Alaska Risks Another Downgrade With Record Bond Sale.

Alaska, whose finances have been roiled by the oil-price crash, is issuing the biggest bond in its history and letting the proceeds ride in financial markets.

Governor Bill Walker is using money from next week's $2.4 billion sale — the equivalent of $3,186 for every resident — to pay down the state's debt to public-employee retirement funds, wagering it can earn more on stocks, bonds and other investments than it will cost to borrow. The scale of the offering may trigger another downgrade to Alaska, with S&P Global Ratings saying last week that it anticipates cutting its general obligations by one step to AA, the third-highest investment grade, after the deal closes.

The state's move comes as government pension funds deal with setbacks brought on by turmoil in equity markets and low interest rates that have cut returns on fixed-income investments. U.S. retirement systems in the year through June posted the smallest gains since the 2008 credit crisis, according to the Wilshire Trust Universe Comparison Service, putting pressure on governments to pour more cash into the funds to make up for lost ground.

Fitch Ratings said Alaska's plan will curb its pension-fund bills, though it also exposes the state to risks if investment returns falter. S&P said the state may raise as much as $3.3 billion for its retirement plan by issuing securities.

"If I like to borrow money and take it to Vegas, it can be a problem if I'm living pay check to paycheck," Elizabeth Kellar, president of the Center for State and Local Government Excellence, said of bond deals like Alaska's. "If your finances are fragile and you go in at the wrong time it can create major difficulties."

Alaska's $6 billion pension-fund shortfall is adding to the financial strain on the state, whose revenue was cut by more than half in 2015 as oil prices fell. Moody's Investors Service, S&P and Fitch all had their top ratings on the state until this year, when they downgraded it because of the energy-industry rout.

With interest rates in the municipal-bond market holding not far from more than half-century lows, Alaska officials anticipate that they can profit by reinvesting the borrowed money. The bonds will carry a higher yield than typical state and local debt because the interest is subject to the federal income tax. Even so, Honolulu sold taxable securities this month for a top yield of 3.2 percent on debt due in 2034.

"At rates of 4 percent or below it becomes compelling," said Deven Mitchell, Alaska's debt manager. "The state faces increasing payments and that's what we want to equalize over time."

While Alaska's retirement plans lost 0.4 percent in the year through June, Mitchell said the state's rolling 5-year return has been 6.5 percent. The pension borrowing, which won't be paid off until 2039, will save the government about $2.5 billion if "historical returns are met," Revenue Commissioner Randall Hoffback said in a Sept. 15 memo to lawmakers.

The strategy has been used by other state and local governments. Kansas sold $1 billion of pension bonds in August 2015, and officials in Houston and Oregon have proposed considering similar steps.

Whether it pays off depends on timing, according to a July 2014 study by the Center for Retirement Research at Boston College. While the tactic proved profitable after the recession because of low interest rates and a rebound in the stock market, governments who employed it before the 2000 and 2008 market crashes lost money.

Detroit's pension-fund borrowing in 2005 and 2006 contributed to the biggest municipal bankruptcy in U.S. history, while New Jersey, Illinois and Puerto Rico borrowed only to see their retirement systems continue to struggle. Former New Jersey Governor Jon Corzine, a one-time Goldman Sachs Group Inc. co-chairman, in 2008 called such bond deals the "the dumbest idea I ever heard."

"The question is whether this is the best alternative when your hands are tied and you behind the eight-ball," said Jean-Pierre Aubry, associate director state and local research at the Center for Retirement Research. "The big thing is that it still doesn't absolve the government of the debt."

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