



Rating Action: Moody's upgrades Duluth Independent School District 709, MN's Issuer & GOULT to A3

12Apr2023

New York, April 12, 2023 -- Moody's Investors Service has upgraded Duluth Independent School District 709, MN's Issuer Rating to A3 from Baa2. Moody's also upgraded the rating on the district's outstanding general obligation unlimited tax debt and the rating on the district's full-term certificates of participation (COPs) (non-contingent lease backed by GOULT pledge) to A3 from Baa2, and the rating on the district's annual appropriation certificates of participation (lease: appropriation) to Baa1 from Baa3. The positive outlook has been removed. At the close of fiscal 2022, the district had direct debt outstanding of about \$209 million.

RATINGS RATIONALE

The upgrade of the issuer rating to A3 reflects improvement of the district's financial reserves to solid levels resulting from voter approval of an operating levy, strengthening of management practices and federal aid. The district will face a budget gap when federal aid is depleted, but management is proactively considering revenue and expenditure options to close the shortfall. The rating also incorporates Duluth's solid economic base that serves as a regional hub, resident income levels that are in line with the nation and declining enrollment trend albeit with recent recovery of some pandemic driven losses. Leverage is in line with sector medians.

The A3 rating on the district's general obligation unlimited tax (GOULT) bonds is at the same level as the issuer rating based on the district's full faith and credit pledge with authority to raise ad valorem property taxes unlimited as to rate or amount.

The A3 rating on the district's outstanding non-contingent lease back by a GOULT pledge (full-term COPs) obligations is at the same level as the district's issuer rating because debt service is not subject to annual appropriation.

The Baa1 rating on the district's lease: appropriation (appropriation COPs) obligations is one notch below the district's issuer rating due to the risk of non-appropriation and the more essential nature of the pledged assets (school facilities).

RATING OUTLOOK

Moody's does not usually assign outlooks to local governments with this amount of debt.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Further growth in reserves and liquidity
- Material reduction in leverage

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Decline in reserves and leverage
- Material increase in leverage and fixed costs

LEGAL SECURITY

The GOULT bonds are backed by the district's pledge to levy a dedicated property tax unlimited as to rate and amount. The GOULT Bonds are additionally secured by statute and supported by the State of Minnesota's School District Credit Enhancement Program which provides for an unlimited advance from the state's general fund should the district be unable to meet debt service requirements.

The full-term COPs do not carry the district's full faith and credit pledge but are supported by a separate, dedicated levy. The obligation of the district to make rental payments is absolute and unconditional and it is not subject to annual appropriation. The full-term COPs are also additionally supported by the State of Minnesota's School District Credit Enhancement Program.

The annual appropriation COPs are supported by lease payments which are subject to annual appropriation. The pledged assets are school facilities, which we deem to be a more essential asset.

PROFILE

Duluth ISD 709 is located along the Lake Superior shoreline about 150 miles north of the Twin City metropolitan area and has a resident population of just under 100,000. The district provides prekindergarten through twelfth grade education to residents of the City of Duluth as well as all or portions of five surrounding townships and has an enrollment of over 8,000.

METHODOLOGY

The principal methodology used in these ratings was US K-12 Public School Districts Methodology published in January 2021 and available at <https://ratings.moodys.com/api/rmc-documents/70054>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

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