MOODY'S INVESTORS SERVICE

Rating Action: Moody's Upgrades South Dakota's Lease-revenue Bond Ratings to Aa1; Outlook Stable

Global Credit Research - 19 Feb 2016

New York, February 19, 2016 -- Summary Rating Rationale

Moody's Investors Service has upgraded to Aa1 the ratings on South Dakota's lease-revenue bonds issued through the South Dakota Building Authority and the South Dakota Health and Education Facilities Authority.

The upgrade reflects governance improvements the state implemented recently combined with very strong credit fundamentals. South Dakota's credit benefits from conservative fiscal practice, low fixed costs and a stable and healthy economy. The Aa1 rating reflects the subject-to-appropriation nature of the lease-revenue bonds. South Dakota has no issuer or general obligation debt rating.

Rating Outlook

The stable outlook reflects our expectation of continued economic stability and that, in the event of a downturn in revenues, expenditures will be adjusted to maintain a high level of reserves.

Factors that Could Lead to an Upgrade

An upgrade is unlikely given the Aa1 ratings and the subject-to-appropriation nature of the lease-revenue bonds

Factors that Could Lead to a Downgrade

Economic deterioration

Sharp reduction in fund balance

Return to use of one-time revenues to resolve budget gaps

Inability to surmount constitutional constraints on fiscal flexibility

Legal Security

South Dakota's lease revenue bonds are secured by lease payments from state agencies or departments to the authorities, subject to appropriation. Rents paid to the authorities are fixed at a rate sufficient to pay debt service. The authorities covenant that they will seek an appropriation from the state legislature to the department or agency sufficient to pay debt service.

Moody's views the risk of non-appropriation as slight, given the state's reliance on subject-to-appropriation lease debt to finance a broad range of projects, both through the South Dakota Building Authority and the Health and Educational Facilities Authority. South Dakota's constitution prohibits significant amounts of general-obligation borrowing. The underlying leases stipulate that should the agency or department fail to pay rent, the authority will exclude the agency or department from all leased facilities, providing an additional incentive for the agency or department to pay the amount due. All lessee payments flow through a single state fund so that default on any one bond would translate to a default on all lease-appropriation bonds of either authority, providing additional incentive for the state to appropriate funds for debt service.

Use of Proceeds

This rating action was not the result of a sale.

Obligor Profile

South Dakota is the 47th-largest state with a population of 845 thousand. It had a gross domestic product of $46 billion in 2014, which ranks 47th in the US and a per-capita personal income of $46,345 in 2014.

Methodology

The principal methodology used in this rating was The Fundamentals of Credit Analysis for Lease-Backed Municipal Obligations published in December 2011. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

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