



Rating Action: MOODY'S LOWERS STATE OF ILLINOIS' G.O. RATING TO A2 FROM A1, ASSIGNS A2 RATING TO PLANNED \$800 MILLION ISSUANCE

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OUTLOOK REVISED TO STABLE; \$32 BILLION OF OUTSTANDING STATE DEBT AFFECTED

New York, January 06, 2012 -- Moody's Rating

Issue: General Obligation Bonds, Series A of January, 2012; Rating: A2; Sale Amount: \$525,000,000; Expected Sale Date: 1-11-2012; Rating Description: General Obligation

Issue: General Obligation Bonds, Taxable Series B of January, 2012,; Rating: A2; Sale Amount: \$275,000,000; Expected Sale Date: 1-11-2012; Rating Description: General Obligation

Opinion

Moody's Investors Service has lowered the State of Illinois' general obligation bond rating to A2 from A1 and revised the state's outlook to stable from negative. The A2 rating has also been assigned to \$800 million general obligation January 2012 Series A and Taxable Series B bonds that the state has scheduled to price on January 11. Proceeds will finance school, transportation and other capital projects. We have also downgraded to A2 from A1 the rated portion of the state's \$2.47 billion of outstanding Build Illinois sales tax revenue bonds, and to A3 from A2 \$2.48 billion of Metropolitan Pier and Exposition Authority and \$73 million of Civic Center Program bonds.

SUMMARY RATING RATIONALE

The downgrade of the state's long-term debt follows a legislative session in which the state took no steps to implement lasting solutions to its severe pension under-funding or to its chronic bill payment delays. Failure to address these challenges undermines near- to intermediate-term prospects for fiscal recovery. It remains to be seen whether the state has the political willingness to impose durable policies leading to fiscal strength, though in the recent past it has reached consensus on difficult decisions, such as temporary income tax increases enacted last year that stabilized state finances and reduced the state's need for non-recurring budgetary measures. Illinois retains the sovereign revenue and spending powers common to all U.S. state governments. These powers, along with Illinois' legal provisions giving G.O. debt service priority over other state spending, support the move to a stable outlook.

STRENGTHS

- Sovereign powers over revenue and spending
- Statutory provisions giving priority to debt-service over other state expenditures

CHALLENGES

- Severe pension funding shortfall
- Chronic use of payment deferrals to manage operating fund cash
- Weak management practices reflected in pension under-funding and payment delays

Outlook

The state's stable outlook reflects its sovereign powers over revenue and spending, as well as statutory provisions establishing priority of payment for G.O. debt service. Although the likelihood of effective, proactive movement on major challenges appears minimal at present, the state's stable outlook also relies on a demonstrated ability to make politically difficult choices as the need arises.

WHAT COULD MAKE THE RATING GO UP

- Adoption of a credible, comprehensive long-term pension funding plan
- Substantial progress in reducing payment backlog, and legal framework or plan to prevent renewed buildup of late bills

WHAT COULD MAKE THE RATING GO DOWN

- Early phase-out of 2011 tax increases without offsetting binding expenditure actions, increasing the structural gap
- Further deterioration in pension funded status or failure to make legally required contributions

PRINCIPAL RATING METHODOLOGY

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.moodys.com for a copy of this methodology.

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