FitchRatings

FITCH RATES ALBUQUERQUE, NM'S $23MM UNLIMITED TAX BONDS 'AA+'; OUTLOOK STABLE

Fitch Ratings-Austin-23 February 2017: Fitch Ratings has assigned a 'AA+' rating to the following Albuquerque, NM bonds:

--$22.9 million general purpose bonds, series 2017A.

Bond proceeds will fund various public improvements and pay issuance costs. The bonds are scheduled to sell competitively on March 6.

The Rating Outlook is Stable.

SECURITY
The general purpose bonds are payable from an annual unlimited property tax levy.

KEY RATING DRIVERS

The city's 'AA+' Issuer Default Rating (IDR) and bond ratings reflect ample revenue flexibility, demonstrated spending control, a modest long-term liability burden, and the maintenance of structural balance. Management's prudent budgeting of its resource base benefits the city's prospects for maintaining structural balance through economic cycles.

Economic Resource Base
Albuquerque is the largest city in New Mexico, accounting for about one-quarter of the state's population. The city's population grew a notable 21.6% from 2000 to 2010, although recent growth trends have been very modest, resulting in an estimated population of 559,121 in fiscal 2016.

Revenue Framework: 'aaa' factor assessment
The pace of revenue growth will likely modestly exceed inflation due to modest population growth and uneven economic expansion. Gross receipts tax revenue-raising flexibility is ample.

Expenditure Framework: 'aa' factor assessment
Fitch expects the pace of expenditure growth to generally track revenue gains. Expenditure flexibility is aided by prudent budgeting and moderate carrying costs for debt service and retiree benefits.

Long-Term Liability Burden: 'aaa' factor assessment
The combined overall debt and unfunded pension liability burden is modest at approximately 9% of personal income. Debt comprises the majority of the liability. Modest direct debt plans and overlapping debt issuances may increase the overall liability burden, but Fitch expects it to remain modest.

Operating Performance: 'aaa' factor assessment
Operational flexibility during economic downturns is derived from the city's ample gross receipts taxing margin and solid spending control, supplemented by state-required reserve levels.

RATING SENSITIVITIES

Shift in Fundamentals: The IDR and GO bond rating are sensitive to material change in the city's strong revenue-raising and expenditure flexibility and solid financial position, which Fitch expects the city to maintain throughout economic cycles.

CREDIT PROFILE

The broad-based economy is led by the government, healthcare/education, and trade/transportation/utilities sectors. Key federal installations include Kirtland Air Force Base and Sandia National Laboratories (SNL) in which troop strength and direct jobs account for a manageable 5% of the MSA's employment base. SNL has attracted a highly educated workforce to the area, but it is vulnerable to budget restrictions and shifts in defense spending priorities.

The area's high-tech hub includes firms engaged in microelectronics (Intel, Raytheon) and aerospace (Boeing and Eclipse Aerospace). Intel's workforce in nearby Rio Rancho (IDR of 'AA') has declined to 1,900 from 3,300 since 2013. Plans are underway for a $600 million replacement of the University of New Mexico Hospital, which is scheduled to start construction in 2017.

The area's recovery from the last economic downturn has been tepid. Employment gains have been stagnant, but the unemployment rate remains in line with the U.S. average. Median home values continue to rise moderately but remain below their peak in 2007 as are building permits.

Revenue Framework
The city's operating revenues are heavily dependent on municipal and state-shared gross receipts taxes (GRTs) which comprise 64% of general fund revenues, followed by property taxes (16%). A trend of moderate GRT revenue growth is likely to continue as recent private investments and associated job gains are partially offset by the uneven performance of the city's employment sectors such as manufacturing.

Fitch expects the city's revenues to grow modestly above the level of inflation (CPI) but below the pace of U.S. GDP based on the city's historical trends.

The city retains ample revenue flexibility in the form of various local-option municipal GRTs that it can impose without a voter referendum. The largest unutilized GRT is the 3/8% hold-harmless GRT, which was authorized by the state in conjunction with the elimination of hold-harmless appropriations for state-shared GRT exemptions on food and medical expenses. The 3/8% hold-harmless GRT would generate $115 million in additional revenue, equal to a large 24% of fiscal 2016 general fund revenues.

Recessionary pressures on the city's revenues were exacerbated by reductions in the local option GRT rate and lapses in GRT levy authority. The city reduced its GRT by 0.125% in fiscal 2008 and authority for a 0.25% GRT lapsed for five months in fiscal 2010.

Expenditure Framework
General fund expenditures are led by public safety which comprises 51% of spending.

The city's pace of spending is expected to remain in line with revenue gains but pressured by growing public safety spending and the service pressures of a population base with a moderately elevated poverty rate.

A high 81% of the city's workforce is represented by labor unions. Management maintains a large degree of control over headcount, but wages and benefits are negotiated through labor contracts. Management can ultimately impose its terms after following a structured framework in the event of an impasse. The terms of the labor contracts are typically one to two years and only one group's contract is currently expired and under negotiation. The city's fixed-cost burden is moderate, with carrying costs for debt, pension and other post-employment benefits equal to 18% of governmental spending.

Long-Term Liability Burden
The long-term liability burden (comprised of ULT bonds, GRT bonds, overlapping debt, and the net pension liability) is low at 9% of personal income. Direct debt, overlapping debt, and the net pension liability each contribute about one-third of the liability. Future direct debt issuance plans are manageable. The city's practice is to hold biennial GO bond elections for about $120 million which management expects to supplement with additional GRT debt issuances. Coupled with a rapid 10-year principal amortization rate (75% of ULT and GRT principal), the city's measured debt plans should keep its liability burden at a modest level.

Full-time city employees participate in the Public Employees Retirement Association (PERA) of New Mexico, a cost-sharing multiple employer defined benefit pension plan. PERA reforms effective in 2013 increased contribution rates and established a new tier of benefits for new hires. The city funds its actuarially-determined pension contribution, and the unfunded pension liability is $671 million (adjusted to reflect a 7% rate of return assumption) or 3% of personal income.

Operating Performance
The city's strong financial resilience is derived from a combination of revenue and expenditure flexibility and solid reserve levels.

The fiscal 2016 audit posted a modest $3.4 million (0.7% of spending) drawdown due to one-time spending and GRT revenue trends that came in modestly under budget (2.2% growth vs. budgeted 3%). The resulting unrestricted fund balance totaled $59.9 million or 11.9% of spending, exceeding the state-required reserve level of one-month (8.3%).

The revised fiscal 2017 budget balances recurring revenues and expenditures but includes a $16 million drawdown (3% of spending) due to one-time spending. However, management typically outperforms its projections, and Fitch expects the city will make progress toward reducing the projected use of reserves. The revised budget projects GRT revenue growth of 2.3%, which Fitch believes is reasonable.

Aggressive budget cuts in the wake of the last recession allowed the city's finances to post operating surpluses in four out of the last seven fiscal years. If adjusted for capital outlays, balanced operations or net surpluses were recorded in every year of that period.

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In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478