FITCH RATES $936MM MISSISSIPPI GO BONDS 'AA+'; OUTLOOK REMAINS NEGATIVE

Fitch Ratings-New York-21 January 2015: Fitch Ratings assigns an 'AA+' rating to the following State of Mississippi general obligation (GO) bonds:

--$157.23 million GO bonds series 2015A (tax-exempt);
--$128.95 million taxable GO bonds series 2015B;
--$460 million GO refunding bonds series 2015C;
--$190 million taxable GO refunding bonds series 2015D.

The bonds are expected to sell via negotiation the week of Feb. 2, 2015.

In addition, Fitch affirms the 'AA+' rating on the state's $3.89 billion in outstanding GO bonds and the 'AA' rating on $201 million of appropriation-backed bonds issued by the Mississippi Development Bank (Dept. of Corrections).

The Rating Outlook remains Negative.

SECURITY

The bonds are general obligations of the state, with its full faith and credit pledged.

KEY RATING DRIVERS

FISCAL IMPROVEMENT: The state has taken steps toward achieving structural budgetary balance, making a sizeable contribution to the rainy day fund in fiscal 2014 when a draw-down had been anticipated, and enacting a balanced budget for fiscal 2015. Continued positive financial results, particularly in light of economic weakness that is somewhat diverging from the national trend, could lead to stabilization of the rating.

CONSERVATIVE FINANCIAL MANAGEMENT: Mississippi's financial management is generally conservative and action to maintain balance at times of revenue weakness has been prompt. Stringent budget control mechanisms exist and reserve levels remain sound, with the rainy day fund funded to the statutory maximum.

MANUFACTURING BASED ECONOMY: The state's socio-economic profile is relatively weak, with wealth and educational attainment indicators that significantly lag national levels. The economy continues to diversify and some successful economic development initiatives should bolster employment in the coming years; however, the manufacturing concentration well exceeds national levels.

COMPARATIVELY HIGH LIABILITIES DUE TO PENSION UNDERFUNDING: Mississippi's debt burden is moderate, but above average, and is largely in the form of GO debt. Unfunded pension liabilities, measured as a percent of personal income, are among the highest of the states.

RATING SENSITIVITIES

The rating may be stabilized upon demonstration of a trend of structural budget balance, as reflected in positive fiscal 2015 results and an enacted budget for 2016 that is balanced. The rating is also sensitive to economic performance that diverges from the national trend and stabilization of funding for pension liabilities.

CREDIT PROFILE

Mississippi's long-term GO rating of 'AA+' reflects the state's history of conservative financial practices and established reserves in the context of comparatively weak socio-economic profile and high long-term liabilities. The Negative Outlook reflects the state's relatively slow economic recovery and the use of one-time revenues to support on-going expenditures despite revenue recovery in recent years. As will be discussed further below, the current fiscal 2015 budget and proposed executive budget for fiscal 2016 do not utilize such one-time resources, a positive development.

FISCAL STABILIZATION

Fiscal operations are stabilizing with strong revenue growth over the past three years, reduced use of one-time revenues, and full funding of the state's rainy day fund (the Working Cash Stabilization Fund). The gradual draw-down of the rainy day fund, which had reached a peak funding level of $362 million in fiscal 2008, allowed the state to manage reductions in tax revenue associated with the recession. However, with revenues rebounding and after depositing $188 million of the fiscal 2013 surplus into the fund, the enacted fiscal 2014 budget anticipated utilizing $109 million of the balance, a factor which contributed to the assignment of the Negative Outlook. As with the anticipated use of the rainy day fund, the fiscal 2014 budget also drew upon balances in the budget contingency fund to cover a significant increase in Medicaid spending.

With revenue performance in fiscal 2014 that outperformed forecast - general fund revenues were 6.3% higher than forecast and increased 5.6% on a year-over-year basis - the state was able to forego the draw on the rainy day fund and instead, made a sizeable contribution. The rainy day fund, as of the end of fiscal 2014, was funded at its statutory maximum of 7.5% of appropriations at $411 million.

The fiscal 2015 budget as enacted is balanced and does not utilize one-time revenues to fund on-going spending. Revenue estimating continues to be conservative, with the forecast for the current fiscal year requiring minimal growth (1.1%) over final prior-year results. Most of this revenue growth is allocated to spending pressure related to growth in Medicaid. Year-to-date, revenues are ahead of forecast, up 3.8% through December. The state did, however, suspend its 98% budgeting policy for fiscal 2015, citing its fully funded rainy day fund.

The governor's budget proposal for fiscal 2016 would also suspend the 98% budgeting policy in order to fund a tax credit that would only go into effect when revenue growth exceeds 3% and the rainy day fund is fully funded. Given these limits, Fitch does not expect the application of the set-aside to finance a tax credit to be material to credit quality. However, repeated suspension of the set-aside lessens its value as a budget control mechanism.

MANUFACTURING BASED ECONOMY

Mississippi's economic and demographic profile is relatively weak. The employment base, when compared nationally, is overweight in the more volatile manufacturing sector. Wealth levels are very low for a U.S. state - per capita income is ranked 50th among the states and the poverty rate is the highest among the states.

The state lost jobs in the recession generally in line with the U.S. experience, with employment down 5.3% between 2007 and 2010 compared to a 5.6% loss for the nation. However, the state lagged the U.S. in the recovery and employment growth has not been consistent. Non-farm employment growth has consistently lagged the U.S. over the past year, and declined 0.1% in November 2014 as compared to a 2% increase in the U.S. Construction employment fell sharply, -7.7% year-over-year, but service sector employment, which is a source of growth nationally, is also weak in Mississippi. The unemployment rate has fallen from its peak of 11% in February 2010, but remains above the U.S. rate at 7.3% in November 2014, compared to 5.8% for the U.S. With the state's investment in economic development projects designed to diversify and expand the economy, continued moderate growth is expected despite recent weakness.

ABOVE AVERAGE LIABILITIES

The state's net tax supported debt of approximately $5.3 billion represents a moderate but above average burden on resources at 5.3% of 2013 personal income. Debt is largely GO and amortization is average, with 51% of outstanding GO debt to be retired in 10 years. However, overall liabilities are quite high for a U.S. state, with the combined ratio of debt and unfunded pension liabilities (adjusted by Fitch) representing 19.3% of 2013 personal income (as of Fitch's May 2014 pension medians report). This ranks the state 46th of U.S. states and is well above the median of 6.1%.

The state utilizes a funding methodology that employs a fixed contribution and variation of the amortization period for its unfunded accrued liabilities. Despite having raised employer contributions to 15.75% of payroll and employee contributions to 9% of payroll, the funding of the state's Public Employees' Retirement System declined to 57.7% as of June 30, 2013 and its amortization period increased to 32.2 years. However, with positive investment returns and five-year asset smoothing that now fully incorporates the deep losses of 2009, pension funding increased slightly as of June 30, 2014 to 61%, and the amortization period dropped below 30 years. As reported under the new reporting requirements of GASB 67, the PERS fiduciary net position as a percentage of the total pension liability was 67.2% as of June 30, 2014. Fitch notes that the demands of debt and pensions on the state's operating budget continue to be manageable.

The current offerings finance various capital improvements as well as refund outstanding bonds for debt service savings.

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In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria'(Aug. 14, 2012);
--'U.S. State 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. State Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686033