

Announcement: Moody's affirms Aa2 rating on State of Hawaii general obligation bonds and Aa3 rating on state' certificates of participation; stable outlook also affirmed

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Approximately \$4.9 billion G.O. debt and \$62 million certificates of participation outstanding

New York, July 03, 2012 -- Moody's Investors Service has affirmed the Aa2 rating on the State of Hawaii's general obligation bonds (approximately \$4.9 billion outstanding) and the Aa3 rating on the state's certificates of participation (approximately \$62 million outstanding). The outlook is stable.

SUMMARY RATING RATIONALE

The Aa2 rating incorporates Hawaii's improving financial operations following the recession-driven revenue fall-off over the last several years; low pension funded ratios and growing expenses for other post employment benefits (OPEB); and high debt ratios that in part reflect debt issues for K-12 school capital projects. The state's vital tourism industry continues to show signs of improvement. The fiscal 2013 revenue forecast was recently reduced to reflect revised estimates of certain temporary taxes that were enacted for fiscal years 2012 and 2013. However, the out-year forecast was not changed amid expectations of continued economic improvement in the state. Hawaii has relatively strong governance practices such as multi-year financial planning and quarterly binding consensus revenue forecasting, and its fiscal 2011 audit was released in a timely manner, reversing four consecutive years of late audits from fiscal 2007 to fiscal 2010.

STRENGTHS

- Financial governance that includes well-established multi-year, quarterly consensus revenue forecasting, and strong executive power to reduce spending
- Historical fiscal conservatism; prompt action to address revenue shortfalls
- Continued military housing construction helps offset slow residential and commercial markets
- A good liquidity position that is sufficient for the state to avoid short-term cash flow borrowing, and rapid amortization of debt; no exposure to variable rate debt or derivative products

CHALLENGES:

- Vulnerability to shifts in Hawaii's tourism-based economy, resulting in revenue falloff and budget shortfalls
- Modest reserve levels reduce the state's ability to address further revenue erosion
- Large state and local government employment sector contributes to spending pressure for salary and benefit settlements
- Debt ratios that are among the highest in the nation and likely to remain there given state-level capital funding, especially for education, combined with relatively low pension funding levels despite recent reforms; high OPEB liability

Outlook

The rating outlook for Hawaii is stable reflecting expectations of continued revenue growth; signs of economic stabilization as tourism rebounds; a decreased reliance on one-time resources to balance the 2012-2013 biennial budget; and the state's proactive measures to improve the funded status of its retirement systems. The stable outlook also reflects our expectation that the state will manage its budget challenges and make appropriate adjustments as needed to restore budget balance in the event that the economic recovery is more prolonged and/or

weaker than currently projected, resulting in revenue shortfalls.

WHAT COULD MAKE THE RATING GO UP

- Rebuilding and maintenance of strong reserve levels and restoration and maintenance of structural budget balance
- Reduced economic volatility and sustained job growth
- Sustained reduction in debt ratios and significant improvement in pension funded ratios, and sooner than currently projected

WHAT COULD MAKE THE RATING GO DOWN

- Economic weakening leading to sustained employment erosion or deterioration of revenue trends leading to budget imbalance, liquidity pressure, and narrowing of financial position
- Increased use of non-recurring solutions to balance budget
- Increased debt or debt service ratios relative to other states or deterioration of pension funded ratios below already low levels

The principal methodology used in this rating was Moody's State Rating Methodology published in November 2004. Please see the Credit Policy page on www.moody's.com for a copy of this methodology.

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Nicole Johnson
Senior Vice President
Public Finance Group
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A.
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653

Nicholas E Samuels
Vice President - Senior Analyst
Public Finance Group
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653

Releasing Office:
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A.
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653



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