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New Issue

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Belen Consolidated School District 2 (Valencia & Socorro Counties), NM

New Issue - Moody's Assigns A3 to Belen Consolidated SD 2, NM's $8.6M in GO, Ser. 2016 A & B; Outlook Remains Negative

Summary Rating Rationale

Moody's Investors Service has assigned a A3 to Belen Consolidated School District 2 (Valencia & Socorro Counties), NM's $5.2 million General Obligation School Bonds, Series 2016A and $3.4 million General Obligation Refunding Bonds, Series 2016B. Moody's maintains the A3 on $24.3 million in outstanding parity obligations. The negative outlook remains. Moody's has also assigned a Aa1 enhanced rating to the Series 2016 A & B GO bonds based on the New Mexico School District Enhancement Program (NMSDEP) - Post March 30, 2007.

The A3 reflects the district's weakened financial position, which caused severe cash flow challenges in fiscal 2015, resulting in use of bond proceeds to service teacher salaries. The rating further incorporates the district's declining enrollment, which is expected to stabilize in fiscal 2017; stable tax base; manageable debt burden with plans to issue in the near-term; and, weak socioeconomic position.

The Aa1 enhanced rating on the Series 2016 A & B General Obligation Bonds is based on our assessment of the NMSDEP - Post March 30, 2007 and a review of the district's proposed financing. For additional information on the program, please see Moody's report dated May 4, 2008.

Credit Strengths

» Stable tax base

» Manageable debt burden with rapid principal payout

» Changes in payroll policies, reducing risks of cash flow challenges

Credit Challenges

» Very narrow fund balance levels due to consecutive General Fund operating deficits; use

» of bond proceeds for salaries in fiscal 2015

» Declining enrollment

» Weak socioeconomic profile

Rating Outlook

The negative outlook reflects the district's limited financial flexibility and reserve position which will remain challenged over the near-term, barring significant enrollment growth or aggressive expenditure management. Further draws on General Fund balance or use of restricted reserves will likely place downward pressure on the rating.

Factors that Could Lead to an Upgrade

» Significant tax base expansion and diversification

» Trends of surpluses, rebuilding fund balance and cash reserves

» Enrollment stabilization and/or increases

Factors that Could Lead to a Downgrade

» Tax base contraction

» Inability to curb expenditure growth; further use of General Fund reserves or restricted fund balance

» Further enrollment declines

Key Indicators

Exhibit 1

Belen Cons.S.D 2 (Valencia & Socorro Cos.) NM	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value ($000)	$ 1,606,802	$ 1,653,761	$ 1,665,913	$ 1,689,302	$ 1,712,094
Full Value Per Capita	$ 52,079	$ 54,628	$ 55,236	$ 56,011	$ 56,767
Median Family Income (% of US Median)	N/A	65.9%	67.9%	67.9%	67.9%
Finances					
Operating Revenue ($000)	$ 37,074	$ 36,728	$ 36,220	$ 35,988	$ 36,832
Fund Balance as a % of Revenues	22.0%	25.1%	27.6%	27.6%	15.8%
Cash Balance as a % of Revenues	20.3%	21.5%	20.8%	28.8%	23.3%
Debt/Pensions					
Net Direct Debt ($000)	$ 24,605	$ 21,955	$ 19,845	$ 31,265	$ 34,220
Net Direct Debt / Operating Revenues (x)	0.7x	0.6x	0.5x	0.9x	0.9x
Net Direct Debt / Full Value (%)	1.5%	1.3%	1.2%	1.9%	2.0%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	2.7x	3.0x	3.2x	2.9x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	5.9%	6.5%	6.9%	6.3%

Source: District's audits; Moody's Investors Service

Recent Developments

Since our last review in June 2016, the district's debt burden has remained stable at 1.8% of fiscal 2016, inclusive of the new issuance.

Detailed Rating Considerations - Enhanced

Moody's has assigned a Aa1 enhanced rating to the Series 2016A General Obligation School Bonds and Series 2016B General Obligation Refunding Bonds, equivalent to the NMSDEP-Post March 30, 2007 programmatic rating. Ratings on individual intercept financings are based on the programmatic rating as well as the evaluation of additional rating factors. These factors include the sufficiency of interceptable revenues as determined by specific coverage tests, the timing of the state's fiscal year as it relates to scheduled debt service payment dates, and the transaction structure.

Based on the district's state equalization guarantee (SEG) funds for fiscal year 2015, interceptable state-aid provides a satisfactory 6.14 times coverage of maximum periodic debt service. Further, state revenues provide an adequate 5.63 times maximum periodic debt service coverage when SEG funds are stressed by deducting the state's final monthly state aid payment within a fiscal year. State-aid funding levels for New Mexico school districts have been stable in recent years, but have been cut mid-year to address fiscal stress at the state level within the last decade. However, this weakness is somewhat mitigated by a continued level of ample debt service coverage as previously discussed. Principal payments are scheduled for August, early in the State's fiscal year mitigating the risk of late budgets. The program requires the appointment of a third-party fiscal agent, who is required to notify the state if an intercept of SEG is required. The Bank of Albuquerque is the fiscal agent for the current sale.

Detailed Rating Considerations

Economy and Tax Base: Stable Tax Base; Declining Enrollment

The district's tax base will remain stable over the medium-term. Located 35 miles south of the City of Albuquerque (Aa1 stable), the district serves the City of Belen and surrounding community. The tax base is moderately-sized, with fiscal 2016 assessed value (AV) reported at $578 million, derived from full value of $1.7 billion. Fiscal 2017 preliminary values indicate further expansion to $598.3 million (full value of $1.8 billion), or an increase of 3.5%. The City of Belen is focused on economic development, and has recently secured a new truck stop, which will bring 50 to 70 jobs to the community. Additionally, officials report a local bank is expanding, and a hospital is considering constructing a facility in the next couple of years.

The district's socioeconomic profile is below average, with median family income of 67.9% of the US, as per the 2013 American Community Survey. Unemployment levels are elevated at 6.2% compared to the nation's 4.7% as of April 2016. Top ten taxpayers comprise a moderate 18.3% of fiscal 2016 AV, with the majority being natural gas pipeline companies.

Enrollment has declined for the past five years. Since fiscal 2012, the district has lost 522 students, or 12.9% in total. Declines are attributed to slow economic recovery, with families moving elsewhere for jobs. Fiscal 2016 enrollment 4,031, a 2.6% drop from prior year. Management is focused on retaining and recruiting students through maintaining strong academic and athletic programs, as well as upgrading and improving facilities. The district has budgeted flat enrollment for fiscal 2017. Sustained declines in enrollment, without corresponding expenditure management, has impacted the district's finances, and is the primary driver in the historic operating deficits. Future credit reviews will focus on the district's ability to manage fluctuations in student levels without resorting to use of fund balance.

Financial Operations and Reserves: Weak Financial Position Following Multiple Deficits

The district's financial position will likely remain challenged over the near-term as management focuses on reducing expenditures in light of declining enrollment. Since fiscal 2013, the district has reported sizeable deficits, severely weakening its financial flexibility. Fiscal 2015 continued this trend, ending with a $981,000 deficit, reducing General Fund balance to a narrow $601,000, or 1.8% of revenues. Notably, the district does retain healthy reserves in the Debt Service Fund, contributing to operating reserves that total $5.8 million, or a satisfactory 15.8% of revenues. Net of the debt service payment due on August 1, 2016, the district still has approximately $2 million of available operating balance.

Teachers' summer salaries were historically paid as one lump payment in May, with the district reimbursing itself with state aid (SEG) received in June, July and August. In fiscal 2013 and fiscal 2014, the district had the reserves necessary to avoid the inherent cash flow challenges this practice presents. However, in fiscal 2015, the district retained staff in excess of budget; thus, in May, the district did not have the operating cash on-hand to pay teachers. With board approval, the district utilized $3 million of bond proceeds for teachers' summer salaries. The district reimbursed their Bond Building Fund in full upon receipt of SEG in July 2015. The state auditors were aware of this interfund loan, but did not qualify the audit. Although the use of bond proceeds for operations is indication of significant financial weakness, because the Bond Building Fund was reimbursed in a timely manner, and all debt was serviced, there are no legal ramifications at this time.

A new superintendent started in fiscal 2016. The district's management is focused on right-sizing operations, as evidenced by the reduction of 20 FTEs and administrative savings of $100,000. Management is anticipating a surplus, increasing General Fund reserves to $771,000, or 2.4% of budgeted revenues.

The fiscal 2017 budget reflects use of cash balance, which is a typical practice for New Mexico school districts. In reality, the district anticipates balancing operations without use of reserves; management is focused on rebuilding fund balance to $3 million. Management is in process of reevaluating its summer payroll policies, with changes expected by the start of fiscal 2017. Furthermore, officials plan to closely monitor staffing levels, making adjustments based on enrollment. Additionally, costs that were traditionally paid for with General Fund revenues, such as capital needs, will now be funded with SB-9 monies or federal grants.

Future reviews will focus on the district's ability to manage its expenditures without use of General Fund balance and/or restricted monies. If management is unable to return to structural balance, further downward movement may be warranted.

LIQUIDITY

The district's cash position is weak. At fiscal 2015 year-end, General Fund cash was reported at $3.3 million, or 10.1% of revenues. However, reserves are inflated by $3 million borrowed from the Bond Building Fund. In reality, cash reserves are approximately $301,000, or a limited 0.9% of revenues. Operating cash, including both the General Fund and Debt Service Fund, is $8.6 million, or 23.3% of operating revenues.

Debt and Pensions: Manageable Debt Burden with Plans to Issue in the Near-term

Despite planned issuances, the district's debt burden will likely remain manageable over the mid-term given rapid principal amortization. The current debt burden is 1.8% of fiscal 2016 full value, which is above average compared to state and national medians. Principal amortization is above average with 95.0% retired in ten years. Voters approved a $16 million authorization in February 2016, and Series 2016A is the first installment. Management anticipates further issuances in 2017 and 2018.

Belen Consolidated benefits from a SB-9 capital levy, which generated $1.1 million in fiscal 2015. The two mill levy expires in 2017, and the district plans to seek reauthorization in early 2018.

DEBT STRUCTURE

All debt outstanding is fixed rate and amortizes over the long-term.

DEBT-RELATED DERIVATIVES

The district is not party to any interest rate swaps or other derivative agreements.

PENSIONS AND OPEB

The district has an above-average employee pension burden, based on unfunded liabilities for its share of the Educational Retirement Board (ERB), a cost sharing plan administered by the state. Moody's fiscal 2015 adjusted net pension liability (ANPL) for the district, under our methodology for adjusting reported pension data, is $107.4 million, or an elevated 2.92 times operating revenues. The three-year average of the district's ANPL to operating revenues is 2.94 times, while the three-year average of ANPL to equalized value is above average at 6.33%. 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 New Mexico pension plan funding structure experienced several changes with the signing of SB 115, including the reduction of a cost-of-living adjustment (COLA) and increases in employee contributions. The legislation will maintain the funding changes until the plan has reached 100% funding, which is estimated to be achieved in 2043. We believe the funding changes adopted in SB 115 will limit budgetary pressure on the district related to future pension costs.

For more information on Moody's insights on employee pensions and the related credit impact on companies, government, and other entities across the globe, please visit Moody's on Pensions at www.moodys.com/pensions.

Management and Governance

The district hired a new superintendent as of fiscal 2016; the board extended his contract through fiscal 2018. The current management team is focused on rebuilding reserves, with a target fund balance of $3 million.

New Mexico school districts have an institutional framework score of “A,” or moderate. Districts have a low ability to raise revenues because state aid provides over 95% of funding, and property taxes are subject to a small 0.5 mill cap. State aid is moderately predictable given a recent trend of increased funding and a history of funding cuts over the past decade. Expenditures, which are primarily comprised of personnel and facility costs, are moderately predicable given flat student enrollment levels. Districts have a moderate ability to reduce expenditures given above average fixed costs.

Legal Security

The bonds are secured by ad valorem taxes that are levied against all taxable property within the district without limitation as to the rate or amount.

Use of Proceeds

Proceeds from the Series 2016A bonds will be used for various capital improvements to district facilities. The Series 2016B bonds will refund Series 2008 bonds (maturities 2017 through 2022) for net present value savings of $201,000.

Obligor Profile

The district encompasses 1,081 square miles in Valencia and Socorro counties, managing 11 schools that educate approximately 4,000 students.

Methodology

The principal methodology used in the underlying rating was US Local Government General Obligation Debt published in January 2014. The principal methodology used in the enhanced rating was State Aid Intercept Programs and Financings: Pre and Post Default published in July 2013. Please see the Ratings Methodologies page on www.moodys.com for a copy of these methodologies.

Ratings

Exhibit 2

Belen Cons.S.D 2 (Valencia & Socorro Cos.) NM

Issue	Rating
General Obligation School Bonds, Series 2016A	A3
Rating Type	Underlying LT
Sale Amount	$5,200,000
Expected Sale Date	08/09/2016
Rating Description	General Obligation
General Obligation School Bonds, Series 2016A	Aa1
Rating Type	Enhanced LT
Sale Amount	$5,200,000
Expected Sale Date	08/09/2016
Rating Description	General Obligation
General Obligation Refunding Bonds, Series 2016B	A3
Rating Type	Underlying LT
Sale Amount	$3,430,000
Expected Sale Date	08/09/2016
Rating Description	General Obligation
General Obligation Refunding Bonds, Series 2016B	Aa1
Rating Type	Enhanced LT
Sale Amount	$3,430,000
Expected Sale Date	08/09/2016
Rating Description	General Obligation

Source: Moody's Investors Service

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