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Ratings

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Summary:

Lenox Community School District, Iowa; General Obligation

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Table Of Contents

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Credit Profile		
US$9.94 mil GO sch bnds ser 2020 due 06/01/2040		
Long Term Rating	A/Stable	New

Rating Action

S&P Global Ratings assigned its 'A' long-term rating to Lenox Community School District, Iowa's general obligation (GO) school bonds, series 2020. The outlook is stable.

Proceeds from the bonds will be used for various capital projects, including the construction of a gym facility, a technical education area, and new classrooms, as well as for roof and window replacement costs and facility upgrades. Securing the bonds is the district's unlimited ad valorem tax pledge.

Credit overview

The district is planning on issuing an additional approximately $3.5 million in sales tax revenue bonds concurrently with the issuance of this GO debt. As a result, its overall net debt burden will grow to a high level and its carrying charges will become moderate. Offsetting this somewhat is the district's robust financial profile with consecutive surplus operating results, sustaining very strong reserves. The COVID-19 pandemic and ensuing recession have, as of yet, had minimal impact on the district's finances. However, we acknowledge that the district could experience financial pressures such as lower property tax receipts and declines in state aid. Given its reserve and liquidity position, we believe the district is well situated to absorb short-term pressures from the pandemic and the recession.

Credit factors include:

- An increasing debt burden with significantly higher overall net debt levels and moderate carrying charges;
- Very strong reserves, supported by strong financial performance, allowing for some flexibility to absorb costs or revenue losses related to the recession; and
- An agriculturally oriented economy with limited residential development.

Environmental, social, and governance (ESG) factors

We analyzed the school district's ESG risks relative to its economy, management, financial measures, and debt and liability profile and determined that all are in line with our view of the sector standard.

Stable Outlook

Downside scenario

If the district's financial profile were to worsen due to imbalance, cuts in state aid, or recession, causing reserves to be no longer comparable with those of similarly rated peers, we could lower the rating.

Upside scenario

If the district's economic metrics were to improve, demonstrated by substantially higher incomes, coupled with a decrease in its debt burden, we could raise the rating.

Credit Opinion

Strong financial performance with consecutive surplus results, sustaining very strong reserves

The district has budgeted a surplus operating result in the general fund for fiscal 2020. Current estimates are in line with budgeted projections. Management has indicated that the COVID-19 pandemic has caused minimal impact on its finances with some savings from cancelled bus routes, supplies, and lower utility bills. While the state of Iowa has, as of this date, made no announcements on funding cuts, it is offering some grants, related to the CARES Act.

Fiscal 2019 estimates are in line with the district's track record of posting surplus operating results over the previous two fiscal years. Generally, the district has been conservative in budgeting and has been saving money by employing shared personnel. The district has also seen some early retirements, which has reduced its staff costs.

The district's enrollment trend has remained stable with a strong increasing trend in open enrollment into the district, which management attributed to its competitiveness. District officials expect this trend to remain stable. Enrollment is a key generator of state education funding in Iowa. Increases or decreases in enrollment can lead to corresponding increases or decreases in revenue. In fiscal 2018, state aid represented 54.5% of revenues and local taxes represented 28.5%.

We understand that the district is not planning on drawing down general fund reserves in the next few years and that COVID-19 and recession impacts have remained minimal. However, given the potential effects on state funding and property tax receipts, we believe some negative variances may materialize in the medium term. Given the district's reserves and liquidity, we believe it is well situated to minimize pressures in the short term.

Rural economy with a strong agricultural tax base and limited development

The local economy remains rural and agriculturally centered (45.4% of the tax base). The actual valuation has decreased over the last year, due to a statewide reevaluation of agricultural lands. This has not affected the district's taxable valuations, which continue to grow.

The district's main employers include the school district, Michael Foods, and Precision Idler. They have generally remained stable and operational through the pandemic, with maybe slight cutbacks to operating hours. The district is also experiencing some residential development due to high demand for housing.

Management indicates it expects additional revenues from a wind turbine project in the corner of the district, which is expected to pay taxes starting next year.

Standard management team producing positive operational results, despite minimal policies and procedures

The district looks at two to five years of historical data and uses available outside sources when budgeting forecasts. It provides the board with monthly budget-to-actual reports that focus mainly on general expenditure categories. The district discusses operational projections and maintains a list of capital projections for future years. While management does maintain a formally approved investment management policy, adhering to state guidelines, and shares investment holdings with the board monthly, it lacks a debt management or reserve policy.

Increasing debt burden with significantly higher overall net debt levels and moderate carrying charges

The district is planning on issuing privately placed sales tax revenue bonds concurrently with these GO bonds. Its debt burden will increase to overall net debt per capita at $6,613, which we believe to be high. In addition, its carrying charge will increase to moderate levels. We also note that 32% of the rated debt is planned to be retired in 10 years, which we consider to be slower than average. Should the district's finances be affected further by the pandemic and the recession, this could result in added pressure on the district's debt service payments. However, its reserves and liquidity somewhat mitigate this risk.

Pension and other postemployment benefit (OPEB) costs are low and likely to remain manageable. Other factors are as follows:

- We do not believe that pension and OPEB liabilities represent a medium-term credit pressure, as contributions are only a modest share of the budget and the district has the capacity to absorb higher costs without straining operations.
- The district participates in a multiple-employer, defined-benefit pension plan, which is relatively well funded. Contributions have fallen short of our static funding metric, and we believe other plan-specific assumptions introduce some long-term risk of funding volatility.
- Retirees may remain on the district's health care plan. The district makes no contributions to premiums for retirees to the plan, but this does result in an implicit subsidy.

Lenox Community School District participates in the following plans:

- Iowa Public Employees' Retirement System (IPERS): 85.5% funded (as of June 30, 2019), with a district proportionate share of the plan's net pension liability of $2.9 million (measured as of June 30, 2018), and
- An implicit rate subsidy arising from retirees staying on the district's plan while paying active premium rates: 0% funded with a liability of $221,000 (measured as of June 30, 2018).

The district's pension contributions of $292,000 are an affordable share of the budget. Total contributions to IPERS were 93.6% and 79.8% of our static and minimum funding progress metrics, respectively, in 2018. Some key risks consist of a 7.00% investment rate of return assumption, which indicates some exposure to cost acceleration due to market volatility, in addition to an amortization method that defers contributions through a lengthy, closed amortization period based on a level 3.25% payroll growth assumption. Overall, the plan is relatively well funded and we think pension and OPEB contributions are unlikely to pressure the district's medium-term operational health.

Lenox Community School District, Iowa--Financial And Operating Statistics					
	Characterization	**Most recent**	**Historical information**		
		(estimate)	**2020**	**2019 (estimate)**	**2018**
Economic indicators					
Population					2,424
Median household EBI % of U.S.					79
Per capita EBI % of U.S.					81
MV per capita ($)	Extremely strong	102,005	118,481	115,676	112,416
Top 10 taxpayers as % of assessed value	Very diverse	15.0			
Financial indicators					
Total adjusted available fund balance ($000)				1,733	1,418
Total adjusted available fund balance as % of operating expenditures	Very strong			31.1	26.2
Governmental funds cash as % of governmental fund expenditures				74.1	63.0
General fund operating result as % of general fund operating expenditures				6.29	6.87
Financial Management Assessment					
Enrollment		487	487	494	485
Debt and long-term liabilities					
Overall net debt as % of MV	Moderately high	6.4	5.6	1.0	1.2
Debt service as % of governmental funds expenditures	Moderate	10.6	4.2	4.3	6.5
Required pension contribution ($000)					292
OPEB contribution ($000)					
Required pension plus OPEB contribution as % of governmental fund expenditures					4.7

EBI--Effective buying income. MV--Market value. OPEB--Other postemployment benefits.

Related Research

- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.