

RatingsDirect®

Summary:

Alaska Municipal Bond Bank; General Obligation; Moral Obligation

Primary Credit Analyst:

Gabriel J Petek, CFA, San Francisco (1) 415-371-5042; gabriel.petek@standardandpoors.com

Secondary Contact:

David G Hitchcock, New York (1) 212-438-2022; david.hitchcock@standardandpoors.com

Table Of Contents

Rationale

Outlook

Related Criteria And Research

Summary:

Alaska Municipal Bond Bank; General Obligation; Moral Obligation

Credit Profile

US\$155.065 mil GO and rfdg bnds (Alaska) ser 2015 THREE due 10/01/2044

Long Term Rating

AA+/Negative

New

Alaska Mun Bnd Bank, Alaska

Alaska

Alaska Mun Bnd Bank (Alaska) GO and rfdg bnds (Alaska) ser 2015 THREE due 10/01/2044

Long Term Rating

AA+/Negative

Outlook Revised

Alaska Mun Bnd Bank GO

Unenhanced Rating

AA+(SPUR)/Negative

Outlook Revised

Rationale

Standard & Poor's Ratings Services revised its outlook to negative from stable on Alaska Municipal Bond Bank's (AMBB) debt following the outlook revision on the state. In addition, Standard & Poor's assigned its 'AA+' long-term rating, and negative outlook, to AMBB's \$155.1 million of general obligation (GO) bonds, 2015 series three. At the same time, Standard & Poor's affirmed its 'AA+' long-term rating and underlying rating (SPUR) on AMBB's debt outstanding. The bond bank is a public corporation of, and benefits from certain credit support by, the state of Alaska (AAA/Negative).

The ratings reflect our view of the strength of the appropriation pledge and the legislature's demonstrated commitment to include the appropriation in the state's annual operating budget.

The bonds are issued under AMBB's 2005 general bond resolution, which includes a standing appropriation feature that we view as integral to the strength of the bond program. Each year, the AMBB is required to submit a budget request to the state for an appropriation to replenish the debt service reserve (DSR) to its defined level if there is a draw because of borrower default. As it has each year since 2009, in fiscal 2016, 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 legislature also appropriated any excess AMBB earnings to the AMBB rather than retain the funds for the state government. With the fiscal 2016 operating budget, the state has now included for eight consecutive years a standing appropriation in its operating budget to replenish the reserve should it be used and brought to below the required level.

We understand that, in practice, AMBB requires loan payment seven business days in advance of bond debt service, and in the event of a default by one or more of its underlying local government borrowers, it would coordinate with state administrative staff to implement the appropriation and would draw upon the DSR as debt service was due, which would immediately be replenished by the state. (It would simultaneously pursue a remedy to the default through

its authority to intercept state aid payments to the borrowing government as provided for in state statute.) And because the debt repayments by local governments occur on a rolling basis throughout the year, the standing appropriation allows AMBB to replenish and to 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 31 borrowers under the 2005 bond bank program.

In addition to the appropriation, AMBB also has additional statutory authority to borrow funds from Alaska's general fund at the discretion of the commissioner of the department of revenue.

During the 2015 legislative session, the state legislature approved Senate Bill 46, which allows AMBB to lend to Joint Action Agencies (JAAs) under the existing borrowing limit and up to \$205 million to "regional health organizations" (RHOs) under a separate borrowing limit. RHOs are nonprofit entities created through state statute for the purpose of delivering health care to state residents, in particular to the Alaskan Native population. Pursuant to Senate Bill 46, AMBB would only be allowed to make loans to an RHO insofar as the Commissioner of the State's Department of Health And Social Services anticipates that the loan would improve the quality of care while reducing costs to the state. For example, providing care locally to patients located in rural locations could reduce transportation- and lodging-related expenses, a portion of which would otherwise fall to the state. AMBB participation in RHO financings is limited to no more than 49% of a project's cost, where the balance of project funding is secured and no more than \$102.5 million per project. JAAs are a form of public utility created per state statute when two or more public utilities purchase power from a power project owned or formerly owned by the Alaska Energy Authority. The legislation also includes some technical amendments to AMBBs governing statutes that are intended to enhance the consistency of terminology with regard to AMBB's borrowers.

The 2015 series three bonds are the 33rd series of bonds issued under the 2005 general bond resolution. The bond bank estimates that, not including the 2015 series three bonds, it will have \$924.7 million of bonds outstanding. Once the 2015 series three bonds have been issued, the bond bank estimates it will have \$1.04 billion in bonds outstanding. Of this, approximately \$1.02 billion will have been issued under the 2005 general bond resolution. There will also be \$2.5 million in AMBB GO bonds issued under its 1976 general bond resolution still outstanding. The AMBB has indicated these will be retired in February 2016. In addition, there will be \$4.2 million under the 2010 general bond resolution, as well as \$10.4 million of Coastal Energy Impact Loan Program obligations outstanding.

The 2015 series three bond proceeds will be used to make loans to:

- The University of Alaska, for a combined heat and power plant at its Fairbanks campus;
- The Haines Borough for upgrades at the Haines High School;
- Two loans to Kodiak Island Borough to expand Kodiak High School and for various renovation projects at borough schools;
- The city of King Cove to finance construction of a hydroelectric facility; and
- Refinance up to \$59 million of prior AMBB loans to four communities issued under the 2005 resolution and to refund prior AMBB reserve bonds.

The bond bank plans to use, for the first time, a surety policy to fund the increase in the common DSR 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. The

bonds are general obligations of AMMB, which receives revenue from a pool of loans to municipalities and investment earnings on assets. According to the bond bank, as of June 30, 2015, the 2005 reserve fund market value was approximately \$53.6 million, an amount sufficient to satisfy the reserve fund requirement. Approximately \$40.9 million of the DSR fund has been funded by a contribution from the custodian account, and \$17.8 million has been funded by reserve obligation proceeds of AMBB. The custodian account is where AMBB holds retained earnings, current-year investment earnings, or unrestricted funds appropriated to AMBB by the state. According to the bond bank, as of June 30, 2015, the custodian account market value balance was \$14.6 million.

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 established 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. The state aid withholding provisions under the bond bank statute say that aid to municipalities will be withheld and paid directly to the bank if the participating unit defaults in the payment of principal or interest on its bonds held by the bank. The state aid intercept mechanism further strengthens the bonds' credit quality in our view. The AMBB tracks the amount of state aid subject to intercept relative to the annual loan payment due by each borrower. In all cases, the amount of state aid subject to intercept is greater than the amount of loan payments due by the borrowers. For fiscal 2016, projected coverage on the loan payments provided by the state aid intercept ranges from 2.78x to 3,134x.

For more information on the state GO rating, see the article published Aug. 18, 2015, on RatingsDirect.

State budget update

Alaska's fiscal structure and budgetary context is unique among the states. Because the state's unrestricted general fund is heavily reliant on petroleum-related revenue, this segment of its finances has deteriorated throughout fiscal 2015 in response to the sharp and largely unanticipated decline in global oil prices. As of early February, Governor Bill Walker's administration estimates a large operating deficit of almost \$3.6 billion for fiscal 2015 in the state's unrestricted general fund (58% of authorized spending).

We have maintained our rating throughout the year despite the fiscal imbalance because of the state's extraordinary budgetary reserve balances. At \$17.3 billion, the state's budget reserves equal 344% of the state's fiscal 2015 expenditures. The reserves serve as a critical fiscal cushion that, in effect buy the state time to develop a strategy for closing its structural gap. Because we view the situation as unsustainable, however, it will require significant fiscal adjustment in order for the state to maintain its rating. Therefore, we assigned a negative outlook to the rating on the state's GO and appropriation-backed debt.

Outlook

The negative outlook mirrors the outlook on our rating on the state of Alaska's debt. The outlook reflects the large structural budget deficit in Alaska's unrestricted general fund. Currently, the state is able to finance its operating deficits by withdrawing funds from its extraordinarily large budget reserves. The outsized reserves have thus far shielded the state's credit quality from the degradation that the large deficits would inflict on most states' credit quality. But the magnitude of the fiscal deficits makes the arrangement unsustainable and, unless corrected, inconsistent with the current rating.

The typical lag that exists between the enactment of fiscal policy adjustments and when they yield results implies the need for lawmakers to act early. Therefore, even with its reserve balances at still-strong levels, we would likely lower the rating on the state rating even within the next year if lawmakers defer enacting corrective fiscal policy adjustments.

In the event policymakers continued to take no action, the initial rating change could represent the first step in a downward migration that would likely accelerate as the state's reserve balances approached depletion. If lawmakers succeed in putting the state on what we view as a glide path to a sustainable fiscal structure, with its strong reserve balances still intact, we could maintain the rating.

Related Criteria And Research

Related Criteria

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- USPF Criteria: U.S. Public Finance Long-Term Municipal Pools, March 19, 2012
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011
- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Moral Obligation Bonds, June 27, 2006
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006

Ratings Detail (As Of August 18, 2015)

Alaska Mun Bnd Bank, Alaska

Alaska

Alaska Mun Bnd Bank (Alaska) GO

<i>Long Term Rating</i>	AA+/Negative	Outlook Revised
-------------------------	--------------	-----------------

Alaska Mun Bnd Bank (Alaska) GO and rfdg bnds (Alaska) ser 2014-3 due 10/01/2049

<i>Long Term Rating</i>	AA+/Negative	Outlook Revised
-------------------------	--------------	-----------------

Alaska Mun Bnd Bank (Alaska) GO and rfdg bnds (Alaska) ser 2015 ONE due 10/01/2039

<i>Long Term Rating</i>	AA+/Negative	Outlook Revised
-------------------------	--------------	-----------------

Alaska Mun Bnd Bank (Alaska) GO (AMBAC)

<i>Unenhanced Rating</i>	AA+(SPUR)/Negative	Outlook Revised
--------------------------	--------------------	-----------------

Alaska Mun Bnd Bank (Alaska) Moral Ob 2015A-B TWO

Ratings Detail (As Of August 18, 2015) (cont.)

<i>Long Term Rating</i>	AA+/Negative	Outlook Revised
Many issues are enhanced by bond insurance.		

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2015 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.