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Summary:
Klamath Falls, Oregon; General Obligation

Primary Credit Analyst:
Santos Souffront, New York (1) 212-438-2197; santos_souffront@standardandpoors.com

Secondary Contact:
Chris Morgan, San Francisco (1) 415-371-5032; chris_morgan@standardandpoors.com

Research Contributor:
Neha Vazarkar, CRISIL Global Analytical Center, an S&P affiliate, Mumbai

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Summary:

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Credit Profile		
Klamath Falls GO bnds ser 2008 due 06/01/2038		
Long Term Rating	A+/Stable	Affirmed
Klamath Falls GO (ASSURED GTY)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services affirmed its 'A+' long-term and underlying (SPUR) ratings on Klamath Falls, Ore.'s general obligation (GO) bonds. The outlook is stable.

The rating reflects our view of the city's:

- Consistent maintenance of a very strong financial position;
- Good financial policies and practices, including a minimum fund policy of 20% of annual operating expenditures; and
- Low debt burden.

Constraining credit quality is our opinion of an economic base with an above-average unemployment rate and merely adequate incomes.

A full faith and credit pledge, including a covenant to levy property taxes without limitation as to rate or amount, secures the bonds.

The city serves a growing population of approximately 21,000 between Crater Lake National Park and the California border. Historically a timber processing center, the city and the surrounding region's economic base has diversified into government (including military), health care, manufacturing, and real estate. Migration of retirees from urban centers and annexations contributed to what we consider a very strong 19.3% average annual market value growth rate in the city between fiscal years 2005 and 2009. Given the recent cooling in home prices, the market value declined by 6% to $2.1 billion in fiscal 2011, or, in our view, a still extremely strong market value per capita of $100,225 in fiscal 2010. Economic indicators in the region are below average; the city's median household effective buying income is adequate, in our view, at 69% of the national level, whereas the unemployment rate in Klamath County, at 10.9%, was higher than that of the state's 9.6% as of Sept. 2011.

Owing to a conservative budgeting approach and strong minimum general fund balance policy, the city has maintained its general fund balance policy of keeping their unreserved fund balance at a minimum of 28% of expenditures, higher than the policy mandated 20% of expenditures. After reporting two consecutive operating deficits in fiscals 2008 and 2009, the city's financial performance improved, with an operating surplus of $74,000 and an unreserved fund balance of $3.3 million, or 31.1% of operating expenditures in fiscal 2010, which we consider very strong. Management estimates that the city ended fiscal 2011 with an ending fund balance of 35.1%

of expenditures, which we consider very strong. For fiscal 2012, management reports that it expects to operate within its budget, with lower-than-expected revenues being offset with less-than-budgeted salary expenses.

The city's management practices are considered "good" under Standard & Poor's Financial Management Assessment (FMA) methodology. An FMA of "good" indicates that practices exist in most areas, although not all may be formalized or regularly monitored by governance officials. Notable among these is the use of a three-year financial forecasting model to provide context for budgeting decisions.

We view the city's combined direct and overlapping debt to be low relative to market value, at 0.5%, and very low relative to its population, at $610 per capita. In fiscal 2010, carrying charges were 10% of government-wide noncapital expenditures, which we consider moderate. We understand that the city does not plan to issue additional GO debt for the foreseeable future.

The city participates in the state-managed Public Employees Retirement System. The city made its annually required contributions of $603,628 for fiscal 2010. These contributions combined represented 1.3% of government-wide noncapital expenditures in fiscal 2010. The city reported its actuarially accrued other postemployment benefits liability at $503,376 as of July 1, 2006. Management reports that the city manages this expense on a pay-as-you-go basis and reported paying $37,693 for fiscal 2010.

Outlook

The stable outlook reflects our view of the city's proactive changes to its operations and its track record of maintaining a very strong available general fund position. In the context of recent softness in the housing market, we expect that the city will adjust its budgets as necessary should a slowdown in assessed values put pressure on operating revenues. We do not expect to lower our rating during our two-year outlook horizon unless a significant operating imbalance develops or the city's available balances fall below very strong levels. We do not expect to raise our rating during our two-year outlook horizon due to our view of the city's economic profile.

Related Criteria And Research

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Key General Obligation Ratio Credit Ranges – Analysis Vs. Reality, April 2, 2008

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