MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns Aaa to $100M Alaska GO bonds and MIG 1 to $163M BANS; outlook remains negative

Global Credit Research - 02 Mar 2015

Approximately $840M of GO, $290M of lease bonds and $870M of state moral obligation bonds outstanding

ALASKA (STATE OF)
State Governments (including Puerto Rico and US Territories)
AK

Moody's Rating

ISSUE		RATING
General Obligation Refunding Bonds, Series 2015B		Aaa
Sale Amount	$100,000,000	
Expected Sale Date	03/25/15	
Rating Description	General Obligation	
General Obligation Bond Anticipation Notes Series 2015A (Non-Callable)		MIG 1
Sale Amount	$162,700,000	
Expected Sale Date	03/10/15	
Rating Description	Note: Bond Anticipation	

Moody's Outlook NEG

NEW YORK, March 02, 2015 --Moody's Investors Service has assigned a Aaa rating to the state of Alaska's $100 million General Obligation Refunding Bonds Series 2015B, and a MIG 1 rating to $162.7 million General Obligation Bond Anticipation Notes Series 2015A. Concurrently, we have affirmed the Aaa rating assigned to the state's GO bonds, the Aa1 rating assigned to subject-to-appropriation debt, and the Aa2 rating assigned to the moral obligation bonds. The GO refunding bonds are expected to price on March 25 and the Bond Anticipation Notes (BANs) on March 10.

SUMMARY RATING RATIONALE

Accumulation of large financial reserves during a period of elevated oil prices left Alaska positioned to manage the potential fiscal challenges associated with its reliance on a volatile revenue source: petroleum. At the end of fiscal 2013, the state's two main reserve funds held more than $16.3 billion, or 2.7 times fiscal 2014 unrestricted general fund operating appropriations. The large size of the state's financial resources in relation to its annual expenditures has offset the fact that Alaska is far more vulnerable than any other US state to the global political, economic and other factors affecting oil supply and demand, as well as to local conditions influencing production. But just as the state has benefitted from high oil prices in recent years, prices well below previous expectations could lead the state to substantially reduce its financial reserves, eroding a key support to its Aaa rating.

OUTLOOK

The negative outlook signals that this year's rapid oil price decline, and expected prices below prior forecasts in coming months, will lead Alaska to substantially reduce financial reserves by the end of fiscal 2016. A rapid reserve-depletion scenario -- especially in the absence of feasible plans to rebuild reserve funds, to diversify tax revenue streams or to impose strict cuts on expenditures -- would be consistent with a lower credit rating.

WHAT COULD MAKE THE RATING GO DOWN

-- Sustained low oil prices relative to prior assumptions

-- Accelerating decline in petroleum production volume

-- Prospect that financial reserves will be fully depleted in the near term

-- Use of non-recurring measures beyond financial reserve expenditures to achieve budget balance

STRENGTHS

-- Very large cushion against revenue volatility in Constitutional Budget Reserve Fund (CBRF) and other funds

-- Conservative fiscal practices, highlighted by use of 2008 oil revenue windfall to rebuild CBR

-- Potential to transition over time to natural gas from oil production as primary revenue source

CHALLENGES

-- Narrow economic base

-- Political challenges to imposition of other significant revenue streams

-- Relatively weak pension funding, although funding will be improved by reserve transfers

RECENT DEVELOPMENTS

On February 5, the Governor released his amended budget for fiscal 2016 with an additional cut of $132 million to agencies' unrestricted general fund operating rating budgets. Total agency unrestricted general fund spending is now $240 million lower than the prior fiscal year and eliminates more than 300 positions. The legislature will approve the fiscal 2016 budget by mid-April.

DETAILED RATING RATIONALE

ECONOMY

Alaska's economy is concentrated in the energy and government sectors. Employment growth has turned negative, with the year-over-year change in payrolls negative in seven months during 2014, reflecting the contraction in the these sectors. However, federal government employment in Alaska has been declining since 2011. The state's labor market had outperformed the US in the recession and during the initial recovery, but job growth began to underperform the US in 2012. Personal income per capita remains strong, at 112% of the US, reflecting oil industry wealth.

FINANCES AND LIQUIDITY

To fund state government operations, Alaska relies on petroleum production taxes and royalties to a greater extent than any other oil-producing state. It derives about 90% of operating revenue from the oil industry, compared with 19% in New Mexico and 11% in Texas. Alaska began its 2015 fiscal year on July 1 projecting that the price of oil produced on its North Slope would hover above $100 per barrel, averaging $105.06. Instead, global supply and demand factors drove oil prices sharply lower this fall. By December 12, the price per barrel of Alaska North Slope crude was $59.50 per barrel, 47% below the $111.56 per-barrel price where it began the fiscal year.

Oil prices are inherently volatile; their exposure to global supply and demand factors and to geo-political conditions means that unexpected upswings and downturns are always possible. While Alaska has established a record of generally conservative price forecasts, we believe the state's current long-term expectation of a return to prices exceeding $100 per barrel may prove aggressive in view of other market projections. The most recent Moody's Investors Service forecast shows West Texas Intermediate crude at $62 per barrel in 2016 and gradually increasing to $74 per barrel in 2019. So far, production from the Bakken Formation and other high production-cost oil deposits shows little evidence of dropping in response to the changed global conditions. Even at $60 per barrel, about 20% higher than the current price, depletion of the CBRF could occur within three to four years, according to the state's forecast.

The budget enacted for the current fiscal year assumed that the state would draw $1.38 billion from the Statutory Budget Reserve Fund (SBRF), one of its main financial reserves. The fiscal 2015 budget was based on unrestricted general fund revenues of $4.52 billion, but collections are now forecast to come in 49% (or $1.9 billion) below that level. As a consequence of this and other factors, the state forecasts an unrestricted general fund deficit of $3.53 billion that will lead it to deplete the SBRF, which began the fiscal year with $2.79 billion. In addition, the state expects to use $740 million from the CBRF, which had $12.8 billion when the fiscal year began. Before the plunge in oil prices, the state passed legislation appropriating $3 billion from the CBRF to improve funding of the State of Public Employees' Retirement System and the Teachers' Retirement System (TRS). The total decrease in the CBRF this fiscal year is therefore estimated at $3.74 billion, or 29%. The state also now anticipates using CBRF funds to help balance a potential $3.64 billion deficit in the following year.

The state has already made significant reductions in its unrestricted general fund capital budget, which declined to $595 million in fiscal 2015 from $1.9 billion in fiscal 2013; this underscores the potential difficulty of achieving balance through spending cuts if oil prices remain below prior forecasts. Alaska's response to lower oil prices could include discussion of new recurring revenue sources. However, the state has not had a tax on individual income since 1980, and this well-established practice will pose a barrier to any moves in that direction. How the government ultimately decides to respond to the downturn in oil revenues will have implications for the state's credit ratings.

Liquidity

Alaska has strong liquidity with approximately $14.7 billion available to the general fund.

DEBT AND PENSIONS

Debt Structure

Alaska's debt is relatively low compared to other Aaa-rated states, with $1.2 billion net tax-supported debt, based on 2014 state medians. However, on a per-capita basis Alaska's net tax-supported debt is $1,573 and ranks 16th in the US, higher than the national median of $1,054. As a percentage of personal income, the state's net tax-supported debt ranks 19th among the states, at 3.2%, which is again higher than the 50-state median, 2.6%. The state's general obligation debt burden rose in fiscal 2013 to $840 million, but has declined in fiscal 2014 to $804 million.

Debt-Related Derivatives

No variable rate debt or swaps.

Pensions and OPEB

Alaska has an above-average employee pension burden among the states, based on unfunded liabilities for its share of multi-employer cost sharing plans. For the state's two biggest pension plans, based on our calculations, the state is responsible for 78.9% of ERS funding and 80.5% of TRS funding. Alaska's overall as-reported liabilities total $8.2 billion.

The state's adjusted net pension liability (ANPL), under our methodology for adjusting reported pension data, is $15.7 billion, or 99.3% of all governmental fund revenues, based on fiscal 2013 data, the fifteenth highest ANPL-to-revenue ratio. The ANPL also reflects 26.4% of the state's 2013 GDP. The state's three-year average ANPL ratio is 76.5%%, 18th highest among the states. Moody's adjusted net pension liability applies a bond index rate to determine the present value of plan liabilities, incorporates the market (rather than actuarial) value of plan assets, and makes certain other changes to improve comparability of reported pension liabilities. The adjustments are not intended to replace Alaska's reported liability information, but to improve comparability with other states. Alaska's share of liability for both pension plans was determined in proportion to its contributions to the plans.

The other postemployment benefits (OPEB) ARC is $460,000 as of June 30, 2014.

GOVERNANCE

Alaska utilizes multi-year financial planning and there is also financial flexibility with no constitutional caps on revenue raising or spending increases, as well as no super-majority requirements for budget passage and/or tax increases.

KEY STATISTICS

Per capita income relative to U.S. average: 112.3%

Industrial diversity (1=most diverse): 0.19

Employment volatility (U.S.=100): 41

Available balances as % of operating revenue (5-yr. avg.): 224.2%

NTSD/total governmental revenue: 7.3%

3-year avg. adjusted net pension liability/total governmental revenue: 76.5%

OBLIGOR PROFILE

Alaska is the 48th largest state, with a population of 736,000. Its GDP ranks 43rd among states.

LEGAL SECURITY

Both securities are backed by the full faith and credit of the state.

USE OF PROCEEDS

Both offerings will refinance prior issues. The long-term GO bonds will refinance $99.5 million of bonds issued in 2009 for interest cost savings estimated at $8.9 million on a present-value basis. The BANs will take out maturing BANs that were issued last year, which had in turn been issued to refinance 2013 BANs issued in connection with a state transportation bonding authorization.

RATING METHODOLOGIES

The principal methodology used in the general obligation rating was US States Rating Methodology published in April 2013. The principal methodology used in the lease-backed rating was The Fundamentals of Credit Analysis for Lease-Backed Municipal Obligations published in December 2011. The principal methodology used in the bond anticipation note rating was US Bond Anticipation Notes published in April 2014. The principal methodology used in the moral obligation rating was Moody's Approach to the Moral Obligation Pledge published in June 1999. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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