

Rating Update: New Orleans (City of) LA

MOODY'S AFFIRMS RATINGS ON CITY OF NEW ORLEANS DEBT

Municipality
LA

Opinion

NEW YORK, Mar 18, 2009 -- Moody's Investors Service has affirmed the Baa3 rating and stable outlook on the City of New Orleans' general obligation unlimited tax bonds affecting \$523.9 million in outstanding debt. In addition, we have also affirmed the Baa3 rating on the City's Downtown Development District Bonds, Series 2001 and Drainage System Limited Tax and the Ba1 rating on the Limited Tax Bonds, Series 2005 and the Audubon Commission Limited Tax Bonds, Series 1997. Finally, Moody's affirmed the Ba3 rating on the City's Pension Obligation Bonds, Series 2000. All of the City's ratings carry a stable outlook.

Assignment of the Baa3 rating on the GOULT debt reflects the Board of Liquidation's strong management and willingness to adjust rates as necessary. The rating also takes into consideration the recovery in key revenues streams and a five year forecast that projects the City will be self sufficient by 2011. The rating also takes into consideration ongoing pressures on financial operations in the General Fund.

The Baa3 ratings on certain limited tax debt take into consideration strong debt service coverage of 8.67 times on the Downtown Development District Bond, Series 2001 and 6.59 times on Drainage System Limited Tax debt. The Ba1 ratings on the remaining limited tax debt reflect adequate yet narrower debt service coverage of 1.10 times for Limited Tax Bonds, Series 2005 and 1.80 times on Audubon Commission Limited Tax Bonds, Series 1997.

Finally, maintenance of the Ba3 rating on the pension obligation bonds reflects the weaker pledge of excess revenues from general fund operations and the exposure to insured variable rate demand obligations, and interest expenditures exceeding those anticipated when the bonds were first issued

BOARD OF LIQUIDATION KEY FACTOR IN RATING ASSIGNMENTS

The Board of Liquidation was established by the State of Louisiana legislature in 1880 and made a "body corporate" separate and distinct from the City in 1890. The Board has exclusive control and direction of all matters related to the issuance and repayment of the city's general obligation unlimited tax (GOULT) bonds. The repayment of these bonds is therefore separated and excluded from the City's operating budget and a dedicated source and security exists for the payment of the City's GOULT. All ad valorem taxes levied by the City for the payment of GO bonds are transferred to the Board. 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. Because of this authority and its distinct separation from the City, Moody's believes this provides strong protection for bondholders. The Board demonstrated its conviction to amply meet debt service when it increased the debt service tax rate for unlimited tax bonds from \$28.4 mills in fiscal 2005 to \$38.2 mills in fiscal 2006, in response to projected declines in assessed value as a result of damage caused by Hurricane Katrina. After collecting 150% of the amount forecasted for 2006, the tax rate was decreased to \$31.7 mills for fiscal 2007. The tax rate has decreased further to \$23.80 mills in 2008 and 2009 in order to keep revenues more aligned with annual debt service requirements. Moody's believes that the Board's actions demonstrate its willingness to adjust the tax rate as necessary and this is a key factor in the Baa3 rating.

Although the Board is not required to maintain reserves for the payment of GO bonds, it has been the policy of the Board, since 1951, to maintain reserves of approximately one-half of the maximum amount of principal and interest on GO bonds payable in one year. The Board had to rely on some of the reserves in 2006 to service debt; however, these reserves were completely replenished to prior year levels and are now at an estimated \$30 million. The presence of the reserve was significant and provided bondholders comfort in the early months after Katrina, when damage to the tax base and the affects on pledged revenues were unknown; therefore, Moody's notes that it is significant that the Board continues to maintain a strong debt service reserve.

POSITIVE GROWTH IN ASSESSED VALUATIONS

Hurricane Katrina resulted in a 5-month delay in the mailing of property tax bills for fiscal 2006. Without

knowing the full extent of damage to the tax base, City officials created a budget that assumed a 50% reduction in property values. The actual valuation loss was only 25% for fiscal 2006. Moody's has noted in prior reports that real property in Orleans Parish qualify for a \$7,500 homestead exemption on the assessed value of an owner occupied home, which is set at 10% of full value. Therefore, on a \$100,000 valued home, the assessed value is only \$2,500 and homes valued at \$75,000 or less are effectively not taxed. For fiscal 2007, the assessment cycle returned to the normal schedule and tax bills were mailed in December of 2006 and due by January 31st of 2007. Total valuations for fiscal 2007 increased 11% over 2006 and remain only 12% below 2005. For fiscal 2008, the full valuation increased another 33% to a sizable \$21 billion which exceeds levels even before the storm. Although the assessed valuation increase only 2.8% in fiscal 2009, millions of Federal dollars are currently beginning to flow which should attract additional population and business growth. Population is currently estimated to be 329,000 which approximates 72% of the pre-Katrina level.

RECOVERY IN KEY REVENUES CONTINUES

In fiscal 2007, sales tax revenues provided 28% of total General Fund operating revenues making it the primary revenue source for the City's general fund. Sales tax revenues are displaying faster than expected recovery which is significant for the Baa3 rating given the City's reliance on this revenue source. Sales tax revenues for 2005 were 24% below 2004 at \$116 million. In 2006, collections totaled \$124 million which was 19% below 2004 but better than earlier estimates that projected a 30% decline. Fiscal 2004 serves as a base year given it was the last full fiscal year before the hurricane. Sales taxes increased but remained 11% under 2004 for fiscal 2007 to \$133 million. Sales taxes are projected to increase in fiscal 2008 to \$142 million which would be 29% of General Fund revenues.

Over the last three fiscal years, the City has been able to establish a higher General Fund balance than before the storm and has created an emergency fund equal to 8% of General Fund expenditure. The total fund balance increased from \$21 million, equal to 4.8% of revenues, in fiscal 2003 to a peak of \$99 million in fiscal 2006 which was equal to 27% of revenues. During this period, the unreserved fund balance increased from \$11.4 million to \$95 million. In fiscal 2007, the total fund balance decreased to \$95 million and the unreserved balance was \$78 million. During the 2005 fiscal year, City officials enacted significant staffing and other cuts to bring expenditures in line with available revenues and appeared committed to making additional cuts if needed. The improvement in the fund balance was assisted by the budget cuts but primarily driven by influxes of cash from Federal and State government funds received after the hurricane. Therefore, during fiscal 2008, the General Fund reserves are expected to decrease significantly as designated funds for capital outlay were spent. Additionally, during 2008, the City experienced cost overruns associated with police overtime which they plan to control during fiscal 2009.

City officials have identified their emergency fund reserve as \$32.5 million equal to 7.98% and close to the 8% target for fiscal 2007. Although this reserve will be \$34 million in fiscal 2008, the 7.2% of expenditures is below the 8% target. For fiscal 2009, the Mayor's budget amended the originally adopted budget to cut expenditure and ensure the emergency fund would equal 8% of expenditures. Moody's believes that this fund balance reserve is significant to demonstrating prudent fiscal management. A trend of healthy reserves will continue to be a consideration in the City's rating assignments.

City officials have provided reasonable financial projections which indicate that the use of one time funding from government sources will end in the 2010 fiscal year so that City revenues are projected to be sufficient for supporting General Fund expenditures during 2011. City officials continue to demonstrate the use of long term projections which is also a favorable factor in the rating. Moody's believes the projections are reasonable and include some conservative amounts. The projections include the increased interest rate costs associated with the pension obligation bonds.

RISK IN PENSION OBLIGATION BONDS

In 2000, the City issued Pension Obligation Bonds, Series 2001 that are secured by excess revenue of the General Fund. Moody's notes that an important distinction in this rating is the bonds were not issued through the Board of Liquidation and there is no authority to increase taxes to repay the bonds.

This variable rate debt is enhanced by a standby bond purchase agreement with JP Morgan (senior unsecured rated Aa3/Stable) and insured by Ambac (Baa1 Financial Strength rating/negative outlook). Ambac's downgrades impacted the ability to remarket the bonds and triggered a change in interest rates on the liquidity facility. The total outstanding variable rate amount of \$138.5 million is hedged by a swap with UBS. With a failed remarketing, the bonds have been held by the bank since February of 2008. The trigger on the bank bonds to become a term loan is the expiration date of the standby agreement. The current standby agreement was extended on December 18, 2008 and expires on December 18, 2009. JP Morgan has provided the City with four annual extensions since December 18, 2006. If the agreement is not extended on December 18, 2009, the term loan will require the city to begin accelerated repayment in semiannual principal payments over 5 years beginning on June 18, 2010. In order to be conservative, officials are planning to include this accelerated payment of almost \$30 million in development of the 2010 budget. However, the City is currently working to provide an alternative solution to prevent the accelerated payments and is working to successfully remarket the variable rate demand bonds. The City is also negotiating with JP Morgan to provide an annual extension to the standby purchase agreement.

Also as a result of the downgrade on Ambac, the interest rate on the variable rate bonds changed from SIFMA to prime plus one which is currently at 4.25%. Under the swap with UBS, the City pays a fixed 6.95% rate and received one month LIBOR. With LIBOR currently at 0.56%, the City is paying approximately 10.6% in interest when the original swap was initiated as a cost of tender swap to net the 6.95% fixed rate cost. The rising cost in interest rates resulted in an increase of approximately \$4 million during the 2008 fiscal year. The 2009 budget includes the higher interest rate for total debt service repayment. Favorably, the UBS swap does not require collateral posting by the city. The current mark to market on the swap is a \$43 million against the City. Termination of the swap could be triggered if one or more of the City's outstanding senior debt falls below Baa3 or BBB- for both Moody's and S&P, respectively. Moody's notes that when the City's highest rating was below investment grade following Hurricane Katrina, by both agencies, UBS worked with the City and did not terminate the swap.

KEY STATISTICS:

Population (2000): 455,000

Population 2007: 329,000

2008 Full valuation: \$19 billion

2008 Assessed valuation: \$2.2 billion

2000 Per Capita Income: 17,258 (79.9% of US)

Payout (10 years): 52%

2007 General Fund balance: \$95 million (22.5% of General Fund revenues)

2007 Unreserved General Fund balance: \$78.6 million (18.6% General Fund revenues)

Outstanding Debt:

GOULT: \$523.9 million

Drainage Tax bond: \$22.7 million

Downtown Development District: \$6.1 million

Limited Tax Bonds, Series 2005: \$28.4 million

Audubon Limited Tax Bonds: \$2.4 million

Pension Obligation Bonds: \$138.5 million

RATING METHODOLOGIES USED AND LAST RATING ACTION TAKEN

The principal methodology used in rating the current issue was "Local Government General Obligation and Related Ratings," which can be found at www.moodys.com in the Credit Policy & Methodologies directory, in the Index of Special Reports - U.S. Public Finance. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Credit Policy & Methodologies directory.

The last rating action for the City of New Orleans was on October 30, 2007 when the Baa3 GOULT rating was affirmed.

Analysts

Kristin Button
Analyst
Public Finance Group
Moody's Investors Service

Douglas Benton
Backup Analyst
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

CREDIT RATINGS ARE MOODY'S INVESTORS SERVICE, INC.'S (MIS) CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MIS 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 ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS DO NOT CONSTITUTE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS ARE NOT RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. CREDIT RATINGS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MIS ISSUES ITS CREDIT RATINGS 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.

© Copyright 2009, Moody's Investors Service, Inc. and/or its licensors including Moody's Assurance Company, Inc. (together, "MOODY'S"). All rights reserved.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY 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, such information is provided "as is" without warranty of any kind and MOODY'S, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. 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 credit ratings and financial reporting analysis 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. 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. Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling.

MOODY'S hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MOODY'S have, prior to assignment of any rating, agreed to pay to MOODY'S for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,400,000. Moody's Corporation (MCO) and its wholly-owned credit rating agency subsidiary, Moody's Investors Service (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 on Moody's website at www.moody's.com under the heading "Shareholder Relations - Corporate Governance - Director and Shareholder Affiliation Policy."