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April 23, 2014

Ms. Teresa Byrd
Deputy County Manager of Finance
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Dear Ms. Byrd:

Fitch Ratings has assigned one or more ratings and/or otherwise taken rating action(s), as detailed in the attached Notice of Rating Action.

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FITCH RATES BERNALILLO COUNTY, NM GO BDS 'AAA'; OUTLOOK STABLE

Fitch Ratings-Austin-21 April 2014: Fitch Ratings assigns an 'AAA' rating to the following Bernalillo County, NM (the county) bonds:

--$8.7 million general obligation (GO) improvement bonds, series 2014;
--$3.2 million GO refunding bonds, series 2014A.

The bonds are expected to sell competitively during the week of April 21.

In addition, Fitch affirms the following Bernalillo County ratings:

--$112.9 million in outstanding GO bonds at 'AAA';
--$137.2 million in outstanding gross receipts tax (GRT) revenue bonds at 'AA+'.

The Rating is removed from Negative Watch and assigned a Stable Outlook.

SECURITY:

The GO bonds are secured by an unlimited annual property tax levy on all taxable property within the county. The GRT bonds are secured by the county's 1st 1/8th GRT for general purposes and the county's 2nd 1/8th GRT for general purposes, excepting $1 million annually (at the rate of $83,333 per month) for indigent care.

KEY RATING DRIVERS:

LIQUIDITY CRUNCH RESOLVED: The Stable Outlook reflects the restoration of ample liquidity which had deteriorated significantly due to a shift to long-term investments by the county's elected treasurer. The county's entire portfolio has been restructured into cash, eliminating significant interest rate risk.

INVESTMENT POLICIES TIGHTENED: The board of county commissioners' and treasurers' new investment policy includes greater oversight of security purchases, restricts average maturity to three years, and requires solid monthly cash balances, which Fitch views positively.

GENERALLY STRONG FINANCIAL PROFILE: The county's financial management is otherwise sound, as evidenced by very large reserves, conservative biennial budgets, and attention to out-year financial projections.

SLUGGISH GRT REVENUES: The county's role as New Mexico's principal population center has resulted in a large GRT revenue base. Sparked by the home building bust in 2008, GRT revenues have declined moderately in recent years, although recent trends indicate stabilization of this revenue source.

SOLID GRT COVERAGE: Debt service coverage of the county's GRT revenue bonds remains solid; furthermore, legal and practical limitations on further leverage are strong.

FAVORABLE DEBT PROFILE: The county's debt profile remains positive, as evidenced by modest debt levels, a rapid GO bond principal payout rate and modest capital plans.

BROAD ECONOMY: The county's economic base is broad but has been slow to recover recessionary employment losses. The unemployment rate remains moderate. The county's recent development into a high-tech hub may aid its recovery while further enhancing economic diversity.

RATING SENSITIVITIES:

LARGE DEFENSE INSTALLATIONS POSE VULNERABILITY: The large presence of military and defense installations exposes the city's economic base to proposed military downsizing. Any resulting financial impact on the city's revenue base without offsetting actions could lead to downward rating pressure.

CREDIT PROFILE:

As the state's largest county, population grew a notable 19% from 2000-2010 and currently exceeds 670,000; the increase was spurred in part by the area's recent development as a hub for high technology. The city of Albuquerque comprises about 80% of the county's population.

LIQUIDITY CRUNCH RESOLVED BUT INVESTMENT LOSSES AFFECT RESERVES
The Stable Outlook reflects the administration's recent actions to restore ample liquidity to its large fund balance reserves. In February 2014, Fitch placed the county on Rating Watch Negative due to a deviation from past investment practices by the current and past county treasurers that led to increased investments in long-term securities. Such practices resulted in a very long average maturity of over 11 years despite reliance on those funds for operations. The resulting liquidity crunch led the county to sell a portion of its investments before maturity, resulting in $12.8 million in unrealized losses in fiscal 2013, equal to 5% of spending. Realized losses rose to $17 million on a portfolio of $268 million in the current fiscal year as the county restructured its entire investment portfolio with the aid of an independent investment advisor. All of the county's funds are now in cash and no additional restructuring will be required.

As part of its reform efforts, the board of county commissioners and the county treasurer approved a new investment policy that requires a new board subcommittee to review and approve all security purchases recommended by the county's elected treasurer, restricts average maturity to three years, and mandates that ample monthly cash balances (equal to 15% of annual appropriations) be available with maturities limited to 30 days. The new policy also requires investments be laddered to match the county's cash needs. Fitch expects such reforms will help mitigate the operational risks associated with an independent elected treasurer.

STATE AUDIT IN PROGRESS
A special audit of the county's treasurer's office has been ordered by the New Mexico state auditor. The special audit, now being conducted by an independent audit firm, will make recommendations to improve the county treasurer's internal controls and management related to investment transactions. Fitch will monitor the findings and management's response.

SUBSTANTIAL FINANCIAL CUSHION
Other elements of the county's financial profile remain very strong, characterized by large reserves. Effective fiscal 2012 the county supplemented its state-mandated three-month reserve for subsequent year's expenditures with a two-month contingency reserve, which Fitch views favorably.

As planned, the county funded significant one-time expenditures and capital outlays in fiscal 2013. Although up to $60 million of such outlays were approved, only $21.8 million was used for such purposes. Together with a nearly $13 million unrealized investment loss incurred by the county's portfolio restructuring, fiscal 2013 posted a large $26 million net deficit (10% of spending). Despite the drawdown, fiscal 2013's total financial cushion, comprised of its unrestricted fund balance and the three-month reserve, totaled a very high $179 million or 69% of spending.

Due to additional portfolio restructuring losses and planned one-time expenditures, fiscal 2014 is projected to post another large drawdown, totaling $19 million (6% of spending). Considered a worst case scenario by management, such a drawdown would still result in an ample fund balance of $161 million or 52% of spending.

The proposed fiscal 2015 budget, to be adopted as part of the fiscal 2015-2016 biennial budget, is balanced and based on 3% growth assumptions for property taxes and GRT,s which Fitch considers reasonable based on recent trends. In response to large investment losses incurred in fiscals 2013-2014, the budget does not include any general fund one-time expenditures. GRT revenues account for 40% of general fund revenues, exposing the county to economically volatile taxes, but this risk is largely offset by the county's healthy fund balances.

SLUGGISH GRT RECOVERY

The GRT is imposed on businesses upon the sale of goods or services, subject to certain exemptions, making it broader than the typical sales tax. Record high homebuilding activity helped fuel GRT growth that averaged roughly 7% annually from fiscal 2003-2007. However, for fiscal years 2008-2011, collections fell by 3% - 4% annually due to the significant contraction in home building activity and the completion of numerous major construction projects. GRT receipts rebounded moderately in fiscals 2012-2013 and year-to-date receipts point to continued slow recovery. Management expects this revenue stream to continue to recover slowly, evidence of a conservative budgeting approach viewed favorably by Fitch.

STRONG DEBT SERVICE COVERAGE OF GRT BONDS

Debt service coverage of the county's GRT revenue bonds remains solid at nearly 3x maximum annual debt service (MADS) based on audited fiscal 2013 revenues. The GRT bonds' debt service reserve requirement is standard, although its additional bonds test is strong - requiring pledged revenues to equal 2x MADS of existing and proposed GRT-secured debt. The county does not plan to further leverage this revenue source as it relies on residual revenue for operations.

MODEST FUTURE DEBT PLANS

The county maintains a formal capital improvement plan, the local portion of which has historically been financed with voter-approved GO bond authorizations every two years. County voters approved a $20 million authorization in November 2012 by wide approval margins. The combined GO and GRT bonds payout rate is very rapid at 76% in 10 years. Including GO bonds and GRT obligations, overall debt levels equal a low $1,797 per capita and a moderate 2.2% of full market value.

SLOW EMPLOYMENT RECOVERY

MSA employment has been slow to recover from recessionary declines, remaining flat in 2013 after posting a modest gain in 2012 and moderate declines during the recent recession. However, the county's 2013 annual unemployment rate remained moderate at 6.4%, below the state average (6.9%) and the U.S. average (7.4%). Recent commercial projects include a new Lowe's customer support center projected to add 900 jobs over two phases and the planned expansion of Eclipse Aviation with 100 jobs.

The proposed federal 2015 budget includes downsizing the country's military operations and might have a significant impact on the area's large federal installations. The combined workforce of Kirtland Air Force Base, Sandia National Labs, and the U.S. Forest Service exceeds 26,000, equal to 7% of the MSA's 2013 employment base. Fitch will continue to monitor the prospects for military downsizing and impacts on Bernalillo County and other communities across the U.S.

PENSION FUNDED POSITION BELOW AVERAGE

Full-time county employees participate in the Public Employee's Retirement Association (PERA) of New Mexico, a cost-sharing multiple-employer defined benefit retirement plan. The county fully funds its annual required contribution. PERA reforms effective in 2013 increased contribution rates and established a new tier of benefits for new hires, which Fitch considers prudent.

Such reforms increased PERA's funded position to 72.9% as of June 30, 2013 from 65% the year prior. Using Fitch's adjustment to reflect a 7% rate of return, the 2013 funded position is lower at approximately 67%.

Other post-employment benefits are provided through the New Mexico Retiree Healthcare Authority on a pay-as-you-go basis from employer and employee contributions. The carrying costs of GO and GRT bonds plus pension and OPEB obligations totaled 11.8% of governmental spending in fiscal 2013 which Fitch considers moderate.

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In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, Zillow.com, and National Association of Realtors.

Related Research:
'Tax-Supported Rating Criteria', dated 14 Aug. 2012.
'U.S. Local Government Tax-Supported Rating Criteria', dated 14 Aug. 2012.

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015
U.S. Local Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314

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It is important that you promptly provide us with all information that may be material to the ratings so that our ratings continue to be appropriate. Ratings may be raised, lowered, withdrawn, or placed on Rating Watch due to changes in, additions to, accuracy of or the inadequacy of information or for any other reason Fitch deems sufficient.

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We are pleased to have had the opportunity to be of service to you. If we can be of further assistance, please feel free to contact us at any time.

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Global Infrastructure & Project Finance

JS/mb

Enc: Notice of Rating Action
(Doc ID: 189452)

Notice of Rating Action

Bond Description	Rating Type	Action	Rating	Outlook/ Watch	Eff Date	Notes
Bernalillo County (NM) GO improv bonds ser 2014	Long Term	New Rating	AAA	RO:Sta	21-Apr-2014	
Bernalillo County (NM) GO rfdg bonds ser 2014A	Long Term	New Rating	AAA	RO:Sta	21-Apr-2014	

Key: RO: Rating Outlook, RW: Rating Watch; Pos: Positive, Neg: Negative, Sta: Stable, Evo: Evolving