FITCH RATES ALASKA MUNICIPAL BOND BANK AUTHORITY'S $113MM GOS 'AA'; OUTLOOK NEGATIVE

Fitch Ratings-New York-27 September 2016: Fitch Ratings has assigned a 'AA' rating to $113.075 million of Alaska Municipal Bond Bank Authority (MBBA; bond bank) general obligation (GO) and refunding bonds consisting of the following series:

--$84.455 million GO and refunding bonds, 2016 series three;
--$28.62 million GO and refunding bonds, 2016 series four (AMT).

The bonds are expected to sell via negotiation the week of Oct. 17, 2016.

The Rating Outlook is Negative.

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 'AA+' Issuer Default Rating (IDR).

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 remain substantial despite recent drawdowns to fund financial operations that have been stressed by a prolonged period of low crude oil prices.

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

LINKAGE TO STATE OF ALASKA: The rating on the bond bank's bonds is sensitive to movement in the state's Issuer Default Rating (IDR) to which they are linked.

NEGATIVE OUTLOOK: Failure to enact measures to improve fiscal balance will result in negative action on the state's IDR and linked ratings.

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 reserve fund replenishment. GO bonds issued under the 2005 resolution also incorporate multiple 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 a City and Borough of Juneau transit project; to the City of Ketchikan for a harbor project; and to refund outstanding bonds issued by the bond bank under the 2005 bond resolution for debt service savings.

The bond bank maintains a pooled program reserve fund for the 2005 resolution bonds, funded at approximately $62.9 million as of June 30, 2016. The reserve balance at that time was comprised of cash deposits from available funds ($36.6 million), cash from bond proceeds ($15.8 million), and surety policies ($10.5 million). Because of the reduction in debt service expense from refunding outstanding bonds, no additional deposit to the reserve fund is required by the current issue.

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 $1 billion 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 2010 and 2016 bond resolutions.

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 as well as for those of a regional health organization (RHO). RHO bond bank obligations are subject to certain limitations and requirements including a maximum outstanding debt limit of $205 million. The first issuance for an RHO under a separately secured, 2016 resolution occurred in May 2016 and the bond bank may issue bonds for a second RHO later this calendar year. While Fitch believes these bond issues 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 was included in the enacted 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 $11.2 million as of Aug. 31, 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.

Payments by the borrowers are due seven days prior to debt service payment; there have been no payment defaults under the program to date. Program reserve funding is required at the IRS maximum and the bond bank has three surety policies meeting 16.7% 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 'AA+' IDR 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 fiscal years 2015 through 2017.

The state's enacted budget for fiscal 2016 funded Unrestricted General Fund (UGF) expenditures of almost $5 billion, a 19% reduction as compared to fiscal 2015. The budget incorporated expected soft crude oil prices and was supported by a planned $2.7 billion draw from reserves. Actual crude oil prices that were below forecast combined with actions taken by the governor and legislature resulted in a larger $3.9 billion budget gap (75% of the UGF budget). The state funded the gap by drawing on reserves, bringing the reserve balance at year-end to $14.4 billion, equal to 2.8x the UGF budget.

The enacted UGF budget for fiscal 2017 totals $4.4 billion, a 16% reduction from fiscal 2016. The enacted budget continues the state's reliance on reserves to fund operations as most revenue raising proposals and a proposed funding shift related to the state's Permanent Fund Earnings Reserve (PFER) were not approved. The legislature did approve changes to the state's tax credit structure for crude oil and natural gas production to provide savings in future fiscal years, but at a cost of $430 million to the fiscal 2016 budget. The enacted fiscal 2017 budget incorporated the governor's veto of one-half of the statutorily-determined permanent fund dividend distribution, reducing the distribution from the PFER by $665 million. Considering these and other measures, the state anticipates a reserve draw of $3.17 billion (73% of the UGF budget) to fund operations. Due to the reduction in expenditures, reserves at the end of fiscal 2017 are expected to total $12.3 billion, equal to 2.8x the UGF budget.

For further information on the state, please see 'Fitch Downgrades Alaska's IDR to 'AA+'; Outlook Negative' dated June 14, 2016, available at 'www.fitchratings.com'.

Contact:

Primary Analyst
Marcy Block
Senior Director
+1-212-908-0239
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Douglas Offerman
Senior Director
+1-212-908-0889

Committee Chairperson
Karen Krop
Senior Director
+1-212-908-0661

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

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478