Research Update:

La Vernia, TX Debt Rating Lowered To 'AA-' On Utility Fund Pressure; Outlook Stable

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Overview

- S&P Global Ratings lowered its rating on the City of La Vernia, Texas' certificates of obligation (COs) outstanding to 'AA-' from 'AA'.
- The outlook is stable.
- At the same time, we assigned our 'AA-' long-term rating, with a stable outlook, to the city's proposed $2.5 million series 2026 combination tax and limited pledge revenue certificates of obligation (COs).
- The downgrade reflects persistent utility fund deficits that have pressured the city's general fund available liquidity below peer levels, weakening its credit fundamentals.

Rationale

Security

The COs are secured by a limited ad valorem tax levied on all taxable property located within the city and by a limited pledge of net revenues of the city's waterworks and sewer system. However, due to the pledge's limited nature, we rate the COs to the strength of the GO pledge.

The state's statutes limit the ad valorem tax rate for general law cities to a maximum of $1.50 per $100 of taxable assessed valuation (AV) for all purposes, including a maximum of $1.00 for debt service. The city's fiscal 2026 levy is well below the maximum at 27.3 cents per $100 of AV, with 12.8 cents dedicated to debt service. We do not differentiate the city's limited-tax debt from its general creditworthiness, since the ad valorem tax is not derived from a measurably narrower tax base and there are no limitations on the fungibility of resources.

Proceeds from the series 2026 COs will fund improvements to the city's water and wastewater systems to ensure reliability and efficiency while building the necessary capacity to support community growth.

Credit highlights

The downgrade reflects the city's sizable utility fund deficits over the last three years, which have required significant general fund support and affected overall liquidity. While reserves remain aligned with city policy, approximately half of these funds are receivable from the utility fund, resulting in available liquidity that is relatively low compared to that of similarly rated peers. We expect management's proactive measures to help restore financial health in the longer term; however, the city's weakened position currently provides a smaller buffer against adverse developments.

Located in northern Wilson County, the city is an affluent bedroom community for San Antonio with a growing population. While recent taxable AV growth has decelerated due to increased exemptions, a strong pipeline of residential developments—including 220 units within the city and 75 units in an extraterritorial jurisdiction (ETJ)—is expected to bolster revenues over the medium term, though this will likely be partially offset by the increased cost of providing services to a much larger population, including investment in new water and wastewater infrastructure.

The city's general fund performance has been mixed, as one-time revenues and expenditures have occasionally obscured underlying operating results, while the utility fund needed substantial support in fiscals 2024 and 2025. Notably, management has taken proactive steps to address utility fund deficits through a multi-year strategy involving strategic rate increases, the replacement of underperforming water meters, and the implementation of an interest & sinking (I&S) levy to decouple debt service from utility revenues. While these measures have successfully narrowed the utility operating deficit in 2025, the accumulated $821,000 owed to the general fund represents approximately half of the city's $1.6 million in unassigned fund balance. Although a five-year reimbursement plan is in place, the current reliance on general fund support has significantly reduced the city's immediate financial buffer.

The rating further reflects our view of:

- Below-average economic metrics and a high concentration in the oil-and-gas sector at the county level, offset by the city's relatively strong income levels and positive local growth prospects.
- Balanced general fund operations despite volatility from non-recurring items, including a fiscal year 2024 surplus driven by large permitting fees and a capital-driven deficit in fiscal year 2025 for a new police station.
- Reserves that remain substantial as a share of operating revenues (approximately 60%) but are relatively low in absolute terms and do not fully reflect immediate liquidity, as 50% of the unassigned balance is receivable from the utility fund.
- Financial policies and practices, including conservative budgeting and monitoring. While formal long-term planning is absent, management maintains a five-year capital improvement plan and a reserve policy targeting 35%–60% for the general fund and 25% for other funds (a target not currently met by the utility fund). We view the issuer's cyber risk mitigation measures as consistent with our view of its credit fundamentals.
- A manageable but growing debt burden, supported by the implementation of an I&S levy to service utility-related debt, with potential issuances in the next couple of years for growth-related infrastructure. Pension and other postemployment benefits are not significant credit pressures due to adequate funding and limited obligations.
- For more information on our institutional framework assessment for Texas cities, see "Institutional Framework Assessment: Texas Local Governments," Sept. 9, 2024.
- Elevated physical risk based on La Vernia's exposure to flooding, which could have a negative economic and financial impact. We believe the city's focused infrastructure planning,

mitigation and emergency response plans, and coordination with higher levels of government mitigate this risk.

Outlook

The stable outlook reflects our expectation that recent measures implemented by management will result in balanced operations in the enterprise fund in the next couple of years.

Downside scenario

We could lower the rating if continued deficits in the utility fund or further volatility in the general fund were to lead to a decrease of the city's already limited available reserves, or if debt load were to increase significantly without offsetting economic growth.

Upside scenario

We could raise the rating if the local economy were to expand, boosting local incomes to levels we consider comparable with those of higher-rated peers, coupled with stronger financial performance and an increase in available reserves.

La Vernia, Texas--credit summary

Institutional framework (IF)	1
Individual credit profile (ICP)	2.73
Economy	3.5
Financial performance	2
Reserves and liquidity	3
Management	2.65
Debt and liabilities	2.50

La Vernia, Texas--key credit metrics

	Most recent	2025	2024	2023
Economy				
Real GCP per capita % of U.S.	38	--	38	37
County PCPI % of U.S.	84	--	84	84
Market value ($000s)	276,465	265,864	231,789	178,700
Market value per capita ($)	176,768	169,990	154,423	131,301
Top 10 taxpayers % of taxable value	14.4	--	13.3	14.7
County unemployment rate (%)	3.7	3.7	3.4	3.4
Local median household EBI % of U.S.	134	134	150	148
Local per capita EBI % of U.S.	110	110	121	116
Local population	1,564	1,564	1,501	1,361
Financial performance				
Operating fund revenues ($000s)	--	2,796	2,947	2,258
Operating fund expenditures ($000s)	--	3,164	2,312	2,330
Net transfers and other adjustments ($000s)	--	65	68	64
Operating result ($000s)	--	(303)	703	(8)

La Vernia, Texas--key credit metrics

	Most recent	2025	2024	2023
Operating result % of revenues	--	(10.8)	23.9	(0.4)
Operating result three-year average %	--	4.2	(1.9)	(6.0)
Reserves and liquidity				
Available reserves % of operating revenues	--	57.9	65.4	53.2
Available reserves ($000s)	--	1,620	1,928	1,201
Debt and liabilities				
Debt service cost % of revenues	--	16.6	8.0	9.9
Net direct debt per capita ($)	3,597	2,040	2,457	1,929
Net direct debt ($000s)	5,625	3,190	3,688	2,626
Direct debt 10-year amortization (%)	59	80	75	--
Pension and OPEB cost % of revenues	--	2.0	2.0	2.0
NPLs per capita ($)	--	31	79	139
Combined NPLs ($000s)	--	49	119	189

Financial data may reflect analytical adjustments and are sourced from issuer audit reports or other annual disclosures. Economic data is generally sourced from S&P Global Market Intelligence, the Bureau of Labor Statistics, Claritas, and issuer audits and other disclosures. Local population is sourced from Claritas. Claritas estimates are point in time and not meant to show year-over-year trends. GCP--Gross county product. PCPI--Per capita personal income. EBI--Effective buying income. OPEB--Other postemployment benefits. NPLs--Net pension liabilities.

Ratings List		
New Issue Ratings		
US$2,500,000 City of La Vernia, Wilson County, Texas, Combination Tax and Limited Pledge Revenue Certificates of Obligation, Series 2026, dated: September 1, 2026, due: September 1, 2046		
Long Term Rating	AA-/Stable	
Downgraded		
	To	**From**
Local Government		
La Vernia, TX Limited Tax General Operating Pledge and Water and Sewer System Subordinate Lien	AA-/Stable	AA/Stable

The ratings appearing below the new issues represent an aggregation of debt issues (ASID) associated with related maturities. The maturities similarly reflect our opinion about the creditworthiness of the U.S. Public Finance obligor's legal pledge for payment of the financial obligation. Nevertheless, these maturities may have different credit ratings than the rating presented next to the ASID depending on whether or not additional legal pledge(s) support the specific maturity's payment obligation, such as credit enhancement, as a result of defeasance, or other factors.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at https://disclosure.spglobal.com/ratings/en/regulatory/ratings-criteria for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings referenced herein can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.