MOODY'S INVESTORS SERVICE

CREDIT OPINION
18 July 2019

Rate this Research

Contacts

Gregory Max Sobel +1.212.553.9587
Associate Lead Analyst
gregory.sobel@moodys.com

Nicole Serrano +1.212.553.4143
VP-Senior Analyst
nicole.serrano@moodys.com

Lower Merion School District, PA (Montg. Co.)

Update to credit analysis

Summary

Lower Merion School District's (Aaa stable) financial position will continue to exhibit strength in the near term despite the planned use of reserves. The district's sizable tax base is poised for continued residential growth, while its debt burden will grow due to future borrowing plans. That said, the debt burden is expected to remain manageable.

Credit strengths

- Robust financial position
- Reserves outside of the General Fund
- Sizable and growing tax base
- Significantly above average wealth levels

Credit challenges

- Plans to use reserves in the near to middle term
- Significant additional borrowing plans

Rating outlook

The stable outlook reflects the district's strong reserve levels which we expect to exhibit near term stability.

Factors that could lead to an upgrade

- Not applicable

Factors that could lead to a downgrade

- Material decline in existing reserve levels
- Significant decline in the tax base

Key indicators

Exhibit 1

Lower Merion School District, PA (Montg. Co.)	2014	2015	2016	2017	2018
Economy/Tax Base					
Total Full Value ($000)	$12,337,556	$12,507,927	$12,549,228	$12,610,038	$13,000,176
Population	62,409	62,480	62,525	62,830	62,830
Full Value Per Capita	$197,689	$200,191	$200,707	$200,701	$206,910
Median Family Income (% of US Median)	234.8%	243.9%	239.5%	235.0%	235.0%
Finances					
Operating Revenue ($000)	$216,697	$227,898	$239,706	$253,268	$266,469
Fund Balance ($000)	$55,922	$56,077	$56,174	$56,017	$58,029
Cash Balance ($000)	$76,390	$74,944	$73,634	$76,387	$84,750
Fund Balance as a % of Revenues	25.8%	24.6%	23.4%	22.1%	21.8%
Cash Balance as a % of Revenues	35.3%	32.9%	30.7%	30.2%	31.8%
Debt/Pensions					
Net Direct Debt ($000)	$284,315	$280,185	$260,535	$245,265	$228,740
3-Year Average of Moody's ANPL ($000)	$277,304	$317,491	$326,442	$360,920	$394,704
Net Direct Debt / Full Value (%)	2.3%	2.2%	2.1%	1.9%	1.8%
Net Direct Debt / Operating Revenues (x)	1.3x	1.2x	1.1x	1.0x	0.9x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	2.2%	2.5%	2.6%	2.9%	3.0%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.3x	1.4x	1.4x	1.4x	1.5x

Sources: Moody's Investors Service, Lower Merion School District audited financial statements

Profile

Lower Merion School District serves 8,649 students in the Township of Lower Merion (Aaa stable) and the Borough of Narberth, and is one of Philadelphia's Main Line suburbs in Montgomery County, PA (Aaa stable).

Detailed credit considerations

Economy and Tax Base: Sizable and growing tax base with robust wealth levels

Lower Merion School District's sizable $13.6 billion taxable base will continue to grow in the near term, as management reports a trend of large estates being broken into subdivisions within the district. The tax base has grown by a solid 2% annually, on average, over the last five years.

Full value per capita is well above the median for PA school districts at $217,000. Additionally, the median family income is robust at 235% of the nation. Unemployment as of May 2019 was below average at 3.1%, compared to the nation (3.4%) and the state (3.8%). Lastly, poverty is limited at under 5% of the population.

Enrollment in the district continues to grow, mirroring the population growth occurring in the district. Enrollment grew by 8.1% over the last five years to 8,649 during the 2018-2019 school year. Favorably, cyber and charter school enrollment is limited at a mere 39 students, which amounts to 0.4% of the district's annual budget.

Financial operations and reserves: Sizable reserve position with planned use of fund balance

The district's financial position is expected to remain strong in the near term despite plans to use reserves for capital needs. The district has a long history of running operating surpluses in its General Fund, and subsequently transferring those surpluses to its Capital Reserve Fund. At the end of fiscal 2018, the district had an available General Fund balance of $55.9 million or 21% of revenues. With the transfer of the $13.6 million operating surplus to the Capital Reserve Fund, the district maintained an additional $21.5 million in reserves outside of the General Fund, bringing total available reserves to $77.4 million or 29.1% of revenue. The district has achieved these results largely through annual property tax increases along with tax base growth. Local revenues grew by 24.1% from 2013 to 2018.

Management reports that, in fiscal 2019, the district transferred a total of $15 million out of the General Fund balance to be used for the acquisition of property. The district also increased its property tax levy by the Act 1 index limit of 2.4%. As such, the district's total reserve position will remain strong. On the other hand, there are additional plans to utilize reserves in fiscal 2020, though the district has historically budgeted conservatively. The district is also exposed to a lawsuit related to its budget practices. Should the verdict of the suit not be in the district's favor, it would need to pay $16 million from its General Fund. Future assessments of the district's highest quality credit rating will focus on its ability to maintain a strong overall reserve position despite the planned use of reserves and the potential negative outcome of the aforementioned suit.

LIQUIDITY

Lower Merion School District's cash position is poised to remain excellent in the near term. At the end of fiscal 2018, the district had $84.75 million in net cash in its General and Debt Service Funds, which equates to 31.8% of revenue.

The district maintains an additional $7.5 million of cash in its Capital Reserve Fund.

Debt and pensions: Manageable debt burden with sizable future borrowing plans; Moderate pension liability

The district's debt burden will remain manageable in the near term due to its above average amortization of principal. After the issuance of the Series of 2019 bonds, the district's debt burden will be 1.8% of full value or $249.8 million. The Series of 2019 bonds are being issued to finance the construction of a new middle school. At the end of fiscal 2018, the district had $228.7 million in debt outstanding, which equated to 1.8% of full value.

Debt service was a moderate 9.7% of expenditures or $25.7 million in 2018. The current issuance will increase debt service requirements by about $1 million through fiscal 2024, when maximum annual debt service (MADS) of $29.4 million occurs. After that, the Series of 2019 debt service increases incrementally to $5.8 million by fiscal 2030, though total debt service drops off precipitously.

The district plans on issuing approximately $75 million more to complete its middle school project. Future assessments of the district's credit quality will assess its ability to cover a growing annual debt service requirement without the use of reserves.

DEBT STRUCTURE

The majority of the district's debt is fixed rate and matures over the long term. Approximately $55.3 million or 22% of outstanding debt is variable rate.

Amortization of principal is above average, with 88% being repaid over the next ten years.

DEBT-RELATED DERIVATIVES

The Series A and B of 2009 have a related floating-to-fixed rate swap agreement with Royal Bank of Canada (senior unsecured rated Aa2). Under the agreement, the district makes fixed rate payments of 4.041% on a semi-annual basis and receives variable rate payments based on SIFMA on a monthly basis on a notional amount of $60.9 million through the life of the bonds (April 1, 2027). Early termination of the swap agreement is optional for the district only, and termination by the counterparty depends upon specified termination events occurring, including rating deterioration below a certain threshold (Baa1).

PENSIONS AND OPEB

The district contributes to the Public School Employee Retirement System (PSERS), a multi-employer cost-sharing plan administered by the Commonwealth of Pennsylvania. During fiscal 2018, the district contributed $19.2 million, which was matched in full by the state's reimbursement for half the annual cost. The fiscal 2018 three-year average Moody's adjusted net pension liability, under Moody's methodology for adjusting reported pension data, was $394.7 million, or an average 1.48 times operating revenues. The adjustments are not intended to replace the district's reported liability information, but rather to improve comparability with other rated entities. We determined the district's share of liability for the state-run plan in proportion to its contributions to the plan.

Total fixed costs for current year post-employment benefits, pensions, and debt service summed to $45.4 million, or a moderate 17.0% of operating revenues in fiscal 2018.

Management and governance: History of strong fiscal practices

Lower Merion School District's formal fund balance policy states that its total available fund balance may exceed 8%. Favorably, the district has a long history of sound fiscal practices and conservative budgeting, which has resulted in its robust financial position.

Pennsylvania School Districts have an Institutional Framework score of A, which is moderate compared to the nation. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. Schools major revenue source, property taxes, are subject to an Act 1 cap, which limits property taxes above an Act 1 index subject to certain exceptions. The Act 1 index is based on inflation. However, the cap still allows for moderate revenue-raising ability. Unpredictable revenue fluctuations tend to be moderate, or between 5-10% annually. Across the sector, fixed and mandated costs are generally less than 25% of expenditures. However, Pennsylvania has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be moderate, between 5-10% annually.

Rating methodology and scorecard factors

The US Local Government General Obligation Rating Methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 2

Lower Merion School District, PA (Montg. Co.)

Rating Factors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$13,609,741	Aaa
Full Value Per Capita	$216,612	Aaa
Median Family Income (% of US Median)	235.0%	Aaa
Finances (30%)		
Fund Balance as a % of Revenues	21.8%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	0.8%	A
Cash Balance as a % of Revenues	31.8%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	6.7%	A
Notching Factors:[2]		
Other Analyst Adjustment to Finances Factor: Significant reserves outside of the General Fund		Up
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	A
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	1.8%	A
Net Direct Debt / Operating Revenues (x)	0.9x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	2.9%	A
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.5x	A
	Scorecard-Indicated Outcome	Aa1
	Assigned Rating	Aaa

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology dated December 16,
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs Updated for 2019 publication

Sources: US Census Bureau, Moody's Investors Service

REPORT NUMBER 1186081

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S
INVESTORS SERVICE