

Management's Discussion and Analysis

The following is a discussion and analysis of the State of Delaware's financial activities for the fiscal year ended June 30, 2003. Readers are encouraged to consider the information presented here in conjunction with additional information that is furnished in the letter of transmittal, which can be found on pages i-ix of this report.

These financial statements have been prepared using the new financial accounting model adopted by the Governmental Accounting Standards Board (GASB). This new model represents the biggest change in the history of governmental accounting and financial reporting. This is the second year of implementation in Delaware for these new standards.

Financial Highlights

- The assets of the State exceeded its liabilities at the close of the most recent fiscal year by \$4.7 billion (net assets). Component units reported net assets of \$525.2 million, an increase of \$5.8 million from the previous year.
- The primary government's total net assets increased by \$50.1 million (1.1%) in fiscal year 2003. Net assets of governmental activities increased by \$146.8 million (9.9%) while net assets of the business-type activities decreased \$96.7 million (3.1%).
- As of the close of the current fiscal year, the State's governmental funds reported combined ending fund balances of \$982.5 million, an increase of \$47.9 million (5.1%) in comparison with the prior year.
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$643.5 million, or 21.9% of total general fund expenditures. For the most part, the unreserved fund balance is not available for new spending. These funds have been committed based on State statutes.
- The State's total general obligation debt increased during the fiscal year to \$854.3 million, an increase of \$144.4 million (20.3%). Approximately 80.9% of new money bonds issued during fiscal year 2003 will be allocated to public and higher education facilities. The remaining 19.1% will be spent on State offices and other facilities.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the State's basic financial statements. The State's basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains this MD&A and other required supplementary information, in addition to the basic financial statements.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the State of Delaware's finances, in a manner similar to a private sector business.

The statement of net assets presents information on all of the State of Delaware's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the State of Delaware is improving or deteriorating.

The statement of activities presents information showing how the State's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the State that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the State include general government, health and children's services, judicial and public safety, natural resources and environmental control, labor and education. The business-type activities of the State include transportation, lottery and unemployment services.

The government-wide financial statements include not only the State (known as the primary government), but also legally separate entities for which the State of Delaware is financially accountable. These entities include the Delaware State Housing Authority, the Diamond State Port Corporation, the Riverfront Development Corporation, the Delaware State University and 13 charter schools. Financial information for these component units are reported separately from the financial information presented for the primary government. The government-wide financial statements can be found on pages 20-21 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The State, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the State of Delaware can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of available resources, as well as on balances of available resources on hand at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for government funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financial decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The State maintains four individual governmental funds: the general fund, the capital projects fund, the federal fund and the local school district fund. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for these funds.

The State budgets and controls its financial activities on the cash basis of accounting. In compliance with State law, the State records its financial transactions in either of two major categories – the General Fund or the Special Fund. References to these funds in this report include the terms “budgetary” or “budgetary basis” to differentiate them from the GAAP funds of the same name which encompass different funding categories. The State of Delaware adopts an annual appropriated budget for its budgetary general fund. A budgetary comparison statement has been provided for the budgetary general fund to demonstrate compliance with this budget. The statement can be found on page 110 of this report.

The basic governmental fund financial statements can be found on pages 24-27 of this report.

Proprietary funds. The State maintains one type of proprietary fund. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The State uses enterprise funds to account for the State Lottery, Unemployment Trust Fund and the Department of Transportation operations.

Proprietary funds provide the same type of information as the government-wide financial statements, but in more detail. The proprietary fund financial statements provide separate information for the State Lottery, Unemployment Trust Fund and the Department of Transportation, all of which are considered to be major funds of the State.

The basic proprietary fund financial statements can be found on pages 30-32 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the State's own programs. The pension trust funds are the primary fiduciary funds for the State. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary fund financial statements can be found on pages 34-40 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 49-106 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the status of the State's legally adopted budget and the maintenance of the State's infrastructure. Required supplementary information can be found on pages 108-115 of this report.

Statewide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the State of Delaware, assets exceeded liabilities for the primary government by \$4.7 billion at the close of the most recent fiscal year.

The largest portion of the State's net assets (69.3%) reflects its investment in capital assets (e.g., land, buildings, vehicles, and equipment), less any related debt used to acquire those assets that is still outstanding. The State uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the State's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. Restricted net assets, comprising 8.5% of total net assets, represents resources that are subject to external restrictions, constitutional provisions, or enabling legislation on how they can be used. The remaining portion, unrestricted net assets (22.2%), may be used at the State's discretion, but, for the most part, these funds have been appropriated based on State statutes.

Net Assets as of June 30, 2003

(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total	
	2003	2002	2003	2002	2003	2002
Current and other non-current assets	\$ 1,557,734	\$ 1,456,111	\$ 735,976	\$ 604,535	\$ 2,293,710	\$ 2,060,646
Capital assets	1,639,195	1,391,083	3,362,818	3,326,760	5,002,013	4,717,843
Total assets	3,196,929	2,847,194	4,098,794	3,931,295	7,295,723	6,778,489
Long-term liabilities outstanding	1,071,017	900,354	885,926	655,340	1,956,943	1,555,694
Other liabilities	492,624	460,364	122,646	158,527	615,270	618,891
Total liabilities	1,563,641	1,360,718	1,008,572	813,867	2,572,213	2,174,585
Net assets:						
Invested in capital assets, net of related debt	762,239	680,717	2,464,049	2,645,902	3,226,288	3,326,619
Restricted	136,460	128,930	256,792	310,619	393,252	439,549
Unrestricted	734,589	676,829	299,855	160,907	1,034,444	837,736
Total net assets	\$ 1,633,288	\$ 1,486,476	\$ 3,020,696	\$ 3,117,428	\$ 4,653,984	\$ 4,603,904

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the State's net assets changed during the fiscal year.

Changes in Net Assets - Primary Government
(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2003	2002	2003	2002	2003	2002
Revenues:						
Program revenues:						
Charges for services	\$ 512,045	\$ 506,860	\$ 994,052	\$ 1,047,300	\$ 1,506,097	\$ 1,554,160
Operating grants and contributions	772,470	718,815		26,415	772,470	745,230
Capital grants and contributions			115,502	106,938	115,502	106,938
General revenues:						
Taxes:						
Personal income taxes	706,277	718,672			706,277	718,672
Business taxes	1,180,281	1,153,025			1,180,281	1,153,025
Other taxes	201,115	167,258			201,115	167,258
Real estate taxes	267,177	238,574			267,177	238,574
Investment earnings	73,911	58,624	25,073	26,915	98,984	85,539
Gain (Loss) on sale of assets	13,536		(287)	(60)	13,249	(60)
Total revenues	<u>3,726,812</u>	<u>3,561,828</u>	<u>1,134,340</u>	<u>1,207,508</u>	<u>4,861,152</u>	<u>4,769,336</u>
Expenses:						
General Government	341,054	445,502			341,054	445,502
Health and Children's Services	1,363,289	1,240,332			1,363,289	1,240,332
Judicial and Public Safety	422,921	389,806			422,921	389,806
Natural Resources and Environmental Control	100,171	111,443			100,171	111,443
Labor	59,521	60,650			59,521	60,650
Education	1,422,820	1,370,137			1,422,820	1,370,137
Payment to Component Unit - General Government	10,107	8,821			10,107	8,821
Payment to Component Unit - Education	64,670	40,571			64,670	40,571
Interest Expense	42,000	31,576			42,000	31,576
Lottery			353,840	380,084	353,840	380,084
Transportation			504,463	446,473	504,463	446,473
Payment to Component Unit			946		946	0
Unemployment			125,270	116,538	125,270	116,538
Total expenses	<u>3,826,553</u>	<u>3,698,838</u>	<u>984,519</u>	<u>943,095</u>	<u>4,811,072</u>	<u>4,641,933</u>
Increase (Decrease) in net assets before transfers	(99,741)	(137,010)	149,821	264,413	50,080	127,403
Transfers	<u>246,553</u>	<u>266,090</u>	<u>(246,553)</u>	<u>(266,090)</u>	<u>0</u>	<u>0</u>
Increase (decrease) in net assets	146,812	129,080	(96,732)	(1,677)	50,080	127,403
Net assets - Beginning of Year	<u>1,486,476</u>	<u>1,357,396</u>	<u>3,117,428</u>	<u>3,119,105</u>	<u>4,603,904</u>	<u>4,476,501</u>
Net assets - End of Year	<u>\$ 1,633,288</u>	<u>\$ 1,486,476</u>	<u>\$ 3,020,696</u>	<u>\$ 3,117,428</u>	<u>\$ 4,653,984</u>	<u>\$ 4,603,904</u>

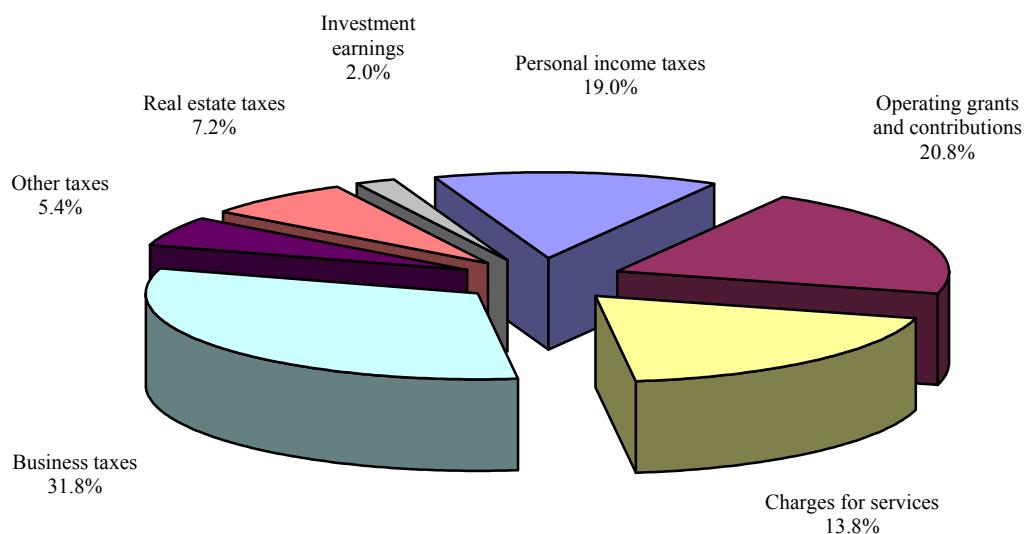
Governmental activities. Governmental activities increased the State's net assets by \$146.8 million. The decrease by the business-type activities of \$96.7 million is explained on the following page. A comparison of the cost of services by function for the State's governmental activities is shown in the following chart, along with the revenues used to cover the net expenses of the governmental activities. Key elements of the increase in net assets are as follows:

Total general revenues increased \$92.6 million (4.0%) based on growth primarily in realty transfer tax of \$28.6 million (12.0%) and abandoned property increases of \$75.4 million (48.4%). For a second consecutive year, the realty transfer tax grew due to low mortgage rates and a continued building boom throughout the State. Growth in abandoned property was due to a large settlement (\$45.0 million) and a strong enforcement program. Personal income tax decreased \$12.4 million (1.8%) due to a sluggish economy, declines in capital gain income and weak wage growth.

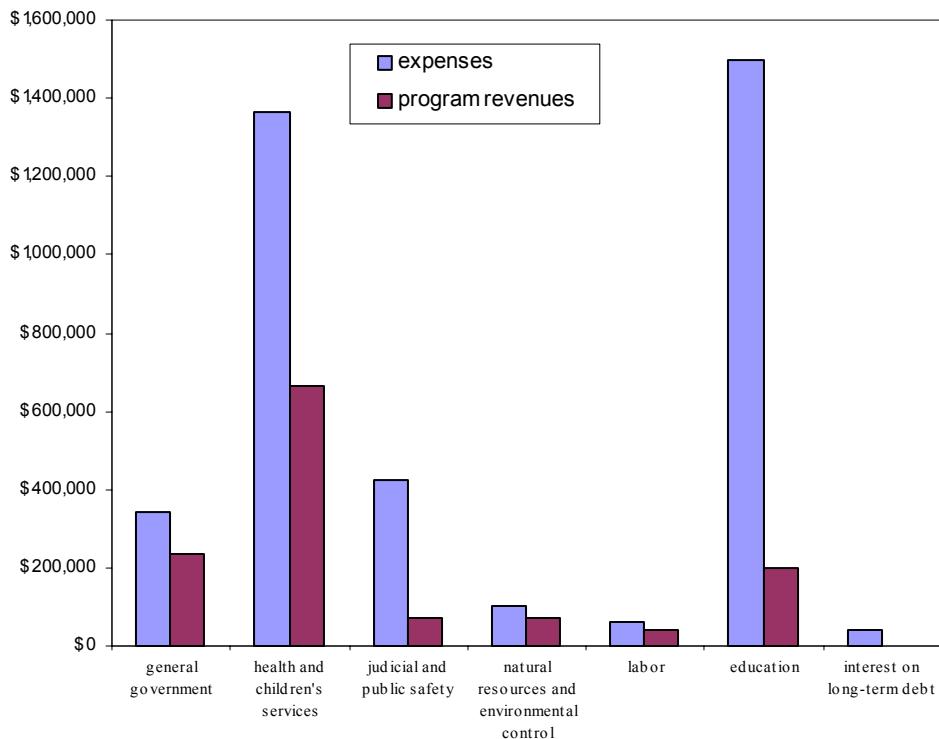
Charges for services and operating grants and contributions increased by \$58.8 million (4.8%). This increase was due primarily to increases in grant revenues at the Department of Health and Social Services (\$32.8 million) and the Department of Education (\$9.6 million).

Expenses for governmental activities increased during fiscal year 2003 by \$127.7 million (3.5%). Of this increase, \$123.0 million was due to increased spending in Health and Children's Services. This increase can be attributable to escalating health care costs and an increase in the population served. Temporary Assistance for Needy Families grew by 6.5% in fiscal year 2003 over the previous year. Salaries increased statewide by \$49.8 million (3.2%). Health insurance costs increased \$51.4 million (16.3%). The General Government function showed a decrease in spending of \$104.4 million (23.4%) due to budget cuts and a hiring freeze enacted by the Governor during the year.

Revenues by Source – Governmental Activities



Expenses and Program Revenues – Governmental Activities



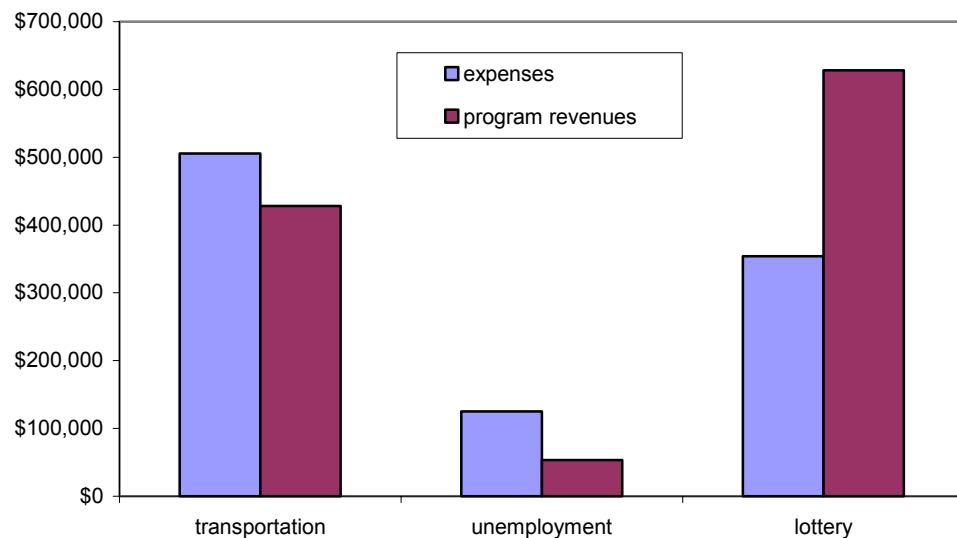
Business-type activities. Business-type activities decreased the State's net assets by \$96.7 million. This resulted from a \$53.8 million decrease in net assets by the Delaware Unemployment Insurance Trust Fund, a decrease in net assets of \$43.3 million by the Delaware Department of Transportation and an increase of \$.4 million in the Delaware State Lottery.

The decrease in net assets of the Delaware Unemployment Insurance Trust Fund can be attributed to unemployment benefits increasing by 14.0% (\$15.5 million), unemployment insurance tax revenues during fiscal 2003 decreasing by 6.6% (\$4.0 million), and benefits expense exceeding tax revenues by \$71.7 million. Based upon a report from the U.S. Department of Labor, as of June 30, 2003, the Delaware Unemployment Trust Fund's net asset's were ranked 5th strongest in the nation. This ranking was based on the AHCM (average high cost multiple) methodology used by the U.S. Department of Labor to evaluate financial strength of states' Unemployment Trust Funds.

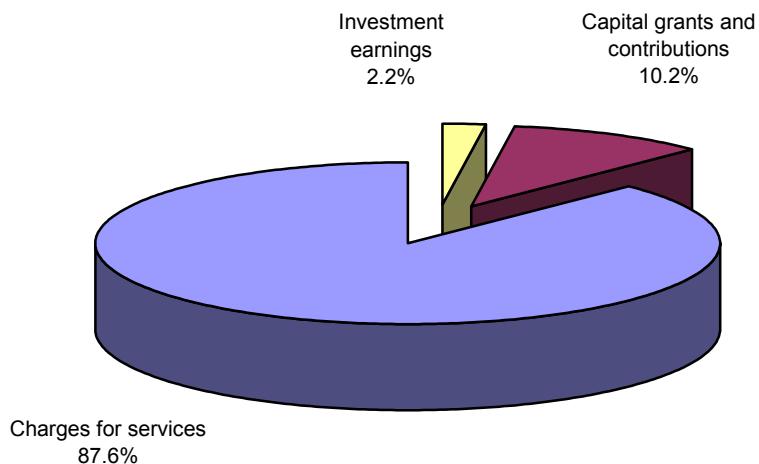
The Delaware Department of Transportation's net assets at June 30, 2003 were \$43.3 million lower than June 30, 2002. The Department's total operating revenues remained fairly constant at \$312.5 million and total operating expenses increased \$42.5 million to \$458.5 million. Contributing factors for the increase in operating expenses for fiscal year 2003 are investments in the maintenance, preservation, and repair of the Department's assets and storm-related costs.

The Delaware Lottery experienced an increase in net assets of \$.4 million. Lottery revenues decreased \$45.9 million, or nearly 7% from the previous year while operating expenses decreased by 12.3% from the previous year. The decline in revenues can be partly attributed to a downturn in the economy and a reduction in the number of patrons who used the State's three gaming facilities.

Expenses and Program Revenues – Business-type Activities



Revenues by Source – Business-type Activities



Financial Analysis of the State's Funds

As noted earlier, the State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds. The focus of the State's governmental funds is to provide information on near-term inflows, outflows, and balances of available resources. Such information is useful in assessing the State of Delaware's financing requirements. Unreserved fund balances may serve as a useful measure of a government's net resources at the end of the fiscal year.

As of the end of the current fiscal year, the State of Delaware's governmental funds reported combined ending fund balances of \$982.5 million, an increase of \$47.9 million in comparison with the prior year. Approximately one-half of the aggregate fund balances, \$547.7 million constitutes unreserved fund balances. The unreserved fund balances, for the most part, are not available for new spending. These funds have been committed to various uses based on State statutes. The remainder of the fund balances are reserved to indicate that they are not available for new spending due to the following: 1) to liquidate contracts and purchase orders of the prior period (\$223.3 million), 2) reserve for long-term loans (\$70.4 million), 3) set aside for the budget reserve account (\$136.5 million), or 4) for inventories and other assets (\$4.7 million).

The general fund is the chief operating fund of the State. At the end of the current fiscal year, unreserved fund balance of the general fund was \$643.5 million, while total fund balance reached \$949.1 million. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 21.9% of total general fund expenditures, while total fund balance represents 32.3% of that same amount.

Total general fund balance increased during the fiscal year by \$27.4 million. Based on anticipated reductions in revenues, budget cuts were initiated and a hiring freeze was implemented early in the fiscal year. However, as of the end of fiscal 2003, general fund expenditures were below the level of appropriations and revenues exceeded budgeted amounts.

Proprietary funds. The State of Delaware's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. The proprietary fund financial statements provide separate information for the State Lottery, Unemployment Trust Fund and the Department of Transportation, all of which are considered to be major funds of the State.

The State's net assets decreased in fiscal 2003 by \$96.7 million as a result of operations in the proprietary funds. See page 10 for a discussion of the business-type activities.

General Fund Budgetary Highlights

The Budgetary General Fund is the chief operating fund of the State. At the end of the fiscal year, total fund balance diminished by \$17.8 million (3.7%). Revenues were \$10.7 million higher (0.4% percent) than the previous fiscal year due to an increase in collections from the realty transfer tax, cigarette taxes, bank franchise tax and increases in abandoned property collections. Expenditures were \$.4 million higher than the previous fiscal year. Salaries, fringe benefits, pension costs and welfare payments were up \$55.1 million (3.4%) whereas contractual services and capital outlay expenditures were down \$65.9 million (20.4%).

The following summarizes the differences between the final appropriated budget (the original budget in addition to encumbrances and multi-year project budgetary carry-forwards from the prior fiscal year) and actual expenditures. As it became apparent in the early months of the fiscal year that the economy was slowing, measures were taken to reduce spending through hiring freezes and budget cuts across all agencies.

- \$86.6 million in decreases in general government activities
- \$64.7 million in decreases in education
- \$37.8 million in decreases in Health and Children's services
- \$12.5 million in decreases in the Department of Natural Resources and Environmental Control.
- \$10.7 million in decreases in the Judicial and Public Safety departments.

Budgetary Special Fund are designated for specific purposes. The appropriated budgetary Special Fund is credited with tax or other revenue allocated to such fund and is charged with the related disbursements. State park operations and fees charged by the Public Service Commission are examples of specific uses of budgetary Special Funds. Federal payments, unemployment compensation and local school funds are examples of non-appropriated Special Funds.

At the end of the fiscal year, total fund balance of the appropriated budgetary Special Funds increased \$6.7 million. Revenues remained unchanged from the previous year while expenditures increased \$10.5 million (2.3%). The differences between the final appropriated budget (the original budget in addition to encumbrances and multi-year project budgetary carry-forwards from the prior fiscal year) and actual expenditures can be accounted for in much the same way as the General Fund.

Capital Asset and Debt Administration

Capital assets. The State of Delaware's investment in capital assets for its governmental and business-type activities, as of June 30, 2003, amounts to \$5.0 billion (net of accumulated depreciation). This investment in capital assets includes land, land improvements, buildings, vehicles and equipment, easements, roads, highways, and bridges. The total increase in capital assets for governmental activities was \$248.1 million (17.8%) and an increase of \$36.3 million (1.1%) for business-type activities.

Major capital asset events during the current fiscal year included the following:

- Completion of the New Castle County Courthouse (\$129.4 million), the archives center (\$15.3 million), new schools and improvements to existing schools (\$76.7 million) and the purchase of various parcels of land by the Division of Parks and Recreation (\$18.8 million). In addition, construction-in-progress as of June 30, 2003 was \$296.8 million for governmental activities. Of this amount, approximately 59.1% is related to the building of new schools and improvements to existing schools.
- As of June 30, 2003, the Department of Transportation had invested \$3,362.4 million in capital assets, including roads, bridges, buildings, land, and equipment. This amount represents a net increase (including additions and net of disposals, and depreciation) of \$36.3 million over June 30, 2002. A contributing factor to the increase of the Department's capital assets is the substantial completion of SR-1. In May 2003, the Department opened the final section of this 41 mile, fully controlled access, highway extending from a connection with the southern terminus of the new SR-1 toll road south of Wilmington, to points south of Dover on U.S. Routes 13 and 113. SR-1 is the largest public works project ever undertaken in Delaware.

State of Delaware Capital Assets as of June 30

Net of Depreciation

(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2003	2002	2003	2002	2003	2002
Land	\$ 286,424	\$ 265,155	\$ 11,230	\$ 11,230	\$ 297,654	\$ 276,385
Land Improvements	23,587	23,160			23,587	23,160
Buildings	914,996	525,653	33,016	33,419	948,012	559,072
Easements	66,822	64,344			66,822	64,344
Equipment and vehicles	50,568	50,652	91,761	80,297	142,329	130,949
Infrastructure			3,226,811	3,201,814	3,226,811	3,201,814
Construction-in-progress	296,798	462,119			296,798	462,119
Total	<u>\$ 1,639,195</u>	<u>\$ 1,391,083</u>	<u>\$ 3,362,818</u>	<u>\$ 3,326,760</u>	<u>\$ 5,002,013</u>	<u>\$ 4,717,843</u>

As allowed by GASB Statement No. 34, the State has adopted an alternative process for recording expense related to selected infrastructure assets. Under this alternative method, referred to as the modified approach, the State expenses certain maintenance and preservation costs and does not report depreciation expense. Assets accounted for under the modified approach include 11,057 center-line miles of roads and 1,386 bridges that the State is responsible to maintain.

The Department of Transportation performs condition assessments of eligible infrastructure assets at least every three years. Currently road condition assessments are conducted every year and bridge condition assessments are conducted, for the most part, every two years.

It is the Department of Transportation's policy to maintain at least 75 percent of its highways and bridge system at a Good or Better condition rating. No more than 10 percent of bridges and 15 percent of roads should be in substandard condition.

Of the State's 1,386 bridges that were rated in 2002, 1,011 or 72.9 percent received a Good or Better BCR rating, 19.7 percent were rated fair, and 7.4 percent received a substandard rating. Of the 8,653,408 square feet of bridge deck that was rated, 75.4 percent or 6,522,812 square feet received an OPC condition rating of Good or Better, 19.1 percent or 1,650,368 square feet received a fair rating, and 5.4 percent or 480,228 square feet received a substandard deck rating.

In 2002, when 4,175 centerline miles were rated, 76.6 percent received a Good or Better OPC rating, 13.6 percent received a fair rating, and 9.8 percent received a poor rating.

The 2003 estimate to maintain and preserve the Department of Transportation's infrastructure was \$129.2 million, but the actual expenditure was \$146.4 million, which is a \$17.2 million increase over the estimate. The variance is predominantly attributed to change orders necessary on jobs that were not estimated when the project was set up and budgeted.

The fiscal 2004 statewide capital budget totals \$576.6 million. Of that amount, \$268.9 million is allocated for non-transportation projects statewide and \$307.7 million for Transportation Trust Fund projects. Major non-transportation projects that will be completed during the upcoming year include the Carvel State Office Building renovations (\$14.9 million), the Stevenson House secure care facility (\$15.3 million), the new Delaware State Police Troop 2 facility (\$11.3 million) and the Smyrna Readiness Center (\$7.6 million).

Additional information on the State's capital assets can be found in Note 1 on pages 57-58, Note 12 on page 85 and on pages 114-115 of the Required Supplementary Information.

Long-term debt. At the end of the current fiscal year, the State had total general obligation bond debt outstanding of \$854.3 million, backed by the full faith and credit of the State. The Delaware Department of Transportation Trust Fund had revenue bonds outstanding of \$863.1 million. The bonds do not constitute a debt of the State or a pledge of the general taxing power or the faith and credit of the State. The Delaware Economic Development Office has \$.2 million of industrial development revenue bonds outstanding, which are supported by the full faith and credit of the State.

**State of Delaware Outstanding Debt
General Obligation and Revenue Bonds**
(Expressed in Millions)

	Governmental Activities 2003	2002	Business-type Activities 2003	2002	Total Primary Government 2003	2002
General obligation bonds	\$ 854.3	\$ 709.9			\$ 854.3	\$ 709.9
Revenue bonds	0.2	0.4	\$ 863.1	\$ 675.7	863.3	676.1
Total	<u>854.5</u>	<u>710.3</u>	<u>863.1</u>	<u>675.7</u>	<u>1,717.6</u>	<u>1,386.0</u>

The State of Delaware's total debt increased by \$144.4 million (20.3%) during fiscal year 2003. The key factors in this increase were public and higher education facilities, prison construction, State offices and other facilities. The State has undertaken a series of bond refundings, which have lowered the overall debt service on outstanding State general obligation debt. The State refunded \$132.7 million of its general obligation bonds in August 2002 and refunded another \$34.5 million in April 2003 for a combined cash flow savings of \$8.7 million.

Transportation Systems Revenue Bonds are issued with the approval of the State's General Assembly, and the State's Bond Issuing Officers (the Governor, the Secretary of Finance, the Secretary of State, and the State Treasurer) to finance improvements to the State's transportation systems. Approval by the General Assembly of the State is not required for the Transportation Fund to issue bonds to refund any of its bonds provided a present value debt service savings is achieved in such refunding. The sale must comply with the rules and regulations of the United States Treasury Department and the United States Securities and Exchange Commission.

At June 30, 2003, the Transportation Fund's debt increased by \$187.4 million (27.7%). During the past year, \$88.4 million of new money bonds were issued in August 2002 and \$85.3 million of bonds were refunded. In April 2003, \$140.5 million on new money bonds were issued and \$136.7 million of bonds were refunded. The bonds were insured and are rated AAA by Standard & Poor's and Aaa by Moody's. Of the 11 outstanding bond issues, three have an AA rating from Standard & Poor's and an A1 rating from Moody's. The remaining eight issues are rated AAA by S&P and Aaa by Moody's.

There is no State Constitutional debt limit; however, in 1991, the State enacted legislation to replace the previous statutory debt limits with a three-part debt limit, one of which restricts new debt authorization to 5% of budgetary General Fund revenue as projected on June 30 for the next fiscal year. Should revenue collections increase during the fiscal year, no additional authorizations are made. For further information concerning the State's debt limits, see page 127 of the Statistical Section.

Additional information on the State of Delaware's long-term debt can be found in Note 5 on pages 69-72 of this report.

Economic Factors and Next Year's Budgets and Rates

Fiscal year 2003's GDP was reduced from 2.8% growth forecasted in March 2003 to an estimated growth rate of 2.6% according to Global Insights. At 3.3% growth, the real GDP forecast for fiscal year 2004 reflects the economy's recent recovery. As of June 2003, the Department of Finance estimated that employment in Delaware had declined by 0.4% during fiscal year 2003. The most dramatic job losses occurred in the manufacturing sector.

A revenue enhancement package was passed at the conclusion of the 2003 Legislative session. House Bills 267 and 268 increased various corporate taxes and fees. House Bill 269 increased the State's share of video lottery proceeds, extends the video lottery operating hours and allows for additional video lottery machines at each licensed racetrack. House Bill 270 increased the cigarette tax from 24 to 55 cents per pack. The revenue package is expected to generate approximately \$143.0 million in new revenues.

The fiscal year 2004 operating and capital budgets meet budgetary spending limitations imposed by law. Although the budget reflects higher growth rates in revenues, the rate of growth in operating programs is expected to decline. Capital budget appropriations closed the gap, increasing from \$19.3 million in fiscal year 2003 to over \$142 million in fiscal year 2004.

Requests for Information

This financial report is designed to provide a general overview of the State of Delaware's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Accounting, 540 South DuPont Highway, Thomas Collins Building, Suite 3, Dover, Delaware 19901. Our CAFR can also be found on the "Department of Finance/Division of Accounting Home Page" at our Internet address: <http://www.state.de.us/account>.

The State's component units publish their own separately issued audited financial statements. These statements may be obtained from their respective administrative offices or from the Office of Auditor of Accounts, the Townsend Building, Suite #1, 401 Federal Street, Dover, DE 19901.