## New Issue: MOODY'S ASSIGNS Aaa RATING TO MECKLENBURG COUNTY'S (NC) $273 MILLION GO BONDS, SERIES 2011A,B,C; OUTLOOK REMAINS NEGATIVE

Global Credit Research - 06 Oct 2011

**AFFIRMATION OF Aaa RATING AFFECTS APPROXIMATELY $2 BILLION OF DEBT OUTSTANDING**

County
NC

**Moody's Rating**

| ISSUE | | RATING |
|---|---|---|
| General Obligation Public Improvement Bonds Series 2011A | | Aaa |
| **Sale Amount** | $49,000,000 | |
| **Expected Sale Date** | 10/15/11 | |
| **Rating Description** | General Obligation | |
| Taxable General Obligation School Bonds (Qualified School Construction Bonds) Series 2011B | | Aaa |
| **Sale Amount** | $51,000,000 | |
| **Expected Sale Date** | 10/15/11 | |
| **Rating Description** | General Obligation | |
| General Obligation Refunding Bonds, Series 2011C | | Aaa |
| **Sale Amount** | $173,000,000 | |
| **Expected Sale Date** | 10/15/11 | |
| **Rating Description** | General Obligation | |

**Opinion**

NEW YORK, Oct 6, 2011 -- Moody's has assigned a Aaa rating and a negative outlook to Mecklenburg County's (NC) $49 million of General Obligation Bonds, Series 2011A, $51 million of Taxable General Obligation Bonds, Series 2011B and $173 million General Obligation Refunding Bonds, Series 2011C. Concurrently, we have affirmed the Aaa rating and negative outlook on the county's $1.7 billion of outstanding GO debt and the Aa1 rating on $552 million of outstanding Certificates of Participation.

RATINGS RATIONALE

Affirmation of the county's Aaa rating incorporates the county's still-healthy financial position despite recent reserve reductions. The rating also factors in recent actions taken by management to stabilize and improve reserve levels and reduce the county's above average debt profile. The county continues to benefit from a large and increasingly diversified tax base which is slowly recovering following a deep economic downturn. The Series A bonds will provide $32.4 million for park and recreation and $16.6 million of schools. The Series 2011B bonds will go to fund various school projects. The Series 2011C bonds will refund the county's Series 2004A with an estimated net present value of 5.9%, 2005A bonds with an estimated net present value of 4% with no extension of maturities. Additionally, the county will be refunding the variable rate General Obligation Bonds Series 2000C, Series 2001B, Series 2006A and the termination payments (approximately $8.8 million) related to the 2000C and 2001 bonds will be funded with bond proceeds. The termination payment on the Series 2006 bonds, approximately $8 million, will be funded with cash.

Moody's negative outlook on Mecklenburg County's Aaa rating is due to its indirect linkages to the weakened credit profile of the US government. The negative outlook relates to Moody's August 2 decision to confirm the Aaa government bond rating of the United States and assign a negative outlook. We believe that Mecklenburg County's rating could be affected by a downgrade of the US government's rating. In the coming weeks we will assess Mecklenburg County's degree of vulnerability to sovereign risk in terms of its reliance on capital markets, dependence on federal revenues, sensitivity to macroeconomic cycles, and available financial resources to offset risks related to the US government, in order to determine whether to maintain the negative outlook. Please see the Press Release from August 4 entitled "Moody's confirms Aaa ratings of 5 U.S. states and 303 other public finance issuers indirectly linked to U.S. Government bond rating; negative outlooks assigned" for more information this rating action.

Credit Strengths:

-- Effective financial management during economic downturns, particularly a willingness to promptly identify and close budget gaps

-- Budget reserves that still provide an adequate cushion, although a reduced one

-- Substantial tax base with healthy wealth indices

Credit Challenges:

-- Economically sensitive revenues which have placed pressures on the budget over the past two years.

-- Above average unemployment persists

--High debt and debt service levels

DETAILED CREDIT DISCUSSION

DOUBLE DIGIT UNEMPLOYMENT EVIDENCES IMPACT OF RECESSION AND EXPOSURE TO FINANCIAL SERVICES AND CONSTRUCTION; LONG TERM PROSPECTS REMAIN FAVORABLE FOR REGION

Growth has slowed in the county's $110 billion tax base as the recession has significantly affected two of the county's key drivers of the last decade, financial services and housing. However, we believe continued positive net in-migration and economic diversification have favorably positioned the county for the longer term. Approximately 80% of the county's assessed value is the City of Charlotte (GO rated Aaa/stable outlook), which, as home to Bank of America (Sr. Unsec. rated Baa1) and Wells Fargo (Sr. Unsec. rated A2, negative outlook), has developed into the second largest financial services sector in the US and as such is vulnerable to the challenges facing the global financial markets. Bank of America has announced plans for significant lay-offs over the next three years. While it is unclear how the downsizing will affect the county's workforce, the company has announced that it will reduce the workforce by approximately 3,000 jobs world-wide. Wells Fargo and Company acquired Wachovia in late 2008 and has committed to maintain its east coast headquarters in Charlotte. Wachovia currently employs about 20,000 people in the region. The two banks, together, account for approximately 7.5% of the workforce, a sizable concentration given the current vulnerability of the financial services sector. We believe the full impact of the downturn in financial services may have yet to be felt, and we will continue to monitor the implications for the county. The losses in the financial services sector and housing downturn have had a direct effect on unemployment within the county which has increased to 11.1% as of July 2011 compared to 10.3% for the state and 9.3% for the U.S.

A level of economic stability is brought about by the presence of major non-profit and educational institutions, including Presbyterian Healthcare/Novant Health, Carolinas HealthCare System and the University of North Carolina-Charlotte (rated Aa3) with its 23,300 students. Diversification in the economy is evident in the presence of Duke Energy (rated Baa2), one of the nation's largest utilities and US Airways (rated B2), which employs several thousand people at its main hub at Charlotte-Douglas International Airport (rated A1/positive outlook). Favorably, there were several significant announcements including the 2012 Democratic National Convention which will be hosted within the county. The convention is expected to have a $150-200M economic impact and be largely supported by federal aid. Additionally, UNC Charlotte's uptown development was completed in August 2011 and includes a $50 million investment into the taxbase. Management notes that eventually rail service will connect the campus and this is expected to drive future expansion of the area. There have been roughly 17 other recent announcements of expansions, relocations and new investments within the county. The county's growing and vibrant economy has historically been a significant factor in the Aaa rating. Protracted unemployment at the current level and a longer than average recession could challenge the county's credit profile.

Wealth levels remain stronger than the state and nation, with per capita income representing 132.1% of the State of North Carolina (G.O. rated Aaa/stable outlook) and 124.3% of the nation. While the full value per capita of $120,266 is strong, Moody's views this statistic as understated, and less comparable to local governments nationally, given that the last six years of appreciation have not been captured.

HEALTHY FINANCIAL POSITION IS EXPECTED TO PERSIST GIVEN CONSERVATIVE MANAGEMENT

The county will likely maintain its healthy financial position, apparent from General Fund balances exceeding 20% of revenues for the last five years, despite the use of reserves in fiscal 2009 and fiscal 2010 given solid management practices and formally adopted financial policies.

The county ended fiscal 2010 with a General Fund balance of $329.5 million (25.8% of General Fund revenues), reflecting a $30 million use of reserves. The county was able to partially replenish its $45 million budgeted fund balance appropriation through better than projected revenues and $20 million of mid-year budget reductions. While revenues were better than previously projected they still represented a negative variance compared to budget of $22 million. This was primarily driven by sales tax ($14.9 million) and charges for services ($13.4 million) being significantly under budget due to the weakening economy. To help offset the weaknesses in revenues the county conservatively budget expenditures with a positive variance of $60.3 million. The largest portion of the expenditure savings was in the conservative budgeting for interest on variable rated debt ($13 million) but the county managed to see savings in most every line item across the board. Unreserved General Fund balance equaled $220.1 million or 18% of revenues, remains well above the county's policy of maintaining unreserved fund balance at between 12% and 14% of revenues. Unaudited fiscal 2011 results show that the county finished the fiscal year with an increase of $41.7 million after replenishment of fund balance appropriation of $22.7 million. Fiscal 2011 is estimated to have ended with a total General Fund balance of $372.6 million (29.1% of estimated revenues). Management attributes the increase to fund balance to both conservative budgeting on revenues ($30.5 million over budget) and expenditures ($36.8 million under budget). The primary drivers in the revenues were intergovernmental revenue exceeded budget by $9.5 million, sales tax exceeded budget by $8.5 million and property tax exceeded budget by $13.4 million. On expenditures low interest rates for variable rate debt continue to factor heavily into the budget finishing the year $15.3 million under budget. The county also realized a considerable amount of savings in administrative services of $15.9 million. Management will implement the GASB 54 accounting changes for fiscal 2011 and the expectation is that unassigned fund balance is expected to be $264 million which would have been compared to $102 million in fiscal 2010 had the county been an early adopter of GASB 54. The difference is attributed in part to the lack of fund balance appropriation in the fiscal 2012 budget.

The county's fiscal 2012 adopted budget includes an increase of $34.8 million or 2.7% from the previous budget, this includes $269 million for a dedicated debt service fund which will be funded at $0.21 per $100 assessed value going forward. The budget includes a slight property tax increase, over revenue neutral, of $0.03 per $100 assessed value and no appropriation of fund balance. Favorably, the budget does not include a fund balance appropriation for the first time in ten years. The budget also includes an increase to the Charlotte Mecklenburg Schools of $26.1 million (8.7%) and an increase of 6.3% for the Central Piedmont Community College. Additionally the budget includes $8 million to restore funding to the county's OPEB trust fund. The county had been funding the trust over 90% from 2007 through 2010 but only did pay-go in fiscal 2011 due to budgetary concerns.

DEBT BURDEN EXPECTED TO REMAIN ABOVE AVERAGE DESPITE REDUCTION OF CAPITAL PLAN; REVISED POLICY ALLOWS FOR ADDITIONAL LEVERAGING

The county's debt burden will likely remain above average, despite the county board's recent decision to go on a "debt diet" given an already above average direct debt burden (1.8% of full value) and slowing in tax base growth. Mitigating the direct debt levels is the fact that approximately $1.2 billion of obligations are for the school system, which increases the direct debt level compared to counties nationwide which do not issue on behalf of their schools. However, the overall debt burden, which allows for better national comparability, is also above average at 3.4% of full valuation, reflecting the obligations of all underlying entities in the county. The county recently began funding a debt service fund at

$0.21 per $100 assessed value and has indicated that additional debt would be required to be issued under the levy amount. Any excess revenues within the fund would be used for pay-as-you-go capital going forward.

The county revised its formally adopted debt policies in the fall of 2008, allowing for additional debt capacity. The policy identifies several debt ratios to be monitored and maximum levels for each; debt as a percentage of assessed value (4%), debt service as a percentage of expenditures (20% target; 22% ceiling) amortization of principal in ten years (64%), and unhedged variable-rate debt as a percentage of total debt (35%). Given that the county's current debt position is already well above Moody's national median for Aaa rated counties (direct 0.5%; overall 2.2% of full value), leveraging to the levels allowable in the debt policy could have a negative impact on the rating. Particularly of note is debt as a percentage of expenditures, which at 22% would be well above the Aaa median (9%); however the county has indicated it would go to this level only in exceptional circumstances. In fiscal 2010 debt service equaled 18.4% of operational expenditures.

VARIABLE RATE EXPOSURE REDUCED TO LESS THAN ONE QUARTER OF TOTAL DEBT FOLLOWING CURRENT REFINANCING; EXPECTATION OF MARKET ACCESS KEY TO RATING ON COUNTY'S LONG MODES VARIABLE RATE

The county's adopted debt policy allows for more variable rate and swap exposure than many similarly rated counties, presenting exposure to market disruption, interest rate risk and counterparty risk. Favorably, the county is taking steps to reduce its exposure to variable rate debt, notably refinancing two variable rate issues as fixed debt in 2009 and another three with the current issuance. Consequently, total variable rate debt now equals $437.9 million (22% of total debt outstanding), approximately $160.7 million, or 36% of which is synthetically fixed through swap agreements. Moving forward, the county plans to issue only fixed rate debt and as such expects variable rate to comprise 22% of total debt in 2012. Mitigating the risks associated with variable rate debt are the county's budgeting practices, currently the county budgets variable debt at 5% and 50 basis points to the fixed rate on swapped transactions. Further mitigating the risks is the county's strong liquidity ($397.4 million in cash and short-term investments across all Governmental Funds as of June 30, 2010). County officials recognize that the use of variable rate debt and derivatives has significantly reduced borrowing costs to the county over the past decade and prudently understand that every year will not necessarily yield a savings. Thus, they are committed to setting aside cash during the strong years to offset increased debt service in higher-cost years.

The county has one series of variable rate bonds, equaling 26% of total variable rate debt, which is not supported by a third party liquidity provider. The county's $115 million Variable Rate Refunding Bonds, Series 2009D (rated Aaa/P-1) are currently in a windows mode. Assignment of the P-1 rating is based on Moody's market access approach to self-liquidity on longer-term variable rate instruments and reflects our estimation of the county's ability to timely pay mandatory tenders at the close of the Mandatory Tender Window. Factored into assignment of the P-1 is the six month notice the county will be given, following a failed remarketing, to restructure the bonds or issue refunding bonds, a time frame we believe is sufficient to execute either strategy. Further supporting the rating assignments is the county's strong cash position. Please see report from July 16, 2009 for more information.

COUNTY IS A PARTY TO NINE DERIVATIVE TRANSACTIONS; FORMAL SWAP POLICY AND PRUDENT MANAGEMENT PRACTICES MITIGATE RISKS

After the refunding the county will be party to nine derivative transactions related to various series of outstanding bonds and COPs with a total notional amount of $160.7 million. Management had intended to rebalance the portfolio given the merger of Bank of America (senior unsecured Baa1, negative outlook) and Merrill Lynch. Post refunding the county will be able to reduce exposure to the bank to $68.5 million or 42.6% from 50%. Additionally the county has $73.9 million with Wells Fargo (senior unsecured A2, stable outlook) and $18.3 million through Natixis (senior unsecured Aa3, stable outlook). All transactions are designed to create synthetic fixed-rate obligations for the county.

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

-Removal of negative outlook on the U.S. sovereign rating.

WHAT COULD MAKE THE RATING GO DOWN:

-Significant declines in liquidity or reserves.

KEY STATISTICS

2010 Population: 876,067

2012 Full Valuation: $110.6 billion

Full Value Per Capita: $120,266

Debt Burden: 1.8% (3.4% direct debt burden)

Payout of Principal (all tax-backed debt): 72%

Unemployment Rate (7/2011): 11.1%

FY10 General Fund Balance: $329 million (26.8% of General Fund Revenues)

Median Family Income as a % of state: 130.8% (121.1% of the US)

Per Capita Income as a % of state: 134.7% (126.7% of the US)

GO debt outstanding: $2 billion

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was General Obligation Bonds Issued by U.S. Local Governments published in October 2009. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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