

Credit Rating Comparison and Review

City of Windsor Heights, Iowa

June, 2013

INTRODUCTION

This *Credit Rating Comparison and Review* is provided to the City to facilitate discussion and, ultimately, preparation or refinement of a credit rating strategy for the City of Windsor Heights. In this *Comparison and Review*, we:

- Briefly discuss the purpose of credit ratings and the methodology by which ratings are prepared;
- Review Windsor Heights's credit rating history and identify how the City compares both nationally and within the state;
- Compare key credit factors for Windsor Heights to comparable entities within Iowa; and
- Review recent rating agency comments.

We look forward to discussing this information with you.

CREDIT RATINGS

A credit rating is an opinion of an organization's overall creditworthiness with respect to a particular debt obligation. For issuer's, the credit rating is a primary determinant of the cost to borrow money. It can also be useful as a guide for management of the organization's finances and operations. For investors, credit ratings are used as part of a comprehensive analysis to determine security and, ultimately, the price to be paid for a debt obligation. In general, credit ratings enhance capital market efficiency by providing independent, unbiased, and timely opinions.

Credit ratings are not a recommendation to buy, sell or hold a security. No consideration is given to future market price, investment objectives or risk parameters of the investor. A rating is simply a risk assessment. The investment grade ratings for the three major rating agencies are depicted in the table below.

	Moody's	S&P and Fitch	
Highest	Aaa	AAA	"Strongest creditworthiness"
	Aa1	AA+	"Very strong creditworthiness"
	Aa2	AA	
	Aa3	Aa-	
	A1	A+	"Above average creditworthiness"
	A2	A	
	A3	A-	
	Baa1	BBB+	"Average creditworthiness"
	Baa2	BBB	
Lowest	Baa3	BBB-	

All rating agencies assign ratings below the Baa/BBB levels. However, they are non-investment grade and are not germane to this discussion.

To assign a credit rating to a debt obligation, the major rating agencies analyze four factors:

- Economic Strength
- Financial Strength
- Debt
- Management

Each rating agency uses slightly differing names, weightings and methods for evaluating these factors. However, the areas of emphasis are roughly the same. The rating agencies emphasize that there is no formula that determines a rating. Each agency uses a set of defined criteria leading to a weighted average as the basis for a rating. But it should be recognized that subjectivity enters into both the identification and weighting of the criteria and, in some cases, the ranking assigned to a given criteria. Rating agencies state that the final rating is determined, not only by the weighted average of the factors, but also by comparison with peer entities, interaction of the individual factors and unique attributes of the entity and the financing.

CITY OF WINDSOR HEIGHTS CREDIT RATING HISTORY

The City of Windsor Heights has historically sought credit ratings for its general obligation debt from Moody's Investors Service. Currently, Moody's has assigned an Aa3 rating to Windsor Heights's outstanding general obligations bonds. The City did not seek a rating for the recently issued series 2013A bonds.

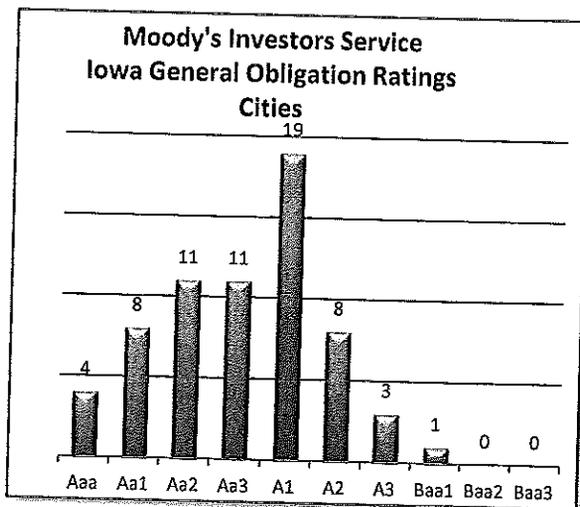
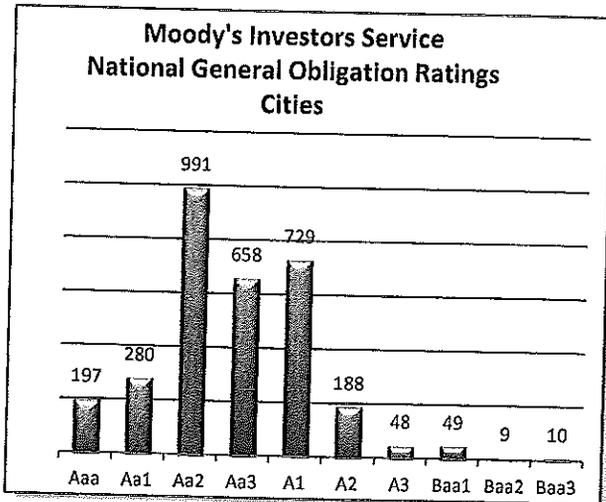
The Aa3 rating was a downgrade in April 2012 from an Aa2 rating. The following is the rationale summary published by Moody's in April 2012 for the downgrade:

"The downgrade to the Aa3 rating reflects the small size of the city's tax base with significant taxpayer concentration, a trend of moderately declining valuations, and declining trends in the city's socioeconomic indices"

It needs to be noted that an Aa3 rating for a community with fewer than 5,000 population is a very good rating and one that the City should be proud of. However, there are some lessons the City can take out of the report. The declining valuations and declining trends in the socioeconomic indices are both factors that a community the size of Windsor Heights has little control. It's important, therefore, for the City to take care in being diligent with the factors that the City has more control with such as fund balances and good management practices. We note that the general fund balance had a decrease and the 2013 budget anticipates a decrease. It is important to be able to explain the decreases as part of a planned reduction and not as a surprise.

National and State-Wide Ratings Distribution

The following graphs depict Moody's general obligation rating distribution nationally and within the state of Iowa as of May 2013. These graphs are helpful in putting the city's credit rating into perspective.



Of the 3,165 cities that Moody's rated nationally as of May 2013, 658 (21%) were rated Aa3. In Iowa, where Moody's reported a total of 65 cities rated, the Aa3 rating category represented 11 entities (17%).

When evaluating rating distributions, it is important to recognize that reporting bias is significant. In other words, only entities that are reasonably sure they will receive a favorable result will seek a rating. Also, these distributions include cities of all sizes, some of which may not be comparable entities. For this reason, we have compared Windsor Heights to the entire universe of Moody's rated cities in Iowa looking at the key statistics outlined in a rating report. We have also conducted a more detailed comparison of Windsor Heights with three peer communities in Iowa using a variety of key credit factors. This comparison is discussed in the following sections.

Comparison to all Moody's Rated Cities in Iowa

In this comparison, a limited number of fundamental statistics are used to create a relative indicator of the city's credit rating position. The comparison is intended to give general evidence of the strengths and weaknesses of the city as compared to similarly rated jurisdictions. This comparison is not intended to be a definitive argument for a credit rating, but rather a tool to monitor the relative financial health of the city and to develop a strategy for working with the credit rating agencies.

	Windsor Heights	Aaa	Aa	A
Number of Cities	Aa3	A	30	30
General Fund Balance as % of Revenues	149.70%	39.00%	36.90%	32.60%
Direct Net Debt as % of Full Value	3.36%	1.80%	2.10%	2.80%
Debt Burden (Overall Net Debt as % of Full Value)	4.69%	3.10%	3.80%	4.10%
Total Full Value (\$000)	\$383,752	\$5,359,761	\$1,260,166	\$375,734
Full Value Per Capita (\$)	\$78,962	\$70,171	\$64,601	\$49,811
Population 2010 Census	4,860	63,414	20,082	6,514

The City of Windsor Heights's general fund balances are well above the medians of other Moody's rated cities. The high general fund balances show flexibility in funding debt in case of economic downturns. The debt statistics are less favorable and show a level closer to communities rated in the "A" category. This is due to the much lower population size. The population size, however, improves the statistics that fall under the Economy Strength criteria. The most notable are the much higher market value per capita and per capita income measures. Overall, the table reflects a City whose financial strength and demographic profile places it solidly within the A category. The Aa3 rating the City currently has is a very good rating for a city this size.

Comparison to Peer Communities

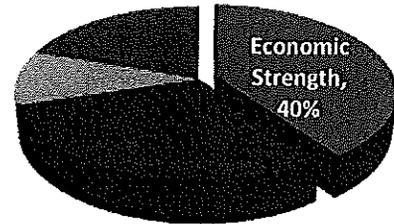
Cities used in this analysis include: Ankeny (Aa2), Indianola (Aa3), and Norwalk (A1). These entities were selected based principally upon having credit ratings above, the same, and below Windsor Heights. This comparison will show the range of values associated with the different ratings.

The description of the rating factors comes directly or is paraphrased from a Moody's published report in October 2009, titled, "Rating Methodology, General Obligation Bonds Issued by U.S. Local Governments." Moody's Investors Service authorizes Springsted to use its publications for educational purposes.

Factor 1: Economic Strength

The economic strength of a city affects its ability to generate adequate financial resources to meet operational and debt service needs. Moody's analyzes four sub factors within the Economic Strength category: 1) size of the community and growth trends; 2) type of economy; 3) socioeconomic and demographic profile; and 4) workforce profile. It is important to recognize that Economic Strength comprises 40% of the overall rating assessment, yet the City has very little direct control over the outcome. The table below shows how Windsor Heights compares with the three comparable cities.

Moody's Factor Weighting



COMPARISON COMMUNITIES	Windsor Heights	Ankeny	Indianola	Norwalk
CURRENT MOODY'S RATINGS	Aa3	Aa2	Aa3	A1
POPULATION				
2010 U.S. Census Population	4,860	45,582	14,782	8,945
2000 U.S. Census Population	4,891	27,117	12,998	6,884
Percent Change to Most Current	-0.63%	68.09%	13.73%	29.94%
PROPERTY VALUE INFORMATION				
	2012-2013	2012-2013	2013-2014	2012-2013
Actual Value (a)	\$383,753,462	\$3,437,356,329	\$820,758,970	\$600,753,529
Taxable Value (with rollback) (b)	\$188,395,992	\$2,049,202,489	\$469,671,458	\$254,468,278
Captured Tax Increment Value	\$46,553,120	\$157,507,600	\$47,507,247	\$74,664,645
% Residential Homestead	79.1%	67.0%	70.9%	87.1%
% Commercial/Industrial	21.5%	31.5%	28.2%	4.9%
% Other	-0.6%	1.4%	0.9%	8.0%
INCOME				
2010 City Median Household Income	\$66,997	\$72,703	\$53,162	\$73,220
2010 State Median Household Income	\$50,451	\$50,451	\$50,451	\$50,451
% of State 2010 Household Median Income	132.80%	144.11%	105.37%	145.13%
Per Capita Income (2010 Census)	\$33,994	\$32,102	\$24,728	\$35,467
% Household Income \$50,000 to \$99,999	39.7%	40.4%	35.2%	39.0%
% Household Income \$100,000 and Over	26.0%	30.3%	18.3%	30.7%
County Unemployment Rates (unadjusted)	4.6%	4.6%	4.5%	4.5%
State Unemployment Rates (seasonably adjusted)	4.7%	4.7%	4.7%	4.7%

Moody's Comments - Strengths:

- Favorable location in Des Moines metropolitan area
- Revenue-raising flexibility through available property tax levies
- Socioeconomic indicators are above state and national medians

Moody's Comments - Challenges:

- Land-locked geographic area with limited land available for future development.
- Significant taxpayer concentration
- Small tax base with modest declines in recent years

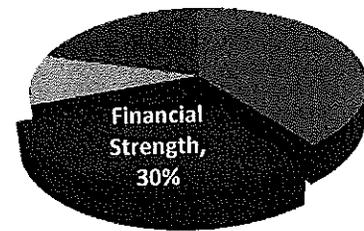
Observations:

- A declining population is a concern for a rating agency since it means fewer people available to repay debt. This coupled with the much lower actual value within the community is a challenge compared with the comparable cities.
- The mix of commercial/industrial compared with residential values is positive.
- The high percent of household income over \$50,000 is very positive and on track with the comparable cities.

Factor 2: Financial Strength

The analysis of financial strength addresses multi-year, historical trends rather than current performance. The focus is on the issuer's financial capacity and flexibility to weather budgetary pressures stemming from economic downturns or other factors. Moody's analyzes four sub factors within the Financial Strength category: 1) general fund balance and liquidity; 2) operating flexibility; and 3) budgetary operations, i.e. structural balance. Financial Strength comprises 30% of the overall rating assessment. The table below shows how Windsor Heights compares with the three comparable cities.

Moody's Factor Weighting



COMPARISON COMMUNITIES	Windsor Heights	Ankeny	Indianola	Norwalk
CURRENT MOODY'S RATINGS	Aa3	Aa2	Aa3	A1
FINANCIAL STATEMENT INFORMATION	June 30, 2012	June 30, 2012	June 30, 2012	June 30, 2012
General Fund:				
Revenues and transfers in	\$2,564,478	\$22,209,326	\$7,664,350	\$4,045,203
Expenditures and transfers out	\$2,822,649	\$21,219,210	\$8,177,617	\$4,529,541
Operating Surplus (Deficit)	(\$258,171)	\$990,116	(\$513,267)	(\$484,338)
Unassigned General Fund Balance	\$3,839,110	\$8,192,665	\$2,868,563	\$1,691,779
Unassigned Fund Balance/Revenues	149.7%	36.9%	34.8%	41.8%
Unassigned Fund Balance/Expenditures	0.0%	38.6%	32.6%	37.3%
General Fund Balance (Asset - Liabilities)	\$3,839,110	\$8,193,792	NA	\$1,714,950

Notes:

- (a) Includes gas and electric and TIF; before reduction for military exemption.
 (b) With rollback and after reduction for military exemption; includes gas and electric and excludes TIF.
 (c) Excludes general obligation debt supported by revenues, revenue debt, equipment leases and community college industrial newjobs and training certificates.
 Includes annual appropriation leases paid from operating levies.

Moody's Comments - Strengths:

- Ample reserves and historically balanced operations..

Moody's Comments - Challenges:

- None.

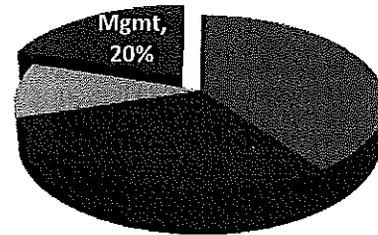
Observations:

- The fund balances are significantly higher than the comparable cities. However, looking through prior financials it is sometimes difficult to track through the transfers from TIF districts. It is very important to be able to document and explain large transfers that contribute to fund balances. The rating agency will want to understand if transfers may be masking operational deficits.
- With the challenges Windsor Heights has with its size and decreasing wealth it is of very high importance to ensure a continued positive fund balance.

Factor 3: Management and Governance

Evaluation of the entity's management examines practices and policies, rather than the individuals who hold positions of leadership within the organization. Moody's analyzes five sub factors within the Management and Governance category, which comprises 20% of the overall assessment:

Moody's Factor Weighting



1. Financial Planning and Budgeting
 - Comparison of budget versus actual performance trends, with particular emphasis on sophistication of revenue forecasting
 - Practices to control and adjust expenditures over the course of the fiscal year
 - Formal adoption of a policy which establishes fund balance requirements based upon fiscal vulnerability
 - Preparation of multi-year fiscal plans – both operating and capital
2. Debt Management and Capital Planning
 - Formal adoption of a debt policy which establishes; (i) target debt burden levels; (ii) maximum allowable debt burden levels; and/or (iii) target levels of debt service as a percentage of overall expenditures
3. Management of Economy/Tax Base
 - Practices to monitor performance of the local economy so that timely adjustments to financial plans, practices and policies may be made on a timely basis
 - Successful economic development practices
4. Governing Structure
 - Management's ability to maximize flexibility, i.e. levy limits, political constraints, impact of external oversight boards
 - Stability and effectiveness of elected officials and staff
5. Disclosure
 - Timely disclosure of financial information, i.e. annual financial audits, and timely adoption of budgets
 - Compliance with Government Accounting Standards Board (GASB) policies and procedures

Moody's Comments - Strengths:

- City maintains a number of debt management policies, including a commitment to utilizing no more than 75% of its statutory debt limit.
- City has reserve target of maintain 25%of budgeted expenditures. (City ended 2012 at 147%).
- City has additional flexibility through ability to levy additional taxes

Moody's Comments – Challenges:

- None

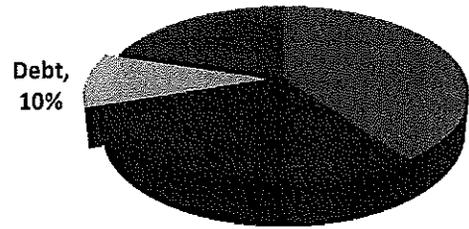
Observations:

- Windsor Heights should be commended on having recognized targets and policies.

Factor 4: Debt Profile

Moody's analyzes how much debt the economic base is supporting, the flexibility to absorb additional borrowing needs, expected future borrowing needs and the resulting impacts. Additionally, Moody's examines the impact of debt on financial flexibility, and management's ability to conservatively structure debt repayment. Moody's analyzes four sub factors within the Debt Profile category, which comprises 10% of the overall assessment:

Moody's Factor Weighting



1. Debt Burden
 - Measures the financial leverage of a community compared to the communities tax base
2. Debt Structure and Composition
 - Measures the City's ability and willingness to repay the debt in a timely fashion (principal amortization)
3. Debt Management and Fiscal Impact
 - Measures the structure and level of debt and its impact to fund financial operations
4. Other Long-Term Commitments
 - Measures pension and other post-employment benefits

COMPARISON COMMUNITIES	Windsor Heights	Ankeny	Indianola	Norwalk
CURRENT MOODY'S RATINGS	Aa3	Aa2	Aa3	A1
OUTSTANDING DEBT (c)				
Direct G.O. Debt	\$12,875,000	\$148,605,000	\$27,370,000	\$20,310,000
Overlapping G.O. Debt	\$5,115,514	\$107,235,155	\$14,838,549	\$14,983,857
DEBT RATIOS				
Direct G.O. Debt/Actual Value	3.36%	4.32%	3.33%	3.38%
Direct G.O. & Overlapping Debt/Actual Value	4.69%	7.44%	5.14%	5.87%
Direct G.O. Debt Per Capita	\$2,849	\$3,260	\$1,852	\$2,271
Direct G.O. & Overlapping Debt Per Capita	\$3,702	\$5,613	\$2,855	\$3,946

Moody's Comments - Strengths:

- Overall debt burden is moderate.
- 78.6% of principal retired within the 10 years.
- Majority of direct obligations are expected to be repaid with tax increment revenues.
- Limited capital needs

Moody's Comments - Challenges:

- Above average debt per capita.

Observations:

- Although Windsor Heights has above average debt per capita it is important to note that Moody's has pointed out that the City has structured its debt to pay off the debt rapidly.
- The comparable cities may not be as comparable in this factor due to Windsor Heights boundaries are set vs. the infrastructure needs as the other cities boundaries are growing. Moody's will take that into account as they assess the other communities.

CONCLUSION AND NEXT STEPS

The City of Windsor Heights has a good credit rating given the size of the City's tax base, which is roughly a third of other Aa rated cities in Iowa. This is due to the very high fund balances of the City and extremely high per capita wealth levels. Given the current criteria used by Moody's, an upgrade back to the Aa2 level would require significant growth in the City's tax base along with maintaining the large fund balances. We also recommend the City implement a long-term financial balanced forecast for its operational funds