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# City And County Of Honolulu, Hawaii; General Obligation; General Obligation Equivalent Security

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# City And County Of Honolulu, Hawaii; General Obligation; General Obligation Equivalent Security

Credit Profile		
US\$378.06 mil GO bnds ser 2009A-C due 04/01/2034		
<i>Long Term Rating</i>	AA/Stable	New
Honolulu City & Cnty GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Honolulu City & Cnty bnds dtd 04/01/1994		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
<b>Honolulu City &amp; Cnty GO</b>		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed

## Rationale

Standard and Poor's assigned it's 'AA' long-term rating on Honolulu City and County, Hawaii's series 2009A-C general obligation (GO) bonds. At the same time, Standard & Poor's affirmed it's 'AA' long-term rating and underlying rating (SPUR) on the city's outstanding GO debt.

The rating reflects:

- The city's role as the service, trade, and government center as well as its status as the Hawaii's main metropolitan area;
- An enduring tourism sector that has been quick historically to rebound from periods of economic weakness;
- Strong financial performance and reserves; and
- A moderate debt burden and affordable property tax rate.

A history of volatility in property values, prior to the current rebound, continues to be a tempering factor, in addition to concerns about affordability for city residents given the area's average resident income levels.

The bonds are secured by the full faith, credit, and unlimited ad valorem taxing authority of the City and County of Honolulu.

With roughly 900,000 residents, or 72% of the state's total population, Honolulu is Hawaii's economic center as well as the center of government, transportation, finance, and education. Tourism accounts for about 25% of the gross state product, and more than 50% of the state's hotel rooms are located in Honolulu. Waikiki, located adjacent to downtown Honolulu, remains the state's most-visited destination. Honolulu's tourism market has rebounded strongly recently, along with the rest of the state. The city and island are additionally anchored by the presence of the U.S. military. Unemployment has usually been better than the nation as a whole, and that is still true in today's economy -- even though the unemployment rate is now 5.2%, more than two times what it was in 2007. Effective buying income levels above the state median and 111% of the national median on a household basis,

although it is slightly lower, at 94%, on a per capita basis.

After years of booming real estate values that averaged 13% annual growth between 2001 and 2009, there was a decline in prices in the third quarter of 2008, albeit a slight one in comparison with other real estate markets. The situation is not unprecedented, as the real estate market for much of the early- to mid-1990s was relatively stagnant.

Honolulu in fiscal 2009 adjusted its tax rate to \$4.83 per \$1,000 in assessed value (AV), compared to \$4.73 per \$1,000 in AV in fiscal year 2008. In fiscal 2008, the unreserved general fund balance was a healthy \$107.3 million; this is expected to be drawn down to \$57.6 million by fiscal 2010. Notably, the reserve for the fiscal stability fund had a balance of \$18.1 million as of fiscal year 2008, which is expected to remain intact in the near term. Fiscal 2010 and 2011 look to be challenging years, as revenues are expected to remain flat due to declining revenues and because some expenditure growth, namely contracted labor agreements, are unavoidable. The mayor's proposed 2010 budget calls for closing a \$128.0 million gap or about 8% of the overall \$1.8 billion budget, mainly through staffing reductions and management pay cuts.

The city's financial management practices are considered 'good' under Standard & Poor's Financial Management Assessment (FMA). An FMA of 'good' indicates that government practices are deemed currently good, but not comprehensive. Highlights include the formal fiscal stability reserve policy, a debt management policy limiting the conditions and amount of debt issuance, and quarterly presentation of actual financial performance to the mayor and city council. Investments are managed by the city treasurer, which publishes an annually reviewed investment policy; investment performance is disclosed annually in the city financial statements. Expenditures are historically budgeted on a conservative basis, with significant positive annual variances generally between actual and budgeted expenditures. The city finance staff maintains a six-year financial forecast that is formally presented to city council for review via the annual budget process.

The city's debt burden after the current issuance remains moderate, at \$2,210 per capita and low at 1.1% of market value, excluding self-supported GO debt and enterprise debt. The city has continued to scale back its GO debt issuances to roughly every two years, including the \$268.6 million new-money issuance in 2007, which is in line with the current administration's focus on the need for ongoing revenues to support new projects and a current emphasis on water and wastewater projects funded with system revenues and revenue debt. Amortization of GO debt is relatively rapid, with 55% of principal amortized over 10 years and 92% over the next 20 years. The city anticipates issuing additional GO debt during fiscal 2009.

The city's pensions and other post-employment benefits (OPEB) are managed by the state pension fund. The state's most recent valuation for the city estimates that the city's total OPEB liability is \$1.95 billion with no pre-funding and \$1.24 billion with pre-funding, although the city is not currently able to pre-fund due to current limitations on accounting for such contributions at the state level. The city did, however, include an appropriation for \$40.00 million in funding for an internal reserve for OPEB in the fiscal 2008 budget along with \$85.60 million in pay-as-you-go retiree healthcare costs.

## Outlook

The stable outlook reflects our expectation that the declines in the city's economic activity will moderate, rather than worsen seriously. The outlook further reflects our expectation that city staff and council will continue to manage deficits with timely decreases in recurring expenditures, as they have to date, which help provide stability

and credit strength during the current economic cycles.

## Economy: Property Values Continue To Increase

The real estate market has a volatile history so the current situation, characterized by moderate declines in value, has precedent in the local economy. From 1995 to 2001, property values dropped 23%, due primarily to the aftermath of a boom in construction and property values in the late 1980s driven by Japanese investment. After the departure of this capital, beginning in 1990, the property market weakened significantly. Since 2001, however, total AV has increased 140%, or more than 17% per year on average and about 20% in both fiscals 2006 and 2007.

Tourism, the main industry in Honolulu, is hurting due to the condition of the national and global economy. Hotel occupancy has declined to 68% from 75% a year ago and the numbers of tourists visiting the island, foreign and domestic, have dropped 5% and 12%.

## Financial Challenges Are Manageable

The city depends primarily on property taxes, which accounted for 72% of general governmental revenues, not including charges for services or grants and contributions derived from property values that are relatively predictable from year-to-year, even during periods of decline in real market value. As a result of property tax dependence, city revenues experienced significant pressure during the 1990s but rebounded strongly through 2007.

During the period of property tax declines, the city was able to cut expenditures, but also maintained lower-than-average fund balances. The average property tax rate was increased in 2004 after several years of reductions. The new city administration, elected in November 2004, has stated its intent to maintain property tax rates to support current service levels while paying close attention to the cost versus the benefit of some more discretionary government expenditures. Property taxes in Honolulu and in Hawaii in general are currently among the lowest in the nation, as is the state's 4% sales tax.

The ending financial position for 2009 is expected to be strong, due to spending constraints as revenue sources weakened. For 2010, some expenditure growth will be unavoidable due to existing labor contracts, and this will require the spending down of some reserves in fiscal 2010 unless the economy recovers sooner than expected.

<b>Ratings Detail</b> (As Of March 25, 2009)		
Honolulu City & Cnty go bnds ser 2003A dtd 08/08/2003 due 03/01/2008-2028		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Honolulu City & Cnty GO bnds ser 1996A dtd 09/01/1996 due 09/01/2000-2016		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Honolulu City & Cnty GO bnds ser 2005A dtd 05/26/2005 due 07/01/2009-2029		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Honolulu City & Cnty GO bnds ser 2007B due 07/01/2028		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Honolulu City & Cnty GO bnds ser 2007C due 07/02/2020		
<i>Long Term Rating</i>	AA/Stable	Affirmed
<b>Honolulu City &amp; Cnty go unlted tax imp rfdg bonds ser 2004B</b>		

<b>Ratings Detail (As Of March 25, 2009) (cont.)</b>		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
<b>Honolulu City &amp; Cnty GO</b>		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
<b>Honolulu City &amp; Cnty GO unlted</b>		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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