FITCH RATES HAWAII'S GOS 'AA'; OUTLOOK STABLE

Fitch Ratings-New York-04 November 2011: Fitch Ratings assigns 'AA' ratings to the following state of Hawaii bonds:

--$800 million general obligation (GO) bonds of 2011, series DZ;
--$382.41 million GO refunding bonds of 2011, series EA;
--$2.8 million GO refunding bonds of 2011, series EB;
--$56 million GO refunding bonds of 2011, series EC;
--$23 million GO refunding bonds of 2011, series ED.

In addition, Fitch affirms the following rating:

--Approximately $4.85 billion outstanding GO bonds at 'AA'.

The Rating Outlook is Stable.

KEY RATING DRIVERS

--Financial management is sound and the state employs quarterly revenue forecasting and long-term planning. Revenue underperformance resulted in deficits in fiscal years 2009 and 2010, and previously large balances were largely depleted. Preliminary results for fiscal 2011 indicate a return to positive operations.

--Hawaii's extensive tourist infrastructure underpins an economy dominated by tourism, and the geographic location limits economic diversification efforts.

--Debt levels are high, reflecting in part the state's broad responsibilities, particularly in education, though debt amortizes at an above-average pace.

--Pension funding levels are considered weak by Fitch's standard. Other post employment benefit obligations (OPEB) are also significant.

SECURITY

General obligations of the state of Hawaii carry a full faith and credit pledge of the state.

CREDIT PROFILE

The state of Hawaii's 'AA' GO rating reflects the state's sound financial management practices, its highly developed tourist economy which adds volatility to its revenue structure, high debt levels, and significant long-term liabilities.

Prior to the recent recession, with strong revenue growth, the combined general fund and Emergency and Budget Reserve Fund (EBRF) balances peaked in fiscal 2006 at $785.8 million or 15.9% of total general fund resources, with the EBRF accounting for $53.5 million of the total. As revenue growth slowed in fiscal years 2007 and 2008, the combined balances declined to $405.2 million at the close of fiscal 2008. Increased reliance on the accumulated general fund balance was most noticeable in fiscal 2009 when Hawaii experienced a significant 9.5% decline in revenues. The state closed the fiscal year with a negative ending balance of $36.8 million after accounting for an overstatement of certain tax revenues, though $60.4 million remained in the EBRF and approximately $180 million was available in the separate Hurricane Relief Fund (HRF).

The fiscal plan for the recently completed biennium spanning fiscal years 2010 and 2011 was initially balanced through a mix of tax increases, reduced spending, modest debt restructuring, the application of federal stimulus monies, and employee furloughs. However, projected revenues had been revised downward several times over the course of the biennium, and despite delaying the payment of income tax refunds to be paid in fiscal 2010 into fiscal 2011 and a $57 million draw from the HRF, which was not previously expected to be drawn upon, the state ended fiscal 2010 in a negative position.

Continuing revenue weakness resulted in a projected $220 million shortfall for fiscal 2011 following an off-cycle meeting of the state's council on revenues in late March 2011 prompted largely by the Japanese earthquake, and the state had planned to maintain balance through spending cuts, fund transfers, and the draw down of remaining balances in the HRF and EBRF. Ultimately, revenue performance for fiscal 2011 was above those projections, and combined with the effects of lapsed spending, full draws on the reserve balances were not necessary. Preliminary projections for fiscal 2011 indicate an ending general fund balance of $126 million, representing 2.5% of fiscal 2011 revenues. An additional $30 million in available balances remained between the HRF and EBRF at the close of the fiscal year.

Hawaii's budget for the biennium spanning fiscal years 2012 and 2013 addressed a gap of over $1 billion, a figure which had widened by $265 million following additional downward revenue forecast revision earlier this year. The gap was closed through a mix of spending reductions, savings resulting from labor concessions, and temporary revenue measures that limit deductions and suspend exemptions for the duration of the biennium. While the plan projects that the general fund ending balance will grow to $275 million over the course of the biennium, the state currently plans to use some of those available funds to restore $175 million to the HRF and EBRF by the end of the biennium.

Hawaii's tourist industry relies heavily on California and Japan, although increased visitation from other countries, most recently Korea and Canada, has provided an offset to declining volumes from Japan following the events there in March. Following a sharp drop in 2001, the tourism sector saw strong growth that began in 2004 and continued to a record high in 2007, due in part to gains in domestic arrivals. The previous loss of two passenger air carriers and limited recovery of that service, combined with previously rising fuel costs and weakening consumer spending in the recession, played negatively on Hawaii's tourism industry in 2008 when arrivals dropped 10.8%. Visitor arrivals declined 4.5% in 2009 before rebounding by 8.7% in 2010. The state is currently projecting modest growth of 3% for 2011; visitor arrivals through the third quarter of the year are up 2.7%.

Following several years of strong gains, employment in the recession generally mirrored the national experience, down 0.9% in 2008, 4.4% in 2009, and 0.8% in 2010. Year-over-year growth in September 2011 was 1.4% as compared to 1.1% for the nation. While tourism remains dominant when compared nationally, Hawaii's employment in the service sectors is relatively near national levels. Unemployment for September 2011 was 6.4%, down slightly from 6.5% one year prior and well below the U.S. rate of 9.1% for the month; Hawaii's unemployment rate has been consistently below that of the nation since 2001. Personal income growth has outpaced the nation for much of this decade, and 2010 per capita personal income now stands at 104.3% of the U.S., ranking Hawaii 17th among the states by this measure.

Hawaii's government is highly centralized, and the state is responsible for many functions, such as education, normally handled at the local level. Largely as a result of this structure, debt is and will remain high. As of July 1, 2011, net tax-supported debt totaled approximately $5.25 billion, which equates to 9.3% of revised 2010 personal income. Principal is retired at an above-average pace, with 67% of bonds due in 10 years. Funding levels for Hawaii's pension system remain a concern, with reported funded ratios having declined from 95% in 2000 to 61.4% as of June 30, 2010 and the unfunded liability exceeding $7.1 billion. Using Fitch's more conservative 7% discount rate assumption, the plan would be 55.3% funded. Fitch notes that the state has recently passed legislative changes including changes to the benefit structure and increased employee contributions which are designed to limit the growth in pension liabilities. Further, the state's OPEB obligation is large.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

In addition to the sources of information identified in Fitch's U.S. Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria', dated Aug. 15, 2011;
--'U.S. State Government Tax-Supported Rating Criteria', dated Aug. 15, 2011;
--'Enhancing the Analysis of U.S. State and Local Government Pension Obligations', Feb. 17, 2011.

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=648898
U.S. State Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=648897
Enhancing the Analysis of U.S. State and Local Government Pension Obligations
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=604785