MOODY'S INVESTORS SERVICE

Rating Update: MOODY'S DOWNGRADES TO A2 FROM A1 THE CITY OF YPSILANTI'S (MI) RATING ON $16 MILLION OUTSTANDING RATED GO LIMITED TAX DEBT; ASSIGNS NEGATIVE OUTLOOK

Global Credit Research - 22 Sep 2011

AFFIRMS A1 RATING ON $9 MILLION GENERAL OBLIGATION UNLIMITED TAX DEBT OUTSTANDING

Municipality
MI

Opinion

NEW YORK, Sep 22, 2011 -- Moody's Investors Service has downgraded to A2 from A1 the rating on the City of Ypsilanti's (MI) $16 million of outstanding rated general obligation limited tax debt. At this time, Moody's has affirmed the A1 rating on the City's $9 million of outstanding rated general obligation unlimited tax debt. Concurrently, Moody's has assigned a negative outlook.

SUMMARY RATINGS RATIONALE

The downgrade to A2 on the city's outstanding general obligation limited tax debt rating reflects the city's satisfactory financial position with declining liquidity, declining tax base, and debt burden while currently manageable, is expected to require General Fund support beginning in 2013. The assignment of a negative outlook reflects the ongoing financial challenges from stressed revenue streams including declining property tax and state shared revenues; declining liquidity to meet debt service obligations on its limited tax debt mostly related to the Series 2006 bonds; and significant chargebacks and tax appeals that may further pressure General Fund operations. Previously, the city's lack of rating distinction between general obligation unlimited and limited tax debt reflected the city's sound liquidity. The current rating distinction reflects narrowing liquidity and lack of dedicated levy that may prove challenging to meet debt service obligations for the city's outstanding limited tax debt.

STRENGTHS:

-Currently healthy General Fund reserve levels

-Institutional stability; Eastern Michigan University

CHALLENGES:

-Declining tax base

-Budgetary pressures from debt service payments related to limited tax debt

-Revenue and expenditure pressure due to declines in state shared and property tax revenues and significant chargebacks and tax appeals pending

DETAILED CREDIT DISCUSSION

MODEST, DECLINING TAX BASE LOCATED ADJACENT TO ANN ARBOR; INSTITUTIONAL STABILITY OF EASTERN MI UNIVERSITY

The city of Ypsilanti is favorably located in Washtenaw County (GO rated Aa1) adjacent to the city of Ann Arbor (GO rated Aa1). The city has seen substantial tax base declines, averaging a decline of 6.9% annually for the last five years due to current economic conditions. The city is expects a 7% decline for fiscal 2012 and has budgeted for 3% declines annually until fiscal 2016. The city is also expecting the loss of a portion of taxable value from their third largest taxpayer, Angstrom Capital, an automotive components company. Due to downsizing coupled with unusable property, Angstrom's assessed valuation is expected to drop to $820,000 from $5.1 million.

The city's taxbase is modestly sized at $707 million; however, this figure does not reflect the sizeable presence of

Eastern Michigan University (rated A1/Stable) with fall 2011 enrollment of 23,000 students between undergraduate and graduate programs. Resident per capita ($16,692) and median family ($40,793) incomes fall well below national figures (77.3% and 81.5% of the U.S. medians, respectively).

SATISFACTORY FINANCIAL POSITION; LIQUIDITY EXPECTED TO NARROW DUE POTENTIAL PRESSURES ASSOCIATED WITH CHARGEBACKS, TAX APPEALS AND FUTURE DEBT SERVICE COSTS FOR LIMITED TAX DEBT.

Moody's expects the city's liquidity to narrow although reserve levels are currently healthy. Total general fund balance increased to $9.4 million or an ample 66.6% of general fund revenues in fiscal 2010 from $4.2 million in fiscal 2006. Preliminary fiscal 2011 numbers show a modest surplus of $349,000 achieved through conservative budgeting and continued expenditure cuts and workforce reductions. Fiscal 2012 will prove challenging as further declines in property tax revenues and state shared revenues will add to budgetary pressures combined with debt service expenditures related to the Series 2006 bonds. In addition to these stresses, the City's liquidity may be affected due to current and pending tax appeals and chargebacks. The City has a total of $122,400 in chargebacks due to Washtenaw County (G.O. rated Aa1) for fiscal 2011 resulting from uncollected special assessments on foreclosed properties. The city is liable to re-pay a total of $122,400 of which, the general fund is responsible for approximately $94,000. In addition to the chargebacks, the City had $11,423 in tax appeals reimbursements in fiscal 2011 and is budgeting for approximately $22,000 in tax appeals reimbursements in fiscal 2012. While the city budgets approximately $70,000 to $80,000 in the General Fund for these contingencies, the total liability exceeds this amount.The city expects to continue to repay chargebacks and tax appeals in fiscal 2012 and beyond.

Management has built sound General Fund reserves in order to prepare for future debt service payments on the city's outstanding limited tax debt, which is mostly comprised of the Series 2006 bonds. The bonds were originally issued to acquire, demolish and remediate the Water Street Project, a 38-acre redevelopment project that has yet to see new development. The city's general fund balance includes a $4.6 million designation for future debt service on the bonds through fiscal 2014, adding a measure of security for bondholders. Annual debt service on the city's limited tax debt, which is paid from the General Fund, is approximately $1.3 million. Including the reservation for debt service payments, the General Fund liquidity is much more narrow, with an undesignated balance of $2.4 million, or 17.2% or revenues at the end of fiscal 2010. Management is contemplating going to voters in February 2012 for an additional mill levy for operations that may be used to pay off the Series 2006 bonds. One mill generates approximately $284,000 in additional revenues annually and the city is contemplating an extra 4.6 mill levy. Assuming fiscal operations remain status quo, the city will be pressured with an annual $1 million budgetary shortfall starting in fiscal 2014. Should the referendum fail, management expects to close the gap through additional expenditure reductions and use of reserves.

MANAGEABLE DEBT BURDEN; NO IMMEDIATE BORROWING PLANS

The city's debt profile is expected to remain manageable, given the lack of additional borrowing plans. After adjusting for the city's current revenue-supported debt, direct debt is an elevated 3.7% of full value. All of the city's debt is fixed rate mode and officials have no immediate plans to issue additional debt over the near term.

KEY STATISTICS

2000 Population: 22,362 (10% decline from 1990)

2010 Population: 19,435 (13.1% decline from 2000)

2011 Full Value: $707 million

Full value per capita: $36,352

City of Ypsilanti unemployment (June 2011): 7.7%

2000 Per capita income (as % of MI and US): $16,692 (75.3% and 77.3%)

2000 Median family income (as % of MI and US) $40,793 (76.3% and 81.5%)

Direct debt burden: 3.7%

Payout of principal (10 years): 57.1%

FY 2010 General Fund balance: $9.5 million (66.6% of General Fund revenues)

FY 2010 Unreserved, Undesignated General Fund balance: $2.4 million (17.2% of General Fund revenues)

General Obligation Unlimited Tax debt outstanding: $9 million

General Obligation Limited Tax debt outstanding: $16 million

The principal methodology used in this rating was General Obligation Bonds Issued by U.S. Local Governments published in October 2009. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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For ratings issued on a program, series or category/class of debt, this announcement provides relevant regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides relevant regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides relevant regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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Outlook

Outlook

The assignment of a negative outlook reflects the ongoing financial challenges from stressed revenue streams including declining property tax and state shared revenues; declining liquidity to meet debt service obligations on its limited tax debt mostly related to the Series 2006 bonds; and significant chargebacks and tax appeals that may further pressure General Fund operations

WHAT COULD CHANGE THE RATING UP (REMOVE NEGATIVE OUTLOOK):

- Material increases in the district's tax base

- Additional revenues leading to structural balance

WHAT COULD CHANGE THE RATING DOWN:

- Declines in General Fund reserves and liquidity

- Further material declines in the district's tax base

- Significant increases to the district's debt burden and inability to meet debt service payments on limited tax debt

Moody's adopts all necessary measures so that the information it uses in assigning a rating is of sufficient quality and from sources Moody's considers to be reliable including, when appropriate, independent third-party sources. However, Moody's is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

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