FITCH RATES ALASKA MUNICIPAL BOND BANK AUTHORITY'S $63MM GOS 'AA+'; RATING WATCH NEGATIVE

Fitch Ratings-New York-29 March 2016: Fitch Ratings has assigned a 'AA+' rating to approximately $63.3 million of Alaska Municipal Bond Bank Authority (bond bank) general obligation (GO) and refunding bonds, 2016 series two, issued under the bond bank's 2005 GO bond resolution. The rating is on Rating Watch Negative (RWN), which is expected to be resolved with the state's enactment of a budget for fiscal 2017.

The bonds are expected to sell via competitive bid on April 12, 2016.

SECURITY

The bonds are general obligations of the bond bank, for which the state also maintains a standing appropriation of state general fund resources to replenish the bonds' reserve fund in the event of borrower default. This standing appropriation is the basis for the assigned rating on the 2005 resolution bonds.

KEY RATING DRIVERS

STATE ANNUAL APPROPRIATION: The state of Alaska includes as part of its annual debt service appropriation in its operating budget an appropriation for reserve fund replenishment in the event of a draw related to default by a participating municipality (borrower), resulting in a rating one notch below the state's 'AAA' GO rating.

PROVEN STATE SUPPORT AND STRONG REPAYMENT HISTORY: The bond bank's programs have a solid history of debt repayment, and the state of Alaska has a demonstrated history of support for and involvement with the bond bank. The bond bank has consistently worked with the state to strengthen bondholder protections while achieving its programmatic goals. The state's own resources are substantial.

MULTIPLE LAYERS OF SECURITY: Multiple layers of security support bond bank issues in the event of a local government's failure to pay debt service on its obligations to the bond bank. Security enhancements include underlying borrower reserve funds in some cases, bond bank reserve funds, unrestricted assets of the bond bank held in the custodian account, the state's standing appropriation for reserve fund replenishment, the state's statutory moral obligation, and the bond bank's statutory authority to intercept state aid to local governments. Coverage of maximum annual debt service by state aid is substantial.

RATING SENSITIVITIES

The rating is sensitive to movement in the state of Alaska's GO bond rating to which it is linked. Fitch will resolve the Watch after analyzing the state's enacted budget for fiscal 2017, which begins on July 1.

CREDIT PROFILE

The 'AA+' rating is based on the state's commitment to GO bonds of the bond bank issued under the 2005 GO resolution in the form of a standing appropriation of general funds for program layers of security on both the borrower level and state level. Issuance requires either a borrower's GO or revenue pledge or other evidence of pledged revenues for allowable debt obligations, with a borrower reserve available for revenue bonds. Bond bank borrowers must demonstrate project essentiality and ability to repay in order to access financing. The current bonds will provide funding to two separate projects for Fairbanks North Star Borough and the City of Ketchikan; and refund outstanding bonds issued by the bond bank under the 2005 bond resolution.

The bond bank maintains a pooled program reserve fund for the 2005 resolution bonds, funded at approximately $53.6 million as of June 30, 2015. The reserve balance is expected to approximate $63 million following the current issuance, with funding comprised of cash deposits from available funds ($37.3 million), cash from bond proceeds ($15.5 million), and surety policies ($10.2 million), including an expected surety policy executed with this issue to meet the reserve fund requirement. The increased reserve requirement associated with the current issue may also include a combination of cash from the custodian account or bond proceeds, as well.

The program reserve fund is backed by a moral obligation of the state established by state statute requiring establishment of a reserve and requiring that the bond bank seek a general fund appropriation in the event of a borrower's payment default. This pledge was strengthened with the bond bank's commitment to seek a standing appropriation for these bonds and the state's subsequent appropriation, beginning in fiscal 2009.

The bond bank was established in 1975 to provide access to low-cost capital financing for Alaska local governments. Not inclusive of the current sale, approximately $987.9 million in 2005 GO resolution bonds are currently outstanding. The bond bank's limit for total bonds outstanding at any one time is almost $1.8 billion; including the current sale, total bonds and obligations outstanding is expected to be just over $1 billion, inclusive of debt issued under a 2010 bond resolution.

BROADENING OF BOND BANK SCOPE

The bond bank was authorized in 2014 to lend up to $87.5 million to the University of Alaska for heating and energy projects, secured by a general revenue pledge from the university. The full authorization for this purpose was issued in August 2015. Additionally, Senate bill 46 was enacted in the 2015 legislative session that permits the issuance of bonds or notes by the bond bank to state joint action agencies under the 2005 resolution. SB 46 also permitted the issuance of bonds or notes by a regional health organization; however, this issuance would occur under a separate indenture and is subject to certain requirements. While Fitch believes these changes do not impact the rating on the bond bank's obligations, Fitch notes the broadening of the bond bank's role beyond its original scope.

STRONG SECURITY PROVISIONS

As noted above, the moral obligation for the bonds was strengthened by inclusion in the state's annual budget, beginning in fiscal 2010, of an appropriation to restore any deficiency in the 2005 program reserve fund. An appropriation for this purpose was included in the enacted budget for the fiscal year that began on July 1, 2015 and is included in the governor's proposed budget for fiscal 2017. Further protections include a state intercept of local aid for borrowers and the ability to access the bond bank's unrestricted funds held in the custodian account. The custodian account, bolstered by recent state deposits, prior reserve releases, and funded at approximately $14.2 million as of Feb. 29, 2016, is expected to be maintained at this approximate level in future years, although direct loans by the bond bank and deposits to reserve funds may diminish the custodian account balance.

no payment defaults under the program to date. Program reserve funding is required at the IRS maximum and following the current issue, the bond bank will have three surety policies meeting about 16% of the funding requirement. The bond bank is considering a gradual move to reserve funding that will be equally comprised of cash and surety policies. Fitch will continue to review the use of surety policies for the reserve requirement in regard to its relationship to our criteria for these types of obligations while noting that the cash-funded custodial account remains available to the bond bank to cure reserve deficiencies.

State statute requires the bond bank chair to certify annually the sum necessary to restore the program reserve to the required level. The appropriation for program reserve replenishment is included in the state's annual operating budget. A supplemental resolution for the 2005 resolution bonds requires the bond bank to seek the appropriation annually.

ALASKA'S RESOURCE-DEPENDENT REVENUE SYSTEM

Alaska's 'AAA' GO rating reflects the state's maintenance of very substantial reserve balances and conservative financial management practices to offset significant revenue volatility linked to oil production from the North Slope and global petroleum price trends. For many years, the state focused on expected declines in production at its oil fields, prudently dedicating a substantial share of its past oil tax revenue to reserves to ease anticipated revenue loss due to the declines. However, the steep drop in crude oil prices beginning in late 2014 exceeded expectations and significantly reduced tax revenues to the state, requiring sizable use of reserves to fund operations in fiscals 2015 and 2016.

For the fiscal year that began on July 1, 2015, the state's budget planned for a $2.7 billion draw on reserves to fund operations; Fitch expects the draw could increase to almost $3.9 billion due to weaker than expected crude oil prices since the budget was enacted, including a recent decrease in expected revenue, contained in the preliminary spring 2016 revenue forecast. The spring forecast also reduced expected revenue for fiscal 2017 due to continued low oil prices; the forecast is not inclusive of the governor's proposed revenue measures.

The governor's recommended budget for fiscal 2017 fundamentally changes the way in which the state finances operations and attempts to shift volatility in the natural resource sector to the state's permanent fund (PF) and permanent fund earnings reserve from the unrestricted general fund. There are several additional fiscally prudent measures proposed in the $4.75 billion budget, including an over 50% cut to the annual PF dividend payment to residents, continued reductions in operating expenditures, and the implementation or increase in several taxes. The budget proposal is being discussed in the current legislative session.

For further information on the state, please see 'Fitch Places State of Alaska on Negative Watch; Rates GO Bonds 'AAA'' dated Feb. 29, 2016, available at 'www.fitchratings.com'.

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Date of Relevant Rating Committee: February 26, 2016

Fitch recently published an exposure draft of state and local government tax-supported criteria (Exposure Draft: U.S. Tax-Supported Rating Criteria, dated Sept. 10, 2015). The draft includes a number of proposed revisions to existing criteria. If applied in the proposed form, Fitch estimates the revised criteria would result in changes to less than 10% of existing tax-supported ratings. Fitch expects that final criteria will be approved and published by the beginning of the second quarter of 2016. Once approved, the criteria will be applied immediately to any new issue and surveillance rating review. Fitch anticipates the criteria to be applied to all ratings that fall under the criteria within a 12-month period from the final approval date.

Applicable Criteria
Exposure Draft: U.S. Tax-Supported Rating Criteria (pub. 10 Sep 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869942
Tax-Supported Rating Criteria (pub. 14 Aug 2012)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015
U.S. State Government Tax-Supported Rating Criteria (pub. 14 Aug 2012)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686033