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Summary:

Polk County, Iowa; General Obligation

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Credit Profile

US\$75.99 mil GO bonds ser 2020 due 06/01/2040

Long Term Rating

AAA/Stable

New

Polk Cnty GO

Long Term Rating

AAA/Stable

Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Polk County, Iowa's series 2020 general obligation (GO) bonds. At the same time, we affirmed our 'AAA' long-term rating on the county's previously rated GO bonds. The outlook is stable.

The bonds are secured by the county's GO pledge, which benefits from an ad valorem property tax without limitation on the rate or amount. The approximately \$76 million of series 2020 bond proceeds will be used for two purposes: to refund the county's outstanding 2015B bonds for interest cost savings and to fund a loan to the Metro Waste Authority.

Polk County's bonds are eligible to be rated above the sovereign because we believe the county can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, U.S. state and local governments are considered to have moderate sensitivity to country risk. (For more information, see "Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions," published Nov. 19, 2013, on RatingsDirect.) The county's local property tax revenues are the primary source of security on the bonds, which significantly limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the county. The institutional framework in the U.S. is predictable for counties, allowing them significant autonomy and independent treasury management, and there has been no history of government intervention. Moreover, the county's financial flexibility is demonstrated by its very strong general fund balance as a percentage of expenditures.

Encompassing the city of Des Moines and its surrounding suburbs, Polk County is the center of the most expansive and developing economic area in the state of Iowa. As its increasing population and abundant growth in most sectors show, the area has continued to thrive, with increasing market values and a local economy that has only been expanding in recent years. Operationally, the county has been very strong, with consecutive general fund surpluses since 2013, and an available fund balance that has seen increases in each of the last eight fiscal years, remaining steadily in compliance with its 20%-25% reserve policy. The county is backed by a strong management team that, over the years, has implemented a number of extensive policies and practices that help guide financial decisions and maintain stability in operations. Unexpected costs are managed well and absorbed into the budget, as oversight is strong and flexibility remains resilient. While our view of the county's debt profile has worsened somewhat with a slight increase in debt service carrying charges, our overall view of the credit profile remains unchanged at this time. These various factors continue to support stable credit quality and the continued affirmation of the county's

long-standing 'AAA' GO rating.

The 'AAA' rating reflects our assessment of the county's creditworthiness, specifically its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA) and a local stabilizing institutional influence;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Very strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 44% of operating expenditures;
- Very strong liquidity, with total government available cash at 55.9% of total governmental fund expenditures and 6.9x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 8.1% of expenditures and net direct debt that is 104.5% of total governmental fund revenue, as well as rapid amortization, with 81.5% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Stable Two-Year Outlook

Downside scenario

Should the county draw down its reserves below its policy target or significantly increase its debt burden, the rating could be pressured downward.

Very strong economy

We consider the county's economy very strong. Polk County, with a population of 484,967, is in the Des Moines-West Des Moines MSA, which we consider to be broad and diverse. It also benefits, in our view, from a stabilizing institutional influence. The county has a projected per capita effective buying income of 100.4% of the national level and per capita market value of \$94,170. Overall, market value grew by 10.0% over the past year to \$45.7 billion in 2021. The county unemployment rate was 2.5% in 2018.

The city of Des Moines, being the state capital of Iowa and its largest city, acts as a stabilizing presence for the county. In addition to the state, which employs 18,000, notable leading employers include Wells Fargo & Co. (12,900 employees), Principal Financial Group (8,169), Mercy Medical Center (5,384), and the Unity Point Health System (5,309). The local economy benefits from a diverse mix of employers and taxpayers. Some of the leading areas include: bioscience and agriculture, financial services, manufacturing, logistics, and data centers and information services.

In regard to valuations, Polk County is experiencing robust growth, with sizable increases in market values (43% from 2015-2019) and taxable values (38%). With building permit activity at record levels, the county is seeing extensive new development, recently highlighted by the construction of data centers for significant technology companies, including Microsoft and Facebook. Continuing development in downtown Des Moines has led to the need for additional living

units to accommodate the increasing nighttime population, and, in surrounding suburbs such as Altoona, Ankeny, Urbandale, and West Des Moines, development in manufacturing and technology continues to pave the way for additional hotels and retail, all of which are contributing to rising valuations. Management expects such increases to continue for the foreseeable future as development is projected to continue at its current rate.

Population in the county and, more specifically, within Des Moines, has seen consistent growth in recent years, increasing by nearly 13% since 2010, with numbers expected to continue rising based on job growth and ongoing development throughout the county. Given these trends and current developments, we expect the county's economy to remain strong over the next two years.

Very strong management

We view the county's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

The county uses at least five years of historical data and external sources when making budget assumptions. Management provides the board with at least quarterly reports throughout the year that include budget-to-actual analysis; investment holdings and earnings are shared with the board semiannually, but monitored and reported among senior staff on a monthly basis. The board also makes semi-annual amendments to the budget. The county produces a financial forecasts for the budget plus five years. It maintains five-year capital plans across all departments, which identify projects, sources, and uses of funds. Its reserve policy is to maintain cash reserves of 20% to 25% of expenditures, and the policy addresses replenishment in cases of draws in its contingency reserve, which is held outside the general fund. The county also has a formal debt management policy which establishes debt affordability metrics. Its history of strong financial performance is evidence that these financial policies and practices are embedded in the financial management.

Very strong budgetary performance

Polk County's budgetary performance is very strong, in our opinion. The county had operating surpluses of 9.1% of expenditures in the general fund and 16.8% across all governmental funds in fiscal 2019.

For our analysis, we have adjusted for routine transfers in and out of the general fund and removed bond-financed expenditures across total governmental funds. The fiscal 2019 budget originally called for a general fund surplus of roughly \$11.6 million, yet the year ended with an increase to fund balance of roughly \$12.8 million. The positive variance primarily reflected unbudgeted revenue increases in items such as care of prisoner revenues and improved interest earnings; however, these increases were countered minimally by an increase to the general fund mental health line item (of \$3.2 million) to cover certain mental health services within the general fund, an expenditure that is expected to continue and will be included in future budgets. Across total governmental funds, results were also positive after adjusting for spending of bond proceeds.

The initial budget for fiscal 2020 called for a \$13.5 million general fund surplus; however, after its midyear amendment, management is expecting an essentially break-even result after incorporating various higher expenditures, including the increased general fund portion allocated for mental health services (\$3.5 million for 2020), and various one-time capital items. In addition, management highlighted the possibility of an additional transfer out to the mental health fund (below the line, as was done in fiscal 2019) if the state is unable to provide additional funding for this issue.

Officials indicated that managing mental health service expenses is a challenge for the county at this time, but at least some of this burden may be offset by state funding in the future; we believe that in the meantime, the costs are manageable for the county and that its budget will be able to absorb increased costs based on management's history of budget oversight and adjustments. Early projections for fiscal 2021 include an intentional spend-down of reserves as the county invests in capital projects, but it still expects to post a slight surplus in the general fund of roughly \$700,000.

In fiscal 2019, property taxes represented 65% of general fund revenues, followed by intergovernmental (19%), then charges for services (8%). While there may be some fluctuation in intergovernmental revenues, we expect the county to adjust its expenditures as it has historically done. Additionally, the general fund receives transfers in from Prairie Meadows Racetrack/Casino, which are about 5% of general fund revenue. Given the county's recently negotiated lease, extending through 2026, and Prairie Meadows' historical presence and strong operations within the county, we expect this revenue source to remain stable.

Given the county's history of strong financial performance, we believe its projected results for 2020 and 2021 are likely, and we expect budgetary performance to remain at least strong over the next two years.

Very strong budgetary flexibility

Polk County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 44% of operating expenditures, or \$84.9 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor. The available fund balance includes \$73.7 million (38.1% of expenditures) in the general fund and \$11.2 million (5.8%) that is outside the general fund but legally available for operations.

We have added \$11.2 million of additional reserves from the contingency reserve fund, which are available for future contingencies to achieve budget and revenue stabilization. We expect the county's budgetary flexibility to remain very strong given general fund projections.

Very strong liquidity

In our opinion, Polk County's liquidity is very strong, with total government available cash at 55.9% of total governmental fund expenditures and 6.9x governmental debt service in 2019. In our view, the county has strong access to external liquidity if necessary.

We have adjusted the county's available cash figure to account for \$27.0 million of unspent bond proceeds at fiscal year-end 2019. Based on past issuance of debt, we believe that the issuer has strong access to capital markets to provide for liquidity needs, if necessary. We don't consider the county's investments aggressive, as it primarily invests in CDs, government notes and treasuries, mutual funds, and a small amount of commercial paper.

In March 2018, the county entered into two guaranty agreements related to debt issued for the Des Moines convention center hotel. The county provided its guaranty for \$4.31 million series C-2 certificates and \$7.8 million series E certificates issued by IEC Hotel Corp. The series E guaranty does not contain any accelerations provisions. The C-2 guaranty contains an acceleration provision if the county's rating falls below investment grade or if it pays six consecutive deficiency payments on behalf of IEC Hotel. Given the size of the guaranty relative to the county's budget (2.2% of 2019 general fund revenue), as well as the county's historical performance and overall credit quality, we view

this event as remote and do not view it to be a contingent liquidity risk.

Adequate debt and contingent liability profile

In our view, Polk County's debt and contingent liability profile is adequate. Total governmental fund debt service is 8.1% of total governmental fund expenditures, and net direct debt is 104.5% of total governmental fund revenue. Approximately 81.5% of the direct debt is scheduled to be repaid within 10 years, which is, in our view, a positive credit factor. The county does not have any additional GO debt plans for the next two years. Following this issuance, it will have approximately \$297 million of debt outstanding, including the \$12.1 million of debt issued by IEC Hotel that the county guaranteed (as described above).

Polk County's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 4.1% of total governmental fund expenditures in 2019. The county made its full annual required pension contribution in 2019.

Pension and OPEB highlights include:

- The county's pension and OPEB costs are modest as a share of total spending and are not likely to accelerate significantly in the medium term, especially given the pension plans' strong funded status.
- Polk County participates in the Iowa Public Employees' Retirement System (IPERS), a multiple-employer, defined-benefit pension plan that use reasonable assumptions.
- Although the county funds its OPEBs on a pay-as-you-go basis, exposing it to potential cost acceleration, we expect that medium-term costs will remain only a small share of total spending and, therefore, not a significant budgetary pressure.

The county participates in the following pension and OPEB plans:

- IPERS: 84% funded (as of June 30, 2019), with a county proportionate share of the plan's net pension liability of \$55.3 million in 2019.
- An implicit rate subsidy arising from retirees staying on the county's plan while paying active premium rates

The county's 2019 actuarially determined IPERS and MFPRSI contributions exceeded 100% of our static funding metric but fell short of our minimum funding progress metric. In general, we expect progress toward full funding to be slower given the IPERS' amortization basis of level percentage over a closed period of 28 years and MFPRSI's amortization basis of level percentage over a 25-year closed period. Furthermore, we believe IPERS' and MFPRSI's discount rates of 7.0% and 7.5%, respectively, could lead to contribution volatility. We expect contributions will remain relatively stable, and, given the plans' strong funded status and strong contribution practices, we expect they will remain affordable.

Strong institutional framework

The institutional framework score for Iowa counties is strong.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

Ratings Detail (As Of March 12, 2020)

Polk Cnty GO rfdg bnds		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Polk Cnty GO (AGM)		
<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Affirmed
Polk Cnty GO (MBIA) (National)		
<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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