Section 2

Loudon County
Current
Bond Rating Report

MOODY'S ASSIGNS A Aa2 RATING TO LOUDON COUNTY'S (TN) $10.0 MILLION RURAL SCHOOL BONDS, SERIES 2011

AFFIRMATION OF THE Aa2 RATING AFFECTS APPROXIMATLEY $21.82 MILLION IN PREVIOUSLY ISSUED PARITY DEBT

Moody's Investors Service has assigned a Aa2 rating to Loudon County's (TN) $10.0 million Rural School Bonds, Series 2011. Concurrently, Moody's has affirmed the Aa2 rating on the county's outstanding $21.82 million in outstanding parity debt. Proceeds from the current issue will fund various projects as part of a $43 million school building program.

RATINGS RATIONAL

The bonds are secured by an unlimited ad valorem tax pledge of the county. The Aa2 rating reflects conservative budgetary practices and solid reserve levels. The rating further takes into consideration a diverse and relatively stable economy and below average debt burden.

STRENGTHS –

-Healthy General Fund reserves

-Below average debt burden

-Stable tax base experiencing modest growth

CHALLENGES –

-Modest tax payer concentration

-Average wealth levels

DETAILED CREDIT DISCUSSION

FINANCIAL POSITION EXPECTED TO REMAIN STABLE DESPITE PROJECTED DECREASE IN FISCAL 2011 RESERVES

Moody's believes that the county's financial position will remain stable despite projected declines in General Fund balance in fiscal 2011. Over the last six years, the county has produced five years of operating surpluses, increasing General Fund reserves to a solid 54.2% of annual revenues ($8.39 million) through fiscal 2009. In fiscal 2010, the county finished with a modest operating deficit and reduction in reserves of $127,000 or 58.5% of annual revenues – management attributes the deficit primarily to underperformance of General Fund revenues. Despite modestly reduced reserves, the county's cash position continued to show improvement, totaling $6.94 million (49.1% of annual revenues).

The fiscal 2011 budget included $1.84 million in appropriated fund balance, $6.87 million in property tax revenues and $8.59 million in local option sales tax revenues (split 50/50 with local cities and schools). County officials estimate that fiscal 2011 ended with an operating deficit and decrease in General Fund reserves of approximately $1.17 million. Total General Fund balance is projected to be at $7.09 million (51.88% of fiscal 2011 revenues – unaudited). Major revenue sources came in close to budget with property taxes estimated to have come in slightly under budget at $6.81 million and local option sales taxes at $8.79 million ($193,000 above budget). Management stated that replenishment of the original $1.84 million in appropriated fund balance would have been greater had they not lost revenues from a state grant or had several federal grant reimbursements delayed.

The county's current fiscal 2012 budget includes $1.06 million in appropriated fund balance, $7.07 million in property tax revenues (2.91% increase budget to budget) and $8.64 million in local option sales tax revenues (0.58% increase budget to budget). While officials believe that revenues will be in line with budget, they don't expect the county will replenish the full fiscal 2012 appropriated fund balance, they project total General Fund reserves will end close to $6.04 million or 44.74% of annual revenues. Moody's will continue to monitor the county's ability going forward to produce balanced budgets and to maintain General Fund reserves at levels seen at the Aa2 rating category. Continued use of fund balance could place negative pressure on the county's rating going forward.

DIVERSE MANUFACTURING SECTOR ENHANCED BY GROWING REGIONAL ECONOMY

Loudon County, located approximately 30 miles southwest of the City of Knoxville (G.O. rated Aa1 stable) along Interstate 75, has a continued large manufacturing presence, but has seen large growth in the service economy as the area develops into a commuter base. The county has eight business and industrial parks, home to large industrial companies including Arvin Meritor (Sr. Unsec. rated B3), Kimberly-Clark (Sr. Unsec. A2) and A.E Staley, a corn products subsidiary of Tate & Lyle (Euro Sr. Unsec. rated Baa3). While manufacturing sector employment shrunk slightly through the 1990's, professional and related service industry employment more than doubled to encompass 30% of the employment base in 2000. Unemployment within the county has consistently remained below state and national averages and as of August 2011, was 8.2% (state 9.6% and nation 9.1%). Tax payer concentration is modest at 11.1%, with AE Staley Manufacturing Company as the largest at 5.0% of the tax base. The county's tax base has continued to experience growth, even through the economic recession, with assessed value growing an average of 9.3% over the last five years. Market values have also continued to grow, averaging 9.5% over the same period. The residential housing market remains relatively stable in Loudon County, with building permits in 2010 of 334 and 230 year-to-date in 2011. Days on the market has continued to increase modestly to 150 in 2011 (140 in 2010). Management believes that the county is still working through its oversupply of developed lots which has kept new residential development at a minimum over the last two years. Wealth levels within the county are average with per capita income of $21,061 (108.6% of state) and median family income of $46,517 (106.9% of state). Full value per capita is above average at $131,351.

DEBT BURDEN MANAGEABLE

Moody's believes that the county's debt position will remain manageable over the near-term given a low debt burden and average payout. The county's direct debt burden is below-average at 0.5% and payout is 61.5% of principal repaid within ten years. The county's debt profile is made up of approximately 46% variable rate debt and 54% fixed rated debt. The variable rate debt consists of loans through the TN-LOANS and TMBF programs, both of which Moody's believes has reasonable term out provisions. In addition, the county has one derivative swap agreement under its loan agreement with the Public Building Authority of Sevier County and related to its outstanding Local Government Improvement Bonds, Series IV-H-1. The Series IV-H-1 were refunded by the Series E-3-C bonds however the swap agreement remained in place. The authority pays the counterparty a fixed rate payment of 3.13% and receives a variable rate payment based upon 59% of the three-month LIBOR rate plus 35 basis points. The notional amount of the swap is $12.5 million. The county expects to issue further new money debt over the next several years as part of a $43 million school building project. The current Series 2011 issue is the first part of the larger building program. Moody's believes the county can afford the additional $33 million in debt, given the county's currently low debt burden and the expected ongoing tax base growth.

WHAT COULD MAKE THE RATING GO UP

-Increasing or maintaining General Fund reserves

-Decreases in variable rate exposure

-Sizeable tax base expansion

WHAT COULD MAKE THE RATING GO DOWN

-Continued use of fund balance

-Sizeable increases in debt burden

-Deterioration of the county's tax base

KEY STATISTICS:

Population (2010): 48,556

2011 full valuation: $6.74 billion

2011 full valuation per capita: $131,351

Overall debt burden: 0.5%

Payout of general obligation principal (10 years): 61.5%

FY09 General Fund balance: $8.39 million (54.2% of General Fund revenues)

FY10 General Fund balance: $8.26 million (58.5% of General Fund revenues)

1999 PCI (% of State): 108.6%

1999 MFI (% of State): 106.9%

Unemployment (August 2011): 8.2%

Post sale parity debt outstanding: $31.82 million