

# RatingsDirect®

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## Summary:

# Northwestern Lehigh School District, Pennsylvania; School State Program

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## Summary:

# Northwestern Lehigh School District, Pennsylvania; School State Program

### Credit Profile

US\$9.71 mil GO bnds ser 2014 due 02/15/2033

<i>Long Term Rating</i>	AA/Stable	New
<i>School Issuer Credit Rating</i>	AA/Stable	New
Northwestern Lehigh Sch Dist GO bnds		
<i>Long Term Rating</i>	AA/Stable	Upgraded
<i>School Issuer Credit Rating</i>	AA/Stable	Upgraded

## Rationale

Standard & Poor's Ratings Services raised its long-term rating, school issuer credit rating (ICR), and underlying rating (SPUR) to 'AA' from 'AA-' on Northwestern Lehigh School District, Pa.'s general obligation (GO) bonds. At the same time, Standard & Poor's assigned its 'AA' rating and ICR to the district's series 2014 GO bonds. The outlook is stable.

The upgrade reflects the district's proactive management and conservative budgeting practices that have resulted in liquidity sufficient to cover principal at risk of acceleration.

The ICR reflects our view of the following:

- A largely residential property tax base with strong-to-very strong income indicators and a very strong market value per capita;
- Access to the broader employment base of Allentown-Bethlehem-Easton;
- Very strong total available general fund balance at fiscal 2012 year-end that is bolstered by a sizable committed balance; and
- Moderate debt burden and limited capital needs for the near and intermediate term.

We believe that the risk associated with the district's variable-rate obligations, which make up about 33% of its debt profile, somewhat constrains the rating.

The district's full faith and credit pledge secures the bonds. Additional security is provided by the Pennsylvania State Aid Intercept Program as fiscal 2012 state aid revenue provides more than 1x coverage of post-refunding projected maximum annual debt service. We understand bond proceeds will current refund the district's series 2008A GO bonds.

Located in central eastern Pennsylvania, Northwestern Lehigh School District encompasses a 107-square-mile section of Lehigh County and has a population of roughly 15,500. The approximate geographic center of the district is about 20 miles northwest of the city of Allentown. Overall trends in enrollment have been slightly negative in recent years; total enrollment fell to 2,262 in fiscal 2014, from 2,375 in 2010. Enrollment projections through 2019 show a continuation of the trend.

The district's assessed value was reassessed at full market value effective fiscal 2014, resulting in a sizable 218% year-over-year increase and several appeals. We understand the bulk of appealed value related to 17 commercial properties. Based on experience, management expected these appeals to settle at 50% of contested value and budgeted accordingly. Management reports only two commercial appeals remain outstanding and that the settlements have been right around the 50% mark. Following the reassessment, the district's market value of \$1.4 billion represents a very strong \$93,000 per capita. The district's median household effective buying income (EBI) measures 143% of the national average, which we consider very strong. On a per capita basis, the EBI of 122% is weaker but still strong. Lehigh County's unemployment rate averaged 7.9% in August 2013, which was lower than the comparable month in 2012 (8.8%).

The district posted general fund surpluses in each of the past five audited fiscal years, which we believe is reflective of financial stability. Fiscal 2012 closed (June 30) with a \$2.6 million general fund surplus on a \$33 million budget; leading revenue sources were current real estate taxes (59% of the total) and state sources (28%). Property tax collections have historically been stable at roughly 95% on a current-year basis. The fiscal 2012 year-end total available balance was \$5.3 million, which we consider very strong at 15.8% of expenditures. Not included in this amount is a \$9.6 million committed balance that we believe significantly enhances the district's financial flexibility. The largest expense categories include other postemployment benefits (OPEB) at \$2.8 million, future retirement rate increases at \$2.1 million, increases in health care premiums at \$1.8 million, and future debt service rate increases at \$1.8 million.

The fiscal 2014 budget totals \$37.3 million and includes a \$400,000 budgetary reserve as well as a \$453,000 reserve appropriation. We believe the district's budgeting practices are conservative as it overbudgets energy expenditures as well as interest on variable-rate debt obligations. The fiscal 2013 budget also included a reserve appropriation, though projections for year-end include a \$1.7 million surplus.

We consider Northwestern Lehigh School District's management practices to be "good" under Standard & Poor's Financial Management Assessment. This indicates that practices exist in most areas, although not all may be formalized or regularly monitored by governance officials. The district has a formal fund balance policy to maintain the unassigned general fund balance at no less than 8% of expenditures.

The district has two variable-rate debt obligations that were issued through the Emmaus General Authority's bond pool program and are supported by letters of credit (LOC). They include:

- The 2007A GO notes issued through the 1989 bond pool that was remarketed in 2008, and supported by an LOC with US Bank N.A.
- The 2009 GO bonds issued under the 2000A bond pool and supported by an LOC between the Emmaus General Authority and US Bank N.A.

The LOCs contain what we deem permissive events of default that, if triggered, could result in the acceleration of the obligations. As a result, we evaluated the district's liquidity to determine its ability to cover the events of default. The district's two-year low general fund cash balance of \$15.8 million (June 2012) would not be sufficient to cover the \$16.8 million of principal at risk. However, when including the district's checking balance, capital reserve balance, capital projects balance, and food service balance, the two-year low rises to \$18.7 million. Management reports interfund borrowing is permissible and that there are not repayment requirements.

The district's overall debt burden, net of state aid, is about \$3,400 per capita and 3.1% of market value. We believe these indicators are moderate. Carrying charges are also moderate, accounting for 10.7% of total governmental expenditures in fiscal 2012. The district may issue additional bonds to finance upgrades at the high school, though there are no firm plans to do so.

The district's pension contributions in fiscal 2012 totaled \$1.4 million. Including \$279,000 for OPEB pay-as-you-go costs, the figure represented 5% of total governmental expenditures. Pension costs are on the rise; the district contributed \$2 million in 2013 and budgeted \$2.9 million in 2014. The unfunded actuarial accrued OPEB liability is \$3.1 million.

## Outlook

The stable outlook reflects Standard & Poor's expectation that the district will continue to maintain a fund balance at or near current levels given that management's conservative budgeting practices have yielded strong results. Though management continues to budget conservatively for its variable-rate notes, we believe the potential for acceleration creates liquidity risk. We will continue to monitor coverage levels relative to principal at risk of acceleration and would view a decline to below 1x as a negative credit factor. However, we do not expect to change the rating within the outlook's two-year horizon.

## Related Criteria And Research

### Related Criteria

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: State Credit Enhancement Programs, Nov. 13, 2008
- USPF Criteria: Contingent Liquidity Risks, March 5, 2012

### Ratings Detail (As Of December 9, 2013)

Northwestern Lehigh Sch Dist GO State Credit Enhancement (AGM)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Upgraded
<i>School Issuer Credit Rating</i>	AA/Stable	Upgraded
<b>Northwestern Lehigh Sch Dist GO State Credit Enhancement</b>		
<i>School Issuer Credit Rating</i>	AA/Stable	Upgraded
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Upgraded

Many issues are enhanced by bond insurance.

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