Fitch Ratings

Fitch Affirms Lake County School Board, FL's IDR at 'AA-'

Fitch Ratings-New York-13 March 2017: Fitch Ratings has affirmed the following Lake County School Board, FL ratings:

--$175 million outstanding certificates of participation (COPs), series 2005C, 2012A and B, 2013A, 2014A, and 2015B at 'A+';
--Issuer Default Rating (IDR) at 'AA-'.

The Rating Outlook is Stable.

SECURITY
The COPs are secured by an undivided proportionate interest in lease payments made by the district to the Financing Corporation for the School Board of Lake County, Florida for the district under the master lease purchase agreement, subject to annual appropriation. The district is required to appropriate funds for all outstanding leases on an all-or-none basis. In the event of non-appropriation the district must surrender possession of all leased facilities under the master lease to the trustee, for disposition by sale or re-letting of its interest in such facilities.

KEY RATING DRIVERS

The IDR at 'AA-' reflect the district's very low long-term liability burden, prospects for solid enrollment-driven revenue growth, a very limited legal ability to independently raise revenues, and strong gap-closing capacity. Reserves have declined in recent years but have stabilized at a lower but still adequate level for the rating.

The 'A+' rating on the COPs is one notch below the IDR, reflecting the slightly higher degree of optionality associated with lease payments subject to appropriation.

Economic Resource Base

The district is coterminous with Lake County (IDR 'AA'/Outlook Stable), which is located in central Florida. The county seat, Tavares, is about 34 miles from the city of Orlando. The county's 2015 population of 325,875 represents a 9.7% increase since the 2010 census.

Revenue Framework: 'a' factor assessment
District general fund operations are funded through a state formula based on enrollment, which includes a combination of state aid and local property taxes. The solid revenue growth of the last decade is expected to continue in future years, given the somewhat improved state funding environment and expectations for continued modest enrollment gains in the near term. The district has very limited independent legal ability to raise revenues.

Expenditure Framework: 'aa' factor assessment
Instructional costs are the main driver of expenditures and are expected to rise in line with to marginally above revenues absent policy action. The district has ample legal control over workforce decisions and moderate carrying costs related to debt service and retiree benefits obligations.

Long-Term Liability Burden: 'aaa' factor assessment
The district's long-term liability burden is very low, comprised mostly of direct and overlapping debt. The district participates in the Florida Retirement System (FRS), and liabilities related to FRS do not constitute a material burden on local personal income.

Operating Performance: 'a' factor assessment
The district maintains adequate reserve levels relative to historical revenue volatility with a midrange level of inherent budget flexibility. Following post-recessionary draws, general fund balance has remained generally stable since fiscal 2013. Fitch expects the district to maintain reserves at similar levels in future years, given prudent fund balance policies.

RATING SENSITIVITIES
FINANCIAL FLEXIBILITY: The rating assumes maintenance of the district's historically adequate reserve levels. A reduction in the district's financial resilience and gap-closing ability could result in downward rating pressure; conversely, prolonged periods of materially stronger reserves in future years

could result in upward rating movement.

CREDIT PROFILE

The district is a primarily residential community with a sizeable retiree population. The local economy was traditionally centered on agriculture but is now largely driven by a growing healthcare and tourism presence. The county tax base growth has been strong in recent years, reflecting the recovering economy and rising home values. Tax base expansion is expected to continue with numerous residential, commercial and major road projects underway and planned. The district has experienced consistent moderate enrollment growth in recent years.

Revenue Framework

The Florida Education Finance Program (FEFP) is the primary mechanism for funding the operating costs of Florida school districts. The FEFP process determines a base per-student funding level. The funding is split between state funds, largely derived from statewide sales tax revenue, and local funds via the required local millage rate established pursuant to state statutory procedure. Discretionary taxes for operations and capital/maintenance are also levied by the district up to the statutory maximum rates of 0.748 mills and 1.5 mills, respectively.

Fitch's view of school district revenue prospects considers the revenue performance of the state as a starting point given its fundamental responsibility for public education funding. Fitch believes Florida's revenue prospects will grow at a pace that is above the rate of inflation but below U.S. economic performance based on a resumption of population growth and stronger economic expansion. School district revenue expectations are somewhat tempered by the state's education funding commitments which have been variable in recent history, with annual changes in the base student allocation as low as a 1% increase for fiscal 2017.

Enrollment trends and expectations are the second key determinant of a school district's revenue growth prospects and are based on Fitch's view of the local economy, demographic patterns, and competition from non-traditional public schools, among other factors.

The district experienced solid general fund revenue growth over the 10-year period through fiscal 2016, above inflation but below GDP growth for the same period. Going forward, Fitch expects the natural pace of revenue growth to continue in line with historical performance, given ongoing enrollment growth. State revenue performance has returned to steady growth, which should benefit FEFP funding levels absent education funding policy changes.

Due to the state funding mechanism, Florida school districts have very limited ability to independently increase general fund revenues. However, this limitation as a factor in the revenue framework assessment is somewhat offset by the recognition of K-12 education as fundamentally a state responsibility and the strong foundation of state support for education funding.

Expenditure Framework

School instruction costs related to personnel constitute the vast majority of district spending. Spending increases are influenced by state mandates regarding classroom size, rising salary and benefit costs and other program requirements from the state. The district has a solid level of spending flexibility with ample legal control over workforce and moderate carrying costs associated with retiree benefits.

Fitch expects the pace of spending to generally match or slightly exceed revenue trends in the absence of policy action, as increased spending is funded by a similar rise in state funding and growth in local revenues.

Wages and benefits are collectively bargained and the district has relatively good control over employee-related expenditures through the ability to ultimately implement a contract after non-binding arbitration. The district is currently meeting state class size requirements in all schools.

Carrying costs related to debt service, pensions and other post-employment benefits (OPEB) are moderate at roughly 12% of fiscal 2016 total government spending. Carrying costs are not expected to rise in the near future, as the district has limited borrowing plans and participates in the Florida Retirement System (FRS). The district provides an implicit retiree health insurance subsidy, which it funds on a pay-as-you-go basis.

Long-Term Liability Burden

The district's fiscal 2016 combined long-term liability burden, comprising debt and the district's share of the net pension liability of the FRS, is low at approximately 4% of resident personal income. The district's direct debt (amortizing roughly 59% of principal retired in 10 years) makes up about half of the district's combined long-term liability burden. The district has no intermediate-term plans for new money debt and plans to fund near-term capital projects with local capital improvement tax revenues that exceed debt service requirements.

Pensions are provided through the state-run FRS and costs are low. FRS is funded at a reported 85% as of July 1, 2016 or an estimated 80% when adjusted by Fitch to assume a 7% rate of return. Pension obligations do not represent a material burden (about 0.9%) relative to county personal income.

Operating Performance

The district exhibits strong gap-closing capacity and a midrange level of inherent budget flexibility, owing to limited legal ability to raise revenues and a solid level of expenditure flexibility, and adequate reserves. Reserves have declined in recent years, stabilizing at about $14 million, or 4% of spending, at fiscal 2016 year-end, providing an adequate cushion relative to Fitch's simulation of a modest 1.3% revenue decline in the event of a 1% drop in national GDP. Historical volatility is generally due to a combination of past modest enrollment declines and state funding changes.

Recent reserve draws for capital and restoration of services have left the district with a still adequate financial cushion. A reserve draw is budgeted for fiscal 2017, though budgets are historically conservative and the district currently projects fund balances to remain around current levels through prudent spending management. Budget management is further buttressed by a fund balance policy requiring a cushion of 4% available reserves.

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In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Additional information is available on www.fitchratings.com

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
(https://www.fitchratings.com/site/re/879478)

Additional Disclosures
Dodd-Frank Rating Information Disclosure Form
(https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=1020504&cft=0)
Solicitation Status (https://www.fitchratings.com/gws/en/disclosure/solicitation?pr_id=1020504)
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