MOODY'S
RATINGS

Rating Action: Moody's Ratings revises New Mexico's outlook to positive; affirms Aa2 issuer and GO ratings and downgrades transportation and severance tax bonds

20 Sep 2024

New York, September 20, 2024 -- Moody's Ratings (Moody's) has revised the outlook on the State of New Mexico to positive from stable, affirmed the state's Aa2 issuer rating and Aa2 rating on $521 million of outstanding general obligation bonds, and affirmed the Aa3 rating on the New Mexico School District Intercept Program.

The positive outlook is driven by our view that the state's strong financial position, reflected in recent growth of operating reserves and permanent funds, will drive an improvement in its credit rating despite underlying risks of economic concentration.

Concurrently, we have downgraded to Aa2 from Aa1 $166M of senior lien transportation tax revenue bonds and confirmed at Aa2 $413M of subordinate lien transportation revenue bonds. Additionally, we downgraded $916 million of senior and $8.9 million of subordinate lien severance tax bond ratings to Aa3 from Aa2 and A1 from Aa3, respectively. The actions on the transportation and severance tax bonds conclude a review for possible downgrade initiated on July 24, 2024, in conjunction with an update to the US States and Territories rating methodology pertaining specifically to special tax bonds.

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBM_PBM908809012 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

The Aa2 issuer rating balances the state's very strong fiscal management and healthy operating reserves with a heavy economic concentration in oil and gas and government employment. The state's strong reserves help mitigate downside risks linked to volatility in key economic sectors and revenue. The rating also considers resident income and wealth that lag the nation and most comparably rated states. The rating further incorporates the state's moderate leverage and fixed costs, as well as exposure to large but improving K-12 teacher pension liabilities.

The Aa2 general obligation rating is the same as the issuer's rating given the state's unlimited tax, full faith and credit pledge.

The Aa2 ratings on the senior and subordinate lien transportation revenue bonds, which are rated at the same level at the state's issuer rating, reflect a somewhat broad pledge of state and federal transportation taxes, very strong maximum annual debt service coverage exceeding 8.6 times across both liens, limited revenue volatility, and lack of physical and legal separation of pledged revenues from the state. The lack of distinction between the senior and subordinate liens reflects the small portion of total debt consisting of senior lien bonds. This share will further decline given the rapid amortization of the senior lien.

The Aa3 and A1 ratings on the senior and subordinate lien severance tax revenue bonds, respectively, reflect a somewhat broad pledge of state oil and gas extraction revenues, very strong MADs coverage of 12.9 times across both liens and high revenue volatility. The one notch distinction between the senior and subordinate lien reflects the priority of liens and the composition of outstanding debt which primarily consists of senior lien bonds.

The Aa3 rating on the New Mexico School District Intercept Program reflects the essential nature of the program (general school funding) and the state's statutory commitment to intercept up to twelve consecutive months of state aid appropriated for the programs' purposes should a program borrower fail to pay debt service. The rating also considers the effectiveness, reliability and timeliness of the programs, which are outlined in state statute and policy and financing agreement documents.

RATING OUTLOOK

The outlook revision to positive is driven by our view that the state's financial position will remain strong and operations will be supported by balanced budgets and elevated reserves. While certain economic challenges will persist, these fiscal strengths, along with further stabilization of long-term liabilities following increased pension contributions, could support an improved credit rating.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Continued adherence to strong fiscal practices that maintain strong operating reserves, robust permanent funds and healthy pension funding

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Multi-year trend of structural imbalance lowering General Fund reserves well below 30% of recurring General Fund revenues

- Material weakness in the oil and gas industry leading to growth in unemployment above 5% or significant negative volatility in oil and gas severance tax revenues

- Growth in leverage (combined debt and retirement liabilities) to in excess of 200% of state own-source revenue

LEGAL SECURITY

New Mexico's general obligation bonds are secured by the full faith and credit of the state and specifically secured by, and paid from, a statewide property tax levy without limit as to rate. The treasurer is required to keep the property tax proceeds separate from all other funds.

The senior and subordinate lien transportation revenue bonds are secured by first and second liens, respectively, on both: state road and highway revenues and federal highway aid received by the state. In fiscal 2023, state revenues made up 52% of pledged revenues. State revenues consisted primarily of special fuel, gas and weight/distance taxes. Federal highway aid consists of all aid received by the state from the federal government for highway construction, improvement and maintenance projects.

The senior lien and subordinate lien severance tax bonds are secured by a first and second lien, respectively, on severance taxes on deposit in and interest earnings of the Bonding Fund. There is no debt service reserve for the bonds. However, state statutes require that on June 30 and December 31 all monies in the Bonding Fund in excess of the next 12 months scheduled debt service be transferred to the state's Severance Tax Permanent Fund. The 12 months' debt service requirement in effect provides an ample reserve for the bonds.

The New Mexico School District Intercept Program includes pledge of up to 12 consecutive months of state aid from its General Fund should the school be unable to meet debt service requirements. The program's mechanics include a provision for third party notification of pending deficiency. If the paying agent has not received payment of principal or interest on school district general obligation bonds on the business day immediately prior to the date on which the payment is due, the paying agent shall so notify the New Mexico Department of Finance and Administration and the district. If the district indicates it will not make the payment, the department shall forward the amount to make the payment due on the bonds to the paying agent.

PROFILE

New Mexico has a population of 2.1 million. Its nominal GDP was $130.2 billion as of 2023. The state's wealth levels are below average, with per capita personal income equal to 87.3% of the US level after adjusting for the regional cost of living. The state is the second largest producer of crude oil and a top-10 producer of natural gas in the US.

METHODOLOGY

The principal methodology used in the issuer, general obligation, transportation and severance tax revenue bond ratings was US States and Territories published in July 2024 and available at https://ratings.moodys.com/rmc-documents/425428. The principal methodology used in the programmatic rating was US State Aid Intercept Programs and Financings published in February 2024 and available at https://ratings.moodys.com/rmc-documents/415020. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

The List of Affected Credit Ratings announced here are all solicited credit ratings. For additional information, please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com. Additionally, the List of Affected Credit Ratings includes additional disclosures that vary with regard to some of the ratings. Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBM_PBM908809012 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and provides, for each of the credit ratings covered, Moody's disclosures on the following items:

- Rating Solicitation

- Issuer Participation

- Participation: Access to Management

- Participation: Access to Internal Documents

- Endorsement

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