FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Alaska's Outlook to Stable; Affirms IDR at 'A+'

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Fitch Ratings - New York - 13 Apr 2022: Fitch Ratings has affirmed the following state of Alaska (AK) ratings:

--Issuer Default Rating (IDR) at 'A+';

--General obligation (GO) bonds at 'A+';

--State appropriation bonds at 'A';

--Lease obligation bonds at 'A';

--Alaska Municipal Bond Bank Authority (AMMBA) GO bonds at 'A'.

The Rating Outlook has been revised to Stable from Negative.

SECURITY

State GO bonds are general obligations of the state of Alaska, to which the full faith, credit and resources of the state are pledged.

Lease-purchase obligations are secured by annual appropriations from the state's unrestricted general fund (UGF).

AMBBA bonds are GOs of the bank issued under 2005 and 2016 resolutions, for which the state maintains an annual standing appropriation of state general fund resources to replenish the bonds' debt service reserve fund in the event of borrower default. The standing appropriation is the basis for the rating at a level one notch below Alaska's IDR.

ANALYTICAL CONCLUSION

The revision of the Outlook to Stable, from Negative, reflects stabilization of Alaska's financial resilience driven by the recent surge in energy prices which should begin replenishing budgetary reserves. Further, the percentage of market value (POMV) formula enacted in 2018 has created a consistent approach to drawing resources from realized earnings of Alaska's massive Permanent Fund (PF) held in the Permanent Fund Earnings Reserve (PFER) account.

Alaska's 'A+' IDR reflects the state's unique economic and budget profile with strong gap-closing capacity, supported by reserves that remain sizable but most are somewhat limited in their direct availability, and a moderate long-term liability burden. Key policy questions including on the manner for determining annual Permanent Fund dividends (PFD) to citizens from the POMV remain unresolved, while ongoing price volatility and decarbonization trends pose longer-term risks to its energy sector.

Economic Resource Base

Alaska's economy is dominated by its abundant natural resource sectors, including oil, natural gas, minerals and fisheries. Energy and mining generate about one-quarter of GDP, while tourism, transportation activity and government, including a sizable military presence, are also significant to economic activity. The dominance of oil and gas leaves Alaska vulnerable both to volatile short-term global price trends and the longer-term shift toward less carbon-intensive energy. After severe price shocks in 2014-2015 and again at the start of the pandemic, energy prices have recently rebounded to levels near $100/bbl. Both the state and Fitch forecast that prices over the medium-term gradually fall by the middle of the decade.

KEY RATING DRIVERS

Revenue Framework: 'a'

Alaska's revenue framework is unique among the states in its overwhelming reliance on volatile energy-related revenues and, since a 2018 statutory change, on a share of investment earnings ultimately derived from its massive PF. Consequently, sustainable management of the state's PF and PFER are critical to the rating over the longer term. The state has complete control over its revenues, with an unlimited independent legal ability to raise operating revenues as needed.

Expenditure Framework: 'a'

Alaska maintains the broad expense-cutting ability common to most U.S. states, although leeway to reduce spending is somewhat diminished given actions already taken to address budgetary weakness over the long period of low energy prices. The spending profile covers broad services to citizens as well as the annual PFD. Lack of a long-term approach to determining the PFD remains an uncertainty.

Long-Term Liability Burden: 'aa'

Alaska's net direct debt and Fitch-adjusted net pension liabilities are elevated but still in the moderate range, relative to both personal income and state GDP. Closure of defined benefit pensions, a commitment to actuarial contributions, and full prefunding of other post-employment benefit (OPEB) obligations diminish risks posed by retirement benefits. Both pension benefits and OPEB are constitutionally protected.

Operating Performance: 'a'

Strong, centralized financial operations, the massive balance in the PF and a propensity to build large budgetary reserves during periods of high energy prices have supported resilience. Lengthy periods of low energy prices remain a risk to steady operating performance. Recent favorable energy trends should enable the state to begin replenishing sizable reserve balances.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to a positive rating action/upgrade:

--State policy consensus on an approach to funding the PFD sustainably over the longer term, allowing for greater certainty in budgeting and strengthening operating performance;

--An extended period of higher energy prices combined with fiscal discipline that prioritizes the rebuilding of budgetary reserves and supports structural balance could improve resilience.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

--State policy changes that erode long-term financial resilience such as draws on the state's accessible reserves, including the PFER, at levels beyond Fitch's current expectations, accelerating the timeframe for depleting the balance and jeopardizing resilience;

--Inability to maintain structural balance and reserves through an expected transition away from carbon-based fuels.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CURRENT DEVELOPMENTS

Rapidly Rising Forecast for Energy Revenues

Alaska's budgetary outlook has improved significantly on surging global energy prices, ending at least temporarily a lengthy period of lower energy prices and fiscal stress that began in late 2014. The Alaska-North Slope (ANS) price per barrel benchmark has moved sharply higher in recent months spurred by post-pandemic economic recovery and by the war in Ukraine. Together with steady production, this is now generating energy revenues well above the projections included in the enacted budget for fiscal 2022 (ending June 30), and in the fall forecast released in December 2021.

As of last year's spring 2021 revenue forecast, the basis for the fiscal 2022 enacted budget, UGF revenue was forecast at $4.7 billion in fiscal 2022 and $5.1 billion in fiscal 2023. The ANS average prices per barrel stood at $61 and $62, respectively, for both years. The spring 2022 revenue forecast, as revised on March 15, now assumes UGF revenues at nearly $7 billion in fiscal 2022 and $8.3 billion in fiscal 2023. ANS average prices per barrel are now forecast at $92 and $101, respectively, and price trends are forecast to remain elevated at least in the near term.

Sizable Surpluses and a Rebound in Budgetary Reserves

The revenue surge is resulting in much higher forecast operating surpluses in both fiscal 2022 and 2023, much of which is expected to be diverted to budgetary reserves. Before the March 15 forecast update, the state's executive budget forecast was anticipating surpluses of $686 million in fiscal 2022 and $952 million in fiscal 2023. Deposit of these surpluses to the state's two primary budgetary reserves, the constitutional budget reserve (CBR) and the statutory budget reserve (SBR), would bring their combined balance to nearly $2 billion as of fiscal 2022 and nearly $3 billion as of fiscal 2023.

Given the improved March 15 revenue forecast, actual surpluses are likely to be considerably higher. Negotiations between the Governor and Legislature are underway on a supplemental budget for fiscal 2022 and a final budget for fiscal 2023, including on the use of expected surpluses. The Governor's executive budget fully funds education formula funding for the base student allocation and sets aside funding for full school bond debt reimbursements, in contrast to recent years when the latter was suspended to balance the budget. It also proposes a $310 million GO bond issuance for port, highway and airport capital improvements, among other needs.

The Legislature is reportedly relying on a more conservative revenue forecast given uncertainty about the durability of the current price surge. Consensus has not been reached on the size of this year's PFD payment to Alaskans (paid in October), which is drawn from investment revenues held in the PFER under the POMV formula. Dividend payments as a share of the PFER have been modified since 2015 as the state struggled to address weak revenues.

For 2022, the governor is proposing making dividend payments at 50% of the POMV, or roughly $2,564, and reportedly supplementing last year's PFD by about $1,200, given that the Legislature last year left the PFD below 50% of the POMV draw. Among several proposals, the Legislature would provide a smaller PFD and supplement it with an energy rebate to Alaskans to offset higher energy costs.

Federal Pandemic Assistance

Even as its energy revenues surge, Alaska like other states is benefiting from sizable federal transfers in response to the pandemic. The state currently calculates that it has received almost $4.7 billion in federal pandemic relief through the range of funding programs enacted since the start of the pandemic, excluding $9.6 billion in funding for individuals and entities outside of state government. State programs have received $2.9 billion, including the enhanced federal match for Medicaid ($435 million), unemployment assistance ($1 billion) and education aid ($648 million), largely via three allocations in Elementary and Secondary School Emergency Relief funds.

Another $1.8 billion has been provided for discretionary funding, including $1.3 billion through the Coronavirus Relief Fund monies under the Coronavirus Aid, Relief and Economic Security Act of 2020 and $506 million from the first tranche of the American Recovery Program Act (ARPA) of 2021 Stat Fiscal Recovery Fund (SFRF).

Proposed spending for the first tranche of ARPA funds includes $375 million for offsetting state revenue losses with the remainder for addressing economic impacts in communities, key industries and other needs. Alaska will receive its second SFRF tranche of approximately $500 million later this year. The state is also eligible for another $112 million from ARPA's Coronavirus Capital Project Fund.

CREDIT PROFILE

Alaska's GDP was flat to declining for much of the last decade due to a 2014 plunge in crude oil prices that reduced energy-related activity, pushed unemployment well above the nation, and triggered annual population declines. GDP took another severe hit in 2020 as the pandemic affected energy prices and other economic drivers, particularly tourism. In the last year, a rebound in global energy demand and the war in Ukraine have driven energy prices to historically high levels. Tourism and other activity have likewise rebounded as pandemic concerns ease.

The state's spring 2022 revenue forecast (as of March 15) has the ANS average oil price per barrel at nearly $92 and $101 in fiscal years 2022 and 2023, respectively, substantially higher than the $52 and $51 averages in place during fiscal years 2020 and 2021, respectively. The forecast anticipates prices dropping thereafter, to the mid-$70 range by fiscal 2026. In the forecast, production would gradually climb through fiscal 2031, the end of the forecast period, as new oil fields come on line, a modestly higher production outlook compared to last year.

Fitch's March 2022 energy price outlook traces a similar path as Alaska's at least near term, but diverges in future years. Fitch anticipates the Brent crude oil benchmark per barrel at $100 in calendar 2022, before falling to $80 in 2023 and to $53 by 2025. (ANS is typically priced at levels comparable to the Brent benchmark over time given its primary destination, refineries on the U.S. west coast.) For additional information, see "Fitch Ratings Raises

Short- and Medium-Term Oil & Gas Price Assumptions" published in March 2022, at www.fitchratings.com.

Revenue Framework

Alaska's revenue profile is unique among the states, with energy-related activity funding both direct levies to the state as well as deposits to the massive PF. There are no broad-based statewide personal income or sales taxes, and other taxes and fees are relatively limited. Investment revenues constitute 44% of UGF revenues in fiscal 2022, largely realized earnings of the PF drawn from the PFER under the POMV formula.

Direct petroleum revenues represented 51% of UGF revenues in fiscal 2022, down from 88% in fiscal 2014, but up from recent years given the recent price surge. Non-petroleum UGF revenue, which consists of excise, corporate income, fisheries, gaming and other fees and charges, totals only 5% of UGF revenues in fiscal 2022.

Under a 1977 constitutional amendment, the PF corpus receives 25% of state-derived oil royalties, rents and bonuses, as well as special general fund transfers and investment earnings. Access to the PF corpus would require an amendment to the constitution, a path the state has not pursued to date. As of Feb. 28, 2022, the PF had a principal balance of $63.8 billion, including $15.9 billion in unrealized gains.

A certain portion of the PF's annual investment earnings are channeled to the PFER, which is accessible through a simple majority vote. As of February 28, the PFER had a balance of $16.8 billion, including $3.3 billion in unrealized gains. The total combined PF balance of $80.6 billion represented a 8.6% increase over the $74.2 billion balance at Feb. 28, 2021.

Prior to the 2018 statutory change creating the POMV, the PFER was the source of appropriations for both the annual PFD paid to all Alaskans and an inflation-proofing transfer back to the PF corpus; resources were not drawn for UGF state spending. The POMV formula allows an annual draw of 5.25% of the PF's average value over the first five of the last six years, falling to 5% from fiscal 2022 onward. The draw covers both the PFD and state financial operations. Inflation-proofing the PF corpus remains subject to appropriation and has been intermittent in recent years.

Political disagreement continues on settling the question of how to split the draw between the PFD and state operations, while ensuring that inflation-proofing can still take place. Legislative proposals include instituting broad based, temporary taxes to augment UGF resources until the PF is sufficiently large to allow a POMV draw is large enough to support multiple demands, while multiple alternative proposals include narrowing the scope of state spending to ensure that a PFD set at 50% of the POMV can be met.

Looking through the inherent volatility of petroleum revenue, long-term growth prospects for energy sector revenues are expected to be relatively flat over time. Production has remained solid on the North Slope, with new fields coming into production as older fields gradually produce less output.

Average annual growth in production between fiscal years 2021-2031 as of the spring revenue forecast is 1.8%. The export of natural gas, long under discussion, has not yet come to fruition but remains a state priority, in part to address the high cost of energy paid by the state's citizens, particularly in the interior. Balanced against this backdrop are the long-term risks that decarbonization efforts and climate change regulations may reduce the industry's long-term viability.

Growth prospects for investment revenues drawn from the PFER are likely higher, although depend on actual PF investment returns, consistent inflation-proofing the PF corpus, the size of dividend payments and other factors. As of the spring 2022 forecast, a short-term bump in investment revenues in fiscal 2023 tails off to 2% annual gains late in the forecast period through fiscal 2031.

In assessing growth prospects for investment revenue, Fitch performs a simulation on PFER balances to estimate potential depletion dates of the PFER under both a lower return stress and a higher POMV draw stress. Using data and base case assumptions from the Alaska Permanent Fund Corporation (APFC, the PF's the investment manager), as of Feb. 28, 2022 Fitch's simulation indicates that the PFER is potentially sustainable through at least fiscal 2048, up from fiscal 2046 estimated last year. The analysis does not project depletion of the PF corpus.

The base case simulation assumes annual asset growth in the 5.5%/5.8% range and uses the currently forecast draws on the PFER. Actual returns that are 1% below APFC's assumed growth would result in the PFER's depletion in 2036 (holding POMV draws at the current forecast). If POMV draws exceed the forecast by $1 billion annually beginning in fiscal 2023 and asset returns match the target, asset depletion would likewise take place in fiscal 2036. The combination of both stresses would deplete the PFER in fiscal 2031.

This analysis is subject to significant assumptions, and is only intended to provide insight on the sustainability of the PFER over time, without consideration of other actions the state could take that could accelerate or delay depletion of the fund.

The state has no legal limitations on its ability to raise revenues through base broadenings, rate increases or the assessment of new taxes or fees. The state does not currently levy personal income or sales taxes. The Legislature continues to consider proposals for implementing a range of income, payroll, sales or other levies to support state operations as part of a broader debate on a permanent approach to funding the annual PFD, although to date no such proposals have been finalized.

Expenditure Framework

As in most states, education and health and human services spending are Alaska's largest operating expenses. Given its broad revenue base and the challenges of delivering public services across its large expanse, the state has taken on substantial funding responsibilities for public services delivered by local governments, school districts and tribal governments.

Additionally, the annual PF dividend is appropriated as a component of the POMV transfer from the PFER. Historically, Alaska has used periods of higher energy revenues to cover current needs and prefund future spending either on one-time or recurring bases, including state and local pay-go capital, school operating aid, and retirement obligations for the state, local governments and schools.

Fitch expects the natural pace of spending growth, absent policy actions, to be ahead of natural revenue growth. In addition to the upward pressure on public service expenses common to states, delivering effective public services imposes higher costs in Alaska than in other states given the size of the state.

Medicaid will remain a cost driver, although full federal funding of Medicaid services delivered to Alaskan Natives eases this burden to some extent. The fiscal challenge of Medicaid is common to all U.S. states. The nature of the program and federal government rules limit the states' options in managing the pace of spending growth.

As with all federal programs, Medicaid remains subject to regulatory changes that could affect various aspects. However, federal action to revise Medicaid's fundamental programmatic and financial structure does not appear to be a near-term priority of the current federal administration or congressional leadership.

Fitch views Alaska's ability to adjust expenditures to meet changing fiscal circumstances to be notably more limited than other states given the actions taken over multiple years to support budgets in the wake of the 2014-2015 plunge in oil prices. Initially in response to that situation, the state was able to reduce pay-go capital, rely on past prefunding of certain operating needs (such as school aid) and narrow transfers to budget reserves. The PFD peaked in 2015 at $2,072 per person but was reduced by 51% the next year to preserve state balances.

Spending was hit harder as budgetary reserves were drawn down, with the state holding school aid flat over multiple years and reducing its share of school construction bond debt service costs by 50% in fiscal 2020 and 100% in fiscal 2021. Since fiscal 2020, spending needs have partly been supported by federal pandemic assistance.

Carrying costs for debt service, pension actuarially determined contributions (ADCs) and OPEBs measure 6.7% of governmental expenditures in fiscal 2020, above the 5% median for the states in that year. Pension benefits and OPEBs are constitutionally protected, but carrying costs for retirement liabilities are not a significant credit risk for Alaska.

Growth in pension contributions over time will slow given closure of the state's main plans in 2006. Contributions for defined benefit pensions include the state's commitment to cover actuarial contributions for schools and local governments above specified percentages of payroll. In fiscal 2015, sizable one-time supplemental contributions from the CBR were also made to improve pension funding and lower the ADC. OPEB benefits are paid from trust funds which are fully funded, in contrast to all other U.S. states.

Long-Term Liability Burden

Alaska's long-term liability burden as of Fitch's 2021 State Liability Report, which relied on fiscal 2020 data, measured 18.8% of personal income, compared to the 4.6% median for all states; this places the state's long-term liability burden among the highest of the states. Based on 2021 data, the long-term liability burden is slightly lower, at 18.7% of 2021 preliminary personal income.

Despite Alaska's elevated liability burden, Fitch views several factors as mitigating risks both for debt and pensions. State debt measures 2.5% of personal income, and the majority is repaid from either unrestricted petroleum revenues or draws from the PFER, so the debt-to-personal income ratio is less meaningful in Alaska than in other states. The state has issued little direct debt in recent years.

Although net pension liabilities adjusted to a 6% discount rate measure 14.5% of GDP, in 2006 Alaska closed its primary defined benefit pension plans, covering general employees (at the state and local levels) and teachers, as noted above. As of the plans' fiscal 2021 audits (to be reflected in the state's own fiscal 2022 audit) and including Fitch's 6%

adjustment, the plans' ratio of assets to liabilities measured 65.9% for general employees and 77.5% for teachers, respectively. Fully-funded retiree healthcare trusts are in place for benefits paid to retirees.

Operating Performance

Operating performance has been closely tied historically to trends in the petroleum sector, although over time the PF may provide a more meaningful share of state operating funds. To remain abreast of changing energy trends, the state updates its 10-year forecasts twice yearly with detailed updates on production, prices and the impact of tax credit programs used to incentivize development. The APFC is a quasi-independent state-owned entity with fiduciary responsibility for the PF; APFC's six-member board is appointed by the governor. APFC updates performance and projections monthly, likewise allowing it to stay abreast of global trends affecting its portfolio.

The POMV mechanism has meaningfully diversified the state's revenue profile but fiscal operations remain subject to disruption from energy-related cyclicality and unresolved questions about the size of PFD payments suggests that Alaska's transition to relying on investment revenues is incomplete.

In response to weak petroleum price cycles, the state cuts expenditures and in the most recent cycle sharply reduced the PF dividend. Financial resilience is also supported by reserve balances. Chief among these is the PFER itself, which is accessible by a majority vote in the case of extreme need. The CBR and SBR have functioned more explicitly as budgetary reserves, receiving certain settlement funds (in the CBR) or revenue windfalls during strong revenue cycles and supporting operations, at least initially, during periods of revenue weakness.

Alaska's ability to support structural balance has been challenged over the last decade. According to the state's nonpartisan legislative finance division, fiscal 2021 was expected to be the ninth straight year of UGF deficit spending, despite UGF spending declining by 43% over that period and implementation of structured draws from the PF. This ongoing structural imbalance places increasing importance on the state's management of its reserves.

The CBR is projected to stand at nearly $2 billion in fiscal 2022, potentially growing to $3 billion by fiscal 2023 due to budgeted surplus operations, earnings and dispute-resolution deposits. The SBR is forecast at only $70 million in fiscal 2023; these projections exclude the impact of the state's March 15 forecast estimate. Together the combined CBR and SBR balances of nearly $3.1 billion at fiscal 2023 equal 56% of projected UGF receipts as of the Governor's executive budget, reflecting the February 15 spring 2022 forecast.

Liquidity is not a significant concern given that the state has access to resources in the PFER, the CBR, a power cost equalization endowment, the Alaska higher education investment fund and certain subfunds of the general fund.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Alaska has an ESG Relevance Score of '4' for Biodiversity and Natural Resource Management due to its exposure to the impact of natural resources management on the economy and governmental operations, which in combination with other factors, has a negative impact on the credit profile and is relevant to the rating in conjunction with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT	RATING		PRIOR
Alaska, State of (AK) [General Government]	LT IDR Affirmed	A+ Rating Outlook Stable	A+ Rating Outlook Negative

Alaska Municipal Bond Bank Authority (AK) /General Obligation - State DSRF Replenishment - 2005 Resolution/1 LT	LT	A Rating Outlook Stable	Affirmed	A Rating Outlook Negative
Alaska Municipal Bond Bank Authority (AK) /General Obligation - State DSRF Replenishment - 2016 Resolution/1 LT	LT	A Rating Outlook Stable	Affirmed	A Rating Outlook Negative
Alaska, State of (AK) /General Obligation - Unlimited Tax/1 LT	LT	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Negative
Alaska, State of (AK) /Lease Obligations - Standard/1 LT	LT	A Rating Outlook Stable	Affirmed	A Rating Outlook Negative
Alaska, State of (AK) /State Annual Appropriation/1 LT	LT	A Rating Outlook Stable	Affirmed	A Rating Outlook Negative

VIEW ADDITIONAL RATING DETAILS

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PARTICIPATION STATUS

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria (pub. 04 May 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Alaska Pension Obligation Bond Corporation (AK)	EU Endorsed, UK Endorsed

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