

Rating Update: Moody's affirms A3 of City of New Orleans' (LA) General Obligation and Limited Tax Debt

Global Credit Research - 13 Sep 2013

Outlook is negative

NEW ORLEANS (CITY OF) LA
Cities (including Towns, Villages and Townships)
LA

Opinion

NEW YORK, September 13, 2013 --Moody's Investors Service has affirmed the A3 underlying rating of the City of New Orleans' (LA) General Obligation and Limited Tax debt. Concurrently we affirm the Baa1 underlying rating of the City's Series 2005 Limited Tax Bonds. The outlook for all ratings is negative. The city's General Obligation bonds are secured by and payable from ad valorem taxes upon all the property subject to such taxation within the city in an amount sufficient to pay the principal of and interest on the bonds. The city has various series of Limited Tax bonds which are limited obligations of the City and are payable from a pledge and dedication of the net avails or proceeds of unique millages approved for the various issuances.

SUMMARY RATING RATIONALE

The rating reflects the city's stable and relatively diverse economy that is anticipated to grow modestly in fiscal 2014, historically weak financial operations, and above average debt position with no plans for additional borrowing through fiscal 2013. The rating also reflects the city's narrow liquidity and weak General Fund reserve position. The negative outlook reflects continued challenges the city faces, which include a weak cash reserve position, significant pending lawsuits, and poorly funded pension and OPEB obligations.

STRENGTHS

- * Continued modest growth in sizeable economy
- * Board of Liquidation oversight
- * Improving sales tax collections

CHALLENGES

- * Weak liquidity and accumulated General Fund deficit
- * Continued operating pressure
- * Expenditures associated with consent decree regarding police, public safety, and sheriffs
- * Significant pending lawsuits

DETAILED CREDIT DISCUSSION

INABILITY TO BOLSTER WEAK LIQUIDITY; OPERATING PRESSURES REMAIN

The city's weak financial position and lack of financial flexibility is a particular credit negative and greatly reduces the City's ability to effectively address challenges in the near-term. Future credit reviews will examine the city's ability to establish structurally balanced operations and improve weak cash reserve levels. Officials report the city continues to face a number of challenges which include rising health care, worker's compensation, and retirement system costs, as well as two pending Federal consent decrees regarding the Police Department and the Orleans Parish Sheriff's Office. City officials previously projected a modest operating surplus in the General Fund for fiscal 2012. Despite a nearly 6% increase in sales tax collections, the General Fund ended fiscal 2012 (December 31) with a modest operating deficit. Revenue collections for the New Orleans Public Library fell modestly short of

expectations. Also, higher than anticipated General Fund spending in 2012 was predominately the result of increased costs related to the city's self-insured workers' compensation program and Hurricane Isaac emergency spending. At fiscal year-end 2012 the city's total General Fund balance was -\$9.3 million or a weak -1.8% of General Fund revenues. The General Fund balance calculation includes significant "due to other funds" and "due from other funds," which represents monies used for hurricane disaster and emergency spending that is anticipated to be restored from various grants and Federal aid. The city's General Fund cash and investment position at fiscal year-end 2012 was also a significantly narrow \$3.6 million, given revenues in the General Fund topped \$500 million in fiscal 2012.

The city's adopted 2013 budget included a General Fund revenue estimate of \$491 million, which has since been amended to \$496 million as of July 2013. Year-to-date revenue estimates are tracking very close to budgeted figures. Current sales tax collections are trending up over last year's collections, the city is benefiting from lower debt service payments due to refinancing of previously issued debt, and health care funding is currently projected to cover expected health care spending. Despite increased expenditures related to workers' compensation, city officials anticipate \$14 million in revenues over expenditures, which will result in an improvement in total General Fund balance and a modest improvement in year-end liquidity. Uncertainty remains for the city's financial performance in fiscal 2013, in part due to risks associated with potential hurricanes. The hurricane season for the Atlantic and Gulf coasts ranges from June to November.

Management reports the fiscal 2014 budget is under development and while officials report the desire to build reserves, uncertainty remains with what costs will be associated with consent judgments related to the Orleans Parish Sheriff's Office. City officials anticipate the additional costs could range from \$5 to \$20 million for fiscal 2014. Revenue forecasts for fiscal 2014 are anticipated by late September.

MODEST GROWTH IN LARGE AND RELATIVELY DIVERSE TAX BASE ANTICIPATED

The continued modest population growth and increases in taxable value are credit positives, and will continue in the near-term. The city's current estimated population is 369,250 which is still below pre-Katrina totals, yet continues to represent steady growth. The city's full valuation for fiscal 2013 is a sizable \$25.7 billion which is derived from an assessed valuation of \$3.08 billion. This represents an approximate 5% increase when compared to the previous year and the city's five year average annual increase in taxable value is roughly 4.0% from fiscal 2008 through 2013. Preliminary numbers indicate modest growth in assessed valuation of 1-2% for fiscal 2014. The city's top ten property tax payers are relatively diverse and make up 11.3% of the city's total assessed valuation, and include Entergy Corporation (rated Baa3 / stable outlook), several large banks, and Harrah's, a casino. The city is also home to Tulane University that has approximately 8,400 undergraduate students and 5,000 graduate and professional students. The city successfully hosted the 2013 Super Bowl and NCAA Women's Final Four basketball tournament, as well as other national meetings and conferences. Officials report the development of University Medical Center (\$1.06 billion project), Veterans Affairs Hospital (\$995 million), and a National World War II Museum (\$325 million) with completion dates between 2015 and 2016. City officials also report retail development of various sizes and scopes continue throughout the City, including the development of a Costco (rated A1 / stable outlook) and two new Walmart stores (Aa2 / stable outlook).

Moody's Economy reported in July 2013 that despite some obstacles, New Orleans will continue to recover as its three mainstays - tourism, trade, and energy - benefit from an accelerating national recovery. But the risks are weighted to the downside. Each of these three industries is tied to the national business cycle, and if U.S. growth slows, so will gains in New Orleans. Over the long term, expansion will not match the U.S. average. A less-educated workforce and weak migration trends limit prospects by discouraging business investment. The city's socioeconomic indices remain below that of the state and nation. Wealth levels, as reported by the 2006-2010 American Community Survey, indicate per capita income which is 91.2% of the nation and median family income which is 73.3% of the nation.

ABOVE AVERAGE DEBT BURDEN; BOARD OF LIQUIDATION OVERSIGHT CREDIT POSITIVE

The City's debt burden will remain above average in the near-term given recent issuances of debt and a below average payout of principal outstanding. A credit strength to the City's debt profile is oversight provided by the Board of Liquidation. However, the city's growing pension and OPEB obligations are significant challenges. The city's direct debt burden is 3.6% which is above average for similarly rated cities. The city's overall debt burden is also above average at 5.1%. Payout of the city's general obligation bonds is below average with 54.7% of principal amortized in the next ten years with all debt maturing in 2039. The city's debt position has stabilized following the refinancing in late 2012 on pension obligation bonds that took the interest from an 11% bank bond rate to a 1.39% to 4.96% fixed rate. At the same time, \$46 million in bond proceeds were used to terminate the swap agreement associated with the obligation. The city has no plans for additional issuances of General Obligation bonds in fiscal

2013, yet do anticipate a sale in mid to late 2014 for various projects.

All ad valorem taxes levied by the city for the payment of GO bonds are transferred to the Board of Liquidation. The Board has the authority to enforce imposition and collection of sufficient taxes for the payment of GO bonds upon a failure of the City Council to do so. Additionally, the Board has the authority to bill and collect taxes itself, although this is not currently envisioned.

New Orleans has a growing employee pension burden, based on unfunded liabilities for its three pension plans. The City is a member of the Municipal Police Employees' Retirement System, which is a statewide plan. The City also contributes to an Employees' Retirement System which is specific to the City and governed by ordinance, as well as a city-specific plan for Firefighters which is governed by the state. Budgetary pressures for providing these benefits are growing. For the Municipal Police Employees' Retirement System, the City contributed \$18.5 million in fiscal 2012. With regards to the City's Employees' Retirement System, and Firefighters' Pension and Relief Fund, the City contributed \$19 million and \$31.7 million respectively for the plans in 2012. We note that the City did not fully fund its combined ARC payments in fiscal 2012 which is a particular credit negative. In 2013 a civil district court judge ordered the City to pay \$17.5 million to meet the City's 2012 obligation to the firefighters' pension plan. The city is currently appealing the ruling. Moody's adjusted net pension liability (ANPL) for the City, under our methodology for adjusting reported pension data, is \$1.6 billion, or 3.1 times general fund revenues, compared to less than 1 times' on average in the sector. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace New Orleans' reported liability information, but to improve comparability with other rated entities. We determined New Orleans' share of liability for the state-run Municipal Police Employees' Retirement System in proportion to its contributions to the plan.

The city contributed \$9.8 million to its fiscal 2012 other post employment benefits (OPEB) cost of \$12.9 million. The City's net OPEB obligation at fiscal year-end 2012 was \$57.5 million. The City's growing pension and OPEB liabilities will continue to be a challenge in the near to medium term.

NEGATIVE OUTLOOK

The negative outlook reflects continued challenges the city faces, which include a weak cash reserve position, growing health care costs, significant pending lawsuits, and poorly funded pension and OPEB obligations. An inability to stabilize financial metrics and restore satisfactory cash reserve levels, as well as address other challenges, will result in a rating downgrade.

WHAT COULD MAKE THE RATING GO UP (OR REMOVAL OF NEGATIVE OUTLOOK)

- * Trend of improved financial metrics coupled with restoration of satisfactory cash reserves
- * Continued growth and diversification of economy
- * Significant improvement in socioeconomic profile
- * Significant reduction in debt burden

WHAT COULD MAKE THE RATING GO DOWN

- * Lack of improvement in financial metrics and prolonged weak cash reserve position
- * Significant contraction of tax base
- * Inability to build reserves to satisfactory level
- * Increase in debt profile

KEY STATISTICS

Population estimate: 369,250

2013 Assessed Valuation: \$3.08 billion (\$25.7 billion full value equivalent)

Top ten property taxpayers as a % of total assessed valuation: 11.3%

Direct Debt Burden: 3.6%

Overall Debt Burden: 5.1%

Payout of Principal (10 years): 54.7%

FYE 2011 General Fund balance: -\$9.3 million (-1.8% of General Fund revenues)

General Obligation and Limited Tax debt outstanding: \$782.8 million

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was General Obligation Bonds Issued by US Local Governments published in April 2013. 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 certain 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 certain 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 certain 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.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Analysts

James Hobbs
Lead Analyst
Public Finance Group
Moody's Investors Service

Timothy Blake
Additional Contact
Public Finance Group
Moody's Investors Service

Kristin Button
Additional Contact
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

© 2013 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. ("MIS") AND ITS AFFILIATES ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND CREDIT RATINGS AND RESEARCH PUBLICATIONS PUBLISHED BY MOODY'S ("MOODY'S PUBLICATIONS") MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. 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. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS,

COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moodys.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

For Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail clients. It would be dangerous for retail clients to make any investment decision based on MOODY'S credit rating. If in doubt you should contact your financial or other professional adviser.