

Fitch Rates Santa Fe, NM's GOS 'AA+'; Outlook Stable

Written by Australian Business

AUSTIN, Texas--([BUSINESS WIRE](#))--Fitch Ratings has assigned the following rating to Santa Fe, New Mexico's (the city) general obligation (GO) bonds:

--\$5.8 million series 2014 'AA+'.

The bonds are expected to sell competitively on July 9. Proceeds from the sale of the bonds will be used for public parks, trails, and drainage improvements.

In addition, Fitch affirms the following ratings:

--\$37.3 million GO bonds at 'AA+';

--\$47.2 million GRT revenue bonds outstanding, series 2010A, 2012A, series 2013A at 'AA+';

--\$27.4 million subordinate lien GRT revenue bonds outstanding, series 2010B, series 2012C, series 2013B at 'AA+';

The Rating Outlook is Stable.

SECURITY

The GO bonds are secured by an unlimited property tax levy on all taxable property within the city.

The GRT bonds are secured by pledged revenues comprised of the 1.225% state shared GRTs, 0.5% municipal GRT, and 0.0625% infrastructure GRT; any portion of the above-mentioned GRTs that would have been remitted to the city but previously exempted; and any other GRT received by the city pledged for payment of the bonds. The subordinate lien bonds are secured by a subordinate lien on the pledged revenues.

RATING DRIVERS

SOUND ECONOMY: Economic stability is provided by the large state government presence, and unemployment rates remain below state and national averages. Wealth indices are also generally above average.

STRUCTURAL BALANCE PRESSURED: The city's structural balance has been pressured from recent hikes in labor costs. Financial cushion is still favorable but remaining expenditure flexibility is limited, leading management to emphasize efficiencies and cost savings in providing city services.

PROMINENCE OF GROSS RECEIPTS TAXES: Given the importance of GRT revenues to general fund operations (73% of general fund revenues), the credit rating for the GRT revenue bonds is tied to the city's overall financial performance and equal to the GO bond rating.

TAXING MARGIN AVAILABLE: The city maintains revenue-raising flexibility through its GRT and property tax rates.

STRONG DEBT SERVICE COVERAGE: Debt service coverage is favorable and legal covenants, particularly the additional bonds test (ABT), are strong.

MODERATE DEBT; RAPID PAY-OUT: Debt levels relative to market value are moderate and the principal pay-out rate for all bonds remains rapid.

RATING SENSITIVITIES

CONSISTENT BUDGETARY BALANCE: The continuance of solid reserves remains integral to maintaining the city's high-grade credit quality given the heavy reliance on economically sensitive GRT revenue. The rating assumes that operating performance will result in consistent reserves at least at current levels.

CREDIT PROFILE

HEALTHY REGIONAL ECONOMY

Santa Fe serves as the county seat and state capital and is located in north central New Mexico. The local economy is anchored by the large state government presence. Other important sectors include tourism and recreation, retail trade, healthcare, and some industry. The commuter rail line between Santa Fe and Albuquerque enhances employment and tourism opportunities for the region.

Historically, Santa Fe unemployment rates have been below those of both the state and nation. However, the city was not immune to the recent economic downturn, as evidenced by a rising unemployment rate that peaked at 6.1% in 2010. Although employment gains remain sluggish, the jobless rate declined to 4.2% as of April 2014, still well below the 5.9% rate of both the state and nation.

Wealth indices for the city are above the statewide average. Property wealth is evident in the city's high market value per capita, which equals \$157,000, despite the large amount of tax-exempt values. After years of healthy annual gains in taxable assessed valuation (TAV), growth flattened over the last three years, although Fitch notes the city did not experience any recessionary declines. A recent annexation increased the city's acreage by 13% and boosted its population by 12,900 residents or 19%. The associated AV is modest and rolls on in fiscal 2015. The annexation incorporated isolated parcels of land within its previous boundaries plus property along its main growth corridors.

CONCENTRATED REVENUES RECOVER SLOWLY FROM LOSSES

Typical of municipalities in New Mexico, the city's general fund is heavily dependent on state-shared and local GRTs for general fund support. The local portion of state-shared taxes is remitted back to local governments based on the point of sale. In fiscal 2013, combined GRTs accounted for approximately 73% of revenues. Property taxes, on the other hand, represented only 5% of operating support.

Combined state-shared and municipal GRT collections declined by 9% and 5% in fiscal years 2009 and 2010, respectively, and subsequently posted modest annual gains through fiscal 2013. Fiscal 2014 projections point to a 3.8% gain.

LABOR COSTS PRESSURE STRUCTURAL BALANCE

The city's general fund reserves thinned during the recession but remained solid. The city posted general fund drawdowns of \$5.9 million and \$5.3 million in fiscal years 2009 and 2010, respectively, each equal to over 7% of spending. Aided by stabilized GRT collections and budget cuts, operating results were positive with a modest addition to fund balance in fiscal years 2011 and 2012.

Fiscal 2013 results were not balanced as expected by Fitch. The general fund posted a \$3.2 million draw down (equal to 4.4% of spending) due to primarily to cost of living increases for the city's three unions plus some pay-go capital outlays. However, its financial cushion remained solid, comprised of its \$8.9 million unrestricted fund balance and the state-required 30-day reserve for operations, totaling \$14.5 million or 20% of spending and transfers out.

Fiscal 2014, during which no union COLAs were funded, is projected to add \$2.7 million to fund balance. The projected surplus has been aided by a 3.8% gain in GRT revenues, compared to budgeted flat revenues. In fiscal 2014, the city began to phase in police services to the newly annexed areas with 10 additional officers.

For the adopted fiscal 2015 budget, the city added five additional police officers to the annexed area and funded COLAs for two unions along with a modest \$200,000 in pay-go outlays. The budget is based on flat GRT revenues, which Fitch views favorably, but includes \$900,000 in new GRTs from the recently annexed areas. Fitch believes limited spending flexibility remains as additional cuts would begin to affect city services.

AMPLE REVENUE FLEXIBILITY REMAINS

The city maintains some important revenue raising flexibility with the availability of an additional 1/4% on the municipal GRT rate as well as substantial property tax margin. The combined revenue margins equal a large \$24 million or 33% of fiscal 2013 spending. The state also authorized municipalities to impose an additional 3/8th GRT (starting in 2015) to offset the gradual elimination of state payments that reimburse local governments for certain GRT exemptions. The elimination will be phased in slowly over a 15 year period with the annual impact estimated at \$640,000 - \$700,000 or about 1% of fiscal 2013 spending. The city chose not to implement any portion of this additional 3/8th GRT in the fiscal 2015 budget. If imposed in its entirety, the 3/8th GRT would generate approximately \$10.5 million or 15% of fiscal 2013 spending.

Reportedly, the city maintains the second lowest property tax rate in the state, behind Albuquerque. Management expects the city council to consider adopting up to a 2 mill or 100% increase for the fiscal 2016 budget (equivalent to \$7 million or 9% of general fund revenues), although such an action may be politically challenging.

ELEVATED DEBT LEVELS; RAPID PAY-OUT

The majority of the city's outstanding tax-supported debt is secured by GRTs. At 400 years old, the city's age and infrastructure needs have driven the overall debt per capita ratio to a high \$5,230, down from \$6,103 due to the recent annexation. Overall debt per market value remains moderate at 3.8%.

The current offering exhausts the \$17 million bond authorization approved by voters in 2012. Assuming continued stabilized GRT collections, management's goal is to issue GRT bonds on a two-year cycle beginning with a planned \$18 million issuance in August. The

combined pay-out rate for GO bonds and GRT bonds remains rapid with 74% of principal maturing in 10 years.

STRONG DEBT SERVICE COVERAGE

Debt service coverage on senior and subordinate lien bonds and New Mexico Finance Authority loans is strong as expected, given the importance of GRTs to operations. Fiscal 2013 pledged revenues provide 4.2x coverage of senior lien MADS and 2.5x coverage on senior and subordinate lien MADS (including debt service paid in practice from other sources but secured by subordinate GRT revenues).

Legal provisions are solid. A multi-tiered additional bonds test calls for, among other provisions, at least 1.0x coverage of senior lien MADS by municipal and infrastructure GRTs only (state-shared GRTs represent the bulk of pledged revenues) and a subordinate lien additional bonds test of 2.0x combined senior and subordinate MADS.

REFORMS IMPROVE PENSION'S FUNDED POSITION

The city's cost-sharing multiple employer defined benefit pension plan and OPEB services are provided through the state-administered Public Employees Retirement Association (PERA). Pension reforms, signed into law in April 2013, reduced PERA's unfunded actuarially accrued liability by \$1.5 billion or a large 15%. As a result, PERA's fiscal 2013 funded position increased to 73% from 65% based on a 7.75% return assumption. Adjusted for Fitch's more conservative 7% rate of return assumption, the funded position is approximately 67%. Although the city has fully funded its annual required contributions, the funded position had declined due to recessionary losses which have now started to reverse.

Employees' pension contributions are negotiated annually with its three unions which comprise 71% of city staff. Three-quarters of current pension contributions for regular employees are paid for by the city as allowed by state statute. Total carrying costs for debt service, pensions and OPEB are sizable at 23% of fiscal 2013 governmental spending.

Additional information is available at ' www.fitchratings.com '.

In addition to the sources of information identified in Fitch's 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, and the National Association of Realtors.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria' (Aug. 14, 2012);

--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

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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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