

Lynchburg, Virginia; General Obligation

Primary Credit Analyst:

Danielle Leonardis, New York (1) 212-438-2053; danielle_leonardis@standardandpoors.com

Secondary Credit Analyst:

Nicole T Ridberg, New York (1) 212-438-4704; nicole_ridberg@standardandpoors.com

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| US\$23.925 mil GO rfdg bnds ser 2010 dtd 10/21/2010 due 12/01/2031 | | |
| <i>Long Term Rating</i> | AA+/Stable | New |
| Lynchburg | | |
| <i>Long Term Rating</i> | AA+/Stable | Upgraded |
| Lynchburg GO | | |
| <i>Unenhanced Rating</i> | AA+(SPUR)/Stable | Upgraded |
| Many issues are enhanced by bond insurance. | | |

Rationale

Standard & Poor's Ratings Services raised its long-term rating and underlying rating (SPUR) on Lynchburg, Va.'s general obligation (GO) debt one notch to 'AA+' from 'AA' based on the city's ongoing economic development and redevelopment, which continues to diversify the economy and expand the property tax base.

We have also factored the city's historically solid financial position with very strong reserves, which has remained constant through various economic cycles, into the upgrade. The outlook is stable.

Standard & Poor's also assigned its 'AA+' long-term rating, and stable outlook, to the city's series 2010 GO public improvement refunding bonds.

In our opinion, the rating reflects the city's:

- Mature, yet still-growing, economy that anchors a four-county central Virginia economy;
- Consistent property tax base growth, resulting from regular expansions of the commercial, industrial, and retail sectors;
- Strong financial position with very strong reserves;
- Strong management policies; and
- Moderate debt burden on a per capita basis and a manageable capital improvement plan (CIP) with a sizable pay-as-you-go component.

The city's adequate wealth and income indicators offset these strengths.

The city's full faith and credit GO pledge secures the bonds. Officials plan to use bond proceeds from this issue to refund portions of the city's series 2001, 2003A, and 2004 GO bonds outstanding for a net present value savings of more than 5%.

Lynchburg, with a population estimate of 69,146, is in central Virginia, approximately 57 miles east of Roanoke, Va. ('AA' GO debt rating). The 50-square-mile city has long served as the employment and retail base of the four-county region in which it is situated. This broader Lynchburg metropolitan statistical area economy, with a population of about 243,700, continues to experience steady growth and diversification. Health care services is the leading employment sector (18% of total), followed by the manufacturing and trade, government, and accommodation and food service sectors with each accounting for at least 10% of total employment. Within the

city, health services, higher education, engineering, and retail services have driven employment growth and development. City unemployment has historically been above the commonwealth's rate yet slightly below the nation's rate. Despite a spike to 9.6% in July 2010, unemployment remains in-line with historical trends.

Centra Health Systems is the city's leading employer with more than 5,300 employees. Centra owns both Virginia Baptist (317 beds) and Lynchburg General (270), which have both received national recognition; the latter recently opened its regional outpatient cancer treatment center. The city also has a sizable and growing engineering employment sector. Areva NP North America -- the world's leading nuclear power plant designer, manufacturer, and service provider -- has 2,046 employees in the Lynchburg area. Although Areva has put its \$25 million planned expansion on hold, it is continuing with its plans to add 500 engineer jobs to the city by 2011. Furthermore, Babcock & Wilcox Co. Technologies, a nuclear components manufacturer, has two of its four main subsidiaries headquartered in the city, employing 2,200 in the area. Liberty University, the city's second leading employer with 3,171 employees, continues to grow and carry on with its ongoing renovations. In addition to Liberty University, there are five other higher education institutions in the city with a total student enrollment of 19,292, or 25.5% of the city's population.

The city's property tax base continues to experience steady growth. Total assessed value (AV) reached \$5.69 billion in fiscal 2010, a 4.12% increase from the previous year and 6.70% from fiscal 2008, at which time the city had its last property revaluation that resulted in an 18.40% AV increase from fiscal 2007. We consider the city's market value per capita to be a strong \$79,136. Leading taxpayers account for a diverse 7.7% of total AV. Despite recent residential and commercial growth in the city, wealth and income indicators remain adequate with median household effective buying income at 64% of the commonwealth average and 73% of the national average. Given the sizable student population, however, these numbers might be somewhat understated.

The city's financial position remains strong with very strong reserves. The city closed fiscal 2009 with a \$2.6 million operating surplus, net of transfers. Transfers in included revenues from the sale of a landfill while transfers out included sizable amounts into the capital projects fund. The city closed fiscal 2009 with a total general fund balance of \$37.18 million, or a very strong 24.7% of expenditures, 24.2% of which was unreserved. The undesignated general fund balance totaled \$24.48 million, or a still-very-strong 15.76% of revenues and 16.30% of expenditures, above the city's formal policy of maintaining 10.00% of revenues. Since fiscal 2001, the undesignated general fund balance has averaged a very strong 15.5% of revenues.

Due to certain revenues exceeding budgeted levels and ongoing expenditure controls, management is projecting fiscal 2010 to close with another healthy operating surplus, increasing the undesignated general fund balance to \$30.15 million, or 19.2% of revenues. The city, however, plans to transfer roughly \$8 million into the capital project fund to finance ongoing city improvements.

The adopted fiscal 2011 budget totals \$162.3 million and includes the use of \$8.5 million of fund balance; it, however, does not include a property tax rate increase. Although the budget has the undesignated fund balance at 10.1% of revenues, the city has established a debt service reserve fund of \$1.072 million. Officials, again, plan to transfer anywhere from \$8 million-\$9 million of reserves into the capital fund in fiscal 2011 for capital projects.

Standard & Poor's considers Lynchburg's management practices "strong" under its Financial Management Assessment (FMA) methodology, indicating practices are strong, well embedded, and likely sustainable.

The city's overall debt burden remains a moderate \$2,022 per capita, or a low 2.6% of market value. In fiscal 2009,

debt service carrying charges were a moderate 8% of general fund expenditures. Amortization of debt, however, is faster than average with officials planning to retire 63% of principal over 10 years and 95% over 20 years.

The city's CIP for fiscals 2011-2015 consists of roughly \$64.360 million of general city and school projects and roughly \$94.700 million of utilities (water and sewer and airport) projects for a total of about \$159.075 million. Funding for these projects includes internal financing (41% of the CIP), followed by Virginia Clean Water Revolving Fund loans (31%) and additional debt issuance (26%). The city continues to meet its special order requirement of combined sewer overflow program and ongoing projects that require the complete separation of storm water and sewer systems. The estimated work for the remainder of the combined sewer overflow separation in 2011 dollars is \$326 million over the next 25-30 years. Sewer projects in the current CIP total \$62.95 million. Furthermore, the city also received a federal stimulus loan of \$19.1 million to date to pay for combined sewer overflow projects previously budgeted for in the CIP. The city plans to issue additional debt within the next year for ongoing capital needs.

Outlook

The stable outlook reflects the growing and diversifying local economy that anchors the larger metropolitan area economy and employment base and the city's historically sound financial position with very strong reserves, which officials use to finance a portion of city capital projects consistently, keeping debt at low levels. In addition, the stable outlook reflects Standard & Poor's expectation that reserves will likely continue to remain at current levels.

Financial Management Assessment: 'Strong'

Standard & Poor's considers Lynchburg's management practices "strong" under its FMA methodology, indicating practices are strong, well embedded, and likely sustainable.

Lynchburg's fiscal and debt practices are based on a series of comprehensive policies adopted by the city in 1999 and strengthened recently as part of a regular review process. The city uses five-year historical trend analysis, commonwealth and federal estimates and data projections, and economic forecasts to develop its annual revenue and expenditure assumptions. Management monitors the budget through formal processes, and it tracks revenues and expenditures daily and makes monthly reports on the results to the city council based on adopted policy. In mid-March, the city's financial management team makes formal recommendations for budget adjustments to the city council based on budgeted numbers compared to actual results.

A six-year CIP serves as the basis for annual capital appropriations and debt financing requirements; management updates the CIP annually with identified funding sources. The city has comprehensive formal debt management policies that it adheres to in planning and addressing its capital needs, including:

- A policy that limits the city's debt service-to-budget to 10.0% of budgeted general expenditures,
- A limit on total debt to 4.5% of full market value,
- A principal amortization target of 60% over 10 years, and
- The city's pay-as-you-go appropriations of at least 10% of the annual CIP.

The city has its own investment policy that it reviews annually with regular quarterly reporting to the city manager and city council. The city recently adjusted and strengthened its long-adopted reserve policy, which calls for the

maintenance of undesignated general fund balance at 10% of operating revenues.

Related Criteria And Research

USPF Criteria: GO Debt, Oct. 12, 2006

| Lynchburg, Virginia | | | |
|--|------------------|------------------|------------------|
| Economic statistics | | | |
| Population | 71,881 | | |
| Median household EBI, % of U.S. | 73.0 | | |
| Per capita EBI, % of U.S. | 75.0 | | |
| Total market value per capita (\$) | 79,136 | | |
| Net direct debt (\$000s) | 145,315 | | |
| Net direct debt per capita (\$) | | | |
| Net direct debt, % of market value | 2.6 | | |
| Assessed value (\$000s) | 5,688,408 | | |
| Market value (\$000s) | 5,688,408 | | |
| EBI -- Effective buying income. Population and income -- Source: Claritas. | | | |
| Financial statistics (fiscal year-end) | 6/30/2009 | 6/30/2008 | 6/30/2007 |
| General fund balance (\$000s) | 37,180 | 34,565 | 32,777 |
| General fund balance, % of general fund expenditures | 24.7 | 24.1 | 24.2 |
| Unreserved fund balance (\$000s) | 36,459 | 32,158 | 31,541 |
| Unreserved fund balance, % of general fund expenditures | 24.2 | 22.4 | 23.3 |
| Total general fund expenditures (\$000s) | 150,534 | 143,550 | 135,314 |
| Total general fund expenditures -- one-year change (%) | 4.9 | 6.1 | (3.9) |
| Total general fund revenues (\$000s) | 155,371 | 156,442 | 146,110 |
| Total general fund revenues -- one-year change (%) | (0.7) | 7.1 | 0.2 |

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