Fitch Ratings

FITCH RATES ALASKA MUNICIPAL BOND BANK AUTHORITY'S $50MM GOS 'AA'; OUTLOOK NEGATIVE

Fitch Ratings-New York-31 March 2017: Fitch Ratings has assigned an 'AA' rating to $49.51 million of Alaska Municipal Bond Bank Authority (MBBA; bond bank) general obligation (GO) bonds consisting of the following series:

--$12.56 million GO bonds, 2017 series one;
--$36.95 million GO bonds, 2017 series two (AMT).

The bonds are expected to sell via negotiation on or about April 13, 2017.

The Rating Outlook is Negative.

SECURITY

The bonds are general obligations of the bond bank, for which the state maintains an annual 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 annual 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 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 an annual 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 series 2017 series one bonds will provide funding to Kenai Peninsula Borough for improvements to Kenai Peninsula South Hospital and to the borough's Central Peninsula Landfill, and funding to the city of Seward for road improvements. The series 2017 series two bonds will provide funding for a port improvement project for the city of Unalaska and a small boat harbor project for the city of Whittier.

The bond bank maintains a pooled program reserve fund for the 2005 resolution bonds of approximately $66.6 million as of Dec. 1, 2016. The reserve balance at that time was comprised of cash deposits from available funds ($37.5 million), cash from bond proceeds ($11 million), and surety policies ($18 million). The bond bank intends that the amount of surety policies comprising the reserve fund will not exceed 50% of requirements but reports no current plans to approach that ceiling. 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. No additional deposit to the reserve fund is required by the current issue as existing assets, including cash and surety policies, exceed the post-issuance reserve requirement.

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 chair seek a general fund appropriation to restore the program reserve to the required level in the event of a borrower's payment default. This pledge was strengthened with the bond bank's commitment in 2009 to seek an annual standing appropriation for these bonds and the state's subsequent annual appropriations. There have been no payment defaults under the program to date.

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, almost $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 approximate $1.2 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. Two individual series of bonds totaling $144.85 million have been issued for RHOs under a separately secured, 2016 resolution. 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.

ADDITIONAL 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, 2016 and was included in the governor's proposed executive budget for fiscal 2018.

Payments by the borrowers are due seven days prior to a debt service payment; providing sufficient timing to access bond bank resources in the event of a missed payment. 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 was funded at approximately $11 million as of Feb. 28, 2017, 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.

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.

For fiscal 2016, the state funded a $3.4 billion (69% of the Unrestricted General Fund [UGF]) budget gap by drawing on reserves, bringing the reserve balance at year-end to about $14.7 billion, almost 3x the UGF budget. The enacted UGF budget for fiscal 2017 totals $4.4 billion, a 12% 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 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, a reserve draw of $2.9 billion (67% of the UGF budget) to fund operations is expected. Due to the reduction in expenditures and interest earnings, reserves at the end of fiscal 2017 are expected to total $14 billion, equal to 3.2x the UGF budget.

The governor's proposed $4.3 billion fiscal 2018 UGF budget is supported by almost $1.6 billion in existing revenue sources, $55 million in new revenue sources, a $2.5 billion use of funds from the PFER, and an $892 million draw on reserves. The budget also proposes a $2.4 billion use of funds from the PFER that would be retroactive to the current fiscal year. These actions incorporate the governor's proposed funding shift related to the PFER that is similar to proposals that have gained legislative traction in both the 2016 and 2017 sessions. The legislature is considering the budget proposal in the current session.

For further information on the state, please see 'Fitch Rates Alaska's $2.3B Pension Obligation Bonds 'AA'; Outlook Negative' dated Oct. 7, 2016, available at 'www.fitchratings.com'.

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Additional information is available on www.fitchratings.com

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