MENDOCINO COUNTY EXECUTIVE OFFICE

NEWS RELEASE

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Ukiah, California… ***2/25/2013***

Fitch Revises Outlook on Mendocino County Finances to "Positive"

Fitch Ratings, one of the three largest credit ratings agencies in the United States, concluded its annual financial surveillance of Mendocino County on February 21, 2013. Fitch is charged with the independent analysis and critique of County finances on behalf of bondholders associated with the County's 2002 issue of $90+ million in Pension Obligation Bond (POB) debt. This annual review helps bondholders, or any other interested stakeholder, to determine the financial health of the County and its trajectory.

Fitch affirmed Mendocino County's 2002 POB issue at "BBB+" the same rating as last year. However, Fitch revised its outlook on Mendocino County finances from stable to positive.

Fitch cited several positive developments that it has been monitoring:

- Management reforms including updated treasury practices
- Updated reserve policies
- Refocusing on capital improvement planning
- Sustained record of surplus operational balances

Fitch also cited several areas of concern:

- Long-term economic decline that preceded the recent downturn
- Poor employment levels
- Stagnated population growth
- Wealth and income levels well below state and national averages
- Substantial long-term debt obligations
- Struggling local housing market

"Overall we are pleased that Fitch is recognizing the financial gains the county has made over the past couple of years." Stated Carmel J. Angelo, Chief Executive Officer of Mendocino County. "We have turned a corner in terms of watching our credit rating drop year after year, and now we're beginning to see signs that a potential upgrade is in our future."

"Fitch's revision to the County's outlook from stable to positive should not negate the fact that Fitch has real concerns about the overall economic picture in Mendocino County." Added Kyle Knopp, Assistant CEO for Mendocino County. "A poor economic outlook directly translates to the long-term revenue outlook of the County."

Current projections show local discretionary revenue growth of less than 1% per year on average over the next five years. The poor revenue growth picture is complicated by cost increases associated with retirement, healthcare and other County obligations.

Released by: ______________________
Carmel J. Angelo
Chief Executive Officer

FitchRatings

FITCH AFFIRMS MENDOCINO COUNTY, CA'S POBS AT 'BBB+', OUTLOOK REVISED TO POSITIVE

Fitch Ratings-San Francisco-21 February 2013: Fitch Ratings takes the following actions on Mendocino County (the county), California:

--$79.6 million pension obligation refunding bonds (POBs), series 2002 affirmed at 'BBB+'.
--Implied general obligation (GO) rating affirmed at 'A-'.

The Rating Outlook is revised to Positive from Stable.

SECURITY

The POBs are an absolute and unconditional obligation of the county imposed by law, the payment of which is not limited to any special source of funds.

KEY RATING DRIVERS

CONTINUED FINANCIAL IMPROVEMENT: The Positive Outlook reflects improvements in the county's financial position following substantial expenditure reductions and management reforms over the last several years.

LONG-TERM ECONOMIC DECLINE: The county continues to face challenges from a long-term economic contraction that preceded the recent downturn. Employment levels have fallen each year over the past decade while population has stagnated. In addition, wealth and income levels remain well below state and national averages.

MANAGEMENT REFORMS: The county has made notable progress in addressing weaknesses cited in past reviews. Management has raised fund balance targets and established policies to help meet these new goals, updated treasury practices, and begun preparations for its first capital improvement plan in seven years.

MODERATE DEBT; ELEVATED PENSIONS: Overall debt levels are moderate but county long-term obligations are substantial due to pension funding requirements.

RATING SENSITIVITIES

IMPROVED FINANCIAL POSITION: A sustained record of surplus operations and enhanced financial flexibility will likely result in an upgrade in the near term.

CREDIT PROFILE

Mendocino County is located in northern California, along the Pacific coast, approximately 115 miles north of San Francisco. The county's estimated population of 88,000 is little changed from the 1990s and is dispersed across a land area larger than several states.

FINANCIAL IMPROVEMENT FOLLOWS CUTS

The county ended fiscal 2012 with strong operating results and appears well-positioned for fiscal 2013. Net operating surpluses after transfers for 2012 were equal to 5.3% of general fund spending, raising unrestricted fund balance to 9.4% of spending ($12.4 million). Year-end cash balances also rose substantially, from $11.5 million in 2011 to $21 million in 2012.

The county's strong performance in 2012 follows substantial expenditure reductions over the past several years, primarily through workforce and payroll reductions. Workforce reductions have eliminated approximately one-fourth of the county's full-time employees over the past five years, while remaining employees have seen permanent wage cuts of 10% to 12.5%. In addition, the county has eliminated other post-employment benefits (OPEB) for current and retired employees.

Management projects further additions to fund balance in 2013, which Fitch considers reasonable given prior year expenditure reductions and revenue improvements through mid-year.

ECONOMIC WEAKNESS PERSISTS

The county continues to face a long-term economic contraction that dates from the late 1990s. Population growth has been very slow over this period and employment levels have dropped steadily. Tourism and wine production have provided some opportunities for growth, but overall employment levels fell by more than 10% over the past decade.

Unemployment rates for the county have generally tracked statewide averages and at 10.0% for 2012 unemployment was well above the national rate of 8.1%. Year-over-year employment growth was positive for the first half of 2012 followed by declines during the second half of the year, indicative of continuing employment challenges. Income and wealth indicators are weak at 70% to 85% of state and national averages.

Taxable assessed valuation (TAV) was relatively unaffected by the national housing boom and has been insulated from subsequent declines. TAV dropped by just 2.2% between 2010 and 2013 after many years of steady increases. The local housing market continues to struggle despite the county's favorable TAV performance. December 2012 home values reported by Zillow showed a 5.7% year-over-year decline as compared to a 9.3% increase for the state as a whole.

MANAGEMENT REFORMS

The county has made notable progress in addressing management weaknesses cited in prior rating reviews. The county adopted a revised fund balance policy in 2012 that increases reserve targets from 2% to 6.35% of general fund expenditures, or a minimum of $10 million. The new policy also provides a mechanism for incremental additions to reserves until targeted levels are reached. Fitch expects these actions to further boost unrestricted fund balances for the county over the next several years.

The county also made substantial revisions to its investment practices in 2012, diversifying investment categories, increasing credit quality, and reducing maturities in general. These actions appear likely to improve the county's ability to meet its chief investment goal of principal protection, and to better serve its cash management needs.

The county has been without a capital improvement plan since 2006, but has recently authorized the development of a new five-year plan as part of its budget process for fiscal 2014. The county faces a large backlog of capital projects due to spending deferrals during the recent downturn, but Fitch views renewed efforts to identify and prioritize capital needs as a positive development.

MODERATE DEBT; ELEVATED PENSION COSTS

Overall debt levels are moderate at $3,188 per capita or 2.8% of TAV. Amortization of direct debt is average with 55% of outstanding principle retired in 10 years. Management has no current plans for debt issuance apart from short-term cash flow borrowing. Amounts borrowed for such purposes declined by nearly one-third in fiscal 2013, providing further evidence of strengthened operations.

As of June 30, 2012, the Mendocino County Employees' Retirement Association had a funded ratio of 74%, or 67% under Fitch's alternate investment assumption of 7% returns. County contributions have increased by 63% over the past five years, largely due to lower than expected investment results.

Total pension costs, including POB debt service and pension contributions, have also accounted for a growing share of governmental spending in recent years. Pension costs represented 9.3% of non-capital governmental expenditures in fiscal 2010 but rose to 12.1% in 2012. As overall governmental spending has declined (due largely to workforce and payroll reductions), such fixed costs have increased as a share of remaining expenditures. Total carrying costs for pensions, other post-employment benefits (OPEBs) and debt service were a somewhat high 16% of non-capital governmental expenditures in fiscal 2012, as compared to 12.3% in fiscal 2011.

The county began a phased elimination of OPEBs in 2010 and will have no related liabilities after the end of the current calendar year.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, Zillow.com, and National Association of Realtors.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

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Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015
U.S. Local Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314