MOODY'S INVESTORS SERVICE

New Issue: Moody's assigns Aaa to $150M New Mexico GO Bonds

Global Credit Research - 12 Feb 2015

Approximately $397.6M GO bonds outstanding; outlook stable

NEW MEXICO (STATE OF)
State Governments (including Puerto Rico and US Territories)
NM

Moody's Rating

ISSUE		RATING
Capital Projects General Obligation Bonds, Series 2015		Aaa
Sale Amount	$150,000,000	
Expected Sale Date	02/17/15	
Rating Description	General Obligation	

Moody's Outlook STA

NEW YORK, February 12, 2015 --Moody's Investors Service has assigned a Aaa rating to the State of New Mexico's Capital Projects General Obligation Bonds, Series 2015, to be issued in the amount of $150 million. Following the issuance of these bonds, the state will have approximately $397.6 million of general obligations bonds outstanding, all rated Aaa. The outlook on these ratings is stable.

SUMMARY RATINGS RATIONALE

The Aaa rating on New Mexico's general obligation bonds reflects its strong General Fund financial performance. Due to timely spending cuts and conservative budgeting for volatile energy-related revenues, General Fund balances remained positive through the economic downturn and have returned to pre-recession levels. Pension liabilities, while notable, are below the medians for US states. The state's GO bonds represent only a small portion of its net tax-supported debt and benefit from strong security provisions. Balanced against these strengths are below-average wealth levels and financial reporting weaknesses.

OUTLOOK

The rating outlook for the state's general obligation bonds is stable, reflecting the expectation that the state will maintain relatively stable reserves despite the volatility of its economy.

WHAT COULD MAKE THE RATING GO DOWN

* A significant and sustained reduction in reserves

* Deterioration in unemployment rates or other economic indicators

* Failure to make planned improvements in financial reporting practices

STRENGTHS

* General Fund financial performance has been strong.

* Conservative revenue forecasting offsets the volatility of energy-related employment.

* Debt levels are moderate; pension liabilities are below average for US states.

* General obligation bonds benefit from rapid payout and strong security features.

CHALLENGES

* Economic diversity is relatively low, with concentration in energy and government employment.

* Financial reporting lacks characteristics typical of Aaa-rated states.

RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

ECONOMY

The state's economy is concentrated in volatile oil and gas extraction, and government. Economic activity and the state revenues vary considerably based on the prices of oil and gas, the levels of production, and the amount of new drilling. The government presence is primarily attributable to the presence of two national laboratories and several major military facilities. Per-capita income is below average, at 81.5% of the US level.

For the most part, oil and gas activity was fairly strong during the economic downturn and federal employment remained a stabilizing factor, moderating the effect of the recession on New Mexico compared to other states. The peak-to-trough decline in housing prices was smaller in New Mexico than in the US as whole. The state's unemployment rate remained consistently below the US rate and below the median for comparably rated states throughout the recession. Although state General Fund revenues fell in fiscal years 2009 and 2010, New Mexico's revenue declines were less than in most other states.

After stalling in 2013, largely due to federal cutbacks, growth in the state accelerated in 2014. Nevertheless, job creation still lags the US and the state's unemployment rate is tracking above the US rate. The impact of federal budget cuts on government employment in the state remains a risk.

FINANCES AND LIQUIDITY

As a result of the state's better-than-average economic performance during the downturn, its generally conservative approach to forecasting energy-related revenues, and the enactment of timely spending cuts, the state's financial performance has been strong. The General Fund balance was drawn down in fiscal year 2009 but remained at $390 million, or 5.7% of revenues. The state has been rebuilding reserves since that year and, based on the statements for the statutory General Fund, the fund balance equaled $674 million, or 11.7% of revenue, at the end of 2014, comparable to pre-recession levels. Based on its December 2014 revenue forecast, fund balances are projected to decline by approximately $18 million in fiscal year 2015.

The state's general fund revenues are very sensitive to the price of oil and natural gas, and the recent drop in oil prices will constrain state spending as it prepares its budget for fiscal year 2016. The governor's proposed budget for 2016 was based upon the state's December revenue forecast, which forecast revenue growth of 1.3% for fiscal year 2015 and 2.8% for 2016. These forecasts reflected assumed oil prices of $71 and $66 per barrel in fiscal years 2015 and 2016, respectively. This month, the state updated its forecasts, lowering its assumptions for oil prices to $61 and $56. The drop in oil-related revenues was slightly offset by strength in other areas, but overall revenue forecasts have been lowered to 1.2% for 2015 and 2.0% in 2016. The adopted budget will be based on these updated forecasts.

Liquidity

Liquidity levels are strong. The balance in the treasurer's general investment pool exceeded $2 billion at the end of December. The state has not issued TRANs since fiscal year 2011.

DEBT AND PENSIONS

Debt Structure

Based on Moody's 2014 debt medians report, New Mexico's debt levels have declined. Net tax-supported debt as a percent of personal income was 3.4%, a decline from 5.6% over three years but still above the 2.6% median for all US states. Net tax-supported debt per capita was $1,406, compared to a median of $1,054. General obligation bonds represent only a small portion, 14.8%, of the state's $2.5 billion net tax-supported debt, the majority of which consists of transportation revenue bonds and severance tax bonds.

The state's general obligation bonds are issued with a maximum maturity of 10 years. As a result, payout is extremely rapid; approximately 60% of principal will be repaid in three years. The general obligation bonds also benefit from strong security features. The bonds are paid from a statewide property tax levy without limit as to rate. The treasurer is required to keep tax proceeds separate from all other funds. The state's practice is to levy the tax in advance so that debt service is pre-funded.

Debt-Related Derivatives

The state has no derivatives related to its general obligation or severance tax bonds. The New Mexico Department of Transportation has $420 million in interest-rate swaps related to its variable rate transportation revenue bonds issued through the New Mexico Finance Authority. The swaps hedge interest rate risk but add counterparty risk and make it difficult for the state to reduce its variable rate exposure. The termination value for the swaps as of November 10, 2014, was $106.6 million. DOT maintains a $50 million line of credit with Bank of America, N.A. to meet any collateral posting requirements on the swaps.

Pensions and OPEB

The state's pensions are primarily provided through the multi-employer Public Employees Retirement Association (PERA). PERA's funding levels have declined in recent years due to investment losses and changes in its earnings assumption. Moody's three-year adjusted net pension liability (ANPL) for the state through 2013 is $6.5 billion. This ANPL equaled 48.9% of fiscal 2013 revenues, slightly below the 52.8% median for all US states.

The state also reports a UAAL for other post-employment benefits (OPEB) of approximately $3.4 billion. The UAAL represent 29.6% of state governmental revenues, above the 15.7% median for all US states.

GOVERNANCE

While the state has several strong governance practices including a consensus revenue forecasting process, multi-year revenue and expenditure projections, and timely budget adoption, its financial reporting has numerous weaknesses and is not characteristic of Aaa-rated issuers. Historically, the financial statements in New Mexico's Comprehensive Annual Financial Report (CAFR) were not audited. The statements were only "reviewed," which indicates a substantially lower standard of verification. In addition, the CAFRs have not always been released on a timely basis. The fiscal year 2011 CAFR was not released until June 2012, 11 months after the end of the fiscal year. The 2012 CAFR was not released until August 2013, 13 months after the end of the fiscal year.

Fiscal year 2014 marked some progress for the state's financial reporting. For the first time the CAFR was audited. Nevertheless, significant weaknesses remain. The audit contained numerous findings related to cash reconciliations and consolidations. And the CAFR was still not timely. The state is committed to a number of initiatives to eliminate the findings and improve the timeliness of the CAFR. It has also established a $100 million reserve to cover adjustments necessary to resolve the cash reconciliation discrepancies. Moody's expects that the state will make continued improvement in its financial reporting.

The state does provide timely, audited financial statements for its major agencies and for its statutory General Fund. The statutory General Fund, also known as the "Component Appropriation Accounts" or the "Component Appropriation Funds," is not exactly equivalent to the GAAP-basis General Fund shown in the CAFR. In particular, it excludes certain departmental revenue accounts that are included in the GAAP General Fund. Even so, the two representations of the General Fund have tracked very closely. These agency statements provide sufficient verified information to evaluate the state's financial performance, but the absence of timely, unqualified comprehensive statements remains a weakness.

KEY SCORECARD STATISTICS

Per capita income relative to U.S. average: 81.5%

Industrial diversity (1=most diverse): 0.7

Employment volatility (U.S.=100): 104

Available balances as % of operating revenue (5-yr. avg.): 6.7%

NTSD/total governmental revenue: 18.9%

3-year avg. adjusted net pension liability/total governmental revenue: 48.9%

OBLIGOR PROFILE

New Mexico is the 36th- largest state by population, at 2.1 million. Its state gross domestic product, $92.2 billion, is 37th-largest . The state's wealth levels are below average, with per capita personal income equal to 81.5% of the US level and a poverty rate among the highest for US states.

LEGAL SECURITY

New Mexico's general obligation bonds are secured by the full faith and credit of the state and specifically secured by and paid from a statewide property tax levy without limit as to rate. The treasurer is required to keep tax proceeds separate from all other funds. The payment of general obligation bonds from other than ad valorem taxes collected for that purpose requires an appropriation by the legislature. If at any point there is not a sufficient amount of money from ad valorem taxes to make a required payment of principal of or interest on state general obligation bonds, the governor may call a special session of the legislature in order to secure an appropriation of money sufficient to make the required payment.

USE OF PROCEEDS

Proceeds of the bonds will be used to fund construction, acquisition or improvement of various projects approved by voters on November 4, 2014, including senior citizen centers, libraries, and higher education facilities.

PRINCIPAL RATING METHODOLOGY

The principal methodology used in this rating was US States Rating Methodology published in April 2013. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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