STANDARD & POOR'S

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January 6, 2012

Summary:
Illinois; General Obligation

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Table Of Contents

Summary:

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Credit Profile		
US$525.0 mil GO bnds ser A of January 2012 due 01/01/2037		
Long Term Rating	A+/Negative	New
US$275.0 mil GO bnds taxable ser B of January 2012 due 01/01/2037		
Long Term Rating	A+/Negative	New

Rationale

Standard & Poor's Ratings Services assigned its 'A+' rating, and negative outlook, to the state of Illinois' $525 million series A general obligation (GO) bonds of January 2012 and $275 million series B taxable GO bonds of January 2012. At the same, Standard & Poor's affirmed its 'A+' rating, with a negative outlook, on the parity debt outstanding.

We understand that proceeds from the series 2012 bond issues will fund the state's capital program.

Key factors supporting the 'A+' ratings include what we view as Illinois':

- Deep and diverse economy, which is anchored by the Chicago metropolitan statistical area;
- Above-average income levels;
- Almost unlimited ability to raise taxes and other revenues due to its sovereign powers and the absence of constitutional revenue-raising limits;
- 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; and
- Recent efforts to improve structural budget balance and enhance financial and budget management capabilities.

Offsetting these generally positive credit factors are what we consider:

- Significant budget-based deficits for fiscal years 2009 through 2011 and the fiscal 2012 forecast, despite what we view as significant revenue enhancement measures implemented in 2011;
- Historically large generally accepted accounting principles (GAAP) general fund deficit, which equaled $9.2 billion (about 24.6% of expenditures and transfers out) in fiscal 2010. 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 some other states;
- Large unfunded actuarial accrued liability (UAAL) for its five pensions that stood at $82.9 billion (43.4% funded) at fiscal year-end 2011, coupled with a large $28.6 billion UAAL for its other postemployment benefits; and
- Moderately high and growing debt burden due to debt authorizations for current pension contributions in fiscal years 2010 and 2011 and the approved long-term capital program.

We consider Illinois' economy broad and diverse, and the state's income levels are well above average. In our view, economic recovery continues at a modest pace. The state's unemployment rate through November 2011 was 10.1% and has moved above the U.S. average after steadily declining in 2010 and the early part of 2011. Per capita personal income in 2010 was $42,057, or 106% of the U.S. average, ranking Illinois 16th nationally and first among the Great Lakes states.

Although Illinois has experienced revenue recovery following the recession and several revenue enhancements have improved structural budget performance, in our view revenues and expenditures are not fully aligned at present and the accumulated budget deficit continues to grow. The state indicates that total revenues for fiscal 2012 are performing in line with the forecast. Despite the positive structural adjustments for fiscal 2012, Illinois now projects a deficit of $508 million (1.5% of total expenditures) for fiscal 2012. In addition, the state estimates that it under appropriated spending for medical assistance by $1.1 billion in fiscal 2012, which will likely increase its total accumulated deficit on both a budgetary and GAAP basis at year-end. The accumulated payables and other general fund liabilities that we believe represent the total accumulated deficit at fiscal year-end 2012 are projected to be sizable at $5.7 billion and $2.7 billion, respectively. The state's lack of action on the current and previous year deficits and the inability to align revenues and expenditures despite significant revenue enhancement is a credit weakness in our opinion. This is especially true when viewed relative to the growing debt and liability burden.

Based on the analytic factors we evaluate for states, on a scale of '1.0' (strongest) to '4.0' (weakest), we have assigned a composite score of '2.4' to Illinois.

Outlook

The negative outlook reflects what we view as the state's large accumulated deficit and improved but still elusive structural budget balance despite significant revenue enhancement for the current financial plan period. The accumulated deficit continues to pressure the state's overall financial condition and liquidity in our view. If Illinois does not make meaningful changes to further align revenue and spending and address its accumulated deficit (accounts payable and general fund liabilities) for fiscal years 2012 and 2013, we could lower the rating this year. The outlook also reflects ongoing weakness in the state's pension funds and the possibility that it might issue a significant amount of additional debt as part of its effort to address the large accumulated budget deficit. A downgrade could also be triggered if pension funding levels continue to deteriorate or debt levels increase significantly, which would pressure the state's near-term financial performance. If pension funding levels stabilize and revenues and expenditures are successfully aligned in the next year, thereby stabilizing Illinois' finances, we could revise the outlook to stable. We do not believe there is upside potential to the rating in the next year given the range of budget and liability challenges the state faces.

Related Criteria And Research

USPF Criteria: State Ratings Methodology, Jan. 3, 2011

Ratings Detail (As Of January 6, 2012)		
Illinois GO		
Long Term Rating	A+/Negative	Affirmed
Illinois GO VRDBs		
Long Term Rating	A+/A-2/Negative	Affirmed
Illinois GO (wrap of insured) (FGIC & AGM) (SEC MKT)		
Unenhanced Rating	A+(SPUR)/Negative	Affirmed

Ratings Detail (As Of January 6, 2012) **(cont.)**		
Illinois GO (wrap of insured) (MBIA) (AGM) (SEC MKT)		
Unenhanced Rating	A+(SPUR)/Negative	Affirmed
Illinois GO (ASSURED GTY)		
Unenhanced Rating	A+(SPUR)/Negative	Affirmed
Illinois GO (FGIC)		
Unenhanced Rating	A+(SPUR)/Negative	Affirmed
Illinois GO		
Unenhanced Rating	A+(SPUR)/Negative	Affirmed
Many issues are enhanced by bond insurance.		

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