

Tax Supported  
New Issue

## City and County of Honolulu, Hawaii

### Ratings

#### New Issue

General Obligation Bonds,  
Series 2004A, 2004B,  
and 2004C..... AA

#### Outstanding Debt

General Obligation Bonds ..... AA  
Rating Outlook ..... Stable

### Analysts

Amy S. Doppelt  
1 415 732-5612  
amy.doppelt@fitchratings.com

Jenny Porec  
1 415 732-5618  
jenny.porec@fitchratings.com

### Issuer Contact

Ivan Lui-Kwan  
Director of Budget and Fiscal Services  
1 808 523-4617

### New Issue Details

\$250,000,000 General Obligation Bonds, Series 2004A, 2004B, and 2004C, are scheduled to sell on or about March 30 through negotiation by UBS Financial Services Inc. The bonds mature serially July 1, 2005–2028. Call features will be determined at pricing.

**Security:** The bonds are secured by the City and County of Honolulu's full faith and credit unlimited ad valorem tax pledge.

**Purpose:** Bond proceeds will be used to refund outstanding variable- and fixed-rate bonds.

### ■ Outlook

The City and County of Honolulu's credit strength rests in the sound fundamentals of its tourism-based economy, good financial operations and reserves, low debt burden, and strong fiscal management. Honolulu's tourism sector has adapted well to a shift to predominantly domestic-based visitors, as well as reduced activity. Elements such as its role as the area's commercial center and state capital and its sizable military presence add stability. Tourism on the island is highly developed and has long-lasting underpinnings providing continual demand, albeit at a reduced level. The city's spending growth has been restrained and kept in line with revenues, resulting in prudent and above-average general fund balances. The low debt burden reflects the state's sizable role in financing capital needs. Expected annual issuance will increase debt levels, although they will remain affordable.

### ■ Rating Considerations

Coterminous with the Island of Oahu, the city encompasses much of the state's economic activity. Honolulu makes up 72% of Hawaii's population, about two-thirds of the visitors, and about one-half of the hotel rooms statewide. The island's tourism draw is based on sustainable elements, such as natural beauty, diverse accommodations and activities, and proximity to sizable North American markets.

As the area's commercial and business center, the state capital, and the home of the University of Hawaii, Honolulu's nontourism private sector employment is substantial. The U.S. military also is a major economic element, taking advantage of the island's strategic location. Federal defense spending makes up about 8% of the gross state product, with most of the activity on Oahu. Tourism is recovering from a long decline and is more dependent on U.S. visitors than those from Asia. While domestic visitors represent much lower spending than Asian tourists on average, they provide more stable demand. Oahu's total visitor count has stabilized, following a 10% decline in 2001, with domestic visitors now making up 71% of the total. However, international visitors continue to decline. The hotel occupancy rate rose to 71% in 2003 from 69% in 2001. The 2003 gain is notable as the first increase accompanied by an average room rate hike since 1998.

The city's real estate market is in good condition, as evidenced by low-to-moderate vacancy rates, rising home sales and prices, and significant new construction. Commercial construction was aided by a temporary tax abatement program. Assessed value has grown for the past four years, with the fiscal 2005 gain the strongest at double-digit levels. This trend reverses several years of taxable value declines as the market adjusted to reduced foreign demand. Total assessed value now exceeds the fiscal 1999 level.

March 25, 2004

Financial operations rely primarily on property taxes; Honolulu's revenue base includes only a small amount that is directly reliant on tourist activity. The general fund had operating surpluses in five of the past six fiscal years. The fund balance rose to \$72.8 million, or 11% of spending, in fiscal 2003, and it has averaged nearly 9% since fiscal 2000. The good results primarily reflect expenditure growth kept to low levels through organizational restructuring, privatization, and employee reductions. Operations in fiscal years 2002 and 2003 also benefited from a sizable capital spending reimbursement. The city expects the recent strong property tax base gain to provide revenue needed to offset these payments, which end in fiscal 2004. Honolulu's fiscal future should continue to be sound but will be challenged by sizable increases in employee health and pension costs, as well as ongoing labor expenses. Good management practices include spending restraint; tax rate increases; and the creation of a rainy day reserve, now equaling \$5 million.

Fiscal management is sound, as evidenced by low expenditure growth and prudent tax and fee rate increases and creation of a rainy day fund reserve, which now totals \$5.0 million. The city plans to increase this reserve over time as surplus city housing assets are sold. For fiscal 2004, the city raised residential property tax rates and enacted other revenue enhancements, including increases in certain fees, the motor vehicle weight tax, and bus fares. The

city expects general fund results to approximately break even this year, resulting in a fund balance similar to those in prior years. In addition, the city will maintain the rainy day reserve at \$5.0 million.

### ■ Strengths

- Tourism-based economy has strong underpinnings, such as physical beauty, public and private infrastructure, and location.
- Role as regional economic center and state capital provides some diversity and stability.
- Good financial operations despite strained revenues, as well as good ending balances.
- Prudent management actions in recent years, including tax rate and fee increases, organization consolidation, and spending controls.
- Low debt burden (average including state bonds).

### ■ Risks

- Tourism-based economy's vulnerability to numerous domestic and international events and economic conditions.
- Labor cost increases and uncertainty resulting from sizable growth in health care and retirement expenses, as well as statewide contract negotiations.

*For more information, see Fitch Research on "City and County of Honolulu, Hawaii," dated July 25, 2003, available on Fitch's web site at [www.fitchratings.com](http://www.fitchratings.com).*