STANDARD & POOR'S

Global Credit Portal
RatingsDirect®

March 26, 2010

Summary:
Illinois; General Obligation; Note

Primary Credit Analyst:
Robin Prunty, New York (1) 212-438-2081; robin_prunty@standardandpoors.com

Secondary Credit Analyst:
John Kenward, Chicago (1) 312-233-7003; john_kenward@standardandpoors.com

Table Of Contents

Summary:

Illinois; General Obligation; Note

Credit Profile		
US$300. mil GO bnds (Build America Bnds) ser 2010-2 due 03/01/2011-2035		
Long Term Rating	A+/Watch Neg	New
US$250. mil GO bnds April ser 2010 due 03/31/2011		
Short Term Rating	SP-1	New
US$56. mil GO bnds ser March ser 2010 due 03/01/2035		
Long Term Rating	A+/Watch Neg	New
Illinois GO		
Long Term Rating	A+/Watch Neg	On CreditWatch Negative
Illinois GO		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative

Rationale

Standard & Poor's Ratings Services has placed Illinois' general obligation (GO) bond ratings on CreditWatch with negative implications due to the state's growing budget gap, ongoing liquidity pressure, and the lack of recurring solutions under consideration for fiscal 2011 and beyond. At the same time, Standard & Poor's has assigned an 'SP-1' rating to Illinois' (GO bonds series of April 2010 and an 'A+' rating to Illinois' $300 million taxable Build America Bonds series of April 2010-1, $56 million GO bonds, taxable series of March 2010.

The governor's proposed budget identifies a cumulative $13 billion budget gap for fiscal 2011, which is sizable, in our view, at 50% of fiscal 2011 general fund revenues. The proposed budget includes no revenue enhancement measures, proposes deep spending cuts, and is highly reliant on debt issuance to address the fiscal 2011 budget gap. The deficits from prior years (fiscal 2008-2010) are carried forward and are not addressed as part of the fiscal 2011 budget. The governor has publicly expressed support for a 1% surcharge on both individual and corporate income tax rates but it is not part of the formal budget proposal so it is not clear what structural solutions will actually be considered for fiscal 2011. Illinois' lack of recurring solutions to address its sizable budget gap and liquidity weakness could result in a downgrade. We continue to believe that Illinois has the capacity to restore budget balance due to the absence of tax limitations or stringent constitutional or legal requirements related to spending that we see in other states, but its willingness to implement difficult and politically unpopular measures to restore budget balance is questionable, in our view.

The 'SP-1' short-term rating on Illinois' GO bonds series of April 2010 reflects Standard & Poor's opinion of the state's direct, full faith and credit GO pledge and adequate projected debt service coverage on the maturity date of March 31, 2011. The notes are authorized by state statute. Note proceeds will be deposited into the Healthcare Provider Relief Fund to fund Medicaid services and enhance federal reimbursements. The state's general fund cash flow projection is uncertain given the absence of an approved budget. There is a significant deficit that is being carried forward into fiscal 2011 that continues to strain liquidity. Although the general fund cash flow position is weak, funds will be transferred from the general revenue fund monthly as required by statute to ensure sufficient resources are in the General Obligation Bond Retirement and Interest Fund for payment of the 2011 maturity. Illinois' monthly cash flow is estimated to range from $1.4 billion-$2.3 billion compared with monthly debt service set-asides of about $250 million (includes all GO debt as well as this issue). There may be additional borrowing required for cash flow purposes in fiscal 2011. Pursuant to statute, the governor, comptroller, and the treasurer are authorized to order the transfer of any money on deposit in the treasury into the GO Bond Retirement and Interest Fund at times and in amounts they deem necessary to provide for the payment of interest and principal on the notes. The most significant nongeneral fund cash resources are found in the special state fund, state trust funds, the debt service fund, and the highway fund. Although these funds may be used to make a payment on bonds or notes according to the state, these nongeneral fund cash balances are not available for interfund borrowing or transfer to the general fund. These balances total $6.6 billion in fiscal 2010.

Bond proceeds from the series 2010-2 and series March of 2010 will fund various capital projects. Key factors supporting the 'A+' rating include our opinion of Illinois':

- Deep and diverse economy, which is anchored by the Chicago metropolitan statistical area;
- Above-average income levels;
- Almost unlimited ability to raise tax and other revenues due to its sovereign powers and the absence of constitutional revenue-raising limits; and
- Ability to adjust disbursements to stabilize cash flow and to access substantial amounts of cash reserves on deposit in other funds for debt service if needed and for operations if authorized by statute.

Offsetting factors include our view of the state's:

- Significant budget-based deficit for fiscal 2009 and forecasted for fiscal 2010 and 2011;
- Historically large generally accepted accounting principles (GAAP) general fund deficit, which equaled $3.9 billion in fiscal 2008 (11% of expenditures). The comptroller estimates that the unaudited GAAP-based general fund balance deficit at June 30, 2009, is $8.2 billion or 25.6% of general fund expenditures. However, we believe the state's general fund deficit, on a GAAP basis, is substantially and negatively affected by several accounting choices that do not affect most other states;
- Large unfunded actuarial accrued liability (UAAL) for its five pensions that stood at $54.38 billion (50.6% funded) at fiscal year-end 2008, coupled with a large $24.2 billion UAAL for its other postemployment benefits attributed to two of the pension systems. We do consider the recent pension reform legislation approved on March 24 to be a positive development in addressing the liability. The effect on overall liabilities and funded status is not quantified at this time;
- Limited action on structural budget solutions; and
- Fairly high debt burden relative to state peers (50 states) that we expect to rise following significant bond authorizations for operating and capital purposes in fiscal 2010. Any borrowing authorized as part of the fiscal 2010 budget process would accelerate the increase.

Standard & Poor's considers Illinois' economy broad and diverse, with income levels well above average. In our view, the economy has weakened considerably in the past year, in line with national trends. The unemployment rate increased to 10.2% in 2009 from 6.5% in 2008. This is in line with the U.S. average. IHS Global Insight Inc. forecasts that rates could increase above 11% through 2010. Per capita personal income is $42,347 or 105% of the U.S. average, ranking the state 13th nationally and first among the Great Lakes states.

Standard & Poor's expects to resolve the CreditWatch action prior to the start of fiscal 2011 (July 1).

Related Criteria And Research

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Short-Term Debt, June 15, 2007

Ratings Detail (As Of March 26, 2010)		
Illinois GO (wrap of insured) (FGIC & AGM) (SEC MKT)		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative
Illinois GO (ASSURED GTY)		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative
Illinois GO (FGIC)		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative
Illinois GO (MBIA) (AGM)		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative
Illinois GO		
Unenhanced Rating	A+(SPUR)/Watch Neg	On CreditWatch Negative

Many issues are enhanced by bond insurance.

Complete ratings information is available to RatingsDirect on the Global Credit Portal subscribers at www.globalcreditportal.com and RatingsDirect subscribers at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.