

CREDIT OPINION

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New Issue

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City of Las Cruces, NM

New Issue - Moody's Assign Initial A1 to Las Cruces, NM's \$9.5M in Subordinate SSGRT Bonds, Ser. 2016

Summary Rating Rationale

Moody's Investors Service has assigned an initial A1 to City of Las Cruces, NM's \$9.5 million Taxable Subordinate Lien State Shared Gross Receipts Tax Improvement Revenue Bonds, Series 2016. Concurrently, Moody's has affirmed the Aa3 rating on the city's \$58.4 million in outstanding senior lien debt secured by the 1.225% state shared gross receipts tax (SSGRT).

The Aa3 senior lien rating reflects the city's economic strength and broad pledged revenue stream, adequate legal structure, solid debt service coverage, and limited historic volatility of SSGRT collections. The initial A1 junior lien rating incorporates the subordinate nature of the pledge, satisfactory legal provisions, and healthy coverage levels. The rating also considers the expectation that the hold harmless phase out will impact future growth in pledged revenues, which may also affect future debt service coverage levels.

Credit Strengths

- » Large tax base with institutional presence
- » Healthy maximum annual debt service (MADS) coverage

Credit Challenges

- » Hold harmless phase out starting in fiscal 2016 expected to mute SSGRT growth
- » Historically stagnant collections
- » Springing Debt Service Reserve on Senior Lien

Rating Outlook

Moody's generally does not assign outlooks to local government credits with this amount of debt outstanding.

Factors that Could Lead to an Upgrade

- » Significant increases in gross receipts tax collections, absent additional debt leveraging
- » Substantial economic growth within the city

Factors that Could Lead to a Downgrade

- » Material declines in SSGRT collections compounded with hold harmless phase outs

- » Weakening MADS coverage
- » Significant leveraging of the pledged revenue sources
- » Contraction of the city's economic base

Key Indicators

Exhibit 1

| | | | | | |
|---------------------------------------|--|--------|--------|--------|--------|
| Las Cruces, New Mexico | | | | | |
| Credit Background | | | | | |
| Pledged Revenues | 33,922 | | | | |
| Legal Structure | | | | | |
| Additional Bonds Test | 1.50 | | | | |
| Open or Closed Lien | Open Lien | | | | |
| Debt Service Reserve Fund Requirement | DSRF funded at lesser of standard 3-prong test | | | | |
| MADS Coverage | | | | | |
| 2015 MADS Coverage (x) | 4.1x | | | | |
| Trend Analysis | | | | | |
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| Debt Outstanding (\$000) | 73,335 | 73,385 | 67,580 | 59,350 | 72,015 |
| Revenues (\$000) | 31,633 | 32,490 | 32,697 | 32,136 | 33,922 |
| Annual Debt Service Coverage (x) | 3.8x | 3.9x | 4.0x | 3.9x | 4.1x |

Source: City of Las Cruces, NM; Moody's Investors Service

Recent Developments

Recent developments are incorporated in the Detailed Rating Rationale.

Detailed Rating Consideration

Tax Base and Nature of Pledge: City Located in Southern New Mexico with Institutional Presence

Moody's believes the city's economy will continue improving, driven by appreciation of residential values, improved trade relations with Mexico and growth in the healthcare industry. Ongoing economic recovery should allow for stable gross receipts tax collections, which is a broad-based sales tax on all goods and services (excluding food and medical expenses). Las Cruces is located in southern New Mexico, about 45 miles north of the City of El Paso, TX, and is the second largest city in the state. The local economy is anchored by [New Mexico State University](#) (NMSU, Aa3 stable) and White Sands Missile Range, which employs approximately 6,500 and 4,500 people, respectively. However, the December 2015 Moody's Economy.com report notes that employment levels in Las Cruces have leveled after steep declines, but state government cutbacks continue to negatively impact NMSU. Moving forward, exports to Mexico and continued expansion within the healthcare sector are expected to drive growth within the city's economy.

After rapid growth in fiscal 2005 through 2009, tax base expansion has slowed. Full value increased an average of 1.3% annually over the last five years to \$6.3 billion in fiscal 2015. Population grew a modest 3.9% between 2010 and 2015 to 101,408 after increasing 31.4% between 2000 and 2010. The slowdown can be attributed largely to reduced federal spending. The city's large student population, including 15,490 students at the New Mexico State University - Las Cruces campus and 8,000 students at Dona Ana Community College, contribute to socioeconomic indices that are below average. Median family income of \$49,879 is equal to 77.1% the U.S. median according to the 2013 American Community Survey. The unemployment rate in Las Cruces of 6.1% in November 2015 was below the state (6.5%) and national rates (4.8%) for the same period.

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Debt Service Coverage and Revenue Metrics: Healthy Debt Service Coverage; Fiscal 2015 and Fiscal 2016 Revenues Show Signs of Improvement

Moody's expects state shared gross receipt tax revenue to remain stable, providing healthy debt service coverage levels over the mid-term. Since fiscal 2006, the city has reported two years of decline: a 5.5% drop in fiscal 2009 due to the recession and a 1.7% drop in fiscal 2014 due to the federal government shutdown. Overall, SSGRT revenues are fairly stable, with minimal historic volatility. Fiscal 2015 showed a 5.6% increase, with pledged revenues of \$33.9 million. Additionally, fiscal 2016 collections are strong, up 7.7% through December 2015. The city budgeted a 1.7% increase.

Fiscal 2015 collections provide a healthy 4.52 time coverage of senior lien MADS. Since fiscal 2011, SSGRT revenues have consistently provided healthy senior lien MADS coverage of over 4 times. Summing senior lien MADS (\$7.5 million) and new junior lien MADS (\$711,000), total MADS increases to \$8.3 million, and fiscal 2015 coverage decreases to a still satisfactory 4.10 times. Assuming fiscal 2016 SSGRT collection increase according to the budgeted 1.7%, the \$34.5 million would provide senior and total debt service coverage of 4.59 times and 4.17 times, respectively.

Starting in fiscal 2016, hold harmless portions of the gross receipts taxes collected by the city will be phased out over a 15 year period. The estimated phase out amounts in the near-term are modest, but compound to a significant \$4 million by fiscal 2030. The phase out amounts are expected to mute growth for the pledged revenues, but not have a material impact on debt service coverage given the overall declining debt service schedule for senior and junior liens combined. Based on pro forma projections, which incorporate the annual phase out amounts, the city expects total debt service coverage to climb from 4.24 times in fiscal 2017 to 7.97 times in fiscal 2030. Moody's notes that improving coverage is contingent on SSGRT revenue growth outpacing phase out amounts. If this assumption does not hold true, coverage may be negatively impacted, which would warrant further review.

Debt and Legal Covenants: Adequate Legal Provisions on Both Senior and Junior Lien Bonds

Post-sale, the city will have approximately \$72 million in outstanding obligations secured by SSGRT revenues. Proceeds from the Series 2016 bonds will be used to construct infrastructure for Metro Verde Voluntary Assessment District, a residential development located in northeastern Las Cruces. Officials anticipate issuing again in three years time to fund phase two of development. Although the subordinate debt is legally secured by SSGRT revenues, the city anticipates assessments collected on the sale of property within the district to sufficiently cover annual debt service. Furthermore, the bonds will be structured with an Anytime Call, allowing for early repayment if assessments warrant. Repayment on Series 2016 bonds does not begin until 2017. Debt service is flat over the 13-year maturity, with MADS of \$771,105 occurring in fiscal 2026. Moving forward, the city plans to issue \$10 million to \$11 million in SSGRT bonds in mid-2017. The debt service payout across all series is structured to allow additional issuances of debt without compromising coverage levels.

DEBT STRUCTURE

Principal amortization is average with 58.6% retired in ten years. Payout is descending in nature, with all debt retired by 2038. MADS for all series is \$7.5 million, and occurs in fiscal 2017.

DEBT-RELATED DERIVATIVES

All of the debt is fixed rate and the dedicated tax revenues have no exposure to variable rate debt or interest rate swaps.

LEGAL COVENANTS

The legal provisions associated with the senior and junior lien SSGRT debt obligations are considered average. The senior lien has an additional bonds test (ABT) of 2.0 times MADS and the debt service reserve is equal to the lesser of the standard three-prong test, but is a springing reserve triggered when coverage of outstanding debt drops below 2.0 times MADS. The junior lien will carry an ABT of 1.5 times MADS and the debt service reserve will be funded with bond proceeds at MADS (\$771,105). Additionally, \$305,000 of bond proceeds will fund a capitalized interest account for the first two maturities.

Management and Governance

New Mexico cities have an institutional framework score of "Aa," or strong. Cities receive the majority of their revenues through gross receipt and property taxes, which in combination, are moderately predictable. Most cities are at the O&M property tax levy cap, but have a moderate ability to raise revenues. Expenditures are moderately stable and management teams have ability to reduce

expenditures related to salaries and public safety. Roughly 20% of all expenditures are fixed costs, and consist of debt service and pensions contributions.

Specific to Las Cruces, the city operates under a home rule charter with a Council-Manager form of government. The six council members and the Mayor are elected for staggered four-year terms.

Legal Security

The bonds are special limited obligations, payable solely from and secured by an irrevocable lien upon the revenues of the 1.225% SSGRT subordinate to the lien thereon of senior lien bonds.

Use of Proceeds

Proceeds from Series 2016 subordinate SSGRT bonds will fund the construction of infrastructure within the Metro Verde Voluntary Assessment District.

Obligor Profile

Las Cruces is the second-largest city in [New Mexico](#) (Aaa stable), and is located approximately 45 miles northwest of El Paso, Texas.

Methodology

The principal methodology used in this rating was US Public Finance Special Tax Methodology published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 2

LAS CRUCES (CITY OF) NM

| Issue | Rating |
|---|--------------------|
| Taxable Subordinate Lien State Shared Gross Receipts Tax Improvement Revenue Bonds, Series 2016 | A1 |
| Rating Type | Underlying LT |
| Sale Amount | \$9,500,000 |
| Expected Sale Date | 03/09/2016 |
| Rating Description | Special Tax: Sales |

Source: Moody's Investors Service

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