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CREDIT OPINION
11 June 2018

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Bernalillo (County of) NM

Update to credit analysis

Summary

Bernalillo County, NM (Aaa stable) has a strong and stable credit profile, supported by a large and regionally-important tax base, which is expected to continue expanding over the near-term; healthy financial position, with conservative budgeting resulting in a trend of sizeable surpluses; and, a modest direct debt profile. These attributes are weighed against the county's increasing unfunded pension liability, with annual contributions to PERA remaining below the treadwater payment. This risk is mitigated, in the near-term, by the county's ample reserve position.

Credit strengths

» Large and diverse tax base that serves as the economic engine for New Mexico

» Healthy financial position

» Low debt burden

Credit challenges

» Moderate reliance on economically-sensitive sales taxes (GRT)

» Below average resident income indices relative to peers

» Above average pension burden and widening treadwater gap

Rating outlook

The stable outlook reflects the county's strong financial position with a recent trend of surpluses. The county's operating performance acts as a mitigant in light of an increasing pension burden and treadwater gap; however, future reviews will focus on Bernalillo's ability to manage its long-term liabilities.

Factors that could lead to an upgrade

» Not applicable

Factors that could lead to a downgrade

» A trend of deficits that reduces fund balances and cash reserves

» Material tax base contractions or sustained declines in GRT collections

» Further increases to the pension and fixed cost burdens; operating surpluses that no longer eclipse the treadwater gap

Key indicators

Exhibit 1

Bernalillo (County of) NM	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$43,226,496	$43,556,335	$44,549,691	$45,402,634	$46,825,538
Population	667,092	671,429	673,943	674,777	676,685
Full Value Per Capita	$64,798	$64,871	$66,103	$67,285	$69,198
Median Family Income (% of US Median)	93.9%	93.1%	91.0%	90.6%	90.6%
Finances					
Operating Revenue ($000)	$258,317	$263,932	$275,977	$309,676	$316,506
Fund Balance ($000)	$128,886	$94,041	$87,600	$91,626	$94,447
Cash Balance ($000)	$200,229	$172,787	$164,629	$183,658	$209,547
Fund Balance as a % of Revenues	49.9%	35.6%	31.7%	29.6%	29.8%
Cash Balance as a % of Revenues	77.5%	65.5%	59.7%	59.3%	66.2%
Debt/Pensions					
Net Direct Debt ($000)	$256,195	$247,851	$245,026	$234,021	$224,835
3-Year Average of Moody's ANPL ($000)	$619,466	$628,947	$579,462	$620,721	$780,370
Net Direct Debt / Full Value (%)	0.6%	0.6%	0.6%	0.5%	0.5%
Net Direct Debt / Operating Revenues (x)	1.0x	0.9x	0.9x	0.8x	0.7x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	1.4%	1.4%	1.3%	1.4%	1.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	2.4x	2.4x	2.1x	2.0x	2.5x

Source: County's CAFRs; Moody's; US Census (MFI)

Profile

Bernalillo County, the economic and population hub of New Mexico (Aa1 negative (m)), is located in the north central region of the state at the conjunction of Interstate Highways 25 and 40. The county has roughly 676,000 residents. Its boundaries encompass the entire City of Albuquerque (GO Aa2 negative) and is home to the University of New Mexico (rev Aa2 negative), Kirtland Air Force Base and Sandia National Laboratories.

Detailed credit considerations

Economy and tax base: large, regionally-important base located in central New Mexico

The county's large tax base is expected to continue expanding due to ongoing residential and commercial development. Located in north central New Mexico, Bernalillo County encompasses the City of Albuquerque (Aa2 negative) and one-third of the state's population. The tax base is large, with fiscal 2018 assessed value of $16.1 billion, derived from a full value of $48.4 billion, and has appreciated modestly with a five year average annual growth of 2.3%. Management reports that the Department of Defense is investing $175 million in constructing a new nuclear research facility, which will employ 1,200 people; Top Golf is opening a location in Albuquerque, which will add around 350 jobs; and Vitality Works (vitamin manufacturer) is expanding, creating 60 new jobs. Additionally, residential construction is steady, with single-family housing permits up 10% comparing Q1 2018 to Q1 2017.

Per the November 2017 Moody's Economy report, the Albuquerque MSA is in “recovery”, and we expect that over the next couple of years, the city will have steady employment growth. Over the long-term, Albuquerque may be challenged to attract private sector industries, especially in tech, resulting in job growth that tracks in line with the US.

Major employers in the Bernalillo/Albuquerque MSA include the University of New Mexico (rev Aa2 negative), Kirtland Air Force Base, and Sandia National Laboratories. The institutional presence provided by these entities is an anchor for the local economy. Healthcare and high-tech industries also have significant presence in the employment base. The county's March 2018 unemployment rate of 4.5% was below the state (5.1%) but above the nation (4.1%) for the same period. Resident income levels are average yet below peers with median family income of approximating 90.2% of the US (2015 ACS).

Financial operations and reserves: trend of surpluses increase fund balances

The county's financial position is expected to remain stable over the near-term given conservative budgeting. Fiscal 2017 (June year-end) ended with a sizeable surplus of $11.5 million, increasing general fund balance to $142.3 million, or a healthy 54.3% of revenues. Revenues primarily consist of property taxes (50%) and sales taxes (40%). The surplus was driven primarily by expenditures being far less than budget ($240 million versus $288 million); departments underspent and only $7 million of the planned $18 million in capital was invested.

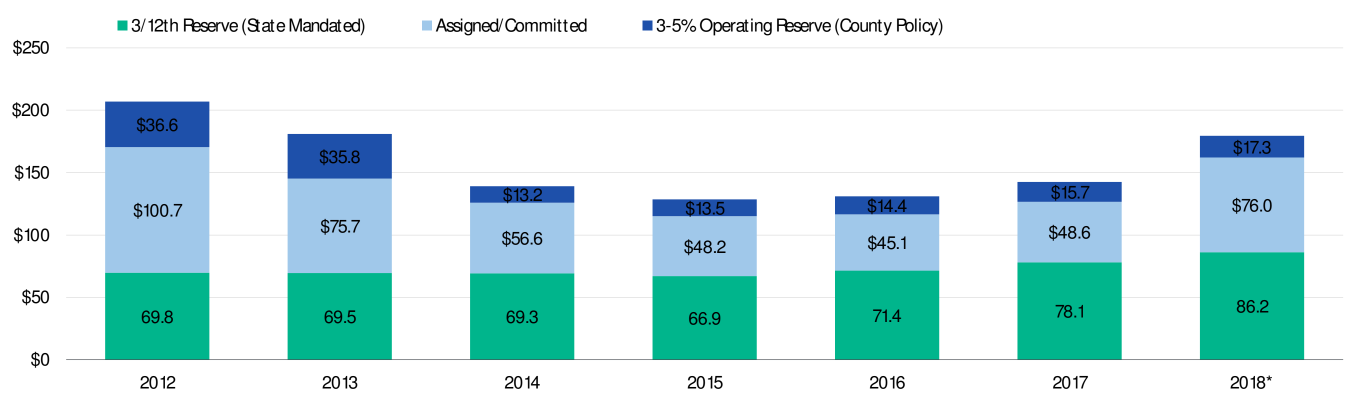
Fiscal 2018's budget was very conservative and assumed revenues of $283.7 million against expenditures of $304.2 million, including $21 million for capital outlay. Based on updated projections, the county expects to report a $48 million surplus due to higher revenues and lower expenses. Revenues are up due to the implementation of two new sales taxes: 1/8th hold harmless GRT (general purpose) and 1/16th county GRT (dedicated to public safety). Going forward, this will generate an additional $30 million in annual revenues. Similar to fiscal 2017, fiscal 2018 expenditures are far below budget at a projected $241 million; as such, general fund balance is expected to increase to $179.5 million, or 62.1% of unaudited revenues. Additional sales tax dollars were not allocated to departments, but instead led to a higher surplus. In fiscal 2019, the county plans to spend a portion of these additional revenues on salary increases and capital.

The county prepares five year financial forecasts. Through fiscal 2022, the county has matched recurring revenues to recurring expenditures, and is not anticipating utilizing reserves to balance the budget. Revenue projections are conservative: for instance, property taxes are projected to increase by 1.6%, below the five year average of 2.3%.

As discussed further in the pension section, unfunded liabilities associated with the county's participation in PERA could eventually impact operations. Currently, the county is generating surpluses in excess of any funding shortfalls (contributions less treadwater). However, in event of reform, the county's contributions may materially increase, which could translate to use of reserves. Moody's will continue to monitor the county's financial position, focusing specifically on whether operating performance is sufficient to mitigate pension pressure.

Exhibit 2

Strong budgetary performance has increased general fund balance since fiscal 2015



*projected; note: the county's policy on operating reserve changed from 16% to 3-5% in fiscal 2015
Source: Moody's

LIQUIDITY

General fund cash tracks closely to general fund balance. At fiscal 2017 year-end, the county had $136.6 million in cash, or an ample 52.1% of revenues. Considering the operating funds, which include the general, debt service and gross receipts tax funds, the total liquidity climbed to $209.5 million, or 66.2% of total revenues.

Debt and pensions: low direct debt burden, but above average pension burden

Given the lack of major capital needs, stable assessed values, and average principal amortization, the county's debt burden will likely remain low and manageable over the long-term. At 0.6% of fiscal 2018 full value, the county's direct debt burden is in line with national medians. Included in the burden is $140.8 million in sales tax (GRT) debt (Aa2). The county plans to approach voters in November 2018 to authorize another $38.5 million in GO bonds, which will likely be issued in two installments in the subsequent years.

DEBT STRUCTURE

The county has $125.6 million in fixed-rate, general obligation bonds. Principal amortization is average with 75% retired in ten years.

DEBT-RELATED DERIVATIVES

The county has no exposure to variable rate debt or interest rate swaps.

PENSIONS AND OPEB

The county has an above average employee pension burden, based on unfunded liabilities for its share of the Public Employees Retirement Association (PERA), a cost sharing plan administered by the state. Moody's fiscal 2017 adjusted net pension liability (ANPL) for the county, under our methodology for adjusting reported pension data, is $953.7 million, or a somewhat above average 3.0 times operating revenues.

The county's tread water gap, which amounted to 4.6% of fiscal 2017 operating fund revenues, has widened since fiscal 2015, and is elevated compared to peers. The “tread water” indicator measures the annual contributions required to prevent the reported net pension liability from increasing under the plan's assumptions. That is, it is the amount that the county would have to pay on an annual basis to ensure the liability does not increase. In fiscal 2017, pension contributions of $14.8 million were below the treadwater payment of $29.4 million, creating a gap of $14.5 million, a credit weakness. Positively, the county is currently generating surpluses in excess of the gap. However, in event that the gap continues widening and/or surpluses are no longer sufficient to close the gap, the credit profile may be negatively impacted.

Fiscal 2017 fixed costs, including debt service, pension and OPEB contributions, are 17.1% of operating revenues, which is average. If the tread water payment is factored into the fixed cost calculation, fixed costs increase to 21.7% of operating revenues.

Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the county's reported liability information, but to improve comparability with other rated entities. For more information on Moody's insights on employee pensions and the related credit impact on companies, government, and other entities across the globe, please visit Moody's on Pensions at www.moodys.com.

Management and governance: moderate Institutional Framework score

Bernalillo County operates under commission-manager form of government and provides for public safety, highways and streets, sanitation, cultural and recreational services, public improvements, planning and zoning, and general administrative services. Legislative and some executive power is vested in a five-member Board of County Commissioners, who are elected for four-year terms from single member districts. Administration is overseen by a county manager, who has responsibility for 25 departments.

New Mexico Counties have an Institutional Framework score of A, which is moderate. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenue sources, such as property taxes and sales taxes, are subject to statutory caps, which cannot be overridden. However, the property tax cap of $11.850 (per $1,000 AV) and the available sales tax authority (varies by type) still allows for moderate revenue-raising ability. Unpredictable revenue fluctuations tend to be moderate, or between 5-10% annually. Across the sector, fixed and mandated costs are generally less than 25% of expenditures. However, New Mexico has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

REPORT NUMBER 1128288

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