New Issue: Moody's assigns A1 to Los Angeles County's (CA) Lease Revenue Bonds Series 2015 B & C and changes outlook to positive

Global Credit Research - 31 Jul 2015

Rating applies to $1.6B in debt outstanding, post issuance

LOS ANGELES (COUNTY OF) CA
Counties
CA

Moody's Rating

ISSUE		RATING
Lease Revenue Refunding Bonds (Master Refunding Project), 2015 Series C (Federally Taxable)		A1
Sale Amount	$85,380,000	
Expected Sale Date	08/12/15	
Rating Description	Lease Rental: Abatement	
Lease Revenue Refunding Bonds, (Master Refunding Project), 2015 Series B (Tax Exempt)		A1
Sale Amount	$120,350,000	
Expected Sale Date	08/12/15	
Rating Description	Lease Rental: Abatement	

Moody's Outlook POS

NEW YORK, July 31, 2015 --Moody's Investors Service has assigned an A1 rating to Los Angeles County's (CA) $120.35 million Lease Revenue Refunding Bonds 2015 Series B (Tax-Exempt) and $85.38 million Lease Revenue Refunding Bonds 2015 Series C (Federally Taxable). Concurrently, we have affirmed the A1 rating on the county's outstanding parity debt and the county's Aa2 issuer rating. The outloo has been changed to positive from stable.

SUMMARY RATING RATIONALE

The Aa2 issuer rating, which is equivalent to a general obligation unlimited tax rating, reflects the county's massive tax base and strong economy, sound financial position supported by healthy reserve levels, strong management team and low debt burden. The rating also incorporates the county's unfunded pension and Other Post Retirement Benefits (OPEB) liabilities representing long term, but manageable, ris s for the county.

The two notch distinction with the county's issuer rating represents the wea er security pledge for lease-bac ed obligations and the additional ris to bondholders from the county's financial, operational, and economic conditions over the more secure assumed general obligation pledge of the issuer rating. Security for the lease payments is a contractual pledge of the county of all of its available financial resources, subject to abatement of the leased property, effectively on parity with other unsecured obligations. Unli e some earlier county lease obligations, the lease does not provide the Authority with the right to re-enter or re-let the leased property in the event of a county payment default. While this change represents a wea ening of bondholder security, it does not materially alter our estimate of the probability of default or loss relative to the county's other A1 rated obligations.

OUTLOOK

The positive outloo reflects the county's improved financial operations supported by healthy reserve levels, the continued decline in general fund subsidies to the department of health services (DHS) and management's on-going progress of addressing its OPEB and unfunded pension liabilities.

WHAT COULD MAKE THE RATING GO UP

-Ongoing operating surpluses and sustaining reserves at a healthy level

-Continued financial stability of the county's health system

-Ongoing progress toward addressing long-term, unfunded pension and OPEB liabilities

WHAT COULD MAKE THE RATING GO DOWN

-Significant deterioration of the county's financial position

-Inability to effectively manage retirement costs

STRENGTHS

-Large and diverse economy

-Sound financial position supported by healthy reserves

-Strong management team

-Low debt burden

CHALLENGES

-Improved yet still moderate health care burden

-Moderate pension and OPEB burden

RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

ECONOMY AND TAX BASE: LARGE AND DIVERSE ECONOMY CONTINUES TO GROW AND FUEL REVENUE GROWTH

The county's extremely large assessed value (AV) continues to exhibit moderate growth and is projected to reach an all-time high of $1.26 trillion in fiscal 2016 which is by far the largest of any county in the nation. The property taxes generated from this base represent the county's largest source of discretionary revenues (at approximately 25%), and its continued growth is a ey credit strength.

The county's AV has remained relatively stable over a long period of time, which serves to moderate revenue swings. During the run-up of housing values, the AV breached 10% annual growth only once, in 2007, while elsewhere in the state double digit annual increases were commonplace. This relative stability is rooted in the generally older, and more mature nature of the housing stoc within the county.

AV experienced modest declines in 2010 and 2011 totaling a very low negative 2.3%. Since then, AV has grown in each of the following years for an aggregate amount of 20%. The twenty largest taxpayers of the county are just 3.24% of total 2016 AV, which is low for the rating category. The county's housing mar et continues to exhibit growth with home sales increasing by an average of 9.0% and home prices are up 7.8% from the prior year. Helping to fuel the county's AV growth are single-family home sale prices that remain well above the median assessed value.

Los Angeles County's unemployment rate at 7.1% is still above the state and U.S. rates but is significantly down from its pea at 12.6%. The county's growing economy is not only a catalyst for regional economic expansion and job creation but remains an economic engine for the state. The county's Gross Domestic Product (GDP) grew from $530 billion in 2009 to $640 billion in 2014, representing roughly 28% of the state's GDP.

The county's improving wealth levels continue to approximate nationwide medians. Estimated 2012 Median Family Income is 97.0% of the US, while in 2000 it stood at 92.8%. Compared to Aa rated large counties, these levels are relatively low, but satisfactory for the rating given the county's other credit strengths.

FINANCIAL OPERATIONS AND RESERVES: SOUND FINANCIAL POSITION WITH HEALHTY RESERVES

We expect the county's trend of strong financial operations to continue, given prudent fiscal management and success at maintaining reserve levels. In fiscal 2014, the county recorded a notable $223 million operating surplus, increasing reserves to $3.1 billion or a healthy 19.8% of revenues. Based on unaudited 2015 figures, the county projects generating its third consecutive operating surplus. The county continues to benefit from revenues outperforming budgetary projections, specifically property and sale tax receipts as well as tight expenditure controls.

One of the county's major expense items involves healthcare for the county's indigent population, provided through its Department of Health Services. Positively. DHS has recently become less reliant on county support for operations. The county's fiscal 2016 budgeted contribution is $633.2 million which is down from $827.7 million or 18.24% of total DHS budget in fiscal 2008. Further, the DHS loan balance owed to the county decreased to $419 million in fiscal 2015, which is a significant improvement from 2011, when the balance was over $1 billion.

DHS's improved financial operations is related to the Patient Protection and Affordable Care Act, the state's improved efficiency in submitting reimbursements and receipt of revenues through the Section 1115 Hospital Financing Waiver (the Waiver). The Waiver became effective in November 2010 and provides partial funding for uncompensated care, a new funding source for system improvements at public hospitals and allows the state to receive Federal funds for Medi-Cal services that would otherwise not be eligible for Federal funding. The Waiver is set to expire on Oct. 31, 2015, though the county anticipates that the Waiver will be renewed. In fiscal 2015, the net benefit from the Waiver was $223.4 million or close to 4.5% of total DHS budget.

Liquidity

The county's liquidity position remains strong with unrestricted cash and investments at $1.9 billion or a solid 12.75% of revenues in fiscal 2014. With the city's continued strong operating performance, the city's liquidity position should remain healthy. The county's liquidity position is further augmented with total of $1.41 billion of alternate liquidity available for borrowing purposes, if needed.

DEBT AND PENSIONS: LOW DEBT BURDEN; MODERATE UNFUNDED PENSION LIABILITY AND NEW PLAN IMPLEMENTED TO ADDRESS GROWING UNFUNDED OPEB LIABILITY

The county's direct net debt burden is low at 0.13% of AV. The above-average overall debt burden of 2.8% of AV, compared to the nationwide median of 1.9% AV for Aa2 counties, reflects the large amount of debt of the overlapping jurisdictions, mainly Los Angeles Unified School district. The county plans to issue approximately $285 million in lease revenue bonds in the early part of 2016 that will retire a li e amount currently outstanding in commercial paper which has funded the capital costs of the new in-patient tower at MLK hospital. Given that the county's AV will li ely continue to grow in the near- to mid-term, the county's debt burden will remain low.

Debt Structure

The county's outstanding debt is in fixed rate mode and amortizes over the long term.

Debt-Related Derivatives

The county has not entered into any derivative agreements.

Pensions and OPEB

The county's three-year adjusted net pension liability (ANPL) is moderate at 2.34% of AV and 1.8 times operating revenues, which equate to an A-rating score on our scorecard. Moody's ANPL reflects certain adjustments we ma e to improve comparability of reported pension liabilities. The adjustments are not intended to replace the county's reported liability information, but to improve comparability with other rated entities.

The county's unfunded OPEB liability is a sizeable $27.19B. In an effort to stem the looming burden of its OPEB liability, the county established an irrevocable OPEB trust in 2012. As of May 31, 2015, the trust had a net position of $497 million. The Board of Supervisors recently adopted a funding plan commencing in fiscal 2016 that would enable the county to fully fund its annual contribution ($2.2 billion) by fiscal 2028. Further, the county has eliminated spousal and dependent coverage and implemented mandatory enrollment in Medicare. This is expected to save more than $840 million in savings over the next 30 years.

MANAGEMENT AND GOVERNANCE

California counties have an institutional framewor score of "A" or moderate. Primary sources of unrestricted revenues come from property tax and sales tax. Service charges and state aid ma e up significant sources of county revenues as well, however are usually restricted to specific purposes. Property taxes are fairly predictable, given the state's constitutional formula, nown as "Prop. 13", while sales taxes are extremely sensitive, either to the local economy or the state's financial position. Expenditure flexibility is similarly limited, although somewhat less so than revenues.

Management has demonstrated its ability to preserve the county's financial position through challenging economic and financial cycles and given their continued prudent budgetary practices, and we expect reserves to remain healthy.

KEY STATISTICS

-Full Value (2015): $1.26 trillion

-Full Value Per Capita (2015): $126,400

-Median Family Income as % of US Median (2010): 96.97%

-Available Fund Balance as % of Operating Revenues (2014): 18.4%

-Five-Year Change in Fund Balance as % of Operating Revenues (2014): 1.07%

-Cash Balance as % of Operating Revenues (2014): 12.75%

-Five-Year Change in Cash Balance as % of Revenues: 0.06%

-Institutional Framewor : A

-Five-Year Average of Operating Revenues/ Operating Expenditures: 1.00x

-Net Direct Debt / Full Value (2015):0.13 %

-Net Direct Debt / Operating Revenues (2015): 0.1x

-3-Year Average of Moody's Adjusted Net Pension Liability / Full Value: 2.34%

-3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues: 1.8x

OBLIGOR PROFILE

Los Angeles County is largest county in the nation both by size ($1.26 trillion tax base) and population (10.1 million). The county's economy continues to improve and while the unemployment rate is still above the state and nation has decreased over the prior year to 7.1% from 8.2%.

LEGAL SECURITY

Security for the lease payments is a contractual pledge of the county of all of its available financial resources, subject to abatement of the leased property, effectively on parity with other unsecured obligations.

USE OF PROCEEDS

2015 Series B & C Lease Revenue Refunding bonds will refund outstanding parity debt and is expected to generate approximately $20 million in present value savings.

RATING METHODOLOGY

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. An additional methodology used in the lease-bac ed rating was The Fundamentals of Credit Analysis for Lease-Bac ed Municipal Obligations published in December 2011. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

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