FitchRatings

Fitch Rates Alaska's $165MM GOs 'AAA'; Upgrades Outstanding GO Debt to 'AAA'

Ratings Endorsement Policy
07 Jan 2013 2:39 PM (EST)

Fitch Ratings-New York-07 January 2013: Fitch Ratings assigns an 'AAA' rating to general obligation (GO) bonds of the state of Alaska (the state), consisting of the following:

--$11.945 million GO bonds, series 2013A (taxable qualified school construction bonds - direct payment);
--$153.215 million GO bonds, series 2013B.

The bonds are expected to sell via negotiation the week of Jan. 14, 2013.

Fitch upgrades to 'AAA' from 'AA+' the rating on approximately $575.8 million of outstanding state of Alaska GO bonds.

In addition, Fitch upgrades the ratings on the state's appropriation-backed debt and other related debt, which are detailed at the end of this release.

The Rating Outlook is Stable.

SECURITY

General obligations to which the full faith, credit and resources of the state are pledged.

KEY RATING DRIVERS

VERY LARGE RESERVES: Alaska has set aside very large reserves for general fund operating needs, principally in the Constitutional Budget Reserve Fund (CBR) and Statutory Budget Reserve Fund (SBR). The state has used recent windfalls from high oil prices to repay past CBR draws and remains committed to maintaining sizable reserves, a key rating factor given forecasted declines in oil production over time. The state's reserves provide multiple times coverage of its debt obligations.

CONSERVATIVE FINANCIAL MANAGEMENT: Conservative financial management is critical given the state's dependency on energy-related revenues and the volatility of energy prices and production. Fitch expects Alaska to prudently manage its reserve funds and promptly adjust its expenditures as needed, consistent with the state's historical practice.

ECONOMY AND FINANCES DEPENDENT ON NATURAL RESOURCES: While both natural resources and the federal government have provided sources of employment and income to Alaska's small population, the volatility inherent in the natural resource industry is the state's area of vulnerability. Petroleum-related revenue accounts for approximately 92% of unrestricted General Fund revenue.

MANAGEABLE LIABILITY POSITION: Alaska's debt burden is moderate. The state has prudently used available cash to fund its capital needs and cash-defeased outstanding obligations when cost-effective. Although the funded ratios of Alaska's major statewide pension systems are weak, the state has undertaken significant pension reforms and closed its defined benefit plans to new employees in 2006. In addition, about half of the state's other post-employment benefit (OPEB) obligations are pre-funded.

CREDIT PROFILE

The upgrade of Alaska's GO rating to 'AAA' from 'AA+' reflects the state's maintenance of very substantial and growing reserve balances and the continuation of conservative financial management practices at a time of strong revenue performance. State revenues are linked closely to oil production from the North Slope and global petroleum price trends, exposing the state to significant revenue volatility. Mitigating this risk, state fiscal practices are generally conservative, with the state dedicating a substantial share of oil-related revenue to reserves and employing long-range forecasting of revenues and expenses. Reserve balances have grown exponentially over the past several fiscal years, and Fitch believes the state is committed to keeping reserve levels high. Development of a natural gas pipeline from the North Slope, completion of which would help diversify state revenues, continues, with a settlement agreement reached with several large gas developers in March 2012. Debt practices are conservative, with limited issuance and average amortization. The economy remains stable. Although the state has potential exposure to federal employment cutbacks tied to budget pressures at the federal level, its revenue system limits its budget exposure.

RESOURCE-DEPENDENT REVENUE SYSTEM

Alaska's economic and financial performance is tied closely to its natural resource base, with 92% of unrestricted general fund revenues derived from petroleum-related activity estimated for fiscal year (FY) 2013. Fluctuating global energy prices in 2007, 2008, and 2009, led to sharp surges and drops in the state's unrestricted general fund revenues in the related fiscal years. Revenues have grown sizably since fiscal 2009 along with petroleum prices, enabling sizable growth in the state's various reserve funds. The CBR and SBR together have grown from $8.1 billion in FY 2009 to $15.9 billion in FY 2012 and the fund balance of the state's permanent fund has increased from $29.9 billion to $40.3 billion over this same time frame.

FY 2012 North Slope West Coast oil prices averaged $112.65 per barrel; well over the $94.70 per barrel forecast on which the budget was based. On a GAAP basis, FY 2012 ended on June 30 with a $3.8 billion general fund surplus, bringing the general fund balance to $21.6 billion; more than 2 times total general fund expenditures. In addition, there was a $192.8 million net positive fund balance change in the state's permanent fund, increasing the fund to $40.3 billion. The fall 2012 forecast projects FY 2013 oil prices at $108.67 per barrel; down from the $110.44 per barrel on which the budget was based. The revised estimate for oil production is also slightly lagging forecast in FY 2013; 0.553 bbl/day now anticipated, down from 0.563 bbl/day forecast.

The fall 2012 revenue forecast points to unrestricted general fund revenue in FY 2013 landing behind budget due to these lagging results. FY 2013 unrestricted general fund revenues are forecast at $7.57 billion, as compared to $7.7 billion in anticipated expenditures. The state maintains several options to close this modest forecast gap in addition to reducing discretionary expenditures, such as capital projects and statewide supplemental expenses.

The governor recently proposed a fiscal 2014 operating budget that forecasts oil prices increasing slightly to $109.61 per barrel, with a slight decline in oil production assumed. Fiscal 2014 unrestricted general fund revenues are forecast at $7 billion, a 6.8% decline from anticipated revenues in FY 2013. The proposed $6.5 billion in recurring and discretionary appropriations is 14.3% less than the prior year, primarily due to a $1.1 billion proposed cut in capital expenditures. The proposal includes a $508 million transfer to the SBR. The budget proposal will be considered in the 2013 legislative session. Fitch also expects the governor to pursue reforms to the oil tax structure, with the goal of encouraging additional investment and drilling to increase future oil production, and will review the details as they emerge.

VERY LARGE RESERVE FUNDS

As noted above, the state has prudently set aside much of its revenue windfall in the CBR and SBR. Deposits of surplus funds as well as dedicated petroleum dispute settlement funds have brought the CBR's balance to over $11 billion. The SBR has grown to $5.5 billion and over $1 billion has been set aside for prefunding school formula payments. Additional balances available to the state include realized earnings of the $40.3 billion Alaska Permanent Fund, measuring almost $3 billion. These reserves may be accessed by the state by a majority vote of the legislature; with access to the CBR restricted to a three-fourths majority vote of the legislature should the general fund not be in a deficit situation. The pre-funded balance for education, equal to about one year of education expense, does not require a vote of the legislature for its use.

The state's fall 2012 forecast of increasing future oil prices combined with declines in production is expected to result in fairly steady but modest unrestricted general fund revenue losses through the FY 2022 forecast period. Should the state take no action to reduce its recurring and discretionary general fund expenditures and baseline spending growth continue, the state forecasts General Fund operating deficits would begin in FY 2015 and grow through the forecast period (FY 2022), resulting in the use of the SBR through the period of the forecast to balance operations until the reserve is depleted in FY 2020.

In the forecast, the CBR continues to grow through the forecast period until 2021, peaking at $16 billion. The permanent fund earnings reserve (PFER) is also expected to grow through the forecast period, reaching $7 billion in FY 2022. On a combined basis, these three reserve funds have a forecast peak of $23 billion in FY 2019, declining to $21 billion in FY

2022. General fund expenses in FY 2022 are forecast at $8.6 billion, compared to $7.7 billion in the current fiscal year and $6.5 billion proposed for FY 2014. Fitch expects the state to prudently manage the application of these reserves, if such action is warranted, and realign its discretionary expenditures as necessary.

MANAGEABLE LIABILITY POSITION

The state is an infrequent debt issuer, meeting most capital needs from current revenues. The debt burden as of June 30, 2012 is manageable, with $894 million in net tax-supported debt measuring 2.7% of personal income after excluding guaranteed debt of the Housing Finance Corporation, which has never required state support, and reimbursable school debt. The debt burden will increase to 3.2% when including the current issue. Expected borrowing for state transportation projects will also increase the debt to per capita income ratio, although Fitch notes that as the majority of state debt is repaid from petroleum-related revenue the debt-to-income ratio is not as meaningful for Alaska as for other states.

The pensions for two major statewide systems, for general public employees and for teachers, were funded at 63% and 54.1%, respectively, as of June 30, 2011 based on the systems' 8% investment return assumption. Using Fitch's more conservative 7% assumption, the funded ratios decline to 56.2% and 48.9%, respectively. OPEBs alone are funded at 50.4% for general public employees and 48.1% for teachers, as of June 30, 2011. The state has undertaken multiple pension reforms in recent years, including switching to a defined contribution plans for new employees beginning July 1, 2006 and legislation enacted in 2007 obligating the state to assume local governments' contributions over a fixed percentage of payroll. Additional pension reform discussions are ongoing and Alaska has no stated plan to issue up to $5 billion in pension obligation bonds that were authorized in 2008.

As noted above, Fitch upgrades the ratings on the state's appropriation-backed debt and other related debt, which are listed below:

--Approximately $11.4 million state of Alaska state certificates of participation to 'AA+' from 'AA';
--Approximately $16 million municipality of Anchorage state lease revenue bonds to 'AA+' from 'AA';
--Approximately $216 million Matanuska-Susitna Borough state lease revenue bonds to 'AA+' from 'AA';
--Approximately $600 million Alaska Municipal Bond Bank GO bonds (2005 bond resolution) to 'AA+' from 'AA';
--Approximately $4.6 million Alaska Municipal Bond Bank GO bonds (2010 bond resolution) to 'AA' from 'AA-'; and
--Approximately $47.8 million Alaska Municipal Bond Bank bonds issued under various bond resolutions to 'AA' from 'AA-'.

The Rating Outlook is Stable.

State certificates of participation and state lease revenue bonds are backed by the state's appropriation commitment for debt service and therefore rated one notch below the state's GO rating.

State bond bank obligations incorporate multiple layers of security on both the borrower level and at the state level. For additional information on the bond bank, please see 'Fitch Rates Alaska Municipal Bond Bank GOs 'AA' dated Sept. 11, 2012.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria', dated Aug. 14, 2012;
--'U.S. State Government Tax-Supported Rating Criteria', dated Aug. 14, 2012.

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