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November 18, 2011

Summary:

Los Angeles County, California; Appropriations; General Obligation

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Credit Profile		
US$59.16 mil Lse Rev Bnds (Lac-cal Equip Fincg) ser 2011A due 06/01/2017		
Long Term Rating	A+/Positive	New
Los Angeles Cnty cap apprec bnds (Disney Pkg Proj)		
Long Term Rating	A+/Positive	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'A+' long-term rating, and positive outlook, to Los Angeles County, Calif.'s lease revenue bonds (LAC-CAL Equipment Program) series 2011A.

At the same time, Standard & Poor's affirmed its 'AA-' issuer credit rating (ICR) and 'A+' long-term rating on the county's lease-secured debt outstanding. The outlook is positive.

The ratings on the lease secured debt reflect what we view as:

- The long-term creditworthiness of Los Angeles County; and
- A covenant to budget and appropriate pledged lease payments on the individual leased assets pledged to each bond series, subject to abatement in the event of damage or impairment to the leased properties.

The 'AA-' ICR and the county's long-term general creditworthiness reflect what we consider:

- A very large, deep, and diverse economic base, although one currently experiencing elevated unemployment levels;
- Relatively stable property tax revenue and assessed valuation (AV) in the county despite large home price declines in the past several years; and
- Historically strong unreserved general fund balances and strong financial management practices.

Partially offsetting the above factors are what we see as Los Angeles County's:

- Responsibility for health care and social service spending for a large urban population;
- Limited revenue-raising capability combined with mandated costs and state funding cuts, including a recent state action to realign certain services at the local level that will require permanent funding sources in the future; and
- Long-term need to address a large $23 billion unfunded other postemployment benefits (OPEB) liability.

The county's covenant to budget and appropriate lease payments for use of equipment secures the 2011 lease revenue bonds.

We understand that the series 2011A bond proceeds will be used to redeem bond anticipation notes (BANs) issued between March 2010 and September 2011 to purchase equipment. The bonds mature on June 1, 2017, and the county reports the average life of the bonds is shorter than the useful life of the equipment. Cash reserves accumulated for the BANs will also be used to take out the full amount of existing BANs. The leased assets securing the series 2011A bonds will consist primarily of vehicles, hospital and medical equipment, technology infrastructure equipment, and helicopters. We understand that bond proceeds will also be used to fund a debt service reserve at $2 million, although this is significantly lower than annual debt service on the bonds. The debt service payment dates of June 1 and Dec. 1, which occur at least five months after the end of the county's fiscal year-end, mitigate the risk of late budget adoption in our view. The lease agreement also requires the county to maintain all risk insurance at least equal to the replacement value of the equipment amount, less a $1 million deductible, as well as two years of rental interruption insurance. The lease agreement permits the county to self-insure for risks other than rental interruption.

In our view, Los Angeles County has a very large and diverse economic base, with a slowly growing population of about 10 million residents, or 27% of California's population. The regional economy has shown signs of recovery with a slight gain in employment in the first quarter of 2011 after declines in recent years. Entertainment, international trade, and tourism are leading employment sectors for the county and IHS Global Insight Inc. predicts average employment growth of 1.3% through 2016 primarily in professional and business service jobs. The county's unadjusted unemployment rate was 12.2% in September 2010, an improvement from 13.0% in August 2010; however, still slightly above the unadjusted unemployment rate of 11.9% for the state, and a national unadjusted unemployment rate of 9.1%.

Los Angeles County AV in fiscal 2012 increased by 1.4% to $1 trillion, after a 1.6% decline in AV in fiscal 2011. Although the county reports median home prices fell by 45% between 2007 and 2011, AV has remained relatively stable due to underassessment of about 15.0% of residential parcels and 17.5% of commercial parcels that have base-year values that predate Proposition 13, which limited AV growth to 2.0% per year without a change in ownership. Since AV for these properties has not reset to market value levels in more than 30 years, home price declines have had less of an effect on AV. County per capita market value is strong, in our view, at $99,500 and median household effective buying income was what we consider good at 105% of the national average in 2010.

Due to stabilized AV, the county projects increases in property tax revenue, which drives most of its discretionary revenue, representing 20% of the total general county budgeted revenue, including the hospital enterprise fund; management estimates only 26.5% of county budgeted costs are discretionary. Charges for services represent another 14% of total revenue and about half of the revenue for the county's general budget comes from the federal and state governments for public service program. A portion of federal and state revenue funds the county's public health system, which serves a large uninsured, low-income population and which has historically operated with a deficit burdening general fund expenditures and cash. According to county officials, after a $680 million general fund transfer to the hospital enterprise funds, the health system posted balanced operations for fiscal 2011. However, state budget pressures, increasing caseloads and a very large uninsured population continues to inflate health care expenditures supported by the county's discretionary revenue.

Los Angeles County has maintained what we view as very strong audited unreserved general fund balances on a generally accepted accounting principles basis for the previous seven years. The county ended fiscal 2010 with a $3.0 billion general fund balance, including a $2.2 billion unreserved general fund balance, or a still very strong 16.7% of expenditures, in our view, despite a small decline compared with the fiscal 2009 unreserved fund balance of 20%. It estimates a $2.72 billion general fund balance at fiscal year-end 2011, of which about $2.00 billion, or what we consider a very strong 15% of expenditures, is unassigned or committed. In fiscal 2012, the county estimates a $175 million budget gap driven by a holdover of one-time budget solutions from previous years as well as the expiration of federal stimulus funding and increased pension costs and public health service caseloads. The budgeted solutions rely primarily on the use of one-time funds previously designated for capital programs. County officials expect their fiscal 2012 year-end fund balance will fall by another $170 million, which we calculate would result in still strong-fund balance levels. In fiscal 2012, California shifted certain mental health and public safety service responsibilities to the counties and budgeted for existing state sales tax and vehicle license fees (VLF) funding to counties to cover these costs in the current fiscal year. Los Angeles County indicates it intends to budget for these additional costs in quarterly intervals with temporary staff to maintain the flexibility necessary in the event of future funding cuts. The county does not expect the realignment plan or potential midyear state budget cuts will significantly affect its finances in fiscal 2012; however, given the state budget pressures and no current guarantee of future funding for additional costs associated with the realignment of services, it could face additional future structural budget gaps.

Overlapping county net debt is moderate, in our opinion, at 3.3% of property market value and $3,281 per capita. Amortization of general fund and special district principal is average with 52% of principal retired in 10 years. The annual debt service carrying charge is low in our opinion at only 2.9% of governmental expenditures, less capital outlay, as of audited fiscal 2010. The county expects to issue additional lease debt of about $300 million for a hospital project, although there is no definitive timeline.

Los Angeles County has contributed 100% of its pension annual required contribution (ARC) in the past 12 years, including $899 million in fiscal 2011. Officials estimate pension contributions of $1 billion in fiscal 2012 and expect increased retirement contributions in fiscal 2013 through fiscal 2015 of between $13 million and $89 million annually after the Los Angeles County Employees Retirement Association board decided to lower its assumed rate of return to 7.50% from 7.75%. It also reported an unfunded OPEB liability of $23 billion at fiscal year-end 2010 and a $1.86 billion OPEB ARC; it contributed $417 million on a pay-as-you-go basis, or 24% of the 2009 actuarial valuation. The county plans to transfer $470 million of previous excess retirement fund earnings into an irrevocable OPEB trust fund to help pay for future obligations. The county's combined pension and OPEB ARC represented a high 14% of the total fiscal 2010 general county budget, in our view. Future OPEB actuarial liabilities are a contributing factor to the county's overall unreserved net asset deficit position of $2 billion at fiscal year-end 2010, despite what we see as the good health of the general fund.

In Standard & Poor's view, Los Angeles County's long-term credit quality is characterized by a very broad and diverse economic base, as well as good financial reserves of $2.2 billion in fiscal 2010, down from $2.8 billion in fiscal 2008, but what we consider a still very strong 16.7% of expenditures. Officials estimate about a $500 million decline in the total general fund balance in fiscal 2011. The recommended fiscal 2012 budget proposes to meet a $221 million budget gap primarily with reserves, departmental savings, elimination of vacant budgeted positions, additional property tax and sales tax revenue, and lower debt service costs; county officials estimate a recent final debt service payment on the county's pension obligation bonds reduced annual expenditures by $372 million. Los Angeles County's budget has been pressured by higher health and social program caseloads and costs and state funding reductions, as well as what we see as a large $23 billion OPEB unfunded actuarial accrued liability (UAAL) as of the most recent actuarial valuation of July 1, 2010. Officials expect to transfer $470 million into a trust fund for the OPEB liability in fiscal 2012 and are evaluating options to reduce the future UAAL.

Outlook

The positive outlook reflects our expectation that Los Angeles County will continue to proactively adjust its budget to minimize reliance on one-time sources and maintain strong fund balances despite recent economic weakness and state funding cuts. The outlook also reflects our expectation that revenue and economic trends in the county will continue to stabilize in the next year given the depth and diversity of the county's economy and the relative stability of the tax base. Although officials indicate health system operations have stabilized somewhat in fiscal 2011, we believe potential rising social service and indigent health care costs and existing health system deficit balances continue to expose the county's general fund budget and cash. In addition, we believe Los Angeles County faces structural budget pressures related to state funding cuts and realignment of services. If it maintains strong reserves while restoring structural balance to its budget as well as obtaining a more dedicated long-term source of ongoing revenue to cover the new mandates associated with realignment, we could raise the rating in the next year. Should potential unfunded realignment measures and mandated programs materially pressure the county's budget, we would revise the outlook to stable.

Related Criteria And Research

USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

Ratings Detail (As Of November 18, 2011)		
Los Angeles Cnty cert of part		
Long Term Rating	A+/Positive	Affirmed
Los Angeles Cnty Cap Asset Lsg Corp lse rev bnds (Lac-Cal Equipment Program) ser 2009A		
Long Term Rating	A+/Positive	Affirmed
Los Angeles Cnty ICR		
Long Term Rating	AA-/Positive	Affirmed
Los Angeles (Los Angeles Cnty) certs of part (Dept of Pub Social Svcs Fac) ser 1999A dtd 08/01/1999 due 08/01/2002-2011 2019 2024 2031		
Unenhanced Rating	A+(SPUR)/Positive	Affirmed
California Infrastructure & Econ Dev Bnk, California		
Los Angeles Cnty, California		
California Infrastructure & Econ Dev Bnk (Los Angeles Cnty) (LA Cnty Dept of Pub Social Svces Fac) (Vermont Village Human Services Corp) (AMBAC)		
Unenhanced Rating	A+(SPUR)/Positive	Affirmed
Los Angeles Cnty Pub Wks Fing Auth, California		
Los Angeles Cnty, California		
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) (Multi Cap Proj I)		
Long Term Rating	A+/Positive	Affirmed
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) (Multi Cap Proj I)		
Long Term Rating	A+/Positive	Affirmed
Los Angeles Cnty Pub Wks Fing Auth (Calabasas Landfill Proj) ser 2005		
Unenhanced Rating	A+(SPUR)/Positive	Affirmed
Sonnenblick-Del Rio El Monte Asset Lse Corp, California		
Los Angeles Cnty, California		

Ratings Detail (As Of November 18, 2011) **(cont.)**		
Sonnenblick-Del Rio El Monte Asset Lse Corp certs of part (Dept Of Pub Soc Svc Fac) ser 1999 dtd 01/15/1999 due 06/01/2001-2014 2019 2030		
Unenhanced Rating	A+(SPUR)/Positive	Affirmed
Many issues are enhanced by bond insurance.		

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