

CREDIT OPINION

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San Luis Obispo Cnty Comm College Dist, CA

Update to credit analysis

Summary

Similar to many California community college districts, rising pension costs and continued small declines in full time equivalent students (FTES) will be ongoing budget pressures for San Luis Obispo County Community College District (Aa2). However, the district is well positioned to afford these costs given its strong financial position that is expected to remain stable coupled with management's conservative fiscal practices. The district also benefits from a diverse and largely residential tax base that is poised for additional moderate growth, solid socioeconomic indicators and low debt and OPEB burdens.

Credit strengths

- » Diverse and largely residential tax base poised for moderate growth
- » Strong financial position that is expected to remain stable
- » Significant operating flexibility inherent to California community college districts

Credit challenges

- » Rising pension costs
- » No significant revenue raising flexibility; an inherent challenge for all California community college districts
- » Continued small declines in FTES

Rating outlook

Outlooks are usually not assigned to local governments with this amount of debt outstanding.

Factors that could lead to an upgrade

- » Sustained strong financial operations and maintenance of reserves at current levels
- » Ability to effectively manage pension costs

Factors that could lead to a downgrade

- » Significant decrease in reserves and cash position

- » Sizeable contraction is assessed value
- » Inability to effectively manage retirement costs

Key indicators

Exhibit 1

San Luis Obispo Cnty Comm College Dist, CA	2012	2013	2014	2015	2016
Economy/ Tax Base					
Total Full Value (\$000)	\$ 38,984,163	\$ 39,355,843	\$ 40,683,939	\$ 43,024,667	\$ 45,666,951
Full Value Per Capita	\$ 144,321	\$ 144,641	\$ 148,382	\$ 155,637	\$ 165,151
Median Family Income (% of USMedian)	116.8%	115.7%	115.9%	116.3%	116.3%
Finances					
Operating Revenue (\$000)	\$ 56,101	\$ 53,974	\$ 56,566	\$ 58,517	\$ 67,003
Fund Balance as a % of Revenues	10.5%	9.9%	10.5%	9.0%	13.0%
Cash Balance as a % of Revenues	6.4%	16.3%	8.6%	13.6%	12.5%
Debt/ Pensions					
Net Direct Debt (\$000)	\$ 26,850	\$ 20,350	\$ 19,660	\$ 83,025	\$ 82,630
Net Direct Debt / Operating Revenues (x)	0.5x	0.4x	0.3x	1.4x	1.2x
Net Direct Debt / Full Value (%)	0.1%	0.1%	0.0%	0.2%	0.2%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.5x	1.9x	2.1x	2.2x	2.1x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.2%	0.3%	0.3%	0.3%	0.3%

Source: San Luis Obispo County CCD and Moody's Investors Service

Profile

San Luis Obispo County Community College District has three locations in San Luis Obispo County. The district is governed by a five member Board of Trustees and its full time equivalent students for fiscal 2018 are projected at 8,309.

Detailed credit considerations

Economy and tax base: Diverse and largely residential tax base poised for additional moderate growth; solid socioeconomic profile

Current and projected development in addition to housing turnover will support continued moderate growth in assessed value (AV) over the medium term. The district's assessed value is largely residential (82.1% of AV) and reached \$50.9 billion in 2018. Assessed value grew 5.5% over the prior year and the five year average annual growth is solid at 5.3%. Assessed value per capita is strong at \$181,322 and its property tax base is diverse with the top ten taxpayers accounting for just 1.53% of secured AV. San Luis Obispo County's median family income, which serves as a proxy for the district, is solid at 116.3% and its unemployment rate is 3.2% which is below both the state (4.3%) and U.S. (3.9%).

Finances and liquidity: Strong financial position that is expected to remain stable

We expect that the district will continue to produce solid financial operations given management's prudent budgetary practices. And while the district's board policy includes maintaining unrestricted general fund reserves at a minimum of 6% of expenditures, management is committed to maintaining reserves within current levels. Based on unaudited fiscal 2017 figures, the district generated a \$1.3 million surplus which was primarily due to the receipt of one-time state revenues combined with savings from reductions in course offerings. Available general fund increased to \$9.8 million or a strong 18.4% of general fund revenues. The district's fiscal 2018 budget includes a \$7.6 million draw on fund balance, which includes \$6 million in contingency accounts that the district does not intend to spend. As such, management expects to end fiscal 2018 with reserves in-line with the prior year which seems reasonable given management's conservative fiscal practices.

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Similar to many community college districts, full time equivalent students have been slowly declining over the past several years. Management has implemented various enrollment strategies and is working toward growing FTES by 1% moving forward.

LIQUIDITY

The district's liquidity position in fiscal 2016 was solid with unrestricted general fund cash at \$8.7 million or 13% of general fund revenues. The district has alternative funds outside of the general fund that totaled \$3.3 million and \$2.9 million in fiscal 2016 and fiscal 2017, respectively that could be used for borrowing purposes if needed. Similar to its reserve position, we expect that the district's liquidity will remain stable.

Debt and pension: Debt burden will remain low; moderate pension burden

The district's direct debt burden will remain low given our expectation that assessed value will continue to grow at a moderate rate. Including the current offering, the district's net direct burden is low at 0.26% of AV. The current offering is the second issuance under Measure L and the district plans to issue the remaining \$125 million in authorized unissued bonds by 2024. The next offering is expected in 2021 with an issuance of \$65 million.

DEBT STRUCTURE

All of the district's long-term debt comprises of fixed current interest bonds.

DEBT-RELATED DERIVATIVES

The district has no debt related derivatives.

PENSIONS AND OPEB

The district provides employees with defined benefit pension plans through the California State Teachers' Retirement System and the California State Public Employees Retirement System. Steadily increasing contribution rates are a growing burden on the district's finances, but should remain manageable in comparison with the district's overall budget. In addition, the district deposited \$3 million into an irrevocable trust during the current fiscal year in order to help offset increasing pension costs. Future contributions have yet to be determined.

Moody's three-year average of the adjusted net pension liability (ANPL) for the district, is a moderate 2.08 times operating revenues, which equates to an A-rating score on our scorecard. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the district's reported liability information, but to improve comparability with other rated entities.

The district does not pay for other post employment benefits, rather retirees have the option to participate in the district's medical, dental or vision plans at their own cost. As such, the district's OPEB unfunded actuarial accrued liability is very low at \$417,031 or a modest 1% of payroll.

Management

California CCDs have an Institutional Framework score of A, which is moderate compared to the nation. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. California CCDs' major revenue sources are determined by the state government or, for the most part, can only be raised with voter approval. Ad valorem property tax rates cannot be increased above 1% except to meet GO bond payments, and assessed valuation growth is also generally limited to 2% annually unless a property changes ownership. Unpredictable revenue fluctuations tend to be moderate, or between 5-10% annually. Across the sector, fixed and mandated costs are generally less than 25% of expenditures. However, California has strong public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be moderate, between 5-10% annually.

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