

# MOODY'S

## INVESTORS SERVICE

### **New Issue: MOODY'S ASSIGNS Aaa RATING TO THE STATE OF NEW MEXICO'S \$19.9 MILLION GENERAL OBLIGATION BONDS SERIES 2011**

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Global Credit Research - 18 Apr 2011

#### **OUTLOOK IS STABLE**

State  
NM

#### **Moody's Rating**

<b>ISSUE</b>	<b>RATING</b>
Capital Projects General Obligation Bonds, Series 2011	Aaa
<b>Sale Amount</b>	\$19,970,000
<b>Expected Sale Date</b>	04/19/11
<b>Rating Description</b>	General Obligation

#### **Opinion**

NEW YORK, Apr 18, 2011 -- Moody's Investors Service has assigned a Aaa rating to the State of New Mexico's \$19.9 million General Obligation bonds Series 2011. The bonds are expected to sell on or around April 19. Proceeds of the Series 2011 bonds will be used to finance various statewide capital projects. The outlook is stable.

#### **Rating Rationale**

The rating reflects the state's history of well-managed fiscal operations, the volatility of energy sector-related revenues and its impact on the general fund, expenditure pressures associated with the state's low-income population, and the state's historic focus on maintaining reserves at healthy levels. The one-notch rating distinction for the lease revenue bonds reflects non-appropriation risk associated with the lease revenue repayments supporting the debt.

#### **Credit Strengths:**

- Historic trend of well-managed finances
- Maintenance of budget reserves
- Limits on G.O. debt issuance and generally short debt maturities

#### **Credit Challenges:**

- Higher than average dependence on government and energy sectors, with a small, concentrated state manufacturing base that relies heavily on the high-tech sector, and reliance on relatively volatile energy-related state revenues
- High debt ratios relative to Moody's 50-state median
- Moderate pension funding levels

#### **DETAILED CREDIT DISCUSSION**

#### **FISCAL 2011 REVENUES FORECAST TO INCREASE**

New Mexico's general fund recurring revenues are projected to grow by 7.6% during the current fiscal 2011, after experiencing a decline of 9.8% in fiscal 2010. The revenue weakness in fiscal 2010 was a result weakness in general and selective sales tax as well as continued weakness in severance tax revenues. The

state utilized roughly \$312 million of federal stimulus funds along with \$173 million in budget reserve funds, and spending reductions to balance the budget in fiscal 2010. Revenue' growth in 2011 primarily reflects an increase in the sales tax rate put in place during the 2010 legislative session. Expenditures are forecast to decline 4% from fiscal 2010, this does not incorporate the additional 3.2% agency reduction implemented after the start of fiscal 2011. The state is on track to end fiscal 2011 with \$264 million in general fund budget reserves, approximately 5% of revenues.

The general fund budget for fiscal 2012 which was finalized and signed into law in early April assumes a 4.8% recurring revenue increase. The fiscal 2012 budget amounts to \$5.4 billion, reflecting a modest 1.5% reduction in K-12 education funding, a shift of 1.75% of state pension contributions from employer to employees, and a reduction in a film tax credit. The enacted budget projects general fund reserves of \$293 million (5.4%) at fiscal 2012 year end.

New Mexico's general fund revenues are made up mainly of sales taxes (43% in fiscal 2011), income taxes (25%), and energy-related taxes (15%). General fund revenues are also enhanced by interest earnings derived from the state's two large permanent funds, the Severance Tax Permanent Fund, which receives severance tax revenues not required for debt service on severance tax bonds and the Land Grant Permanent Fund, which receives royalty revenue from mineral production on state lands and was created to support educational and other social service needs. These funds provide significant income to the general fund and cushion state finances against energy-related revenue volatility. In fiscal 2011 interest income will be about 12% of total general fund revenues.

#### NEW MEXICO ENJOYS FULLY FUNDED GAAP BALANCES AND ADEQUATE BUDGET RESERVE LEVELS

The states' 2010 CAFR shows ending fund balances of \$387.8 million, approximately 8% of fiscal 2010 audited revenues. New Mexico has a long history of positive ending fund balances, reaching a peak of 14.8% in fiscal 2006. It is expected that the state will continue the trend of positive fund balance at the close of fiscal 2011. The state has also maintained positive budgetary reserves as well, which is notable given the impact the economic downturn had on state finances in fiscal 2009 and fiscal 2010.

#### JOB GROWTH HAS DECLINED; UNEMPLOYMENT IS RISING BUT STILL BELOW NATIONAL LEVEL

Annual state job growth has declined, as in much of the nation, since 2008. New Mexico's employment showed a slight gain of 0.3% in 2008 vs. a decline of -0.59% for the U.S., followed by a 3.9% employment decline in 2009 and flat employment in 2010. The state is expected to have minimal employment growth of 0.2% in 2011 followed by modest growth in the out-years. Unemployment remains a problem in the state having risen from 8.5% in September 2010 to 8.7% in February 2011 versus 8.9% for the U.S. The 8.7% unemployment rate for the state represents a significant jump for New Mexico, which averaged roughly 4% unemployment in 2008.

New Mexico's economy had been diversifying away from a dependence on mining and government, with the state experiencing growth in the trade, services, and construction sectors. Energy-related and government employment, however, still account for a higher percentage of total jobs as compared to the US. The government sector makes up about 24.5% of total state non-farm payroll employment, as compared to about 17% for the nation. Federal government employment, whether through direct federal government jobs or affiliated private sector employment, has long been an important component of the state economy that has provided a cushion against weakening in other sectors.

The state's reliance on energy-related employment, and on energy-related revenues, introduces some volatility to the state's financial operations, as this sector produces major swings. However, the state has also benefited from growth in this sector at times when other sectors have shown weaker performance. Currently the sector is experiencing mixed results, with oil production increasing and natural gas production decreasing. Both oil and gas prices are expected to rise in fiscal 2012.

#### ABOVE AVERAGE STATE DEBT BURDEN

Moody's 2010 State Debt Medians Report indicates that New Mexico's debt ratios are above national medians, with net-tax supported debt at 4.1% of personal income and net-tax supported debt per capita at \$1,398, versus state medians of 2.5% and \$936, respectively, for these ratios. The above average debt ratios largely reflect the state's transportation revenue bond program.

New Mexico's state employees are covered by two pension plans: the Public Employees Retirement

Association and the Educational Retirement Board. These were 78.5% and 65.7% funded, respectively, as of their most recent valuation dates (June 30, 2010). The funded ratio is modest within the Aaa category, however the state has taken steps recently, such as increasing employee and employer contribution rates in the Education Retirement Fund which will benefit that pension plan.

The New Mexico Retiree Health Care Authority administers other post-employment benefits (OPEB) coverage for retired state workers. According to the state, authorizing legislation would allow benefits currently offered to be modified or even eliminated by the state legislature. Based on preliminary figures and benefits currently offered, the state's unfunded OPEB liability is about \$3.3 billion.

### **Outlook**

The rating outlook for New Mexico is stable. The outlook reflects Moody's expectation that the state will continue its history of sound financial management through the current downturn, and continue to maintain reserves to buffer against additional economic pressure or unexpected expenditure needs.

What could change the rating DOWN

- Aggressive economic assumptions regarding the energy sector, upon which the state is highly dependent.
- A shift away from the state's well-managed operations towards trends including depletion of reserves and reliance on non-recurring resources for budget balance
- Significant deterioration in the funding of state pension systems

The principal methodology used in this rating was Moody's State Rating Methodology published in November 2004.

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