Aa1 in January 2007.
[2] Rating upgraded to Aa2 from Aa3 in August 2007.

Scorecard Reflects Moody's State Rating Methodology; State Rankings and Trends Influence, But Do Not Determine Rating

The states scorecard was developed to reflect and support Moody's fundamental approach to rating state governments, by assembling and comparing select data points and other variables in the areas of economy, debt, finances, and governance framework, the four main areas of our state analyses. The approach generates relative rankings of the 50 states on each of thirteen variables (described in the Appendix), averages them by factor or category, and then generates an overall ranking by weighting each of the four factors. As discussed in our 2004 methodology report, the finances and governance framework categories are weighted more heavily relative to the economy and debt categories.

The resulting overall rankings are finally grouped into quintiles that are relative "tiers" of performance on the scorecard. This approach helps separate changes in relative position over time from general changes affecting the entire class of state credits. Moody's maintains G.O. or equivalent ratings on 46 states, 44 of which are in the Aa and Aaa categories. However, a strong upward or downward tier movement, especially if sustained over time, could be an indicator of a meaningful change in relative performance, and could warrant re-examination of a state's G.O. rating.



It is important to note the limitations of the scorecard, including the fact that it is retrospective, only providing a backward look at a state's performance. For example, financial data is from the fiscal 2006 audits which ended June 30, 2006 for most states, while they are currently engaged in managing their fiscal 2008 budgets. In addition, economic and debt trends are assessed on a five or ten-year trend reflecting past performance. By comparison, Moody's state G.O. ratings are forward-looking opinions of relative financial strength, with an emphasis on the quality of a state's governance framework. These latter variables in particular capture only a portion of the governance framework analysis that is included in Moody's G.O. rating opinions. While backward-looking the historical performance statistics captured on the scorecard are important and, in general, higher ratings can be expected among the states with the highest statistical scores and rankings from the scorecard. However, there is no rule that a particularly high or low scorecard ranking, even if it persists over time, will necessarily have implications for a state's bond rating.

While the thirteen variables have not changed from the 2006 scorecard, Moody's does expect to refine the scorecard in the future to include new data and variables as they become available, such as OPEB liabilities. Other changes or refinements could also be made over time if appropriate.

States Scorecard's Finance, Economy, Debt and Governance Framework Variables*

Finance Variables

1. Five -Year Average Fund Balance Ratio.
2. Five-Year Tax Revenue Growth.
3. Five-Year Expenditure Growth.
4. Borrowing for Operations
   a. Short-term cash-flow borrowing for any of the past two years.
   b. Long-term borrowing for budget purposes in the most recent fiscal year.
   c. Long-term borrowing for budget purposes in any of the three prior fiscal years.

Debt Variables

1. Ten Year Growth in Net Tax-Supported Debt as % of State Personal Income.
2. Net Tax-Supported Debt to State Tax Revenues.
3. State Pension Funding Ratio.

Economic Variables

1. Ten Year Growth in State Per-Capita Income as % of US Average.
2. Five-Year State Employment Growth.
3. Five-Year Domestic Net Migration as % of US Total.
4. State Poverty Rate.

Governance Framework

1. Institutional Financial Flexibility - presence of each of the following either detracts from or enhances the score on this variable:
   a. Inflexible spending mandates or revenue restrictions in state constitution.
   b. Voter initiative/referendum process in state constitution.
   c. Super-majority requirement for budget passage or tax increases.
   d. Timely budget adoption.
2. Fiscal Best Practices - presence of each of the following enhances the score on this variable:
   a. Consensus revenue forecasting process.
   b. Multi-year financial planning oriented around structural budget balance.
   c. Executive branch legal power to make mid-year spending adjustments w/out legislative approval.
   d. Regular and effective debt affordability analysis.
   e. Timely GAAP-basis audited financial reporting.

**See Appendix for detailed description of variables.*

APPENDIX A

Detailed Description of Finance, Debt, Economy, and Governance Framework Variables

FINANCE VARIABLES

1. Five-Year Average Fund Balance Ratio

The most recent five-year average of the ratio of Unrestricted Fund Balance plus Available Reserves to Operating Revenues. The data are for the state's primary operating funds, on a GAAP basis, as reported in Moody's MFRA.

2. Five-Year Tax Revenue Growth

The most recent five-year total growth in state tax revenues. The data are for the state's primary operating funds, on a GAAP basis, as reported in Moody's MFRA.

3. Five Year Expenditure Growth

The most recent five year total growth in state operating expenditures. The data are for all governmental funds (including federal special revenue funds), on a GAAP basis.

4. Borrowing for Operations

This variable is an amalgamation of three yes/no questions: (i) has the state incurred short-term cash-flow borrowing in any of the past two years? (ii) has the state incurred long-term borrowing for operating budget purposes in the most recent fiscal year? (iii) has the state incurred long-term borrowing for operating budget purposes in any of the three prior fiscal years? The scoring for this variable is relatively more sensitive to question (ii), as this is an indicator of current structural budget imbalance pressure in addition to the recent incurrence of long-term deficit-related debt. States rankings for this variable are generated in a manner that is proportionally consistent with the 1 to 50 rankings used for other variables.

DEBT VARIABLES

1. Ten-Year Growth in Net Tax-Supported Debt as % of State Personal Income

A measure of the growth of the state's debt over the past ten years relative to the state's economic base, as measured by total state personal income. Each state's net tax-supported debt data are compiled annually by Moody's and published in our annual State Debt Medians Report. The last five years' of debt data and debt as a percent of personal income are also reported in Moody's MFRA.

2. Net Tax Supported Debt to State Tax Revenues

A current measure of state tax-supported indebtedness, relative to the current tax revenue base of the state's operating funds. Both data points are reported in Moody's MFRA.

3. State Pension Funding Ratio

The most recently reported ratio of state defined benefit pension system assets (on an actuarial valuation basis) to the present value of actuarial accrued liabilities. If the state is involved in the funding of multiple defined benefit systems, a combined funding ratio is used. The data are collected by Moody's from publicly-available sources. The scorecard rankings are based on the most recent year for which a great majority of states have reported data – for example, the 2006 scorecard ranks pension funding data predominantly reported as of 2004. Despite the effort to ensure reporting period comparability, the use of differing actuarial methods and assumptions by the states may still limit the true comparability of the data.

ECONOMIC VARIABLES

1. Ten-Year Growth in State Per-Capita Income as % of US Average

The most recent ten-year growth in the ratio of state per-capita income to U.S. per-capita income. The data are on a calendar year basis, as reported by the U.S. Bureau of Economic Analysis.

2. Five Year State Employment Growth

The most recent five-year total growth in the state's total payroll employment (both private sector and government sector), as reported by the U.S. Bureau of Labor Statistics. The data are on a calendar-year average basis, and are not seasonally adjusted.

3. Five-Year Domestic Net Migration as % of US Total

The state's most recent five-year total net domestic migration, as reported by the U.S. Census Bureau, as a percentage of total U.S. domestic migration over the same period. It is an indicator of the relative attractiveness of the state's economy, and is naturally skewed by absolute size of the economies in question. The largest states will typically be at either the top end (e.g. Florida) or the bottom end (e.g. NY) of this ranking. Foreign migration, which can also be a positive state economic indicator, is not included in this measure.

4. State Poverty Rate

The current percentage of the state's population living in households with income below the national poverty level, as defined and reported by the U.S. Census Bureau. The data are for the most recent year reported by the Census Bureau (i.e. 2005 data in the 2007 scorecard), and is currently reported in MFRA.

GOVERNANCE FRAMEWORK VARIABLES

1. Institutional Financial Flexibility

This variable is an amalgam of four yes/no questions:

a. Inflexible spending mandates and/or revenue limits – does the state constitution contain (i) one or more significant and inflexible minimum spending mandates, or (ii) an inflexible limitation on overall revenue collection and/or requirement to refund "excess" revenues?

b. Initiatives and referenda – does the state constitution authorize a process of voter initiative and/or referenda which has in the past led to significant fiscal policy uncertainties?

c. Super-majority requirements - does the state constitution require greater than majority approval of legislators for adoption of the budget and/or for raising new revenues?

d. Timely budget adoption – has the state, on more than one occasion over the past five years, passed its budget later than one month after the start of the fiscal year or had a budget delay of any length that resulted in a partial or full state government shutdown?

2. Fiscal Best Practices

This variable is an amalgam of five yes/no questions:

a. Consensus revenue forecasting - does the state adhere to an institutionalized consensus revenue estimating process, supported by nonpartisan and objective economic analysis?

b. Multi-year financial planning - does the state regularly publish multi-year financial plans, including out-year analysis of revenue and spending forecasts?

c. Executive branch mid-year spending reduction powers – does the executive branch have the legal power to make mid-year spending reductions, without need for legislative approval, and is this supported by strong budget monitoring and control processes?

d. Debt affordability analysis - does the state regularly publish a debt affordability analysis that effectively informs capital budgets and legislative debt authorization decisions?

e. Timely audited financial reporting – for each of the past two fiscal years, has the state published its audited, GAAP basis financial statements within nine months of the fiscal year-end?

Appendix B

2006 Scorecard and 2007 Scorecard State Rankings
(states listed alphabetically by quintile)

Tier	2006	Rating as of Jan. '06	2007	Current Rating
Tier 1	Delaware	Aaa	Delaware	Aaa
	Florida	Aa1	Florida	Aa1
	Maryland	Aaa	Idaho↑	Aa2
	Minnesota	Aa1	Maryland	Aaa
	Nebraska	-	Nebraska	-
	North Dakota	Aa2	North Dakota	Aa2
	Utah	Aaa	Utah	Aaa
	Vermont	Aa1	Vermont	Aaa
	Virginia	Aaa	Virginia	Aaa
	Wyoming	-	Wyoming	-
Tier 2	Arkansas	Aa2	Alabama↑	Aa2
	Georgia	Aaa	Georgia	Aaa
	Idaho	Aa2	Indiana	Aa1
	Indiana	Aa1	Iowa	Aa1
	Iowa	Aa1	Minnesota↓	Aa1
	Montana	Aa3	Montana	Aa2
	New Hampshire	Aa2	North Carolina↑	Aaa
	South Carolina	Aaa	South Carolina	Aaa
	Tennessee	Aa2	Tennessee	Aa1
	West Virginia	Aa3	Washington↑	Aa1
Tier 3	Hawaii	Aa2	Alaska↑	Aa2
	Kansas	Aa1	Arkansas↓	Aa2
	Nevada	Aa1	Connecticut↑	Aa3
	North Carolina	Aa1	Hawaii	Aa2
	Oklahoma	Aa3	Kansas	Aa1
	Pennsylvania	Aa2	Nevada	Aa1
	Rhode Island	Aa3	New Hampshire↓	Aa2
	South Dakota	-	Rhode Island	Aa3
	Texas	Aa1	South Dakota	-
	Washington	Aa1	Texas	Aa1
Tier 4	Alabama	Aa2	Arizona	Aa3
	Alaska	Aa2	Colorado	-
	Arizona	Aa3	Massachusetts	Aa2
	Colorado	-	Michigan	Aa3
	Connecticut	Aa3	Missouri	Aaa
	Louisiana	A2	New Mexico	Aa1
	Massachusetts	Aa2	Oklahoma↓	Aa3
	Michigan	Aa2	Oregon↑	Aa2
	Missouri	Aaa	Pennsylvania↓	Aa2
	New Mexico*	Aa1	West Virgina↓	Aa3
Tier 5	California	A2	California	A1
	Illinois	Aa3	Illinois	Aa3
	Kentucky	Aa2	Kentucky	Aa2
	Maine	Aa3	Louisiana↓	A2
	Mississippi	Aa3	Maine	Aa3
	New Jersey	Aa3	Mississippi	Aa3
	New York	Aa3	New Jersey	Aa3
	Ohio	Aa1	New York	Aa3
	Oregon	Aa3	Ohio	Aa1
	Wisconsin	Aa3	Wisconsin	Aa3

↑ Upward tier movement
↓ Downward tier movement

** NM has not yet released GAAP financial audits for fiscal 2005 and fiscal 2006. As a result, some of their financial measures are not comparable with those of the other 49 states.*

Appendix C
2006 Scorecard and 2007 Scorecard Rankings by Finance, Economy, Debt, and Governance Framework Categories
(states listed alphabetically by quintile)

	FINANCE RANKING		ECONOMY RANKING		DEBT RANKING		GOVERNANCE FRAMEWORK	
	2006	2007	2006	2007	2006	2007	2006	2007
Tier 1	Alaska	Alabama↑	Arizona	Arizona	Arizona	Delaware	Delaware	Delaware
	Arkansas	Alaska	Delaware	Delaware	Delaware	Idaho	Illinois	Illinois
	Delaware	Delaware	Florida	Florida	Georgia	Iowa↑	Indiana	Indiana
	Florida	Florida	Maryland	Idaho↑	Idaho	Montana↑	Maryland	Kansas↑
	Hawaii	Hawaii	Nevada	Montana↑	Nebraska	Nebraska	Minnesota	Maryland
	Kansas	Maryland↑	New Hampshire	Nevada	South Dakota	South Dakota	North Carolina	North Carolina
	Montana	Montana	North Dakota	Texas↑	Tennessee	Tennessee	South Carolina	Rhode Island↑
	North Dakota	Nebraska↑	Vermont	Virginia	Texas	Texas	Utah	South Carolina
	Vermont	North Dakota	Virginia	Washington↑	Vermont	Vermont	Virginia	Utah
	West Virginia	Virginia↑	Wyoming	Wyoming	Wyoming	Wyoming	Washington	Virginia
Tier 2	Alabama	Arizona↑	Colorado	Colorado	Arkansas	Arizona↓	Connecticut	Florida
	Georgia	Arkansas↓	Idaho	Hawaii↑	Indiana	Florida↑	Florida	Iowa
	Louisiana	Connecticut↑	Maine	Maryland↓	Iowa	Georgia↓	Iowa	Massachusetts↑
	Maryland	Georgia	Minnesota	New Hampshire↓	Maine	Maine	Kansas	Michigan
	Minnesota	Idaho↑	Montana	New Mexico↑	Maryland	Maryland	Michigan	Minnesota↓
	Missouri	Minnesota	Nebraska	North Dakota↓	Minnesota	Minnesota	Nevada	Nevada
	New Mexico	Missouri	Rhode Island	Oklahoma↑	Montana	New Hampshire↑	Oregon	Vermont↑
	Oklahoma	Oklahoma	South Dakota	South Dakota	North Dakota	North Carolina↑	Rhode Island	Washington↓
	South Dakota	Vermont↓	Texas	Utah↑	Pennsylvania	North Dakota	West Virginia	West Virginia
	Wyoming	Washington↑	Washington	Vermont↓	Virginia	Utah	Wyoming	Wyoming
Tier 3	Arizona	Indiana	Alaska	Alabama↑	Alabama	Alabama	Arkansas	Connecticut↓
	Idaho	Kansas↓	Georgia	Alaska	Florida	Arkansas↓	Georgia	Georgia
	Indiana	Nevada	Hawaii	Arkansas↑	Kentucky	Colorado↑	Hawaii	Hawaii
	Nebraska	Ohio↑	Massachusetts	Georgia	Michigan	Indiana↓	Louisiana	Louisiana
	Nevada	Pennsylvania	New Jersey	Minnesota	Missouri	Michigan	Massachusetts	Maine↑
	Pennsylvania	South Carolina	New Mexico	New Jersey	New Hampshire	Missouri	Mississippi	New Hampshire
	South Carolina	South Dakota↓	Oklahoma	North Carolina↑	North Carolina	New York↑	New Hampshire	New Jersey
	Tennessee	Utah	Oregon	Oregon	Oklahoma	Pennsylvania↓	New Jersey	New Mexico↑
	Utah	West Virginia↓	Utah	Tennessee↑	Utah	Virginia↓	Tennessee	Oregon↓
	Virginia	Wyoming	West Virginia	Wisconsin↑	Wisconsin	Wisconsin	Vermont	Tennessee
Tier 4	Colorado	Colorado	Arkansas	Connecticut	Colorado	Alaska↑	Alabama	Alabama
	Connecticut	Iowa	California	Kentucky↑	Connecticut	Connecticut	Idaho	Arkansas↓
	Iowa	Kentucky	Connecticut	Maine↓	Louisiana	Kentucky↓	Kentucky	Idaho
	Kentucky	Massachusetts	Iowa	Massachusetts↓	Nevada	Nevada	Nebraska	Mississippi↓
	Massachusetts	Mississippi	Kansas	Missouri	New York	Ohio	New Mexico	Nebraska
	Michigan	New Hampshire	Missouri	Nebraska↓	Ohio	Oklahoma↓	New York	New York
	Mississippi	New Jersey↑	Pennsylvania	Pennsylvania	Oregon	Oregon	North Dakota	North Dakota
	New Hampshire	New Mexico↓	South Carolina	Rhode Island↓	Rhode Island	Rhode Island	Pennsylvania	Pennsylvania
	Ohio	North Carolina↑	Tennessee	South Carolina	South Carolina	South Carolina	Texas	Texas
	Washington	Tennessee↓	Wisconsin	West Virginia↓	Washington	Washington	Wisconsin	Wisconsin
Tier 5	California	California	Alabama	California↓	Alaska	California	Alaska	Alaska
	Illinois	Illinois	Illinois	Illinois	California	Hawaii	Arizona	Arizona
	Maine	Louisiana↓	Indiana	Indiana	Hawaii	Illinois	California	California
	New Jersey	Maine	Kentucky	Iowa↓	Illinois	Kansas	Colorado	Colorado
	New York	Michigan↓	Louisiana	Kansas↓	Kansas	Louisiana↓	Maine	Kentucky↓
	North Carolina	New York	Michigan	Louisiana	Massachusetts	Massachusetts	Missouri	Missouri
	Oregon	Oregon	Mississippi	Michigan	Mississippi	Mississippi	Montana	Montana
	Rhode Island	Rhode Island	New York	Mississippi	New Jersey	New Jersey	Ohio	Ohio
	Texas	Texas	North Carolina	New York	New Mexico	New Mexico	Oklahoma	Oklahoma
	Wisconsin	Wisconsin	Ohio	Ohio	West Virginia	West Virginia	South Dakota	South Dakota

↑ Upward tier movement
↓ Downward tier movement

** NM has not yet released GAAP financial audits for fiscal 2005 and fiscal 2006. As a result, some of their financial measures are not comparable with those of the other 49 states.*

Appendix D
2006 Scorecard and 2007 Scorecard Underlying Data Medians for Finance, Economy, and Debt Variables*

	High	Median	Low
Finance Variables			
Five Year Average Fund Balance Ratio			
2006	79.9%	3.8%	(18.4%)
2007	88.0%	4.4%	(19.2%)
Five Year Tax Revenue Growth			
2006	66.0%	23.1%	4.1%
2007	135.8%	36.6%	10.8%
Five Year Expenditure Growth			
2006	81.3%	33.3%	6.5%
2007	61.4%	22.1%	0.0%
Number of States that Inccured Deficit Borrowing in the Most Recent Year			
2006		2	
2007		2	
Economy Variables			
Ten-Year Growth in Per-Capita Income as a % of U.S. Average			
2006	16.7%	0.9%	(13.2%)
2007	24.0%	0.4%	(7.3%)
Five-Year State Employment Growth			
2006	19.2%	1.5%	(6.2%)
2007	19.8%	4.5%	(2.7%)
Five-Year Domestic Net Migration			
2006	1,029,341	6,283	(960,686)
2007	1,039,467	7,643	(1,022,954)
State Poverty Rate			
2006	18.1%	11.2%	5.8%
2007	20.1%	11.7%	5.6%
Debt Variables			
Ten-Year Growth in Net Tax-Supported Debt as % of State Personal Income			
2006	4.3%	0.3%	(4.2%)
2007	10.6%	2.4%	0.1%
Net Tax-Supported Debt to State Tax Revenues			
2006	162.0%	45.0%	1.6%
2007	154.5%	41.5%	1.3%
State Pension Funding Ratio			
2006	111.2%	85.0%	43.5%
2007	132.4%	83.3%	43.4%

**The 2007 Scorecard rankings are based predominantly on underlying data from 2006, and the 2006 Scorecard rankings are based predominantly on data from 2005. Pension funding and poverty rate data lag by an additional year. See Appendix A for information on the calculation and reporting of each variable.*

Related Research

Special Comment:

U.S. States Credit Scorecard, August 2006 (98088)

Moody's State Rating Methodology, November 2004 (89335)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

PAGE INTENTIONALLY LEFT BLANK

To order reprints of this report (100 copies minimum), please call 1.212.553.1658.
Report Number: 104389

Author

Nicole Johnson

Senior Production Associate

Charles Ornegri

© Copyright 2007, Moody's Investors Service, Inc. and/or its licensors and affiliates including Moody's Assurance Company, Inc. (together, "**MOODY'S**"). All rights reserved. **ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY COPYRIGHT LAW AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT**. All information contained herein is obtained by **MOODY'S** from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind and **MOODY'S**, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. Under no circumstances shall **MOODY'S** have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of **MOODY'S** or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if **MOODY'S** is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The credit ratings and financial reporting analysis observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. **NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.** Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling.

MOODY'S hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by **MOODY'S** have, prior to assignment of any rating, agreed to pay to **MOODY'S** for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,400,000. Moody's Corporation (MCO) and its wholly-owned credit rating agency subsidiary, Moody's Investors Service (MIS), also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually on Moody's website at www.moodys.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

RESEARCH

State Review: Vermont

Publication date: 07-Feb-2007
Primary Credit Analyst: Colin A MacNaught, Boston (1) 617-530-8312; colin_macnaught@standardandpoors.com
Secondary Credit Analyst: Karl Jacob, New York (1) 212-438-2111; karl_jacob@standardandpoors.com

Credit Profile

GO debt rating

AA+/Stable; $468.6 mil

Rationale

Vermont's 'AA+' GO debt rating, with a stable outlook, reflects the state's:

- Strong financial management, including conservative debt and budgeting practices, that has helped maintain its favorable financial position with ample reserves and liquidity;
- Stable economy that continues to experience modest growth; and
- Favorable debt position with a low debt burden and rapid amortization of debt outstanding.

The state pledges its full faith and credit to the repayment of GO debt.

Vermont's economy remains stable and continues to experience growth, albeit at levels that lag the national average. Most major economic indicators continue to reflect growth trends that are, in general, above average for the New England region but are slower than overall national levels. The economic forecast for the state was updated in November 2006 with most of the major indicators realizing a modest expansion. Employment growth is forecast to grow by an average of 0.8% year-over-year for fiscal 2006. This is significantly lower than the 1.5% growth rate in 2005, and it reflects a labor market slow down. The labor market, however, remains tight with low unemployment and positive personal income growth. Unemployment rates have been consistently lower than the national average for at least the past 10 years; through December 2006, unemployment was 3.8%. According to Global Insight, employment increases led to healthy personal income growth of 3.3% year-over-year in 2006; the professional and business services sector and the education and health services sector drove this growth. Leisure and hospitality services, which is a sector that plays a bigger role in the state economy compared with the national economy, experienced below-forecast growth due to a mild 2006 ski season. The real estate market is slowing in Vermont, which is in-line with national trends; this slow down poses some risk to the state's overall economy. Construction and new development, especially focused on the state's major ski resorts, however, remains robust; and state officials expect it to contribute to an orderly housing correction.

Positive economic performance over the past several years has translated into steady and consistent operating results. Financial reserves were at their statutory limits in both the general and transportation funds at fiscal year-end 2006, providing the state with sound revenue flexibility. Management has maintained general fund budget stabilization reserves at their maximum level since fiscal 2004 due, in part, to detailed and conservative budget planning and experienced fiscal management. The January consensus revenue forecast made a slight upward revision to fiscals 2007 and 2008 revenues. State officials are projecting general fund revenues to reach $1.124 billion in fiscal 2007 and $1.152 billion in fiscal 2008. The governor's fiscal 2008 budget recommendation calls for a general fund increase of 3.16%.

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

Vermont's management practices are considered strong under Standard & Poor's Financial Management Assessment (FMA) methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Vermont's debt burden has remained a credit strength over the past several years with debt capacity steadily increasing as state officials retire more debt than they issue. The state's debt affordability committee has recommended increasing bonding to $49 million in fiscal 2008. The state's debt burden is low, and its debt structure is conservative. Nearly all of the state's direct debt consists of fixed-rate GO bonds, which amortize rapidly. At fiscal year-end 2006, debt ratios were a manageable $811 per capita and 2.4% of personal income, including the $45 million the state will issue in fiscal 2007.

Outlook

The stable outlook reflects Standard & Poor's Ratings Services' expectation that the state's prudent financial and debt management practices will continue to lead to positive financial operations and structural budget balance. Vermont's strong revenue growth has allowed it to increase its reserves beyond statutory levels, providing the state some measure of revenue flexibility should revenue growth moderate. The stable outlook also reflects ongoing budget pressures associated with the growing service demands of the state's Medicaid program. Standard & Poor's will continue to monitor the state's ability to maintain its favorable financial position while meeting its growing health services obligations. The state's long-term economic outlook remains moderately positive for job growth and output.

Table 1

Vermont's Rating History			
Date	**Rating Action**	**Rating**	**Outlook/Watch**
Sept. 11, 2000	Upgrade	AA+	Stable
Oct. 14, 1998	Upgrade	AA	Stable
June 10, 1991	Outlook Assigned	AA-	Stable
April 25, 1986	Upgrade	AA	
Oct. 16, 1973	Withdrawn	NR	
Feb. 28, 1973	Upgrade	AA	
March 23, 1971	Withdrawn	NR	
Oct. 2, 1963	Initial Rating	AAA	

Economy: Stable Yet Growing Modestly

Manufacturing and service sector industries -- like tourism, education and health services -- and professional and business services drive Vermont's relatively small, but stable, economy. Vermont's population is an estimated 624,000. The economy is focused on Burlington, Vt., with a population of 39,000; Burlington is the state's only MSA. Although somewhat limited compared with other states on a gross state product per capita basis, Vermont's economy has maintained stable employment levels over the long term; improving wealth ratios; and strong real estate development, which are all credit strengths (see table 2). The economy exhibited resiliency during the recent recession with relatively small job losses and state tax revenue reductions. Although employment levels contracted some in 2002 and 2003 due, in large part, to losses experienced in the manufacturing sector, unemployment levels remained well below the nation's rate. During this recessionary period, the state's unemployment rate tracked about 1.7% below the nation's rate, which reflected the employment base's resiliency and low volatility. State employment levels recovered and began expanding in late 2004; this expansion carried over into 2005 and 2006. As of December 2006, the state's unemployment rate was 3.8% -- the 14th lowest nationally. Unemployment has been lower than the national rate since June 1991. Vermont's long-term economic diversification played a central role in weathering the recent national recession, which resulted in less unemployment and revenue dislocation than most states. The state's leading private employers are Fletcher Allen Health Care (6,300 employees), which is based in Burlington, and IBM Corp. (6,200). Vermont's output, measured in real gross state product, grew slightly faster than the nation's output in

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

2005: 2.7% compared with 3.6%, respectively. According to Global Insight, the state experienced 1.5% job growth in 2005, driven, in part, by strong construction activity and growth in the health care industry (see chart 1). Wealth and income indicators, while improving, are still slightly below the national average. According to the Bureau of Economic Analysis, personal income reached $33,327 per capita in 2005, a 4.9% increase over 2004, or roughly 96% of the national average.

The manufacturing and service sectors form the state's economic base. Health care, in particular, is an ever-growing part of the economy. The recession did not have an effect on employment in this sector. In 2005, the health care industry accounted for 12.3% of the state's total employment, a higher proportion than the nation's 11% average. Burlington-based Fletcher Allen Health Care is the state's leading health care provider; Fletcher Allen also partners with University of Vermont to provide the state's only teaching hospital. With its capital expansion, Fletcher has added to its employment levels since 2001 and has recently undertaken a $364 million expansion for a new ambulatory care center. Given the state's older population, state officials expect the demand for health services to grow over the long term. Federal reductions to Medicaid and Medicare service-provider reimbursements, however, could constrain job growth over the short term.

Like health care, manufacturing accounts for a larger share of Vermont's economy than the nation's economy. Making up 9.5% of total employment in 2005 compared with the nation's 8.5%, manufacturing remains a key component to Vermont's job and income growth. Within manufacturing, strong concentration exists in high-tech manufacturing due to IBM's presence. An estimated 80% of all state exports are high-tech manufactured goods, mostly produced at IBM's Essex Junction, Vt. facility. Although its wage, employment levels, and output contributions to the economy are positive, changes at IBM could have a large multiplier effect across the state. Layoffs of about 2,500 at the plant from 2001-2003 had a direct effect on statewide employment figures for some time. Although employment at IBM has modestly increased its workforce and the company has secured long-term contracts for its image sensors with private industry and the military, its ability to have a real effect on statewide economic indicators belies some potential weakness to Vermont's economy.

Tourism related to the fall foliage and winter ski seasons also plays an important role in Vermont's economy. Tourism-related revenues from sales, meals, gasoline, and lodging taxes provide significant revenue streams to the state's operating budget. Over the past two years, real estate and construction have been strong near, and around, the state's major resort areas, where second-home sales and construction activity dominate the regional housing market. Areas like Killington, Vt. are increasingly being marketed as locations for summer recreational activities in addition to traditional ski resorts, lengthening the tourist season. In addition to Killington, nearly all of the state's resort areas have multiyear facility expansions and upgrades underway, including Okemo, Vt.; Stowe, Vt.; and Stratton, Vt. This has led to strong property tax base growth and real estate valuations. Full market value of the property tax base for the statewide property tax reached $64 billion in fiscal 2005, an increase of 46% over five years. Construction activity also contributed to the state's labor market recovery and expansion. An estimated 46% of the total net new payroll added since late 2004 can be attributed to the construction industry. Through November 2006, Vermont was second in New England and 20th nationally in year-over-year job growth in construction. Colorado is Vermont's chief competitor for the desirable ski tourism revenue. Vermont's weak 2005-2006 ski season led to lower leisure and hospitality job growth, and tourism activity could be off again for the 2006-2007 season due to a warm and wet first half of the winter period.

The economy's outlook is, in general, positive. Employment and payroll growth are expected to continue at a modest pace through 2010; actual levels, however, could lag the national average. Vermont's employment growth through the next five years will be on par with growth in 2006, averaging 0.8% annually; but it will be lower than 2005's 1.5% year-over-year job growth. State officials have pointed to the captive insurance market, a segment of the professional and business services industry, as a potential source of long-term job growth. Vermont's captive insurance industry generates an estimated $20 million in annual tax revenues and contributes more than 1,400 direct and indirect jobs to the employment base. According to economic forecasts, the state's output is forecast to grow by about 3% annually through 2010, reflecting a slightly lower growth trend than what was experienced from 1999 through 2005. In terms of personal income, continued employment expansion will lead to a 4.1% year-over-year increase in personal income in 2006 and 4.9% year-over-year growth for the next five years. The professional and business services and education and health care sectors are expected to drive growth.

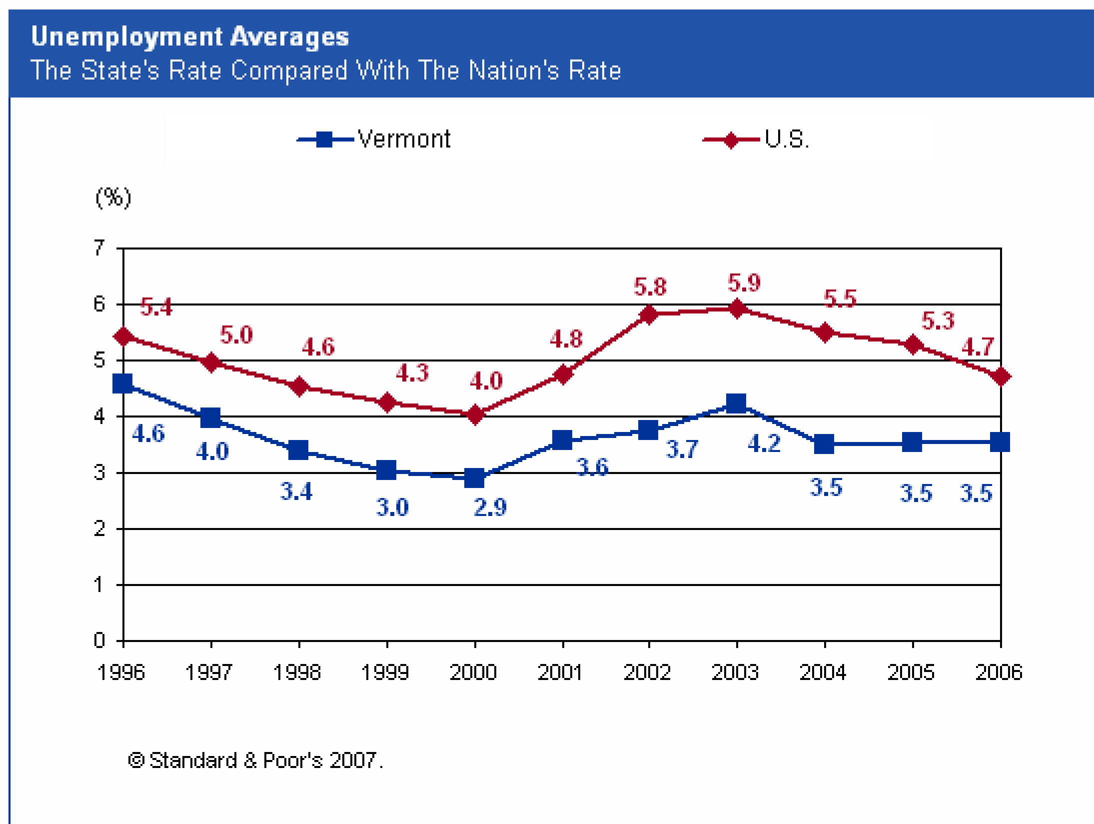
Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

Table 2

Vermont Economic Data							
(000s)	**2002**	**2003**	**2004**	**2005**	**2006p**	**2007p**	**2008p**
Real gross state product (bil $)	18.91	19.61	20.48	21.04	21.61	22.01	22.67
Employment	333.68	335.81	339.87	343.52	350.91	354.43	357.27
Unemployment rate (%)	4.01	4.46	3.70	3.48	3.49	4.02	4.02
Personal income (bil $)	18.05	18.75	19.56	20.39	21.28	22.27	23.43
Personal income growth (%)	1.74	3.87	4.34	4.24	4.36	4.62	5.23
Population	616.47	618.88	620.96	622.57	624.20	626.43	628.87
Net migration	0.37	0.20	0.07	(0.01)	0.08	0.25	0.32
Housing starts, private single-family	2.16	2.51	2.81	2.09	1.76	1.31	1.31
Housing starts, private multifamily	0.53	0.24	0.56	0.31	0.26	0.26	0.28
New vehicle registrations	39.55	41.96	43.12	38.73	38.17	38.15	38.44

Source: Global Insight. p--Projected.

Chart 1



Population Demographics

Vermont's population continues to grow at a pace that is consistent with the New England region but still lags the national average. The state's population is older, on average, and more educated compared with the national average. The state is currently seventh in the nation for the percent of its population with a college degree, which contributes to the workforce's skill level. Data from the 2000 U.S. Census indicates Vermont's population remains primarily rural. About 62% of the entire population lived outside Burlington,

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

the state's single metropolitan area, which is tops among the 50 states and about double the national average.

The state's constituency is also the nation's second oldest population, only behind neighboring Maine. The average age of Vermont's residents -- 33 years in 1980, 35 in 1990, and 38 in 2000 -- has been increasing faster than the national average. As of 2005, the average age exceeded more than 40 years, or 4.3 years older than the national median of 36.4 years, which reflects a widening gap. According to Global Insight, the state's aging population presents long-term economic concerns. Although higher average ages are good for home ownership, which was 71% in 2000 compared with 66% for the nation, it indicates that more people are leaving the state to find work elsewhere. As residents age, more of their income will come from transfer payments rather than economic development while, at the same time, placing heavier demand on government-funded social and health care services.

State income levels have improved but remain slightly below the national average. Median household effective buying income was 92% of the national average. As reported by the U.S. Department of Commerce, per capita personal income indicates Vermont's wealth has been growing by a slightly slower pace than national levels over the past five years. Personal income reached $33,327 per capita in 2005, or a 4.9% increase over 2004 levels, which was about 96.0% of the national average.

Finances

Vermont's financial position remains positive with sufficient reserves due to its conservative debt and budgeting practices and strong financial management (see table 3). Vermont adopted consensus revenue estimating in the mid-1990s to improve its current- and subsequent-year budgeting. Semiannual estimates reflect a consensus forecast for the nation's and state's economies; the major individual revenue components of each fund; and an overall forecast of receipts for the general and transportation funds, as well as receipts other than property taxes in the education fund. Around the same time, the state adopted stabilization fund policies to reduce the effect of annual revenue variations on the state's finances. In 1993, the state created separate budget stabilization reserves within the general and transportation funds. The amount in each of these reserves is not to exceed 5% of previous-year appropriations. Officials created an education fund budget stabilization reserve in fiscal 1999 with provisions for slightly lower reserves at 3.5%-5.0% of expenditures.

The consensus revenue forecasting and reserve policies have been effective tools in managing the state's financial position over the past decade. Reserves remained adequate during the recent economic recession; and recent operating results have been strong, allowing fund balance levels to grow. Unlike many other states, Vermont never fully depleted its reserves during the 2001-2002 recession. A 6% decrease in general fund revenues led to the appropriation of roughly half the amount of reserves available to close operating deficits in fiscals 2002 and 2003. By fiscal 2004, however, as revenues for personal income, corporate income, and sales and use tax rebounded, the state fully replenished its reserves to statutory levels.

Following a surplus in fiscal 2005, the state closed fiscal 2006 with a $36 million operating surplus. General fund revenues were 7.4% higher than fiscal 2006 levels and 3.9% higher than forecast amounts. The budgetary surplus was reduced by transfers into reserves and for onetime appropriations like pay-as-you-go capital. Roughly $24 million was used in the so-called year-end windfall, including funds for one of the state's pension systems. Roughly $10 million was transferred into the transportation fund for road repair projects because revenues were below budgeted levels. Including the carry-forward amounts from fiscal 2006, the state used excess funds for fiscal 2007 appropriations, including appropriations for the budget stabilization funds. The state transferred roughly $6 million of the operating surplus into the general fund budget stabilization reserve, fully funding it to its statutory maximum of 5% of previous-year appropriations. An additional $16 million is available in the general fund surplus reserve for management to appropriate in fiscal 2007. Total general fund reserves for transportation; human service caseload reserves; and budget stabilization reserves, coupled with an education budget stabilization fund, reached nearly $117 million for fiscal 2007, more than double fiscal 2002 reserves. Additional revenue flexibility is available due to the $68.3 million unreserved, undesignated fund balance, which is equal to 6.1% of general fund revenues.

Fiscal 2006, which ended on June 30, was Vermont's fifth year of GASB 34 implementation. Vermont's

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

negative $85.7 million of unrestricted net assets is due mainly to debt issued by the state for the capital purposes of its municipal, nonprofit, or component units and the statutorily mandated restricting of net assets for budget stabilization reserves. Although the state recognizes the liability, it does not record a corresponding asset. Since this debt is already captured in debt ratios, it does not have any additional effect on the state's credit quality. The state's ending governmental activities net assets were a positive $1.2 billion.

Revenues

Vermont's tax structure is broad, and its revenue sources are diverse across several operating funds. The general fund relies on unrestricted revenues from personal and corporate income, sales and use, and meal taxes. The personal income tax generated $546 million of revenues in fiscal 2006, which accounted for about 49% of total general fund revenues. The sales tax accounted for about 19%. Following essentially zero growth in collections in 2001 and 2002, officials increased the sales tax to 6% from 5% in October 2003. The education fund relies on earmarked sources, such as statewide property and sales and use taxes, as well as state lottery profits. The statewide property tax accounted for a significant 85% of total education fund revenues. The transportation fund relies on revenues from the motor fuels tax, motor vehicle license fees, and federal-match grants. Vermont officials estimate they will receive roughly $60 million of federal transportation match grants annually over the next five years.

Expenditures

On the expenditure side, education and Medicaid appropriations continue to account for a larger share of additional tax dollars. Total education expenditures were roughly $1.53 billion, including general fund transfers, in fiscal 2006 due mainly to an increase in state aid to local school districts related to Act 68 of 2003, which eliminated local share property taxes and replaced them with state-imposed tax rates. Expenditures for human services, such as Medicaid, also continue to grow and account for a larger share of total state appropriations.

State appropriations for Medicaid have grown by an average of about 10% annually since fiscal 1999. Vermont's Medicaid population and benefits are more generous than in other states. The program pays some or all of the health care costs of roughly 25% of the state's population; by contrast, about 20% of Massachusetts residents receive some Medicaid assistance. The state has expanded coverage beyond traditional Medicaid-eligible populations to cover children and working-class families. About half of current Medicaid beneficiaries are mandatory with one-quarter being optional and one-quarter classified as expansion. The federal government (60%) and state (40%) share expenditures. Due to the program's rising costs, triggered by enrollment and service expansions, as well as medical inflation, the state has struggled to meet its share of total costs.

To address significant projected out-year funding deficits, state officials petitioned for, and were granted, a Medicaid Section 1115 waiver from the federal government, which provides an additional premium of federal revenues and a five-year cap on total Medicaid expenditures in return for more operating flexibility. Fiscal 2007 represents the first year of Vermont's Medicaid demonstration program, known as "global commitment." Although additional premiums from the waiver program and carryover balances are expected to cover fiscal 2008 Medicaid costs, the administration is forecasting an $8.3 million funding deficit in fiscal 2008, a $40.0 million funding deficit in fiscal 2009, and an $84.0 million funding deficit in fiscal 2010.

Table 3

Vermont Financial Data

	--Fiscal year-end June 30--						
(Mil $)	**2006**	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**
General Fund—GAAP							
General fund revenues	1,123	1,049	968	822	876	905	886
General fund expenditures	637	673	561	588	628	547	549
Net transfers & other adjustments	(488)	(387)	(352)	(284)	(271)	(354)	(305)
Net general fund operating surplus (deficit)	(2)	9	55	(49)	(23)	4	32

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

Table 3

Vermont Financial Data (cont.)							
Total general fund balance¶	161	164	155	100	150	173	169
Unreserved general fund balance	68	69	62	47	98	87	55
Rainy day operating reserve funds	52	46	45	24	8	43	41
Combined unreserved general fund + reserve fund balance/general fund expenditures (%)	18.8	17.1	19.1	12.1	16.9	23.8	17.5
Net surplus (deficit)/general fund expenditures (%)	(0.3)	1.3	9.8	(8.3)	(3.7)	0.7	5.8
Total Government Funds							
Revenues	3,798	3,583	3,296	2,913	2,805	2,635	2,567
Expenses	3,817	3,674	3,213	3,055	2,895	2,567	2,505
Total governmental fund balances	429	381	399	251	340	325	323
Total governmental unreserved fund balances	256	201	244	152	234	204	173
Unreserved fund balances as % of total governmental revenues	6.7	5.6	7.4	5.2	8.3	7.7	6.7
Debt							
Direct GO debt	506	463	469	474	486	480	503
Appropriation debt	0	0	0	0	0	0	0
Operating lease (noncancelable)	31	29	26	18	0	0	0
Other contingent debt (Vermont Bond Bank, Vermont Economic Development Authority, and Vermont Housing Finance Agency)	642	652	606	553	522	492	458
Other contingent debt (less: reserves)	(652)	(652)	(606)	(553)	(522)	(492)	(458)
All tax-supported state debt (net)	506	463	469	474	460	454	503
Per capita GO state debt ($)	811	742	755	727	745	741	835
All tax-supported debt to personal income (%)	2.4	2.2	2.4	2.5	1.9	2.6	3.0
Debt service/general fund expenditures (%)	11.8	11.8	11.8	11.5	9.8	12.3	12.9

Basis of Accounting: Accrual for fiscals 2002-2006. Modified accrual for fiscals 2000-2001.

Medicaid Reform: Global Commitment

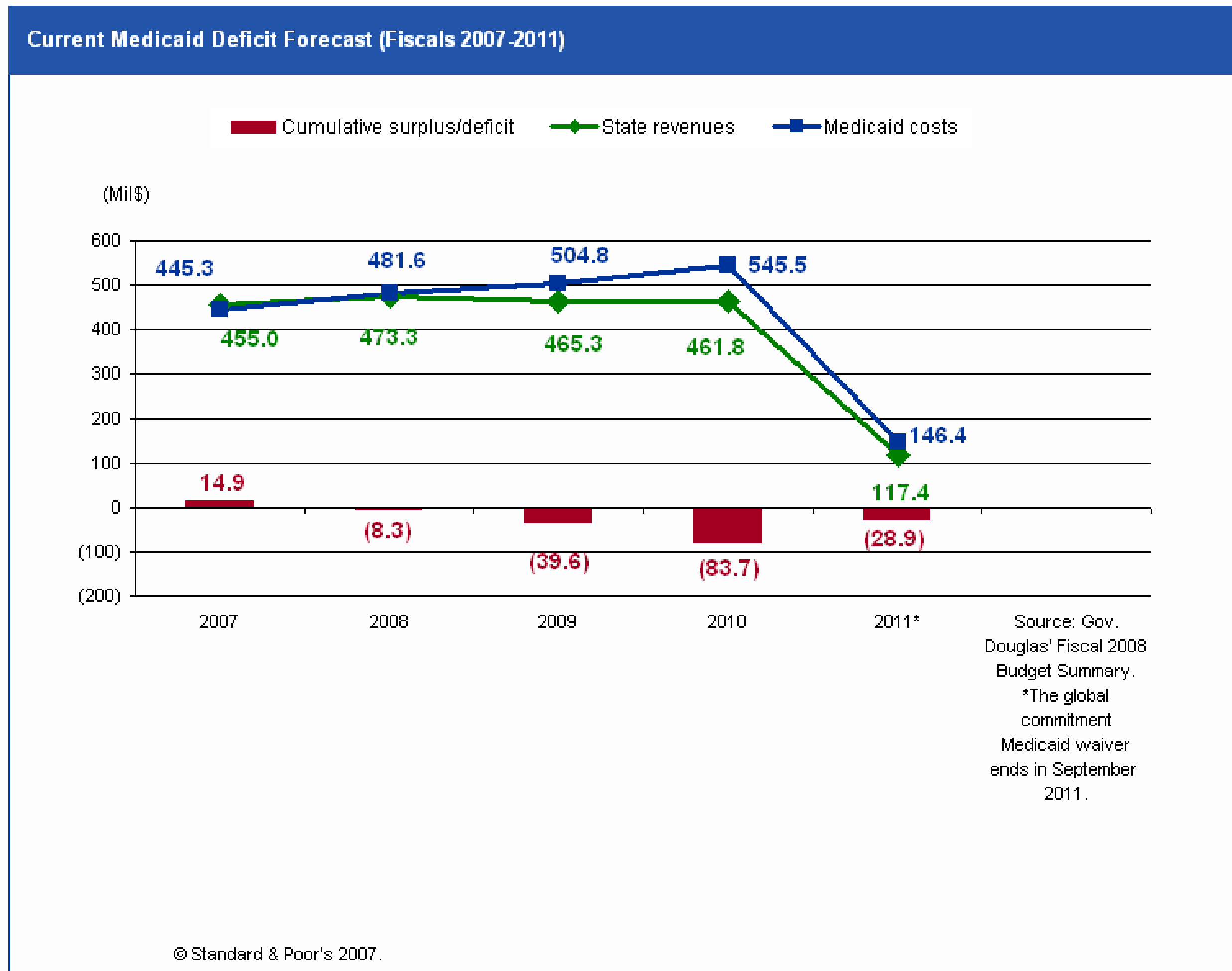
In October 2005, Vermont entered into the Global Commitment to Health Section 1115 Medicaid waiver program. The waiver gives the state greater flexibility to administer and coordinate programs, using a state-run managed-care model to manage all Medicaid programs. The state will be at-risk to manage costs within a capped amount and will benefit from any achieved savings. The waiver caps overall state and federal Medicaid spending at $4.7 billion over the next five years, which management estimates will exceed projected actual costs of $4.2 billion. In return for the cap, the federal government will provide an additional premium to the state for Medicaid costs; using fiscal 2004 appropriations as the base year, the premium will increase revenues by 9% annually. To manage program costs better, state officials will convert the Medicaid agency into a public managed-care organization. The additional premiums allow the state to cover more residents with less state funding; officials estimate the state will save roughly $300 million over the five-year waiver period. Vermont, however, still needs additional state revenues to meet growing program costs. Cumulative revenue deficits to meet the state's share of program costs should reach $38 million in fiscal 2009 and $122 million in fiscal 2010, the last full year of the waiver period. In addition, some program risks remain. Although it is unlikely, should costs exceed the $4.7 billion cap over the next five years, the state will be at-risk to cover the full share of expenses (see chart 2).

Catamount Health, which begins in October 2007, is Vermont's new public health insurance program for the low-income and uninsured. The program provides access to subsidized or low-cost comprehensive insurance at no cost to patients for preventative care or recommended services. State officials expect new revenues to cover the program's costs. They expect state funding to come from Medicaid waiver financing, two increases in tobacco taxes, and an assessment on employers for employees who were not

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

offered insurance or those that were offered but chose not to enroll. The cigarette tax increased by 60 cents per pack on July 1, 2006, to $1.79; it is then scheduled to increase by an additional 20 cents to $1.99 per pack as of July 1, 2009. Vermont officials will seek a waiver from the federal government under the global commitment program to include Catamount Health in the state's existing Medicaid waiver. If granted, the federal government could pay about 60% of some of the new program's costs.

Chart 2



Financial Management Assessment: 'Strong'

Vermont's management practices are considered strong under Standard & Poor's FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Much of Vermont's debt and financial management practices are embedded in state statute. These, along with internally developed policies, guide the state's long-term budget and capital planning, debt management, and investing practices.

The state has a well-established consensus revenue-estimating process. According to statute, the joint fiscal office and administration provide their respective revenue estimates for the general, transportation, and federal funds for the current and next succeeding fiscal year to the Vermont Emergency Board. Revenues are monitored and results are published monthly; and the emergency board meets at least twice annually, in July and January, to evaluate the revenue forecast and make adjustments, if necessary. The emergency board includes the governor and the legislative chairs of the house and senate appropriating committees. The forecasting process includes traditional economic and revenue forecasting, which is performed with the assistance of outside economists, for the current and next

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

succeeding fiscal year, as well as a less detailed forecast for the next eight years. Medicaid revenues and spending are also forecast. The governor has statutory authorization to adjust the budget within certain revenue and expenditure change limits when the Vermont Legislature is not in session. Vermont maintains stabilization reserve funds at statutory levels to reduce their effect on annual revenue variations. In 1993, the state created separate budget stabilization reserves within the general and transportation funds. The amount in each of these reserves is not to exceed 5% of previous-year appropriations. An education fund budget stabilization reserve was created in fiscal 1999 with provisions for slightly lower reserves at 3.5%-5.0% of expenditures. Vermont statute requires annual funding of such reserves.

Vermont law also requires a long-term capital plan. The governor submits a capital budget annually to the General Assembly based on debt management provisions outlined by the state's Capital Debt Affordability Advisory Committee. The committee's estimate is nonbinding, but the state legislature has never authorized new long-term GO debt in excess of the committee's estimated amount. The state has formal debt management policies, including a statutory debt affordability analysis that is developed by the Capital Debt Affordability Advisory Committee and is integrated into the operating budget development process and updated at least annually. The state has not entered into any interest rate swaps and does not have an adopted swap management policy. Statutory restrictions and adopted administrative policies govern investment management, and the office of the state treasurer monitors compliance.

The Fiscal 2008 Budget

After his reelection to a third term in November 2006, Gov. Jim Douglas released his fifth budget proposal in January 2007. In the budget, the governor recommends roughly $4.7 billion of total appropriations, reflecting a 2.8% increase over fiscal 2006 appropriations. Two large components of that increase are education funding and human services programs, such as Medicaid and transitioning youth programs. General fund spending accounts for a 3.16% increase while education and federal funding account for much of the remainder. The fiscal 2008 budget also maintains reserves at their statutory requirements.

The governor's budget also proposed caps on the state's general fund spending, as well as local education spending. At the state level, the governor's plan would create a statutory limit on general fund spending to the rate of inflation plus population growth. For fiscal 2008, this would limit general fund spending to an estimated 3.90% compared with the proposed 3.16%. Gov. Douglas has proposed ending the year-end practice of earmarking surplus funds, referred to as the waterfall. Instead, the governor has recommended establishing a capital reserve to begin building the necessary funds to construct a new state hospital, with an estimated cost of $80 million-$100 million. At the local level, the governor has proposed a five-year limit on education spending to provide a measure of property tax relief. The local spending limit would be subject to override by a 60% vote of the local electorate. Additional proposals include the creation of the Vermont Telecommunications Authority with an initial bonding capacity of $40 million to pay for advanced communications authority.

In January 2007, the Vermont Emergency Board raised its revenue projections for fiscals 2007 and 2008, over its previous forecast made six months earlier. The latest forecast increases projected general fund revenues in fiscal 2007 by $1.4 million to $1.124 billion from $1.122 billion, indicating overall receipts are stable through the first half of the year. Monthly tax revenues were off as of December 2006, according to the latest report of state revenue collections. General fund revenues were 3% below the consensus forecast for the month, but that fund is cumulatively above targeted levels for the fiscal year. Transportation fund receipts were 4.7% below forecast levels for the month and 1.3% below forecast figures for the year.

Debt Burden Is Low; Amortization Is Rapid

Vermont's debt profile is favorable with a low debt burden and rapid amortization schedule. Nearly all of the state's debt outstanding is GO debt. The state does not have any variable-rate debt outstanding nor does it use swaps or other derivative products.

Debt management, which the state treasurer handles, remains an important piece of the state's overall financial management and planning. The annual recommendation for debt issuance made by the Capital Debt Affordability Advisory Committee is based on 10-year forecasts of the effect the additional debt will

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

have on the state's key debt ratios. In fiscal 2006, the committee increased its recommendation for the state's annual GO debt issuance to $49 million for fiscal 2008, a 9% increase over the fiscal 2007 amount. Even with the increase, Vermont will initially continue to retire more debt than it issues annually. At fiscal year-end 2006, debt ratios were a manageable $811 per capita and 2.4% of personal income, including the $45 million the state will issue in fiscal 2007. Vermont's conservative debt practices compare well to national practices (please see the report titled "Public Finance Report Card: U.S. States Debt" published on May 15, 2006, on RatingsDirect). Vermont ranks 41st when its total tax-supported debt is compared with its peers. The state was in the middle of the peer group, 21st and 24th, when comparing debt per capita and debt-to-personal income, respectively.

Pensions/Other Postemployment Benefits

Vermont maintains three statutory pension plans but appropriates funding for pension costs for only two: the $1.69 billion Vermont Teachers' Retirement System and the $1.23 billion Vermont State Employees' Retirement System. (The Vermont Municipal Employees' Retirement System is another pension fund, but municipal and employee contributions support all payments to that fund.) The state's combined unfunded liability increased after the funding method was changed to entry age normal effective with the 2006 actuarial valuation from entry age normal with frozen initial liability. The teachers' system funding status declined to 84.6% through June 30, 2006, while its unfunded liability increased to $259 million. The state employees' system funding was 99.3% fully funded with just a $9 million unfunded liability. Over the past year, Vermont has adopted a unified investment process that the state's pension investment committee recommended, which has led to an increase in the actuarial assumed rate of return to 8.25% from 8.00%, reflecting the expected benefits of the unified investment process.

With the change in the actuarial valuation method, the teachers' system's unfunded liability was reamortized over a 30-year period, beginning in fiscal 2007. This resulted in an annual required contribution for the teachers' system of $38.2 million. The state legislature fully funded the annual required contribution in 2007 by increasing the base appropriation an additional $5.0 million to roughly $29.4 million and by using onetime general fund revenues of $7.8 million. According to legislation, base budget appropriations by fiscal 2010 will fund the annual required contribution for the teachers' system.

The state's nonpension other postemployment benefit liability for both the state employees' and teachers' systems has also been recently valued. Like most states, Vermont currently funds such benefits with pay-as-you-go financing rather than prefunding these benefits in the same manner as traditional pension benefits. Assuming no prefunding, the employees' system's other postemployment benefit liability was $552 million as of June 30, 2006. To amortize that fully over a 30-year period would require state officials to make a $40.9 million annual required contribution in fiscal 2007, which is significantly higher than the current $15.0 million contribution. The liability for the teachers' system's other postemployment benefit costs are higher: Assuming no prefunding, the accrued other postemployment benefit liability was $952.5 million; this would require a $76.0 million annual contribution in fiscal 2007, more than five times the system's current other postemployment benefit expenditure. Vermont officials have yet to make a decision on when or how they will fund the full annual required contribution; but management has already taken several steps, including the establishment of an irrevocable trust in which the state treasurer will manage other postemployment benefit specific assets.

Standard & Poor's. All rights reserved. No reprint or dissemination without S&Ps permission. See Terms of Use/Disclaimer on the last page.

Copyright © 2007, Standard & Poors, a division of The McGraw-Hill Companies, Inc. (S&P). S&P and/or its third party licensors have exclusive proprietary rights in the data or information provided herein. This data/information may only be used internally for business purposes and shall not be used for any unlawful or unauthorized purposes. Dissemination, distribution or reproduction of this data/information in any form is strictly prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P, its affiliates or its third party licensors, S&P, its affiliates and its third party licensors do not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P, its affiliates and its third party licensors be liable for any direct, indirect, special or consequential damages in connection with subscribers or others use of the data/information contained herein. Access to the data or information contained herein is subject to termination in the event any agreement with a third-party of information or software is terminated.

Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

Any Passwords/user IDs issued by S&P to users are single user-dedicated and may ONLY be used by the individual to whom they have been assigned. No sharing of passwords/user IDs and no simultaneous access via the same password/user ID is permitted. To reprint, translate, or use the data or information other than as provided herein, contact Client Services, 55 Water Street, New York, NY 10041; (1)212.438.9823 or by e-mail to: research_request@standardandpoors.com.

Copyright © 1994-2007 Standard & Poors, a division of The McGraw-Hill Companies.
All Rights Reserved.

The McGraw·Hill Companies

NEW ENGLAND ECONOMIC PARTNERSHIP
(NEEP)

Vermont Economic Outlook

May 2007

VERMONT ECONOMIC OUTLOOK

Summary Observations

- The May 2007 NEEP forecast expects that growth in the Vermont economy will slow in 2007 followed by healthier rates of growth throughout the remainder of the forecast period. Among the major macro-variables:

  - Job growth will remain sluggish throughout the forecast period with an improving tone to the rate of job growth in the later years of the forecast period.

  - Output growth (GSP), with the exception of the initial calendar year of the forecast in 2007, is expected to grow at a slightly higher pace than New England as a whole.

  - The unemployment rate, despite the relatively slow employment growth environment, will continue to remain among the lowest in the New England region—if not among states in the entire county.

- The housing market correction in Vermont remains as the most significant unknown and the largest source of downside forecast risk—given the current shakeout in subprime lending and the higher than average contribution that home construction (particularly second home construction) made to Vermont's recent job and economic growth.

  - Although the forecast shows that housing prices are expected beginning later this calendar year through the middle of calendar 2008, these declines are not expected to be of the magnitude or persist for the length of time necessary to derail the current economic upturn either nationally or in the state.

  - Vermont had the lowest rate of foreclosures in the United States in 2006, and the state was below the national average in change in percentage of sub-prime delinquencies between 2005 and 2007.

  - However, it is unmistakable that the housing market correction has and will continue to be a drag on the pace of the state's economic forward progress over at least the next 6 quarters—especially with respect to the heretofore robust level of second home construction around the state's major resort areas which has slowed to a crawl during the current construction season.

- On the upside, the fundamentals of the U.S. economy and the Vermont economy overall remain sound, and the global economy is experiencing strong, broad based growth.

  - This is creating healthy demand for American goods and services (including Vermont goods and services, and this is helping to off-set the drags from the housing market correction).

  - The week dollar is reinforcing the demand created by a healthy global economy, and is being particularly helpful to northern Vermont where Canadian activity is boosting activity.

- The other major factor of significance in this outlook revision concerns the resumption of the upward creep in energy prices, just as the summer driving season is about to begin.

    - Continued conflict in the Middle East continues to create a hefty risk premium in the price of oil.

    - Vermont's tourism economy remains highly sensitive to high and rising fuel prices as vehicular ground transportation remains as one of the principal sources for the way out-of-state visitors find their way to the state.

    - Money spent by visitors on higher gasoline prices siphons dollars away from those that otherwise might be spent on entertainment-recreational activities and on other goods and services that drives Vermont's tourism sector.

    - More dollars spent by resident households likewise pinches household budgets and diverts spend-able income away from products and services that move the Vermont economy forward—to the detriment of output, job and income growth.

- Looking more closely at the state macro-variables, growth overall in the Vermont economy is expected to remain positive but restrained.

    - Payroll job growth is expected to remain between 0.5% and 1.0% throughout the forecast period,

    - While personal income is expected to grow at relatively healthy rates of between 2.3% and just under 3.5% over the forecast period.

    - Not surprisingly, labor force growth will remain very slow, nudging about the ½% level towards the end of the forecast period.

    - Manufacturing employment is expected to remain slightly positive for the next two years for the first time in the last 6 years, but will be offset by declining construction employment over the same period.

    - Output growth is expected to have its second weak year in a row in calendar 2007, followed by rates of growth ranging between of 2.5% and 3.0% over the rest of the forecast period.

- Every one of Vermont's 12 major NAICS sectors is expected to see positive growth over the forecast time horizon with the exception of the Government sector.

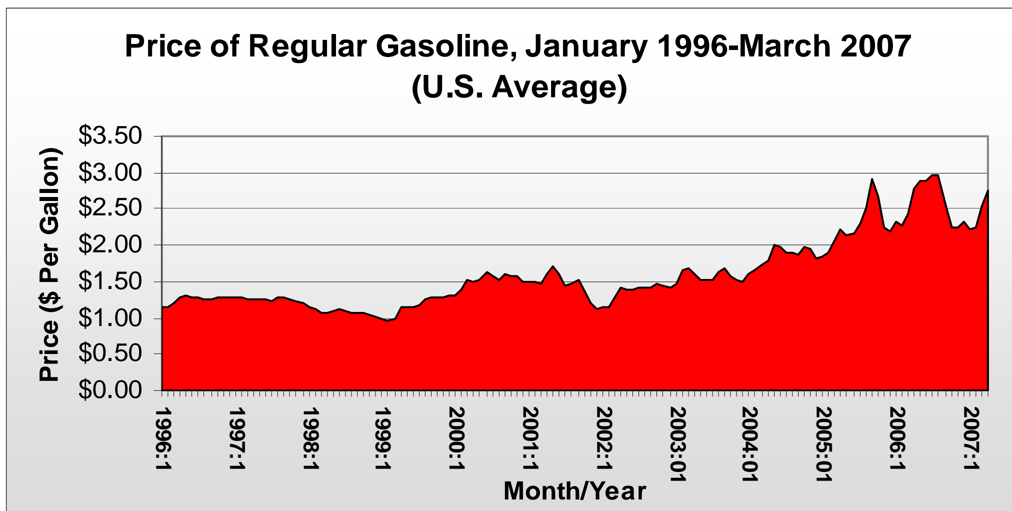
    - The sectors showing the strongest potential for growth are the Professional & Business Services and Leisure and Hospitality sectors at average rates of growth over the forecast period of 1.9% and 2.0%, respectively.

    - The weakest sectors will be the Government sector which is expected to post an average annual rate of payroll job change of -0.2%.

Overview of the U.S. Economy's Recent Performance and the Near-Term Outlook

The U.S. economy as of the beginning of calendar year 2007 continues to grow at a comparably healthy rate from a business cycle perspective—albeit somewhat below potential. For the 4th calendar quarter of 2007, inflation-adjusted GDP growth posted a 2.5% rate, a slight rebound from the 2.0% rate of growth experienced during the third quarter of 2006. Overall for calendar year 2006, the U.S. economy finished with a respectable 3.3% GDP growth rate—an artifact of conditions where: (1) the economy's fundamentals remain strong (e.g. corporate balance sheets remain about as pristine as could be expected at this point in the economic cycle), (2) labor markets continued to post decent job although less than spectacular job growth, (3) there have been no major shocks of significance in recent times, and (4) the housing market began its "correction" without dragging the overall economy down with it (at least as of this point in the correction process). However, there were drags on the U.S. economy during calendar year 2006 and into the beginning of 2007, including: (1) an unwelcome run-up in inventories during the second half of the calendar year, (2) increased volatility in U.S. equity markets—especially during the first quarter of calendar year 2007, (3) a significant decline in mortgage equity withdrawals, and (4) energy prices—which once again began to rise as the moved into early 2007—after peaking in mid-July of 2006. While these drags in fact exerted significant restraining effects on the pace of economic growth during the past calendar year, they did not result in the type of serious detrimental effects that could serve to derail the current 5½ year expansion.

Over the near-term, there is some concern that the less than smooth operations at the nation's already stretched-thin oil refineries (including a recent clustering of fires and operational problems with seasonal changeovers) and the beginning of the Summer driving season could serve to intensify the recent upward pressure on energy prices. At this point, energy prices do not have too far to go to establish yet another price record—to the detriment of energy sensitive sectors of the economy, the budgets of households in rural, higher than average energy consuming parts of the country, and states with larger than average visitor sectors—especially those states where gasoline prices impact the level of visitor activity. Coming at the same time as the still unfolding housing market correction, these two factors represent perhaps the most significant of the near-term risks to the current U.S. economic expansion.



Is West Texas Intermediate Crude Still the Correct Crude Oil Benchmark?: The above-referenced refinery issues have not only decreased the supply of gasoline on the market (and

therefore driving up prices), but they have also shaken the status of the West Texas Intermediate Crude as the crude oil price benchmark. Most of the world's oil is priced based on the WTIC price as traded at the NYMEX. The physical delivery point for West Texas Intermediate Crude oil is Cushing, Oklahoma. A fire at a Valero Energy Corporation refinery in Louisiana has reversed the flow of crude back to Cushing where it must be stored since it can not be refined. This, coupled with increased pipeline supply of Canadian oil, has distorted the price of oil at Cushing with respect to other types of crude, is currently calling into question the validity of the West Texas Intermediate Crude benchmark price as being a true benchmark price. This is perhaps best illustrated by the recent drop in WTIC prices due to a supply glut in Oklahoma. This occurred at the same time that other benchmark oil prices (e.g. Brent Crude and other crudes) experienced increases in price. The situation with the erosion in the quality of the West Texas Intermediate crude oil benchmark could make it more difficult for economists and the Fed to accurately monitor oil prices and to create credible forecasts using that oil price benchmark as a forecasting variable. This comes at an inopportune time as forecasters and monetary policy wonks speculate about the future path of inflation and how the Federal Reserve might act on the monetary policy front. At this point, inflation still appears to be running in the upper part of the range widely viewed as the Fed's "comfort zone."

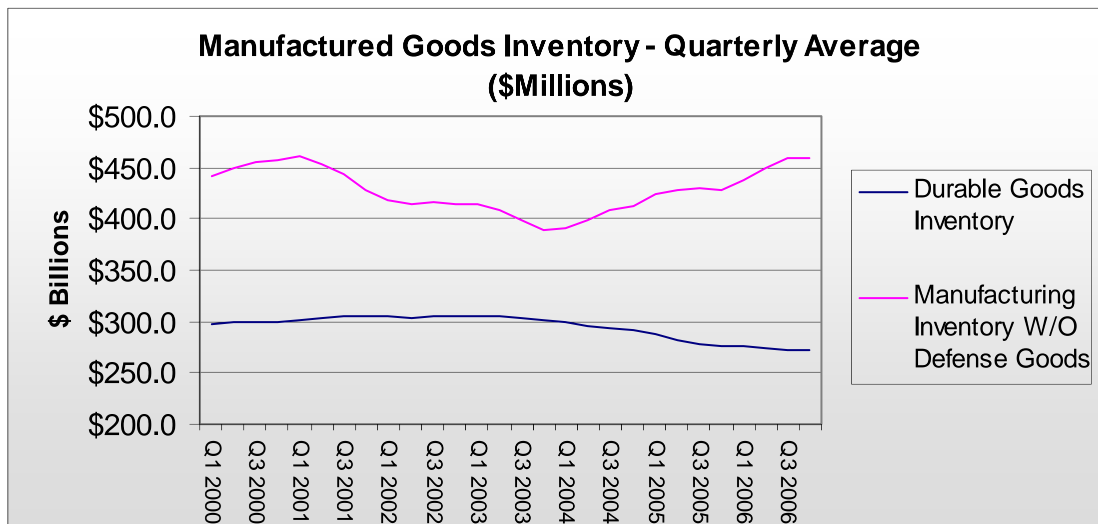
As energy prices once again creep up, the question of how far they can go without creating a more perceptible drag on the economy will move to the forefront. Gasoline prices, on a national average basis, are creeping northward of the $3.00 a gallon mark even before the traditional summer driving season begins. With crude oil prices remaining above $60 per barrel level, little relief in the upward pressure on energy prices seems likely in the near-term future to the detriment of the impact on business costs, household income (especially for moderate- and low-income households), and visitor activity—for those areas dependant on motor vehicles as a primary means for bringing visitors into a state economy.

In short, the current macro situation represents a dichotomy of pluses and minuses. On one side, fuel prices have been on the rise but much of the volatility of the past few years is not present. On the upshot, most of the world's economies are experiencing strong growth simultaneously for the first time in 40 years. This, coupled with a fall in the value of the U.S. dollar, has created strong growth for American good exports abroad. Also on the plus side are the still favorable conditions supporting corporate profitability and growth. Corporations have pristine balance sheets and strong profitability has recently been translating into new records for equity markets.

However, these conditions have not translated into strong payroll job growth during the first quarter of calendar 2007. The number of new jobs created in the first quarter of 2007 was down by 100,000 payroll jobs from the first quarter of 2006, and was roughly 30,000 payroll jobs off the pace of last year's quarterly average of about 180,000 jobs added per quarter. Recent readings indicate that month-to-month payroll job gains could slip beneath even that relatively restrained level over the next several months.

Despite the weak payroll job growth numbers, the unemployment rate[1] has remained in a tight bandwidth of 4.4% to 4.6% since September of 2006. It appears that although businesses are not hiring in large numbers, they do not appear to be laying off many employees either. The hiring slow down may be one of the signs of change in the heretofore favorable corporate profit environment after the astounding run they have had over the last several years. This caution is not necessarily a negative sign for the economy overall as corporations begin to adjust to the changing profitability climate. A more gradual adjustment would be preferable to an abrupt change where a significant number of corporations may have become overextended.

Industrial production remains healthy, despite a decline of 0.2% between March and February. Production increased on an annual basis coming in at 2.3% above its March 2006 level. Much of the March decline can be blamed on the warm weather during the month which drove down utility production. Utilization of industrial capacity also fell 0.2 percentage points in March although it remains above its historic average of 81.0%. Durable goods orders are also showing healthy gains, rising 3.4% in March. Of some concern are the rising inventories in non-defense manufactured goods and durable goods as a whole.



[1] As determined through the household survey.

It is noteworthy that the last time inventories of manufactured goods reached their current levels was the first quarter of 2001—just before the last recession. This economic variable is typically a leading indicator of economic slow down or recession. Another traditional leading indicator has been the comparison between the yields of long and short term Treasury securities. The inversion of this yield curve has become more pronounced over the past two quarters. Although no recession is expected at this point in the near-term outlook, the risk of recession is rising. Taken in combination with the rising economic fallout from the housing market correction that is to be at its most pronounced level later this Summer and into the Fall, the longevity of the current U.S economic expansion will likely be tested. This will put increasing pressure on the Federal Reserve to "make the right calls" on the monetary policy front, or the current U.S. economic expansion could come to a premature end over this upcoming tricky transitional period.

Overview of the Vermont Economy's Recent Performance and the Near-Term Outlook

Looking at the Vermont economy, the data show an economy that continues to add jobs—but at a pace that recently has been, and will likely continue to be, at a slower pace than recent years or for the national economy as a whole. The reasons for this slower relative job growth performance are somewhat perplexing—given the strong surge again this Spring in state tax receipts and the decent year-over-year growth performance of the PI Withholding Tax. Although some analysts have attributed this relative performance to perceived business climate issues (e.g. higher relative cost of doing business, higher relative cost of living, etc.), it also is true that demographic forces (e.g. slow population growth, including the second oldest state population that is aging at a rate that is faster than the nation as a whole) also appear to be at work as well. These statistics coupled with Vermont's low unemployment rate point to the fact that Vermont's labor force is not growing fast enough to support a high rate of job creation. This is evident in the table below that shows that Vermont's rates of job growth have dropped to the bottom half of the New England region in most of the twelve major NAICS sectors.

Table 1: Vermont's Year-Over-Year Job Change Rank By Selected NAICS Sector

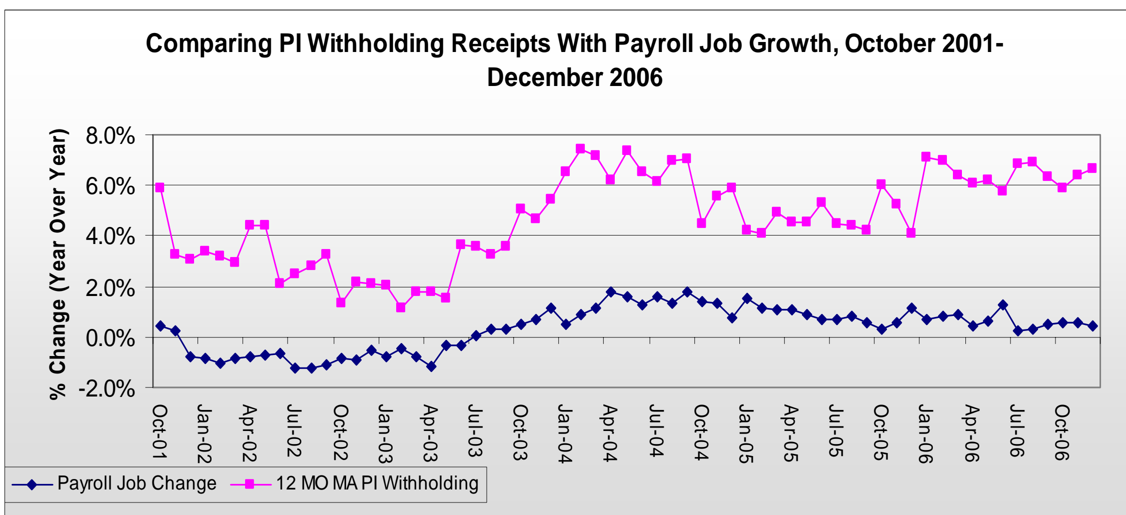
March 2007 versus March 2006	Highest Ranked New England State	Rank in New England	Rank in U.S.
Total-Private and Public Sector Jobs	26th (CT)	6th	45th
Total-Private Industries	22nd (RI)	6th	45th
Construction	7th (RI)	5th	36th
Manufacturing	12th (CT)	3rd	24th
Trade, Transportation and Utilities	21st (NH)	3rd	41st
Financial Activities	1st (RI)	5th	46th
Professional & Business Services	11th (RI)	6th	43rd
Education and Health Care	11th (NH)	4th	41st
Leisure & Hospitality	19th (CT)	5th	44nd
Government	15th (MA)	4th	36th

Source: U.S. Department of Labor

Prepared By: Economic & Policy Resources, Inc.

The table shows that overall, year-over-year payroll job growth numbers have been very restrained, with Vermont ranking in the lower quartile of states in two total payroll job and private sector payroll job growth through March of 2007. Outside of the Trade, Transportation and Utilities sector and the Education and Health Care sector, there has been little notable payroll job growth. Rising exports have helped the manufacturing sector stabilize and begin a slight turnaround. In addition, there has recently been a small positive forward push in payroll job growth from the Leisure & Hospitality and Wholesale trade sectors. Beyond those categories, however, there has

been a curious paucity in payroll job growth that belies logic or intuition. This is perhaps best illustrated by the curious discrepancy between the lack luster, year-over-year job growth numbers over the past 5 quarters and the healthy growth of personal income withholding tax—perhaps the most accurate coincident tax revenue indicator of job-wage growth. Since this tax is closely related to the number of payroll jobs in Vermont movements, the two indicators should mirror one another relatively closely. This has not been the case over the last half calendar year 2006 where there appears to have been a significant divergence between the two variables as indicated in the chart below.



The graph shows that during calendar year 2006 and particularly over the last 3-6 months, the spread between growth rates in personal income withholding tax and employment growth has apparently grown—exceeding the average spread between payroll job change and the 12 month moving average of personal income withholding tax being roughly 4.0 percentage points between October 2001 and December of 2005 by a wide margin. In calendar year 2006, the spread has increased to average roughly 5.9 percentage points—perhaps indicating some under-counting of job growth in the employment data series. While this does not indicate that Vermont payroll jobs are growing at a rapid pace, it does suggest that the pace of job growth is somewhat stronger than that which is indicated by the survey-based job growth data. If the relationship between jobs and personal income withholding tax were to remain within the bounds of its long-standing historical range, it could logically be expected to see payroll job growth of at least ½ to 1 full percentage point higher than now is indicated by the survey data.

Conference Theme: From Sublime to Subprime

The root of the housing market correction we are seeing now goes back to the beginning of the housing market boom in the early 2000's. The combination of the bursting of the equity market bubble in the aftermath of the so-called dot.com bust, the tragic terrorist attacks of September 11, 2001, and the onset of a full-fledged economic downturn during early-mid 2001 led the Federal Reserve to slash interest rates to generational lows to maintain liquidity and to prop up the economy in the aftermath of those unprecedented challenges to our economic system and chosen way of life. This continued to fuel the popularity of mortgage backed securities, which with the

help of the implicit guarantee of the federal government, provided extremely high levels of liquidity to the mortgage markets.

These factors contributed to setting off one of the most significant housing booms in modern economic history. With easy money, housing prices skyrocketed, and speculators jumped into the market—further fueling the boom. The housing market was humming along as the rest of the economy started to catch up, forcing the Fed to eventually begin its campaign to gradually raise interest rates. As these past generational lows in mortgage interest rates crept higher, affordability pressures mounted, and demand for homes declined. Builders-developers were slow to recognize the market shift, and were left with unsold supply as speculators left the market. Lenders, for their part, responded to rising affordability pressures for buyers with an easing in credit requirements for borrowers and they increased their originations of more creative, non-traditional lending products (interest only loans, loans to 125% of market value of the properties, 50 year mortgages, low introductory rates with 5 year balloons, and low documentation loans) in order to keep loan volume and lending activity up. With this activity, the dynamics that led to increased subprime lending activity in the current housing market situation-correction had been put in place.

Until recently after the peak in the housing market, a subprime borrower[2] or a borrower with a non-traditional lending product generally did not have to worry about building equity or defaulting on his/her loan. This because the "hot" housing market generally meant that they could sell their property and still receive much more than they paid for it if they got into financial trouble with their real estate purchase. In fact, in the run-up of the market and until near the market's peak, many borrowers with non-traditional loan products did not even plan to hold their property long enough for their adjustable rates to reset or before whatever "financial stretch" it was that they had to deal with would come home to roost. These market dynamics all began to change in calendar 2005 and calendar 2006 when interest rates rose back above those generational lows and demand for new and existing homes began to ease. This peaking began the first phase of the housing market correction, the one that the economy is now in. So far the correction has been "orderly"—at least in Vermont—where a slow down in the rate of housing price increase has begun. In other parts of the New England region and the nation, the slowdown started before the Vermont slowdown—with some parts of the region now in full-fledged housing price declines.

From the above dynamics, the subprime issue, as we now know it today, was born. This leaves us in the current market situation. The National Association of Realtors reported that March existing home sales showed the largest month to month drop in 18 years and the national average median home price declined 0.3% year over year. The weather in February and March certainly played a role in this drop but this illustrates the point that the housing market has yet to reach its trough. The weakness in the housing market is now multi-faceted. At the root of the housing market decline is the pullback in prices, the magnitude of which seems to be closely related to the run up in prices. That is, the more overheated the individual market the deeper the decline has been in that individual market. The strong growth in the Sunbelt and northeast corridor has turned these regions into the areas demonstrating the greatest housing market and price weakness.

The issue that has permeated the housing correction more recently, the sub prime lending situation, is partially a function of the affordability gap. Mortgage originators and borrowers alike were forced to use creative or exotic lending products to allow more financially stretched households

[2] A subprime borrower is typically defined as one with either no credit history or a blemished credit history. Subprime borrowers also include the so-called Alternative A borrowers who generally have good credit, but have a loan that may lack all or at least some documentation on that loan and/or have a loan as investors in a property.

afford mortgage loans. In many cases the borrower's ability to pay back the loans was only based on the payments during the first two or three years of the loan. As these loans reset two or three years after origination, borrowers are faced with large increases in monthly payments—at times as high as 30% and 50%. The alternative to paying the higher payments is to try to get out of these obligations by selling their homes. If they have trouble doing so in a soft or declining market they may be faced with default. Under these circumstances it is not surprising that 14.4% of sub-prime borrowers with ARMs were at least 60 days delinquent on their loans. The lowest quality loans were originated towards the end of the housing market boom in 2005 and 2006, meaning that the bulk of the ARMs have not yet reset. As they do over the next several years, it is possible that the number of sub-prime borrowers with ARMs in delinquency and default could continue to increase. Calendar year 2006 saw 1.2 million defaults, an increase of 42% over 2005. It is possible, if not probable, that calendar year 2007 will see defaults surpass even those elevated 2006 figures.

The sub-prime situation could have broader, more far reaching effects than just the mortgage markets, perhaps even creating issues for global financial markets. As of this writing, it is estimated that 6% of the global financial system's total capitalization is U.S. mortgage debt—a large portion of which accounts for 15% of foreign U.S. holdings. A significant shock to this sector of the global economy could cause very serious problems with the global financial system. The main enabling factor to the sub-prime mortgage binge was the liquidity made available by the packaging of these debt obligations into mortgage backed securities. If this liquidity were to dry up, it could affect the U.S. mortgage market as well as the investment quality perception of U.S. debt around the world causing foreign investors to diversify away from all types of American securities. This would make it much more difficult and expensive for U.S. corporations to continue to finance the expansions-modernizations of their facilities—which for the most part have made substantial contributions to their recent strong profitability record.

In local markets where supply has already increased, a rash of foreclosures would continue to increase supply in already soft markets, driving prices lower, possibly pushing more distressed borrowers to resort to default. The other factor affecting the demand for housing is related to the affordability issue outlined above. Not only have prices increased above affordability levels for many households, but it is becoming increasingly difficult to obtain financing. Mortgage companies and law makers alike have seen the rash of foreclosures and are taking steps to insure that standards of credit worthiness are revised, making to make it more difficult for the sub-prime or first time buyer to enter the market. Without this portion of the market, demand will decline.

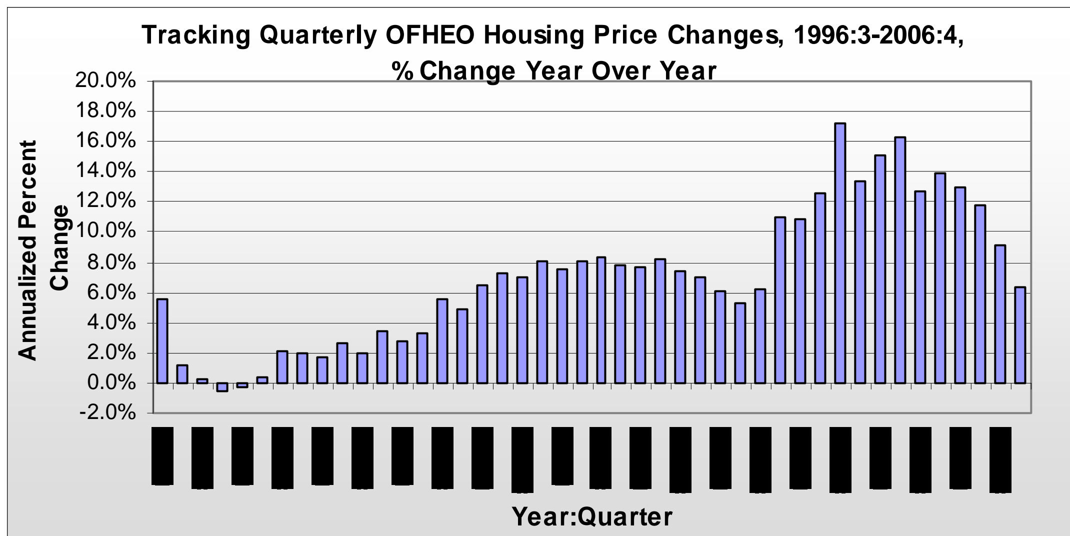
This spiral of events could harm more than just homeowners. Employment in housing dependant industries such as construction and real estate will also be adversely impacted. Housing starts statistics were surprisingly positive in February and March although permitting was off. Much of the March gains in housing starts were due to a strong increase in the Midwest which has not experienced the widespread declines in the previously overheated housing markets in the Northeast, South, and West—which all experienced declines during the month of March.

In addition to the impacts felt by those employed in the housing related industry are the impacts to the broader economy. The majority of the wealth of the American family is tied to their investment in their home. During the run up in prices over the last several years, homeowners were able to cash out equity in their homes (so-called MEWs[3]) to spend on consumption (which could not be supported by their weak wage-salary gains) and to reduce-restructure their debt burdens. As consumption is the largest component of GDP, it comes as no surprise that losing this source of spend-able cash will almost certainly slow overall GDP growth at least to some significant extent.

[3] MEWs means mortgage equity withdrawals.

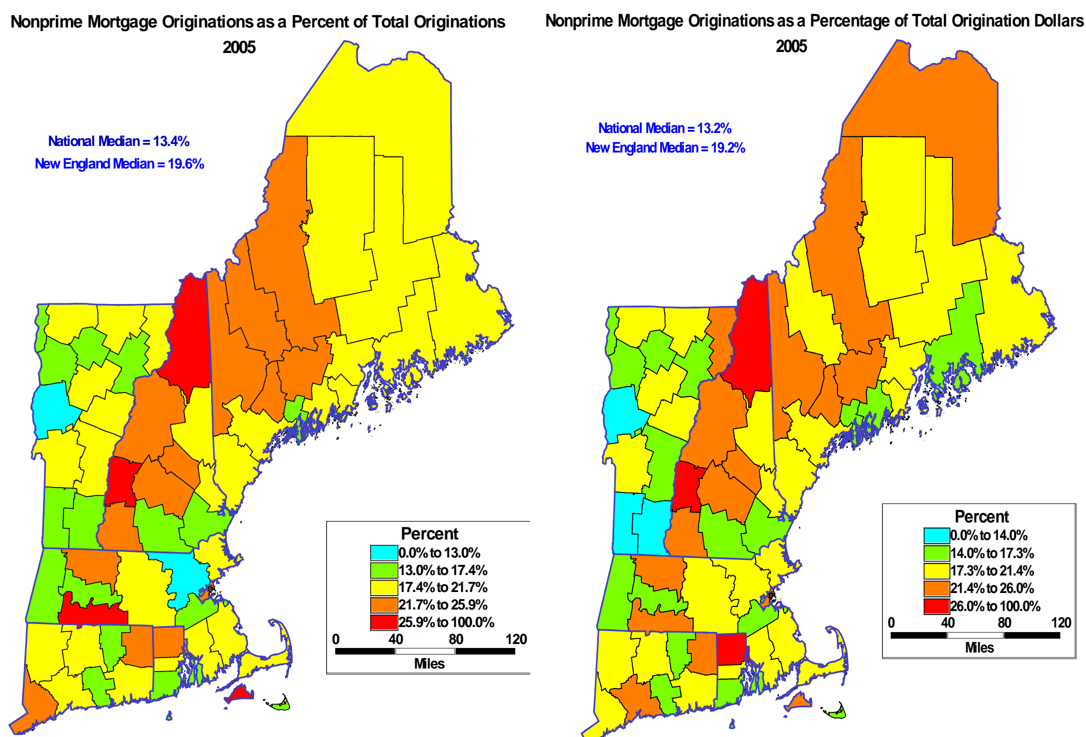
From Sublime to Subprime: The Vermont Situation

With respect to the subprime lending situation, at this point Vermont so far appears to be in a better situation than New England as a whole in the still developing housing market correction. For the most part, this appears to be the result of the state so far being able to avoid the potentially economically lethal combination of: (1) declining housing prices (e.g. through the 4th quarter of 2006 housing prices are still increasing—but at a decreasing rate—see the chart below tracking OFHEO[4] price changes), and (2) increasing foreclosure rates. In fact, in 2006 Vermont had the lowest ratio of foreclosures to households in the country, and the state on a year-over-year basis still is experiencing modest increases in housing prices while many surrounding states have been flattened or are beginning to experience outright price declines. This situation so far has removed a key variable in the subprime meltdown equation for Vermont—where stressed borrowers in subprime lending situations are still for the most part able to sell their homes for at least what they paid for them. If borrowers are not forced into default in a negative equity situation, the negative, self-reinforcing downdraft on housing prices from subprime liquidation cycle is either stopped or at least slowed at its source.



However, the potential for the subprime contagion to materialize in Vermont still remains. Like the rest of the county, mortgage originators were apparently more than willing to finance homes with creative mortgage products for households that were in the margin of affordability guidelines. Although this problem is not as persistent in Vermont as it is in the rest of New England, it does exist in certain parts of the state. The county by county data shows that the areas with the highest percentages of subprime originations occurred in the areas with either the highest affordability pressures (or lowest household incomes) and in those counties where second homes are more prevalent

[4] OFHEO stands for Office of Federal Housing and Enterprise Oversight.



The data show that the median percentage of subprime loans made as a percentage of total originations in Vermont's counties in calendar 2005 was 17.0%--a level which compares favorably to New England's 19.6% average in calendar year 2005 but is well above the 13.4% national median. It appears in Vermont that the main factor driving the higher than national average subprime originations was the issue of affordability for lower income households. This appears to be supported by the fact that the percentage of total dollar volume of subprime originations in 2005 was somewhat less than the percentage of total originations at 15.4% versus 17.0%.

The NEEP outlook for Vermont does suggest going forward that the state is in no way "out of the woods" when it comes to the subprime issue. This is especially true since the state has yet to traverse through the 5 quarter period (bordered by Q3:2007 through Q4: 2008) where there will likely be outright price declines in state housing markets overall. The highest risk of greater economic fallout will be present during this critical time in the next 5 year outlook. This in fact will correspond to the period when the state will be most vulnerable to a housing correction induced recession—if one is to occur in Vermont.

Beyond the housing price situation, one of the main reasons this housing market correction-subprime lending situation is a significant issue for this Vermont economic outlook revision is the disproportionately high degree to which housing construction contributed to overall job creation in the Vermont economy over the last 3 years (or over calendar year 2003-2006 time frame). From the table, construction employment in Vermont accounted for nearly 28½ % of the net positive job addition which occurred in the state over the period. This was true despite accounting for only 6.7% of all private sector employees in 2003. This represents nearly double the relative contribution the Construction sector made to job growth in the New England region as a whole, and nearly 12 percentage points higher than the 16.5% share the Construction sector contributed to overall job growth nationally. Clearly, the housing market slow down has and will continue to

negatively impact Vermont's economic performance in a number of ways. Curtailed construction activity will be particularly painful for regions surrounding the state's major resort areas where the slow down in second home building has exerted a significant drag on output, job and income growth rates recently. Given the current dynamics of the housing market—particularly for second homes—it is difficult to envision the beginnings of a turnaround before mid-calendar year 2008.

Table 2: Construction Job Change as a Percentage of Total Job Change 2003-2006

	Private Sector Job Change (000s)	Construction Job Change (000s)	Construction as % of Total
United States	5768.0	954.0	16.5%
New England	121.5	14.8	12.2%
Vermont	6.7	1.9	28.4%

Source: BLS Current Employment Statistics Series

Prepared By: Economic & Policy Resources, Inc.

Overview of the Moody's Economy.com U.S. Outlook

The main stories in the economy in calendar year 2006 were the initial stages of the housing market correction, the volatile and once again escalating energy price situation, and a still healthy rate of gains in U.S equity markets. The first two factors continue to be the main causes for concern about the health of the expansion through the rest of calendar year 2007. With almost all of the other sectors of the economy contributing significantly to national economic growth, the only part of the economy that now is restraining economic growth is the declines in residential fixed investment. The May 2007 Moody's Economy.com national forecast scenario, which formed the national basis for the Vermont economic forecast update, reflects this view. Moody's Economy.com expects the national GDP growth rate to remain below its potential of 3.0% for another two quarters during calendar 2007—as GDP growth did during the final quarter of calendar 2006. GDP growth is expected to pick up during the third quarter of 2007 until it reaches its potential during the 4th quarter of 2007. GDP growth is then expected to at least match its potential rate of growth throughout the remainder of the forecast period. On a year-to-year basis, inflation-adjusted GDP growth is expected to range from a high of +3.1% in 2008 to a low of +2.4% during calendar year 2007—the initial year of the forecast period.

The Moody's Economy.com scenario also reflects the view that the fundamentals in the U.S. economy remain sound boding well for continued U.S. economic growth. Recent positive reports on durable goods orders and blockbuster profit disclosures likewise support such a continued growth scenario. This situation is expected to translate into a very healthy personal income increases for the U.S. economy, with personal income rising at a +7.3% clip on a per capita basis due mainly to non wage income created by capital gains. Going forward the Moody's Economy.com forecast scenario predicts that this high per capita personal income growth rate will moderate, slowing considerably this year and posting only a 1.4% increase in the 3rd quarter of 2007, followed by only a slight bounce back into the 2.0% to 2.5% inflation adjusted range for the remainder of the forecast period. Because much of the initial gain in per capita personal income is related to non-wage capital gains, it is not surprising that employment growth is expected to crawl along—averaging between a high of +1.4% in calendar 2011 to a low of +1.0% in calendar 2008 over the calendar 2007-2011 forecast period.

Another key growth supporting factor in the U.S. economic outlook is the continuing positive outlook for the global economy. The global economy is in the midst of a solid, broad-based expansion, with economic activity in every developed economy and many developing economies growing strongly. The economic outlook for the U.S.'s largest trading partner, Japan also has improved as that previously struggling economy has strengthened. The weak dollar adds another positive to the American export situation making U.S. goods cheaper abroad—and foreign imports more expensive. That outlook bodes well for continued growth in exports for U.S. businesses over both the near-term and longer-term time horizons. The climb of oil prices does pose the possibility of reversing the gains in exports if more must be spent to import fuel. The positive situation in global capital markets could be derailed by a deep subprime mortgage crisis in the U.S. due to the huge capitalization of these types of loans.

To continue on the housing market front, the Moody's Economy.com forecasts predicts a decline in home prices nationally for five out of the next six quarters with a low of -7.1% this quarter to highs of 4.6% in individual quarters of 2009 and 2010. The OFHEO Index is expected to decline as well, but at a smaller magnitude through the next six quarters with the deepest decline expected in quarter 3 of this year of -3.2% and the highest rate of change during the 4th quarter of 2010 of 4.4%. The other important gauge of the real estate market is the quarterly change in residential fixed investment. The Moody's Economy.com baseline forecast predicts a dramatic decrease in this variable in the first half of this year resulting in a -11.6% decline this year. All of this depends on the performance of the large number of subprime loans and how borrowers deal with the ARMs that are expected to be resetting over the next 18 months.

The drag the housing market correction is creating on the economy is offsetting the increases in consumption which make up about 70% of GDP. Moody's Economy.com baseline forecast predicts a healthy 3.0% rate of growth this year dropping to 2.2% next year followed by a rebound back to 2.9% in 2010. Consumption of services will be the leading component of consumption posting a 3.4% increase this year, showing lower growth next year followed by a rebound to 3.5% by 2010 following a the similar trend of consumption as a whole of which it comprises about 55% of. The only major component of consumption expected to post a decline in the forecast period is motor vehicle sales, which are not expected to post a positive growth rate during the forecast period. This will almost certainly help to deepen the already declining housing market situations in the upper Midwest.

On the inflation front, higher energy and commodity prices have worked their way into the economy's general inflation rate to a significant degree, higher energy prices remain as one of the principal threats to the inflation outlook. So far, businesses—with their record profit margins—have apparently been willing to absorb energy cost increases (and high commodity prices in general) to-date. Although energy prices appear to be rising once again, inflationary expectations appear to be moderating slightly. The Moody's Economy.com forecast expects that the price of the benchmark West Texas Intermediate Crude Oil price per barrel will average just between $55 and $60 per barrel during calendar 2007. The baseline forecast then expects the price to begin to decline steadily and fall back into the $40 per barrel (by calendar 2010 and 2011). The Moody's Economy.com baseline acknowledges that forecasting energy prices is a risky endeavor. The recent spike in prices is expected to moderate demand for energy, and these prices are likewise expected to engender some type of positive production response from producers over both the near-term and longer term time horizons.

Overall, the baseline forecast calls for inflationary pressures to continue to follow their downward bias over the forecast period, with GDP Chain Deflator declining from its current +3.1% to a 2.5% pace in 2008 and 2009 to close to 2.0% in 2010 and 2011. Beyond that point, CPI inflation is

expected to remain relatively well-contained declining to 2.1% by the 4th quarter of this year. This is consistent with longer-run price expectations that by most counts (e.g. inflation-protected treasury securities) remain well contained.

Closely related to inflation rates are interest rates. The Moody's Economy.com baseline forecast expects that monetary policy will remain committed to fighting inflationary pressures. The forecast expects the Fed will hold the federal funds rate to 5.25% until sometime in 2008. The 5.25% federal funds rate is a level that many monetary policy observers believe is a more neutral rate, one that is neither stimulating nor constraining to economic growth. Driving that expected action is an economy that is operating near capacity, a dark and still eroding long-term federal budget outlook, and increasingly tight labor market conditions—including the lowest unemployment rate in 5 years (which is now below the economy's natural unemployment rate) and a rate of payroll job addition that exceeds 150,000per month (a level that is understood to be needed to keep up with productivity gains and labor force growth).

The composition of growth has shifted from a housing and wealth dependent consumer spending-led expansion to one led by increased business investment and services consumption. Export growth will also be a key driver to U.S. economic growth over the forecast period. Exports are expected to grow over the forecast period within a range of between +7.5% (in calendar year 2007) to +8.9% (in calendar 2010) while imports grow at a pace of between 3.2% (in calendar year 2007) to 6.2% (in calendar 2011). That trade performance will depend on a tricky and still evolving interaction between global financial flows from regions with surplus financial reserves (e.g. China and Asia) and U.S. domestic monetary policy and the duration of the weakness in the U.S. dollar.

The Updated 2007-11 Vermont Economic Outlook

Against the backdrop of that national economic scenario and existing Vermont conditions, the Spring 2007 Vermont Economic outlook update again charts a familiar, well-worn course. Once again, the overall tone to the Vermont outlook is positive, but the pace of economic and labor market activity is expected to remain restrained throughout the 2007-11 forecast time horizon. Payroll job growth is expected to for the most part remain under +1.0% over the next five years. On a quarterly basis, job growth is expected to experience a low of 0.5% this quarter and in the first quarter of 2008 with a quarterly high of 1.2% in the last quarter of 2008. Output growth in inflation-adjusted dollars is forecasted to grow at a higher rate over the course of the forecast, averaging a meager +1.4% in calendar 2007, followed by a more healthy rate of increase of +3.1% in calendar 2008, then declining relatively uniformly to the level of +2.5% in calendar 2011. The +2.5% average annual rate of output growth in the Vermont economy expected over the calendar 2007-11 period corresponds to a level that is roughly 0.7 percentage points below the +3.2% output growth average experienced during the first half of the decade of the 2000s.

The following table presents comparative statistics from this NEEP outlook update for the Vermont, New England regional, and U.S. economies. The U.S. data correspond to the assumed macroeconomic environment for the Vermont economy as provided by Moody's Economy.com for the upcoming five year period. The New England data reflect the composite forecast for all six New England states. The Vermont statistics present the specific detail for the Vermont economic forecast that was developed over that same period. Looking more closely at the Vermont data, the State's rate of job growth-recovery and income growth performance through March 2007 has been somewhat more restrained than the U.S. average and the New England regional average. Over the rest of calendar 2007 and into early calendar year 2008, Vermont is expected to experience somewhat lower rates of growth in output, jobs, and income versus the U.S. economy due in part to

the relatively greater negative impact that the housing market correction and the still increasing energy prices have had, and are expected to have, on the state's economy.

The pace of economic activity in Vermont is expected to lag behind the nation as a whole in every major variable with the usual exception of the state's relatively lower unemployment rate. At the same time, the state's economic performance after calendar year 2007 is expected to be somewhat stronger than the New England regional average—although by only a slim margin for most macro indicators in the out-years of the forecast period. The main reason for this is the housing situation and the prediction that the worst of the housing market correction's effects will be felt early on in the forecast time horizon. Therefore, as the impacts of housing market correction run their course, Vermont's relative economic performance will begin to improve and the state will begin to once again approach more "normal" rates of output, job, and income growth that will exceed the rates of growth in these macro-indicators for the New England region as a whole.

Table 3: Calendar Year Forecast Comparison: United States, New England, and Vermont (Spring 2007 NEEP Forecast)

	Actual					Forecast				
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Real Output (% Change)										
U.S. Gross Domestic Product	1.6	2.5	3.9	3.2	3.3	2.4	3.1	3.0	3.0	3.0
N.E. Gross Domestic Product	-0.3	2.3	4.1	2.3	2.7	2.4	2.8	2.8	2.7	2.5
Vermont Gross State Product	2.0	3.7	4.5	2.7	1.6	1.4	3.1	2.9	2.8	2.5
Non-Farm Payroll Jobs (% Change)										
U.S.	-1.1	-0.3	1.1	1.7	1.9	1.1	1.0	1.3	1.3	1.4
New England	-1.5	-1.1	0.4	0.6	0.9	0.9	0.9	0.9	0.9	0.9
Vermont	-0.9	0.0	1.3	0.9	0.6	0.6	0.7	1.0	0.9	0.8
Personal Income %Change (2000 Dollars)										
U.S.	0.4	1.2	3.5	2.3	3.5	4.5	3.2	3.3	3.2	3.1
New England	-0.7	0.1	3.0	1.5	2.6	2.9	2.7	2.6	2.4	2.3
Vermont	0.3	1.8	1.7	1.3	1.6	3.2	3.1	2.8	2.5	2.3
Unemployment (Percent)										
U.S.	5.8	6.0	5.5	5.1	4.6	4.7	4.8	4.7	4.6	4.6
New England	4.8	5.4	4.9	4.7	4.6	4.8	4.8	4.7	4.7	4.7
Vermont	4.0	4.5	3.7	3.5	3.6	3.9	3.9	3.7	3.6	3.6

Notes:
[1] 2006 variables are subject to further revision, and 2007 through 2011 values in this table reflect projected data as of May 2007.

Sources: Moody's Economy.com (U.S.), New England Economic Partnership November 2006 Forecast Update (New England, Vermont)

Although the State's relative economic performance in output, jobs, and personal income is expected to be mixed over the 2007 to 2011 forecast period relative to the U.S. and New England averages, this revised forecast includes the expectation that Vermont's unemployment rate will continue to track consistently below both the U.S. and New England averages. This continues the long-standing trend where the State's unemployment rate has consistently tracked roughly 1 to 1¼ percentage points below both the New England regional and U.S. averages. In fact, Vermont's unemployment rate has consistently tracked among the lowest of any state in the country—along with the state of New Hampshire—over the most recent five year period.

The table below highlights the direction and magnitude of the changes for payroll job growth and inflation-adjusted personal income in this Spring outlook revision versus the previous six NEEP forecast updates. As with previously published economic forecasts for the state, the size of the forecast revisions are for the most part relatively small, falling within a +/-0.5 to +/-1.0 percentage points range for these key macro indicators. What is important to note is that all of the revisions except for the 2007 payroll job growth forecast are positive, the largest being the +0.8 percentage point increase in the growth rate for inflation-adjusted personal income in calendar year 2007. This reflects a combination of revisions in the historical data series and the apparent strong underlying income growth momentum in the state economy despite relatively recent tepid performance by the state's major labor market and output indicators. The forecast seems to indicate that the weak labor

market growth displayed in the statistics may not be telling the whole story as discussed previously. The upward forecast revision in employment translates into higher real personal income growth.

On the sector-by-sector front, the highest rates of job growth over the 2007-11 forecast period are expected in the Leisure and Hospitality Sector (at 2.0% per year), Professional & Business Services sector (at +1.9% per year) and the Education & Health Services sector (at +1.8% per year). Almost surprisingly, employment in the manufacturing sector is expected to remain almost flat during the period—thanks in part to stronger export growth in response to a strongly growing global economy and the decline in the value of the U.S. dollar. Overall, 11 of the 12 of the state's major NAICS categories are expected to recover-add jobs over the 2007-11 forecast period with only the government sector losing jobs. Notably absent among the leading job growth sectors is the Construction sector, which is expected to gain only modestly over the over the forecast period—at the rate of 0.7% per year. That represents a significant down-shifting from the heady +2.6% average job growth rate per year experienced by the Construction sector during the 2001-2006 time frame.

Table 4: Historical Comparison of NEEP Forecasts for Vermont (May 2007)

Calendar Years	2003	2004	2005	2006	2007	2008	2009	2010
Real Gross State Product				<History<	>Forecast>			
Payroll Job Growth								
May 2004	-0.2	1.1	1.7	1.3	1.0	1.0		
November 2004	-0.2	1.1	1.9	1.1	0.9	1.1		
May 2005	0.0	1.4	1.6	1.2	0.7	0.9		
November 2005	0.0	1.4	1.5	1.4	0.2	0.7	1.2	
May 2006	-0.1	1.3	0.8	1.2	1.2	0.8	1.1	0.9
November 2006	-0.1	1.3	0.8	0.8	0.7	0.7	0.8	0.8
May 2007	0.0	1.3	0.9	0.6	0.6	0.7	1.0	0.9
Diff. Pct. Pts. 11/06-5/07	**0.1**	**0.0**	**0.1**	**-0.2**	**-0.1**	**0.0**	**0.2**	**0.1**
Real Personal Income								
May 2004	2.1	2.7	2.4	2.0	2.3	2.3		
November 2004	2.1	3.1	2.3	1.7	2.2	2.4		
May 2005	1.7	3.7	3.9	1.8	1.9	2.2		
November 2005	2.0	3.6	2.9	0.8	-0.2	2.0	2.4	
May 2006	1.4	3.1	2.3	1.7	1.5	1.9	2.2	2.0
November 2006	1.4	3.1	2.3	2.0	2.4	3.0	2.8	2.4
May 2007	1.8	1.7	1.3	1.6	3.2	3.1	2.8	2.5
Diff. Pct. Pts. 11/06-5/07	**0.4**	**-1.4**	**-1.0**	**-0.4**	**0.8**	**0.1**	**0.0**	**0.1**

Source: New England Economic Partnership (May 2007)

Forecast Risks: The Housing Market Correction Against the Backdrop of Rising Energy Prices…

The risks associated with this May 2007 NEEP forecast revision is centered on the conference theme of the subprime mortgage fallout against the backdrop of the still evolving housing market correction. While the housing market correction has the potential to boil over into many other parts of the economy and potentially derail the current expansion, there also are a number of other risks that need to be listed and considered. Several have become regular inclusions in this listing. The forecast risk of high and volatile energy prices has become a regular, while others have rotated in and out of this list. For this May 2007 NEEP forecast update, the list of forecast risks include:

(1) High and now rising energy prices which threaten to increase business costs (reduce corporate profits), erode disposable household income (reduce consumption), and curtail tourism activity,

(2) The housing market correction and the growing fissure in subprime mortgage lending that threatens to spillover into the broader economy by eroding business and consumer confidence and potentially touching off a broader global financial-liquidity crisis,
(3) The curtailment of mortgage extractions from homes—which heretofore had been a significant source of financial resources for making "big-ticket" purchases and home improvement expenditures,
(5) A further deterioration in the military operations currently underway in Iraq and/or a political impasse in another major oil producing country (such as Iran) and its impact on U.S. consumer and business sentiment, and
(6) The continuing threat of another psyche-damaging terrorist attack or major national disaster in the U.S., somewhere in the western world, and/or in the oil producing regions of the world.

Vermont-specific threats to this revised NEEP outlook that deserve mention as well. These include:

(1) The perception of Vermont as a high tax state with an inadequate workforce that threatens to slow economic growth and job creation further,
(2) The relatively high, even non-competitive, level of electrical energy costs in Vermont versus the national average (which threatens Vermont's fragile manufacturing sector) and the possibility of more upward pressure from current fossil-fuel indexed long-term power supply contracts, and
(3) The perception of an overall high cost of doing business and cost of living in Vermont which creates a negative perception about the ability to invest and grow a business here and for the critically important entrepreneurs to live and raise their families in the Green Mountain state.

Many of the same risks that have been outlined in the past few forecast updates remain and will most likely remain for years to come. The biggest concern to the economy is the depth of the housing market correction and its affects the outlook locally, regionally, nationally and globally. Recent economic data indicates that the housing market is already taking a bite out of GDP growth. The housing market correction has not yet reached bottom, and this needs to be monitored closely over the next 18-24 months.

Jeffrey B. Carr, President
Kerry G. Mayo, Research Economist
Economic & Policy Resources, Inc.
P.O. Box 1660
Williston, Vermont 05495
(802) 878-0346