Bernalillo County, New Mexico

New Issue Report

Ratings

Long-Term Issuer Default Rating	AAA
New Issue	
$16,000,000 General Obligation Bonds, Series 2018	AAA
Outstanding Debt	
General Obligation Bonds	AAA
Gross Receipts Tax Revenue Bonds	AA+

Rating Outlook

Stable

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New Issue Summary

Sale Date: Competitive sale on July 10, 2018

Series: $16,000,000 General Obligation (GO) Bonds, Series 2018

Purpose: Finance improvements to Bernalillo County's libraries, public safety facilities, parks and recreation projects, transportation projects and storm drainage and utilities.

Security: The GO bonds are payable from an annual unlimited property tax levy.

Analytical Conclusion

The 'AAA' Issuer Default Rating (IDR) and general obligation (GO) bond rating are based on the county's ample revenue-raising flexibility, solid expenditure flexibility, low liability burden and exceptionally strong financial resilience through economic downturns.

The 'AA+' Gross Receipts Tax (GRT) bond rating reflects ample resilience to revenue declines and limited future leveraging plans balanced against sluggish revenue growth prospects.

Economic Resource Base: Bernalillo County is the largest county in New Mexico and is the home to about one-third (estimated at about 677,000) of the state's population. The county's population grew by a notable 19% from 2000-2010, spurred in part by the area's recent development as a technology hub. Recent population growth trends have declined below the U.S average. The city of Albuquerque comprises about 80% of the county's population.

Key Rating Drivers

Revenue Framework: 'aa'
Fitch Ratings expects that the long-term pace of revenue growth will likely approximate the rate of inflation. Property tax revenue-raising flexibility is ample.

Expenditure Framework: 'aa'
Fitch expects the pace of expenditure growth to be above natural revenue growth. Expenditure flexibility is aided by prudent budgeting, annual pay-go capital outlays and moderate carrying costs for debt service and retiree benefits.

Long-Term Liability Burden: 'aaa'
The combined overall debt and unfunded pension liability burden is modest at less than 8% of personal income. Overlapping debt comprises the majority of the liability. Overlapping debt issuances may increase the overall liability burden, but Fitch expects it to remain low.

Operating Performance: 'aaa'
The combination of revenue and expenditure flexibility, supplemented by reserve funding, should enable the maintenance of a high level of financial flexibility throughout economic cycles.

Rating Sensitivities

Revenue Growth Trends: The 'AAA' IDR would come under pressure if revenue growth trends do not meet Fitch's expectations of keeping up with inflation.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	6/18/18
AAA	Affirmed	Stable	4/21/14
AAA	Affirmed	Negative[a]	2/18/14
AAA	Revised	Stable	4/30/10
AA+	Assigned	Stable	10/07/04

[a]Rating Watch.

Pledged Revenue Declines: Large and sustained GRT revenue declines, beyond the range of historical experience and Fitch's expectations, could pressure the GRT revenue bond rating, as could substantially higher than expected leveraging.

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 about 5% of the MSA's employment base. SNL has helped attract a highly educated workforce to the area but is vulnerable to federal budget restrictions and shifts in defense spending priorities. Fitch expects the magnitude of any potential cuts to the military installations would be tempered due to their unique role in maintaining the country's nuclear assets.

The area's high-tech hub includes firms engaged in microelectronics (Intel, Raytheon) and aerospace (Boeing and Eclipse Aerospace), although some contraction is occurring. Intel's workforce in nearby Rio Rancho (IDR of 'AA') has declined to 1,900 from 3,300 since 2013. Presbyterian Healthcare Services, the county's largest private employer, plans to construct a new hospital. The film industry in the area has grown to four major studios, reportedly leading to $506 million in direct spending in 2017.

The area's recovery from the last economic downturn has been tepid. Employment gains have been modest, and the unemployment rate has exceeded the U.S. average. Median home values rose by 5% to $192,800 in April 2018 from a year prior, according to Zillow.com, but remain below their peak in 2007, as do building permits. IHS Insights anticipates population growth will accelerate in the future along with payroll gains. A growing retiree population is expected to make healthcare a leading employment sector in the medium- to long term.

Revenue Framework

Property taxes and GRTs accounted for nearly equal proportions of total general fund revenues in fiscal 2017, comprising 49% and 43% of revenues, respectively. In fiscal 2018, the proportion of GRTs increased moderately due to the adoption of additional GRT increments.

Adjusted for property tax and GRT policy changes, total general fund revenues grew by a CAGR of less than 1% for the 10-year period ended fiscal 2017, a rate below CPI, although numerous one-time revenue losses make a clear view of historical trends difficult. Fitch expects the county's long-term revenue growth to approximate the level of inflation.

The county retains ample revenue flexibility in the form of 1.10 mills in remaining property tax margin, which it can impose without a voter referendum. The additional revenue from the unutilized property tax mills totals $16.6 million, or 6.3% of fiscal 2017 revenues, assuming a collection rate of 94%.

In fiscal 2016, the state began a 15-year phase-out of its hold-harmless payments to municipalities for the exemption of food and medicine from the GRT. The hold-harmless reduction totaled $1.2 million (0.4% of fiscal 2017 general fund revenues) for the county in fiscal 2017 and is projected to grow to $12.6 million (4.8% of revenues) by fiscal 2030. To offset these reductions, the state authorized municipalities to impose additional GRTs up to $^{3}/_{8}$th of 1%. The hold-harmless GRTs, in $^{1}/_{8}$% increments, can be imposed through ordinance only and are not subject to referendum.

After imposing two $^{1}/_{8}$% hold-harmless GRT increments in fiscal 2016 (one of which is collected in the mental health special revenue fund), the fiscal 2018 budget imposed the last remaining $^{1}/_{8}$% hold-harmless increment, effective Sept. 1, 2017. Concurrently, the county imposed the last remaining

Related Research
Fitch Rates $16MM Bernalillo County, NM GO Bonds 'AAA'; Outlook Stable (June 2018)

Related Criteria
U.S. Public Finance Tax-Supported Rating Criteria (April 2018)

$^{1}/_{16}$% GRT increment for general purposes. The aggregate revenue increase to the general fund in the fiscal 2018 budget totals $24.7 million (9.4% of fiscal 2017 general fund revenues).

Expenditure Framework

Public safety comprised approximately 55% of general fund expenditures in fiscal 2017. General government, public works and culture and recreation are the other major areas of expenditures.

The pace of spending growth absent policy actions is likely to be generally in line with revenue growth, aided by the recent county jail reforms that have reduced overcrowding and stabilized operational costs.

Expenditure flexibility is derived from the county's moderate carrying costs for debt service, pension and OPEB, which totaled about 15% in fiscal 2017. Additional flexibility is provided by the county's annual pay-go capital spending, averaging 2% of spending per year, which can be reduced, deferred or eliminated. A high 60% of the county's workforce is represented by seven 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.

Long-Term Liability Burden

The county's long-term liability burden, comprised of overall debt and net pension liability, is modest at almost 8% of personal income. The large majority of the overall burden is composed of overlapping debt.

Aggregate direct GO and GRT debt totals $269 million, and the 10-year amortization rate is rapid at 74% due to the county's policy to structure GO bond principal payments level year to year. Future direct debt issuance plans are manageable. The county's practice is to hold biennial GO bond elections for about $36 million–$40 million. The county currently does not have plans to further leverage the GRT with additional bonds.

Full-time county 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. Based on Fitch's 6% rate of return assumption, the county's assets-to-liabilities ratio is equal to 57%. The county funds its actuarially determined pension contribution, and the Fitch-adjusted net pension liability totals approximately $514 million, or 1.8% of personal income.

Operating Performance

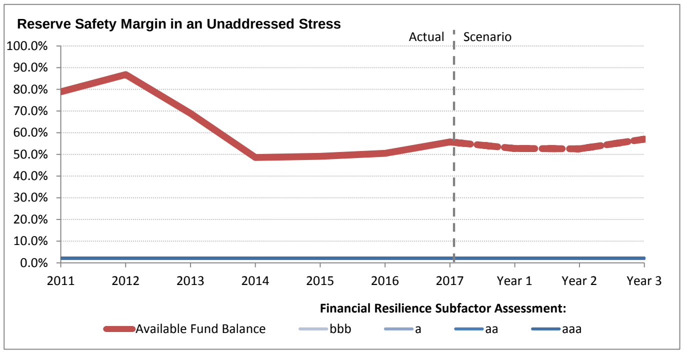
The county's high gap closing capacity is derived from a combination of revenue and expenditure flexibility and ample reserve levels. For details, see Scenario Analysis, page 4.

Financial reserves remained ample relative to expected revenue volatility despite sizable drawdowns in fiscal years 2013–2015 for one-time capital outlays and elevated public safety spending related to the county's overcrowded detention center. Enhanced revenues and stabilized detention center spending allowed the county to restore structural balance by fiscal 2016. The fiscal 2017 audit posted an $11.5 million (4.6% of spending) net operating surplus. The resulting financial cushion comprising the unrestricted fund balance and the state-required 25% restricted reserve totaled nearly $140 million, or almost 56% of spending. Management projects a large operating surplus in fiscal 2018 due to the adoption of the last remaining $^{1}/_{8}$% hold-harmless GRT and $^{1}/_{16}$% operating GRT (designated for public safety). The county's five-year forecast projects balanced operations based on modest annual gains in GRT and property taxes.

Bernalillo County (NM)

Scenario Analysis

v. 2.0 2017/03/24



Analyst Interpretation of Scenario Results:

The county's high gap closing capacity is derived from a combination of revenue and expenditure flexibility and ample reserve levels. Prudent budgeting has allowed the county to maintain a reserve safety margin well above the 25% of spending required by the state, which is far above the 2% reserve safety margin needed to achieve a 'aaa' financial resilience assessment given expected modest revenue volatility.

Based on historical results, Fitch expects a moderate economic downturn would result in a modest decline in general fund revenues in the first year of a downturn, followed by a prompt rebound. Fitch would expect the county's financial position to remain solid throughout the economic cycle.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(1.1%)	2.6%	6.3%
Inherent Budget Flexibility	Superior		

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2011	2012	2013	2014	2015	2016	2017	Year 1	Year 2	Year 3
Total Revenues	223,886	247,483	232,490	234,552	244,283	258,483	261,928	258,989	265,715	282,498
% Change in Revenues	-	10.5%	(6.1%)	0.9%	4.1%	5.8%	1.3%	(1.1%)	2.6%	6.3%
Total Expenditures	219,388	222,379	248,856	258,700	242,537	241,003	239,737	244,532	249,423	254,411
% Change in Expenditures	-	1.4%	11.9%	4.0%	(6.2%)	(0.6%)	(0.5%)	2.0%	2.0%	2.0%
Transfers In and Other Sources	173	274	693	328	817	68	140	67	69	74
Transfers Out and Other Uses	12,970	10,621	10,403	17,960	13,108	12,650	10,864	12,903	13,161	13,424
Net Transfers	(12,797)	(10,347)	(9,710)	(17,632)	(12,291)	(12,581)	(10,723)	(12,835)	(13,091)	(13,350)
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	(8,299)	14,757	(26,076)	(41,780)	(10,545)	4,899	11,467	1,622	3,201	14,736
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	(3.6%)	6.3%	(10.1%)	(15.1%)	(4.1%)	1.9%	4.6%	0.6%	1.2%	5.5%
Unrestricted/Unreserved Fund Balance (General Fund)	115,720	132,435	109,073	64,999	58,707	56,661	61,773	63,395	66,596	81,332
Other Available Funds (Analyst Input)	67,669	69,770	69,463	69,344	66,940	71,405	77,908	71,405	71,405	71,405
Combined Available Funds Balance (GF + Analyst Input)	183,389	202,205	178,536	134,343	125,647	128,066	139,680	134,800	138,001	152,737
Combined Available Fund Bal. (% of Expend. and Transfers Out)	78.9%	86.8%	68.9%	48.6%	49.1%	50.5%	55.7%	52.7%	52.6%	57.0%

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	18.0%	9.0%	5.6%	3.4%	2.2%
Reserve Safety Margin (aa)	13.5%	6.7%	4.5%	2.8%	2.0%
Reserve Safety Margin (a)	9.0%	4.5%	2.8%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.4%	2.2%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.