Moody's
INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS Aa1 RATING AND STABLE OUTLOOK TO CITY AND COUNTY OF HONOLULU'S G.O. BONDS 2011

Global Credit Research - 07 Jul 2011

Approximately $2.6 Billion of Debt Affected, Including Current Offerings

County
HI

Moody's Rating

ISSUE		RATING
General Obligation Bonds, Series 2011A		Aa1
Sale Amount	$137,645,000	
Expected Sale Date	07/13/11	
Rating Description	General Obligation	
General Obligation Refunding Bonds, Series 2011B		Aa1
Sale Amount	$175,145,000	
Expected Sale Date	07/13/11	
Rating Description	General Obligation	

Opinion

NEW YORK, Jul 7, 2011 -- Moody's Investors Service has assigned a Aa1 rating and stable outlook to the City and County of Honolulu's General Obligation Bonds, Series 2011A and General Obligation Refunding Bonds, Series 2011B expected to be issued in the aggregate amount of approximately $312.8 million. The Series 2011A ($137.6 million) will finance various capital improvement needs. The Series 2011B bonds ($175.1 million) will refund outstanding general obligation bonds for debt service savings. In conjunction with the current credit review, Moody's has also affirmed the Aa1 rating and stable outlook on the city's approximately $2.5 billion of outstanding general obligation bonds. The bonds are secured by an unlimited property tax pledge; debt service payments represent a first charge on the city's General Fund.

SUMMARY RATINGS RATIONALE

The Aa1 rating primarily reflects the city's sizable economic base, above average resident wealth, and sound financial operations with recently improved reserve levels, as well as a manageable debt profile. Although the local economy has begun to recover slightly, Moody's will continue to monitor management's ability to prudently address long-term fixed costs, improve reserve levels, and maintain overall fiscal stability.

STRENGTHS

-Improving tourism sector complemented by substantial military and government sectors

-Prudent fiscal management demonstrated by conservative budgeting practices and recently improved reserve levels

CHALLENGES

-Above average cost of living and relative isolation act as barriers to growth

-Rising pension, health and benefit costs

DETAILED CREDIT DISCUSSION

HONOLULU'S ECONOMY CONTINUES TO SLOWLY RECOVER, YEAR-TO-DATE VISITOR TRAFFIC IMPROVES; ASSESSED VALUE INCREASES SLIGHTLY IN 2012

Honolulu's economic recovery continues, albeit at a gradual pace. After softening in 2006, visitor arrivals and hotel occupancy percentages remained somewhat sluggish until improving in 2010 and again through April 2011. Despite rising fuel prices, the local airline, Hawaiian Airlines, appears to be solid with plans for additional aircraft purchases over the next four years. Moody's also notes projects in renewable energy, the film and television industry, and sustainable agriculture continue to lend support to ongoing diversity in the Honolulu economy alongside traditional economic anchors including the military, health care, and banking sectors.

Real estate has also been another important element of Honolulu's economic success. However, between 2007 and 2009 home prices declined, although modestly relative to the rest of the nation. After trending gradually upward, as of May 2011, home sales and prices dipped slightly year-to-date and overall construction has slowed, although only slightly from a year ago. Over the medium-term, numerous residential and commercial projects are in various stages of planning and construction and are expected to provide support for assessed value growth. Between 2006 and 2011, assessed valuation (AV) has grown by an average of 6.1% annually, including a significant decline of 7.8% in 2011 to a still sizeable $153.1 billion with slight growth in 2012 and estimated flat growth in 2013. Moody's notes Honolulu has not experienced high foreclosure activity given the relative rarity of sub-prime financing in Hawaii. Despite the moderating influence of many tourism-related service jobs, wealth indicators in Honolulu are favorable with per capita and median family income at 107.1% and 149.3% of the U.S., respectively. The city's full value per capita totals an impressive $160,625.

Honolulu's unemployment rate continues to be a credit strength and stood at 4.6% as of April 2011, compared with 5.6% for the state and 8.7% for the nation. The substantial military and government presence provides a stable employment base while business services as well as education/ healthcare and leisure /hospitality sectors have provided some job growth. Construction of the $5.3 billion, 20-mile rail transit system appears to be on track with a recent ground breaking in February 2011 and should help to boost the city's recovery, in particular, by facilitating new development along the east-west corridor between Kapolei and Ala Moana Center.

PRUDENT REVENUE ADJUSTMENTS AND CONTROLLED SPENDING IMPROVE RESERVE LEVELS IN FY 2010 AND AGAIN IN FY 2011

Despite continued budget stress over the last two years, the city's financial operations are characterized by prudent budgetary and revenue enhancement measures and controlled spending. As a result, management improved reserve levels in FY 2010 and again FY 2011. Management's commitment to maintaining budget balance and adequate reserve levels has been an important factor in Moody's credit evaluation of Honolulu.

Audited results for fiscal 2008 showed a $10.3 million operating surplus in the General Fund which resulted in total fund balance of $166.1 million, or 13.1% of General Fund revenues; unreserved fund balance totaled $107.3 million, or 8.5% of revenues, which exceeds the city's target range of 5% to 8% of expenditures. Fiscal 2009 reserves declined due to sluggish revenue growth combined with increased salaries and retirement system contributions, a higher transfer amount to the city's OPEB reserve as well as a small increase to the city's Reserve for Fiscal Stability Fund (RFSF). The FY 2009 unreserved General Fund balance was 5.2% of general fund revenues ($67.8 million); combined with the RFSF ($26.1 million), available reserves totaled 7.2% of general fund revenues ($93.9 million).

Going into FY 2010, although management implemented aggressive spending restrictions, department cuts and a hiring freeze to offset a significant budget gap (approximately $127 million), the budget had also indicated a sizeable drawdown of the unreserved general fund balance. Positively, management outperformed budgeted expectations and increased the FY 2010 unreserved general fund balance to 8.1% of general fund revenues ($104.0 million); combined with a slight increase to the RFSF available reserves totaled 10.2% of general fund revenues ($130.9 million). For FY 2011 management continued various spending restrictions and prudently increased the residential non-homeowner property tax rate from $3.42 to $3.58 per $1,000 AV. In addition, management again contributed to its RFSF resulting in an estimated unreserved general fund and RFSF available balance increasing to 13.3% of general fund revenues.

For the current fiscal year (2012) management projects reserves will remain similar to the prior year despite remaining budgetary challenges given conservative budgeting policies, an ongoing hiring freeze and, subject to collective bargaining, 5% labor savings. Moody's notes, to close its own budget deficit, the state capped transient accommodation taxes distributed to counties, including Honolulu, through FY 2015. Given the small amount of the distribution relative to other operating revenues, county officials do not believe the cap will have a material adverse impact on county finances.

Moody's believes prudent budgeting measures will support both preservation and gradual improvement of reserve levels in the near term. Nevertheless, similar to most major municipalities, Honolulu will continue to face its share of budget challenges in the near-term, in part due to the rising pension, health and benefit costs. The city faces a substantial OPEB liability, currently estimated at $1.95 billion (with no prefunding), with an associated annual cost of $142.4 million. As mentioned above the city contributed $40.1 million to its OPEB liability and plans to resume fully funding the annually required contribution when economic conditions improve.

MANAGEABLE DEBT POSITION; AVERAGE PAYOUT

Moody's expects that Honolulu's debt levels will continue to remain manageable given reasonable borrowing assumptions and a relatively conservative debt structure. In addition, Honolulu benefits from the active role the state government plays in financing traditional municipal capital needs more typically funded at the local level throughout the rest of the country including transportation, health, justice, and education. In addition, management has begun to fund the construction activities of various enterprise systems from system rates rather than property taxes. As a result, future borrowings will emphasize revenue bond offerings in addition to general obligation issuances. The city's debt burden compares favorably to other cities and counties in the U. S. with overall debt representing only 1.4% of fiscal 2011 taxable values, although debt per capita is above average ($2,151). Including the current offering, the city has approximately $2.6 billion of outstanding general obligation bonds; the city has no exposure to long-term variable rate debt or derivative instruments in its G.O. borrowing program. Approximately 48.4% of the city's general obligation debt is retired in ten years.

Outlook

The stable rating outlook on Honolulu's general obligation bonds reflects Moody's expectation that the city's gradual economic recovery will continue, albeit slowly, over the medium-term supported in part by the large and stable government and military sectors. The stable credit outlook also incorporates Moody's expectation that city management will continue to take the actions necessary to ensure fiscal stability in light of flat revenue growth and rising pension, health and benefit costs over the near- to medium-term.

WHAT WOULD MAKE THE RATING GO UP

-Significant diversification of economic base

-Significant and sustained increase in reserve levels

WHAT WOULD MAKE THE RATING GO DOWN

-Deterioration of financial operations and reserve levels

-Prolonged declines in assessed valuation

KEY STATISTICS:

2011 population: 953,207

2007 per capita income: $28,033 (107.1% of U.S.)

2007 median family income: $74,667 (149.3% of U.S.)

2011 full valuation: $153.1 billion

2011 full value per capita: $160,625

Direct and overall debt burden: 1.4%

Payout of principal, 10 years: 48.4%

FY 2010 total General Fund balance: $150.0 million (11.6% of General Fund revenues)

FY 2010 unreserved General Fund balance: $104.0 million (8.1% of General Fund revenues)

FY 2010 unreserved GF balance and other available reserves (RFSF): $130.9 million (10.2% of general fund revenues)

The principal methodology used in this rating was General Obligation Bonds Issued by U.S. Local Governments published in October 2009. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides relevant regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides relevant regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides relevant regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

Information sources used to prepare the credit rating are the following: parties involved in the ratings, public information, and confidential and proprietary Moody's Analytics information.

Moody's considers the quality of information available on the rated entity, obligation or credit satisfactory for the purposes of issuing a rating.

Moody's adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable including, when appropriate, independent third-party sources. However, Moody's is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

Please see ratings tab on the issuer/entity page on Moodys.com for the last rating action and the rating history.

The date on which some Credit Ratings were first released goes back to a time before Moody's Investors Service's Credit Ratings were fully digitized and accurate data may not be available. Consequently, Moody's Investors Service provides a date that it believes is the most reliable and accurate based on the information that is available to it. Please see the ratings disclosure page on our website www.moodys.com for further information.

Please see the Credit Policy page on Moodys.com for the methodologies used in determining ratings, further information on the meaning of each rating category and the definition of default and recovery.

Analysts

Dan Steed
Analyst
Public Finance Group
Moody's Investors Service

Matthew A. Jones
Backup Analyst
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
USA

MOODY'S
INVESTORS SERVICE

professional adviser.