

RatingsDirect®

Summary:

Sheldon, Iowa; General Obligation

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Credit Profile

US\$3.5 mil GO cap ln nts ser 2022 due 06/01/2033

<i>Long Term Rating</i>	A+/Stable	New
Sheldon GO (BAM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Sheldon GO (BAM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Credit Highlights

- S&P Global Ratings assigned its 'A+' long-term rating to Sheldon, Iowa's \$3.5 million series 2022 general obligation (GO) capital loan notes.
- At the same time, S&P Global Ratings affirmed its 'A+' underlying rating (SPUR) on the city's existing GO debt.
- The outlook on all ratings is stable.

Security

The city's full-faith-credit-and-resources and unlimited ad valorem property tax pledges secure the series 2022 capital loan notes and existing debt. Officials intend to use the proceeds to finance the construction of a new water tower and street improvement projects.

Credit overview

Sheldon's financial health steadily improved in recent years, specifically the general fund balance, although still what we consider to be somewhat thin (\$1.3 million at year end fiscal 2021). The city built up reserves from a fund balance of \$363,000 in fiscal 2018, which we consider to be a nominally low level. Surplus results in fiscal 2021 reflect performance in line with budgeted assumption, higher revenues interest earned on cash accounts, and receipt of American Rescue Plan (ARP) funds. Based on the unaudited results for fiscal 2022, we anticipate financial performance will be consistent with recent years, and we believe that conservative budgeting will continue to generate balanced financial operations. Although the local economy is limited, management reports a rise in building permit revenue in fiscal years 2021 and 2022 stemming primarily from residential growth with some commercial development. In our view the city's debt profile is very weak, due to its increasingly high fixed costs and leveraged position. We believe the debt profile is unlikely to materially change in the near term as the city layers on more debt with future capital projects.

The 'A+' rating reflects our view of the city's:

- Adequate economy with projected income levels below the national average;

- Positive operating results with growing reserves from surplus results;
- Standard financial-management policies and practices under our Financial Management Assessment (FMA) methodology and strong institutional framework score; and
- Very weak debt profile with additional debt plans.

Environmental, social, and governance

The city is currently engaged in a lawsuit that alleges that the city failed to follow due process of law as a direct result in a deficiency in public safety officer training. This situation is evolving and we will continue to monitor whether it represents an ongoing risk management, culture, and oversight governance weakness that we incorporate into our credit rating analysis, particularly should additional risk management concerns arise. However, we have analyzed the city's environmental and social risks relative to its economy, management, budgetary outcomes, and debt and liability profile, and view them as neutral within our credit analysis.

Outlook

The stable outlook reflects our expectation the city will generate at least balanced operations based on management's conservative budgeting practices, and unaudited fiscal 2022's positive results.

Downside scenario

We could lower the rating if reserves decrease to levels that we no longer consider strong due to capital spending or budgetary stress, specifically if reserves drop significantly below \$500,000 with no plan to replenish them.

Upside scenario

We could raise the rating if economic metrics increase to levels that we consider commensurate with those of higher-rated peers, coupled with more embedded and sustainable management policies and practices, while sustaining recent financial performance. Additionally, we would expect to see a reduction in the overall debt burden.

Credit Opinion

Trend of positive financial operations and building reserves

Our analysis includes adjustments for revenues and expenditures that we view as one-time in nature, and adjustments for recurring transfers. Fiscal 2021 resulted in about \$532,00 surplus after our adjustments. Management attributes the higher-than-budgeted surplus to favorable interest rates for cash accounts held with a local bank, and conservative revenue and expense assumptions.

Officials report fiscal 2022 (year-end June 30) trended well with the budget, and the city anticipates posting a general fund surplus. Management made midyear adjustments to account for increased costs due to inflation. The city will receive a total allocation of \$704,000 in ARP funds, which will be dedicated to the construction of the new water tower.

The fiscal 2023 budget is structured similarly to prior years, with no major budgetary pressures. Management anticipates fiscal 2023 will result in a smaller surplus than prior years. Overall, fiscal 2023 is reported to be in line with

the budget.

The general fund relies mainly on property taxes (29%), charges for services (18%), and miscellaneous revenue (23%) to fund operations. The city has recently had a history of reporting positive general fund operations, and its other governmental funds have remained fairly steady with positive balances.

Sheldon's reserves are very strong on a cash basis, ending fiscal 2021 with \$1.3 million available for general fund operations, and \$2.1 million in total governmental cash and investments after removing unspent bond proceeds. The city has additional cash, approximately \$535,775 in fiscal 2021, for routine library, airport, park, and museum operations. Due to the potential to spend this down on capital projects, we have not included this cash in available fund balance.

Limited local economy, with some residential growth

Sheldon is in northwest Iowa and covers O'Brien County and Sioux County. O'Brien County is primarily agricultural. The city is home to an array of employers; leading employers include:

- Sanford Health Systems (325);
- Village Northwest Unlimited (285), rehabilitation services;
- Van Wyk Trucking (282); and
- Rosenboom (280), a manufacturer of hydraulic cylinders.

Officials report on going residential development single family homes and multi-family units. Additionally, a new hotel is under construction.

Adequate financial-management policies that have produced consistently strong finances

Policies include management's:

- Predictable budget process that involves analysis of expenditures, major goals, and Iowa's revenue environment to validate assumptions;
- Monthly updates to the city council on budget-to-actual performance;
- Lack of formal long-term financial projections;
- Annually updated capital planning that addresses timing and capital project costs;
- Internal investment-management policy with monthly performance-and-holdings reports to the council;
- Lack of a formal debt-management policy; and
- Lack of a formal fund-balance policy, coupled with maintaining 25% of general fund expenditures in reserve for cash flow.

In addition, the city is managing its cyber risk by using a third party to manage its IT services.

The institutional framework score for Iowa municipalities is strong.

Very weak debt profile with additional debt plans

We calculate direct debt at \$19.9 million, approximately \$7.4 million of which the city's sewer enterprise fund supports. Officials currently plan to issue \$2.4 million in new GO debt in the next two years to finance a water system and street project costs. We estimate fixed costs will double from fiscal 2021-2023 due to a large initial principal payment of the series 2022 GO capital loan notes. However, based on the amortization schedule, principal payments will level out and decrease significantly in fiscal 2024.

Manageable pension and other postemployment benefits (OPEB) obligations with long-term pension funding volatility risk

We consider Sheldon's pension and OPEB costs modest as a share of total spending; costs are not likely to accelerate significantly during the next few fiscal years, especially due to the pension plan's relatively strong funding.

The city participates in:

- Iowa Public Employees' Retirement System (IPERS), a multiple-employer, defined-benefit pension plan that uses reasonable assumptions, which was 83% funded, as of June 30, 2020, with a proportionate share of the plan's net pension liability of \$1.3 million; and
- Sheldon's single-employer health-care plan for retirees--plan retirees pay the full active premium, resulting in an implicit liability for the city; management finances the plan on a pay-as-you-go basis.

Sheldon's 2020 actuarially determined IPERS contribution fell slightly short of our minimum funding progress and status funding progress metrics. We generally expect progress toward full funding will be slower due to IPERS' level-percent amortization during a closed 26-year period. Furthermore, we think IPERS' 7% discount could lead to contribution volatility. We expect contributions will likely remain relatively stable. Because of IPERS' strong funding and contribution practices, we expect contributions will likely remain affordable.

Sheldon, Iowa--Key Credit Metrics				
	Most recent	Historical information		
		2021	2020	2019
Weak economy				
Projected per capita EBI % of U.S.	82.4			
Market value per capita (\$)	74,835			
Population		5,301	5,338	5,306
County unemployment rate(%)	3.0			
Market value (\$000)	396,701	336,584		
Ten largest taxpayers % of taxable value	26.2			
Strong budgetary performance				
Operating fund result % of expenditures		16.5	7.2	3.9
Total governmental fund result % of expenditures		2.7	14.1	(3.4)
Strong budgetary flexibility				
Available reserves % of operating expenditures		41.4	29.3	21.5
Total available reserves (\$000)		1,335	827	637

Sheldon, Iowa--Key Credit Metrics (cont.)				
	Most recent	Historical information		
		2021	2020	2019
Adequate liquidity				
Total government cash % of governmental fund expenditures		22.3	62.2	63.2
Total government cash % of governmental fund debt service		53.0	330.2	139.0
Adequate management				
Financial Management Assessment	Standard			
Very weak debt & long-term liabilities				
Debt service % of governmental fund expenditures		15.1	18.8	45.5
Net direct debt % of governmental fund revenue	132.7			
Overall net debt % of market value	3.5			
Direct debt 10-year amortization (%)	61.0			
Required pension contribution % of governmental fund expenditures		2.1		
OPEB actual contribution % of governmental fund expenditures		0.0		
Strong institutional framework				
Data points and ratios may reflect analytical adjustments. EBI--Effective buying income. OPEB--Other postemployment benefits.				

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- 2020 Update Of Institutional Framework For U.S. Local Governments

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