S&P Global Ratings

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Summary:

Alaska
Alaska Municipal Bond Bank; Appropriations; General Obligation; Moral Obligation

Primary Credit Analyst:
Timothy W Little, New York + 1 (212) 438 7999; timothy.little@spglobal.com

Secondary Contact:
David G Hitchcock, New York (1) 212-438-2022; david.hitchcock@spglobal.com

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Credit Profile		
US$18.195 mil GO bnds (Alaska) ser 2019 THREE due 10/01/2034		
Long Term Rating	AA-/Stable	New
US$4.21 mil GO bnds (Alaska) ser 2019 FOUR due 10/01/2029		
Long Term Rating	AA-/Stable	New
US$3.66 mil GO rfdg bnds (Alaska) ser 2019 FIVE due 10/01/2030		
Long Term Rating	AA-/Stable	New
Alaska GO		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Alaska Mun Bnd Bank, Alaska Alaska		
Alaska Mun Bnd Bank GO		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA-' rating to Alaska Municipal Bond Bank's (AMBB) approximately $25.8 million in 2005 master resolution general obligation (GO) bonds, series 2019 Three, Four, and Five (refunding). The bond bank is a public corporation of, and benefits from certain credit support by, the state of Alaska. The outlook is stable.

We also affirmed our 'AA' rating on the state of Alaska's GO debt outstanding, our 'AA-' rating on the state's lease appropriation-backed debt, our 'AA-' rating on AMBB debt secured through continuing appropriations and a moral obligation pledge from the state, and our 'A+' rating on bonds issued by the Alaska Energy Authority and backed by a moral obligation pledge from the state. The outlook on all ratings is stable.

The series 2019 Three, Four, and Five bonds are rated one notch off the state of Alaska's general creditworthiness based on a standing appropriation to replenish the debt service reserve (DSR) to its required level if there is a draw because of a borrower default. Our rating reflects the strength of the appropriation pledge and the legislature's demonstrated commitment to include the appropriation in the state's annual operating budget.

Alaska remains fiscally stable despite uncertainty

The trajectory of the state's fiscal reform pivoted in a different direction this year as a new gubernatorial administration advocated steeper expenditure cuts, restoring a full dividend payment to residents, and proposed fiscal reforms that may limit the state's budgetary flexibility.

The state has relied on reserves to balance its budget since fiscal 2015 when oil prices precipitously fell and have never fully recovered. Despite expenditure cuts from fiscal years 2013 to 2017 of 45%, the state's structural deficit swelled to 73% that year. However, the state maintained an extremely strong reserve position of approximately 380% of expenditures while its total available reserve position improved due to strong investment earnings in its Permanent Fund Earnings Reserve Account (ERA).

The state has made incremental progress on reforms since 2017 to improve its structural deficit and its revenue profile. Notable reforms over the past three years include:

- Moderating general fund expenditures growth as oil prices increased;
- A diminished Permanent Fund dividend to residents below the 1982 statutory formula that retains earnings in the ERA;
- Overall growth in total available reserves due to retained earnings in the ERA and strong investment returns above the fund's 6.5% target return; and
- Revenue diversification that now includes a statutory formula to draw from the ERA for general fund operations.

The adopted 2020 budget continues to advance the state's conversation on fiscal reforms, but greater uncertainty returned as to what a permanent fiscal profile for the state will look like. In our opinion, the provisions of the enacted budget, despite the governor's opposition to a diminished permanent fund dividend, provide near-term rating stability. While the enacted budget reduced Alaska's structural deficit to 3% of expenditures, the state restricted a sizable portion of funds ($4 billion) in the ERA by transferring it to the Permanent Fund corpus account. However, the reserve position is expected to remain at 380% of unrestricted general fund expenditures at the end of fiscal 2020, the same as in fiscal 2017.

In our opinion, political uncertainty remains a significant long-term factor weighing on the rating and has been since 2015. The length of time the state has taken to respond and adapt to its new fiscal environment of persistently low oil prices is a product of its vast available reserve balances, insulating it from more significant credit deterioration.

Political uncertainty has been an ongoing factor affecting the state's rating

Political discourse surrounding use of the ERA and the amount of a dividend residents should receive remains contentious and is unlikely to be resolved in the near term. Currently, the executive and legislative branches are divided on this issue.

Outside of the proposed budget, the governor has also advocated for several measures that, in our opinion, may limit budgetary flexibility. These initiatives include voter approval of new or increased revenues, restrictive expenditure caps, and protecting the state's Permanent Fund dividend payment to residents with a constitutional amendment (currently in statute). If approved by legislatures and voters this year, the earliest fiscal year this could take effect is fiscal 2022. Nevertheless, a higher legislative hurdle to approve revenue increases or retain earnings in the ERA may weaken our view of the state's revenue structure flexibility in its fiscal policy framework.

The state's next legislative elections will not occur until 2020. In our opinion, should the political make-up of the state change to where the legislative branch is in agreement on some of the governor's fiscal measures, we would likely take a more negative view of the state's credit trajectory.

Other factors affecting the state's general creditworthiness include:

- A countercyclical economy that demonstrates above-average unemployment rates compared to the nation and a weak demographic profile characterized by an increasing aging population and overall population declines;
- Economic and budgetary dependence on oil-related revenues that pressure the state's ability maintain budgetary balance;
- Proposed measures by the governor for voter approval of new or increased revenues, restrictive expenditure caps, and protecting the state's Permanent Fund dividend payment to residents with a constitutional amendment that, if adopted, may limit budgetary flexibility and slightly weaken our view of revenue structure flexibility in the state's fiscal policy framework;
- Very strong reserve position of between Constitutional Budget Reserve Fund (CBRF) and Permanent Fund ERA representing approximately 3x fiscal 2020 budgeted expenditures; and
- Strong debt and liability profile characterized by moderate debt levels and adequately funded pension and other postemployment benefit (OPEB) obligations.

Fiscal 2020 adopted budget

The state's enacted 2020 budget totals $5.5 billion in appropriations for operations, capital spending, and the Permanent Fund dividend. The budget is funded with an estimated $2.3 billion (42%) in oil-related revenues, $2 billion (37%) from the ERA for operations, $896.5 million (16%) from the ERA for the Permanent Fund dividend, and $156.7 million (3%) from the state's CBRF. The enacted budget marks the second consecutive year of using the ERA for operations and significantly reduced the state's draw from the CBRF. Use of the latter is primarily to fund the capital budget and may be mitigated based on the fund's investment returns for the year. From the budgeted expenditures, $4.2 billion applies to unrestricted general fund appropriations.

The fiscal 2020 budget is based on the Department of Revenue's (DOR) spring 2019 forecast of an average production of 530,000 barrels of oil per day at $66.00 per barrel. Actual price and production of amounts for the year have proven volatile and if not realized, could materially worsen the state's year-end results.

The state projects that at fiscal 2020 year-end, the undesignated reserves, consisting primarily of the ERA ($13.9 billion) and the CBRF ($2.3 billion) will be $16.2 billion. This includes expected investment returns into the ERA, use of the funds, and separate legislation to transfer $4 billion from the ERA to the corpus to essentially restrict those reserves from future use.

We estimate that based on enacted appropriations and estimated reserve balance at year-end 2020, the state is able to cover a very strong 380% of unrestricted general fund expenditures. Actual year-end amount will vary based on investment returns into the ERA and actual receipts of estimated oil-related revenues.

The expenditure base includes a dividend payment to residents of $1,600, below the formulary amount established in statute. This marks the fifth consecutive year of a reduced dividend payment. This year, the budget includes a number of expenditure cuts, with much of it applied to health and human services, particularly Medicaid. Some of the enacted expenditure cuts are likely to face legal challenges and budgeted savings may not be realized, which will affect year-end performance.

The governor has advocated retroactively paying residents the full dividend difference from prior years and for a full dividend this year. The dividend is paid from the ERA and a reduced dividend equates to retained earnings or higher reserve balances in the state reserve account and more funds available to fund government operations. We expect debate to continue as it has for some years, on how the state plans to fund government operations, pay a dividend operations, and adapt to a persistent economic state of low oil prices.

The series 2019 Three, Four, and Five bonds

The series 2019 Three, Four, and Five bonds are, respectively, the 44th, 45th, and 46th series to be issued under the AMBB's 2005 master bond resolution, which includes the annual standing appropriation feature that we view as integral to the strength of the bond program. Each year, AMBB is required to submit a budget request to the state for an appropriation to replenish the DSR to its required level if there is a draw because of borrower default. We have confirmed that the DSR balance required under the resolution is greater than any individual semiannual debt service payment. In recent years, the legislature has also appropriated any excess AMBB earnings to AMBB rather than to the state's general fund as otherwise required by statute.

We understand that, in practice, AMBB requires borrower loan payments be made seven business days in advance of bond debt service, and in the event of a default by the borrower(s), it would coordinate with state administrative staff to implement the appropriation and would draw on the DSR as debt service was due, which would immediately be replenished by the state. And because the debt repayments by local governments occur on a rolling basis throughout the year, the standing appropriation allows AMBB to replenish and maintain the DSR balance at its required level. Related to this credit strength, in our view, is the diversity of the pool provided by the 38 borrowers under the 2005 bond bank program.

In addition to the appropriation, AMBB has additional statutory authority to borrow funds from Alaska's general fund at the discretion of the commissioner of the DOR. As it has each year since 2009, the legislature included and the governor signed within the enacted operating budget an open-ended appropriation to AMBB's reserve in the event of a borrower default. The fiscal 2020 budget represents the 12th consecutive year the standing appropriation has been included in the state's operating budget to replenish the reserve should it be used and brought below the required level. However, the bonds are GOs of the AMBB, payable from sources pledged under the 2005 master resolution, which assigns borrower payments to the trustee for the repayment of the bonds. There has never been a borrower default in the history of the program or draw on the DSR.

Series 2019 Three and Four proceeds provide new-money loans to the City and Borough of Juneau for construction and capital improvements for the Juneau International Airport and to the Kenai Peninsula Borough to purchase new emergency response vehicles. The series Five proceeds allow the Kodiak Island Borough to refund a portion of its currently outstanding 2013 long-term care center revenue bonds (originally issued through AMBB).

No additional reserve deposit will be required for the 2019 Three, Four, and Five bonds as existing assets in the 2005 resolution reserve fund (including cash and DSR sureties) exceed the post-2019 issuance requirement, which, according to the 2005 resolution, is required to equal the lowest of 10% of the principal amount of bonds outstanding, 125% of average annual debt service on all the bonds outstanding, or maximum annual debt service (MADS). The bonds are GOs of AMBB, which receives revenue from a pool of loans to municipalities and investment earnings on assets.

According to the bond bank, with the sale of the 2019 Three, Four, and Five bonds, the 2005 reserve fund requirement is estimated at $61.9 million as of June 30, 2019, and sufficient to satisfy the reserve fund requirement, consisting of the following:

- $41.6 million of cash contributions from the custodian account (where AMBB holds retained earnings, current-year investment earnings, or unrestricted funds appropriated to it by the state);
- $2.3 million in reserve obligation proceeds of AMBB; and
- $18 million from a surety policy provided by National Public Finance Guarantee.

In addition to the appropriation support, the bonds are backed by Alaska's moral obligation pledge to maintain a DSR for the bank's bonds and by state aid withholding provisions that, since June 1988, have applied to both GO and revenue bonds issued by the bank. The 2005 resolution establishes a common reserve fund to comply with a state statute requiring a reserve fund for any bond bank bond issues. Per state statute, on or before Jan. 30 of each year, the bond bank is required to deliver a statement to the governor and state legislature stating the amount, if any, necessary to replenish the reserve fund. If a draw on the reserve fund were to occur, the state legislature might--but is not required to--appropriate funds to replenish it to the required amount. However, we view this provision as having been strengthened by the state's standing appropriation to backfill the DSR in the event of a draw due to a borrower default.

In the event of a borrower default on a loan payment, the 2005 master resolution permits AMBB to pursue an intercept of any grant aid from the state to the borrower. The grant intercept provision further strengthens the bonds' credit quality, in our view. AMBB tracks the amount of state grants subject to intercept relative to the annual loan payment due by each borrower.

Based on the analytic factors evaluated for Alaska, on a four-point scale of '1.0' (as the strongest) to '4.0' (as the weakest), S&P Global Ratings has assigned a composite score of '2.0' to the state, which is associated with an 'AA' indicative credit level.

For more information on the state's general credit worthiness, see our full analysis on Alaska, published April 2, 2019 on RatingsDirect.

Outlook

The stable outlook reflects our view of Alaska's continued use of its ERA for operations based on a structured draw outlined in statute. The state's ability to ease its reliance on oil-related revenues and reduce its structural deficit is an important factor for its future credit trajectory. It has been able to insulate itself from significant credit deterioration due to its vast reserve balances of approximately 3.8x expenditures, which provides rating stability.

While the state has made strides to improve its fiscal position in recent years, proposed measures by the current administration to limit budgetary flexibility may leave it more vulnerable to fiscal stress when oil prices decline. However, a change in our opinion of the state's government framework would depend on if and when various proposed reforms would be adopted. If adopted, we view such measures as placing an undue burden on the state's fiscal flexibility as it continues to adapt to a new fiscal environment.

While our outlook on the state remains stable, downward pressures exists from potential reforms to limit budgetary flexibility and potential deterioration of reserves if the state were to fully fund prior-year dividend reductions and further transfer significant amounts from the ERA to the Permanent Fund corpus. Political discourse surrounding use of the ERA and the amount of a dividend residents should receive remains contentious and is unlikely to be resolved in the near term. The state's next legislative elections will not occur until 2020. In our opinion, should the political make-up of the state change to where the legislative branch is in agreement on a majority of the governor's fiscal measures to limit budgetary flexibility and reduce reserves in the ERA, we would likely take a more negative view of the state's credit trajectory.

Upward movement on the rating will depend on the state's ability to grow and maintain its reserve levels while eliminating its structural deficit. Despite the large reserve balances, Alaska is more sensitive to economic volatility than its peers due to its unique revenue structure, which requires it to maintain above-average reserve levels. The rating could further benefit from economic diversification and an improved demographic profile. However, should unanticipated economic shocks reduce budgetary flexibility or weaken its ability to further structurally align its budget, we may lower the rating.

Ratings Detail (As Of September 18, 2019)		
Alaska approp		
Long Term Rating	AA-/Stable	Affirmed
Alaska GO		
Long Term Rating	AA/Stable	Affirmed
Alaska GO		
Long Term Rating	AA/Stable	Affirmed
Alaska Energy Auth, Alaska		
Alaska		
Alaska Energy Auth (Alaska) (Bradley Lake Hydroelec Proj) MORALOB		
Long Term Rating	A+/Stable	Affirmed
Alaska Mun Bnd Bank, Alaska		
Alaska		
Alaska Mun Bnd Bank (Alaska) APPROP		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP FOUR		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP FOUR		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP ONE		

Ratings Detail (As Of September 18, 2019) (cont.)		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP THREE		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP THREE		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP THREE		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP TWO		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) APPROP (AMBAC)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) GO bnds		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) GO bnds		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) GO (AMT)		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) (Master Resolution) APPROP		
Long Term Rating	AA-/Stable	Affirmed
Alaska Mun Bnd Bank (Alaska) (Master Resolution) GO		
Long Term Rating	AA-/Stable	Affirmed
Matanuska-Susitna Borough, Alaska		
Alaska		
Matanuska-Susitna Boro (Alaska) APPROP		
Long Term Rating	AA-/Stable	Affirmed
Preliminary Rating	NR(prelim)	
Matanuska-Susitna Boro (Alaska) APPROP		
Long Term Rating	AA-/Stable	Affirmed
Matanuska-Susitna Boro (Alaska) APPROP (ASSURED GTY)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.