MOODY'S INVESTORS SERVICE

New Issue: MOODYS AFFIRMS A1 RATING ON LOS ANGELES COUNTY'S LEASE SUPPORTED OBLIGATIONS

Global Credit Research - 02 Nov 2010

ISSUER RATING OF Aa2 AND PENSION OBLIGATION BOND RATING OF Aa3 ALSO AFFIRMED

Los Angeles (County of) CA
County
CA

Moody's Rating

ISSUE		**RATING**
Lease Revenue Bonds (Multiple Capital Projects I), 2010 Series A (Tax-Exempt)		A1
Sale Amount	$89,780,000	
Expected Sale Date	11/09/10	
Rating Description	Lease Rental	
Lease Revenue Bonds (Multiple Capital Projects I), 2010 Series B (Build America Bonds/Recovery Zone Economic Development Bonds)		A1
Sale Amount	$700,980,000	
Expected Sale Date	11/09/10	
Rating Description	Lease Rental	

Opinion

NEW YORK, Nov 2, 2010 -- Moody's Investors Service has assigned an A1 rating to Los Angeles County's Lease Revenue Bonds (Multiple Capital Projects I) Series 2010 A (Tax Exempt) and 2010 Series B (Build America Bonds and Recovery Zone Economic Development Bonds) to be issued by Los Angeles County Public Work Financing Authority. At this time we have also affirmed the following ratings of the county: Issuer Rating, Aa2; pension bonds, Aa3; fixed asset lease obligations, A1. In addition we have affirmed the stable outlook on these ratings.

RATINGS RATIONALE

The ratings reflect the county's large and diverse economy, although it is currently stalled and, according to Moody's Analytics, robust annual growth in the regional economy of 3.0% or more is not expected until 2011. The rating also reflects the county's generally strong financial operations with sufficient reserves, and its easily manageable debt position despite the near doubling of the county's lease supported obligations with the current offering. The sizable burden of the county's health care system on its financial operations also weighs on the rating.

The proceeds of the current offering will be used for upgrades and expansions throughout the county's health care system and other facilities, most notably at the Harbor-UCLA Medical Center and the Hall of Justice. The bonds are secured by lease payments for use of the county's new 600 bed medical center valued at above $1.05 billion.

The two notch rating distinction between the A1 for the current offering and the county's Aa2 Issuer Rating represents Moody's standard notching differential for fixed asset leases relative to a California issuer's general obligation rating. Broadly speaking the two notches reflect the risk of abatement and the narrower, general fund security pledge for leases compared to the very strong unlimited property pledge implied in the Issuer Rating.

FINANCIAL OPERATIONS ARE VERY STRONG WITH AMPLE RESERVES

The county's ability to preserve its slightly above average financial strength, even through the current climate of sluggish economic conditions and the state's budgetary challenges, is notable. During periods of strong economic expansion and revenue growth the county has balanced its budgets with tight controls on expenditures, and with the embedded conservatism of these budgets, the general fund yielded notable surpluses adding to the county's sizable reserves. Key to the county's fiscal discipline has been its ability to maintain a significant number of positions unfilled during the recent period of financial uncertainty, particularly related to the financial difficulties of the state. The county has also been decisive in eliminating positions, which has at times resulted in actual lay-offs, but the 2010 and 2011 budgets were free of lay-offs and furloughs.

As of June 30, 2009, the end of the most recent fiscal year for which there are audited financial results, the county's general fund enjoyed a total balance of $3.2 billion and unreserved balance of $2.6 billion million equaling 22.9% and 19.0% of general fund revenues respectively. Both of these figures are slightly greater than the figures for similarly rated counties in California, although somewhat less than the figures for similarly rated counties nationwide. The 2009 balance reflects a decrease of $208 million for the year, which was the first decrease after twelve consecutive surpluses since 1996, during which time the general fund balance increased from $160 million to $3.4 billion in 2008. The 2009 general fund deficit was largely the result of expenditure reductions not keeping pace with decreasing revenues. As general fund revenues decreased by 1.6%, expenditures continued to grow by 1.3%. While the disparity in these trends is evident, we note that in 2007 and 2008, during periods of revenue growth, expenditures increased by 5.7% and 8.4%, respectively, and decisive measures by the county reduced the growth to 1.3%.

While the county's commitment to strong financial operations is evident, we believe that the key pressure on the county's expenditures remains its enormous health care system. In 2009 the county spent $2.48 billion in health related expenses from the general fund, which represented 18.9% of expenditures before transfers. In addition, the county's five major health care facilities had combined operating expenses of $3.2 billion, and received $802 million in inter-fund transfers from the general fund. In total, the county estimates that its net cost for health services is $1.1 billion in 2009, up from $803 billion in 2006. For many years, the health care system has operated with structural deficits, relying on its reserves, general fund transfers and other one- time measures. The latter include state and federal waivers which, in return for operating improvements, allow the county to seek reimbursements for certain normally ineligible expenditures. In the current year, the health services budget deficit is estimated at $253 million, which will once again be bridged with one time measures. The county recognizes the financial burden of its health care system and the structural flaws imbedded in the system. Time and again comprehensive restructuring plans have been presented without significant improvement. It appears that for the foreseeable future the county will continue to bear this financial burden. The county has demonstrated that it can absorb these costs without severely damaging its financial position. It is important for the county's financial health and creditworthiness to continue to manage this sizable burden as long as it persists.

The county's unaudited 2010 results point to another relatively small general fund deficit of about $185 million, decreasing the general fund balance to $3.0 billion and the unreserved balance to $2.2 billion, the relative sizes of both of which remain consistent with similarly rated large counties in the state. Once again, the small deficit was due to expenditure reductions failing to match revenue shortfalls, although significant reductions were made. The county has had a hiring freeze in place since 2009 and made expenditure cuts across the board, especially in services and supplies. Most notably, however, there were no salary increases. Cuts from the state were generally not backfilled.

The county's 2011 budget indicates no dramatic changes from 2010. The budget appears to rely less on cancellation of reserves and designations of fund balance than in 2010, which may reflect incrementally closer structural balance. The hiring freeze and reducing headcount is still the county's primary tool for controlling expenditures. Some labor concessions, including 0% COLA in 2010 and 2011, also result in $55 million a year in savings. Based on the county's initial assessment, the state budget impact on its 2011 budget is minimal. The total gross impact is about $88 million, and the net should be much smaller. Overall, we expect a 2011 general fund deficit on the order of those experienced in fiscal 2009 and 2010, which would keep the general fund balance within the range consistent with the current rating.

LARGE, DIVERSE AND AGAIN GROWING ECONOMY WITH BELOW AVERAGE WEALTH AND INCOME LEVELS

Los Angeles is by far the largest county in the state. The economy remains diverse with higher education, manufacturing, healthcare and biotech firms, trade, tourism and perhaps most importantly, the TV/motion picture industry prominent among the county's largest private sector employers. The county's population and employment recovered strongly through the 1990's following the severe contraction of the defense industry in the early 1990's. However, since 2000 population growth has moderated with out-migration outpacing in- migration.

Through 2008 total employment remained between 4.4 and 4.7 million and the unemployment rate in mid single digits approximated the rates of the state as a whole. During the most recent recession the county seems to have lost approximately 325,000 jobs with over 80% of the losses occurring in 2009, when the metro area gross product contracted by 4.0%. Between August 2009 and August 2010 only approximately 55,000 jobs seem to have been lost, with the unemployment rate climbing to a very high 13%. The county's recovery is still weighed down by its stalled labor market, but the gross metro area product is expected to increase by 2.0% in 2010. Employment has been flat even with temporary census hiring. Entertainment and tourism are among the few industries to add to payrolls in recent months. The housing market has slowed as home sales and prices began to weaken in the spring when temporary supports began to be lifted. We don't expect the unemployment rate to be in single digits until 2013.

The county's trillion dollar tax base has fared somewhat better than other counties' in the state. The county's assessed value (AV) decreased by 0.6% and 1.9% respectively in 2010 and 2011, which are relatively modest declines due to the more built out and aged nature of the county's residential base. The county's 2011 full value per capita of $105,500 remains notably lower than the California county median of $117,000 but higher than the national median of $75,800. The 2000 census indicated that while nominal income levels grew in Los Angeles over the prior decade, the average resident's socio-economic profile weakened in real terms and relative to state and national averages. For example, as of the 2000 census, median family income in Los Angeles County was only 87.6% of the state average and 92.8% of the national average, compared to 96.2% and 110.8% respectively as of the prior, 1990 census. Going forward, although the county's economy, wealth and income levels may not grow as rapidly as in the recent past, we believe the county will continue to enjoy one of the most diverse and steadily growing economies in the state.

MANAGEABLE DEBT POSITION

The proceeds of the current offering will fund capital improvements throughout the county, most notably at the Harbor-UCLA Medical Center and the county Hall of Justice This is the county's first significant borrowing in over a decade and it nearly doubles the county's lease supported obligations. These lease revenue bonds will be secured by the county's lease payments for the use of its new 600 bed hospital, which is valued at over $1.05 billion and has no outstanding debt because it was funded with large grants, mostly from the federal government.

Including the current offering the county will have approximately $1.8 billion in outstanding direct debt, including $118 million in pension obligations (net of accreted interest) and $1.7 billion in lease rental obligations. The county's direct debt burden is 0.2% and overall debt 3.1% of assessed value. While the county's direct debt is below the state average of 0.3% for counties, overall debt is above the median of 1.9% due to the significant debt of overlying entities, most notably the Los Angeles Unified School District. Moody's nonetheless believes that the county's debt levels remain very easily manageable. It is noted that the county's lease ratios - perhaps the best measure of the budget burden of county debt - compare better with medians. The typical median lease burden for a California county is 1.5% of general fund revenues while the total burden of lease and General Fund obligations (e.g. pension obligation bonds) is 1.8%. With the current offering the county's peak lease payment, as a percent of general fund revenue, will be about 1.1% and total lease burden and General Fund obligation burden about 3.6% of general fund revenues. The total burden is driven by the county's annual pension obligation debt service of $372 million, which is in its final year. Beginning in 2012, the county's budget will be free of this annual burden, which will enable the county to better address rising cost of health care and other expenses. The county's annual actuarially required contribution for its Other Post Employment Benefits (OPEB) is $1.2 billion but the county's practice is to fund its OPEB on a pay-as-you-go basis, which in 2011 is approximately $430 million. At this rate, the OPEB liability is likely to continue to grow each year. The county recognizes the importance of better managing its OPEB liability, and hopes to take concrete measures with the recovering economy. In the meantime, the retirement of the pension obligations will afford the county some relief in the short term. The county's pension systems are in healthier positions. The Los Angeles County Employee Retirement Association's Retirement plan had a funding ratio of 88.9% as of June 30, 2009.

LEGAL PROVISIONS FOR THE CURRENT OFFERING ARE SATISFACTORY FOR THIS TYPE OF TRANSACTION.

The County pledges to annually budget and appropriate funds for lease payment and deposit them with the trustee. The County will also provide rental interruption insurance for 24 months, title insurance, and a reserve fund subject to the standard three tier test, to be cash funded with proceeds.

Outlook

Moody's outlook on Los Angeles County's long-term ratings is stable. The stable outlook reflects the county's demonstrated ability to preserve its financial position through challenging economic and financial cycles. The financial health with which the county emerges from the expected fiscal challenges in the current and coming years will be an important contributor to future rating considerations.

WHAT COULD MAKE THE RATING GO UP

Long term financial stability of the county's health system with structural budgetary balance

Significant improvement in the area economy with fundamental improvement in area income levels

WHAT COULD MAKE THE RATING GO DOWN

Significant deterioration of the county's financial position

KEY STATISTICS

2010 estimated population: 10 million.

2000 median family income, $46,452 (87.6% of state)

2000 per capita income, $20,683 (91.1% of state)

2011 full valuation: $1,042 billion

Overall debt burden: 3.1%

FY 2009 General Fund balance: $3.2 billion (22.9% of 2009 General Fund revenues)

FY 2009 Undesignated General Fund balance: $1.7 million (19.0% of 2009 General Fund revenues)

Net lease burden, est. 1.5%

Net Lease and GF Obligation Burden, est 1.7%

The principal methodology used in rating County of Los Angeles CA was General Obligation Bonds Issued by U.S. Local Governments rating methodology published in October 2009. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found on Moody's website.

REGULATORY DISCLOSURES

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

Moody's Investors Service considers the quality of information available on the credit satisfactory for the purposes of assigning a credit 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.

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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.

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