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Summary:

Mesquite Independent School District, Texas; General Obligation; School State Program

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Credit Profile

US\$86.235 mil Unltd Tax Sch Bldg Bnds ser 2016C dtd 11/01/2016 due 08/15/2042

<i>Long Term Rating</i>	AAA/Stable	New
<i>Underlying Rating for Credit Program</i>	AA/Stable	New
Mesquite Indpt Sch Dist GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' program rating and 'AA' underlying rating for credit program and stable outlook to Mesquite Independent School District, Texas' series 2016C unlimited-tax general obligation (GO) school building bonds and affirmed its 'AA' long-term rating and underlying rating, with a stable outlook, on the district's existing GO debt.

The program rating reflects our view of the district's eligibility for, and participation in, the Texas Permanent School Fund bond guarantee program, which provides the security of a permanent fund of assets the district can use to meet debt service on bonds guaranteed by the program. (For more information on the Texas Permanent School Fund, please see the article, published July 7, 2015, on RatingsDirect.)

An unlimited ad valorem tax secures the bonds. Officials intend to use series 2016C bond proceeds to fund various capital projects districtwide.

The rating reflects our opinion of the district's:

- Location and participation in the broad and diverse Dallas-Fort Worth metropolitan statistical area (MSA),
- Strong budgetary support from state aid, and
- Sustained very strong finances with available reserves averaging slightly above 30% of expenditures during the past four fiscal years.

We believe somewhat offsetting factors include, what we consider, the district's:

- Growth-supported operating and capital pressure; and
- Limited revenue-raising flexibility, which, however, is currently sufficient.

Economy

Mesquite Independent School District serves an estimated population of 172,685. In our opinion, median household effective buying income (EBI) is good at 94% of the national level, but per capita EBI is adequate at 74%. Market value totaled \$7.1 billion in 2017, which we consider adequate at \$40,949 per capita. Net taxable assessed value (AV) grew

by a total of 11.9% since 2015 to \$7.1 billion in 2017. The 10 leading taxpayers make up an estimated 5.9% of net taxable AV, which we consider very diverse.

The district is on the eastern border of Dallas, which provides convenient access to the deep and diverse MSA employment base. Mesquite is a largely residential city with active retail, industrial, and health care industries.

Finances

A wealth equalization formula, based on property values and average daily attendance (property wealth per student), determines state funding for all school districts. Therefore, increases or decreases in average daily attendance (enrollment) can lead to increases or decreases, respectively, in the amount of state revenue a district receives. Student enrollment for 2017 totals 41,000. Enrollment increased in each year from 2013-2017, and it is projected to increase by roughly 200-300 per year in the future.

The district's available fund balance of \$98.7 million is very strong, in our view, at 31% of general fund expenditures at fiscal year-end Aug. 31, 2015. The district reported a surplus operating result of 2.3% of expenditures in fiscal 2015.

Available reserves have averaged slightly above 30% of expenditures during the past three fiscal years. Management indicates it ended fiscal 2016 with roughly break-even operations, maintaining current reserves from fiscal 2015. For fiscal 2017, officials are projecting to add \$3 million-\$4 million to reserves despite a one-time administrative building purchase for \$7.5 million. Not accounting for any positive budget variances throughout each fiscal year, the district could use some reserves for capital needs but will not reduce available reserves below 22%-25% of expenditures, a level we still consider very strong. State aid and local property taxes accounted for 77% and 22%, respectively, of general fund revenue in fiscal 2015 and federal sources accounted for just 1%.

The fiscal 2016 property tax rate of \$1.41 per \$100 of AV was unchanged from fiscal 2015. The operations-and-maintenance tax rate is currently \$1.04 per \$100 of AV and the debt service rate is 37 cents.

Management

We consider the district's management practices strong under our Financial Management Assessment methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Highlights include management's:

- Use of historical trend analysis to project revenue and expenditures, and
- Conservative budgeting.

Management provides monthly budget reports at school board meetings, and the board can amend the budget at any meeting. Management formally monitors district investments and reports the results to the board quarterly, which is in-line with the state's conservative investment guidelines. While the district does not have a formal debt management policy, officials institute practices that manage debt issuance to minimize the tax rate effect on district residents and maximize savings in case of refunding bonds.

Debt maturities match the life of the financed asset. The district has issued variable-rate debt with swap agreements; it updates the board periodically on swap performance. The district's formal swap management policy is to govern the existing and future use of derivatives.

The capital improvement plan (CIP) corresponds to the district's planned bond election. The CIP identifies costs and projects to fund through fiscal 2020. The district's long-term financial plan includes revenue and expenditure projections in-line with meaningful assumptions regarding AV growth, enrollment, and instructional costs. While the state's school finance mechanism is subject to change through legislative action or pending litigation against the state, there is revenue flexibility to modify assumptions appropriately. We understand the district will continue to update the CIP according to its project schedule in subsequent fiscal years based on future needs.

Debt

At 6.7% of market value, we consider overall net debt moderately high, but at \$2,738 on a per capita basis, we view it as moderate. With 47% of the district's direct debt scheduled to be retired within 10 years, amortization is slower than average. Debt service carrying charges were 11.4% of total governmental fund expenditures excluding capital outlay in fiscal 2015, which we consider moderate.

We understand the district plans to issue approximately \$98 million in fall 2017, which will be the remainder of its authorized, but unissued, debt after this series 2016C issuance.

Variable-rate debt exposure is approximately 8% of the total debt portfolio, as of audited fiscal 2015. The district hedges the total amount of variable-rate debt outstanding with a floating- to fixed-rate swap. The 'A-1' short-term rating on the series 2003A variable-rate bonds reflects a liquidity facility provided by JPMorgan Chase Bank N.A., previously scheduled to expire on Dec. 13, 2016, that has had its maturity extended by two years. The district hedges this debt with a swap with JPMorgan Chase Bank to create a synthetic fixed-rate liability. Under the swap, the district is paying 4.458% or LIBOR and receiving a floating-interest rate based on the Bond Market Assn. Index. The termination rating trigger for both parties is 'BBB', which we consider remote.

The district does not carry swap insurance to cover termination payments. However, in our opinion, a termination payment, currently estimated at \$6.7 million, would not pressure liquidity. According to the fiscal 2015 audit, the general fund had \$19 million in cash and \$92.8 million in investments. Furthermore, the district could issue bonds to cover termination payments.

Pension and other postemployment benefit liabilities

The district paid its full required contribution of \$2.9 million to its pension obligations in fiscal 2015, or 0.7% of total governmental expenditures. Also, the district paid \$1.2 million, or 0.3% of total governmental expenditures, to its other postemployment benefit (OPEB) obligation in fiscal 2015. Combined pension and OPEB carrying charges totaled 0.9% of total governmental fund expenditures in fiscal 2015.

The district participates in the Texas Teachers' Retirement System (TRS), a cost-sharing, multiemployer, defined-benefit pension plan. The state's contribution to the plan in fiscal 2015 totaled \$13 million. For retiree health care benefits, the district contributes to the Texas Public School Retired Employees' Group Insurance program (TRS-Care), a cost-sharing, multiemployer, defined-benefit plan. Contributions to TRS-Care from the state were \$2.25 million in fiscal 2015.

Outlook

The stable outlook on the program rating reflects S&P Global Ratings' view of the Texas Permanent School Fund's strength and liquidity. The outlook on the underlying rating reflects our opinion of the district's steady economic growth and sustained very strong finances. Therefore, we do not expect to change the rating during the two-year outlook period.

Upside scenario

If the local economy were to continue to expand and diversify, leading to stronger wealth and income in-line with the district's higher-rated peers, we could raise the rating, assuming all other rating factors improve or remain stable.

Downside scenario

We could lower the rating if finances were to weaken materially or if overall debt were to increase to levels we no longer consider commensurate with the district's peers.

Ratings Detail (As Of October 31, 2016)

Mesquite Indpt Sch Dist PSF / CRS		
<i>Long Term Rating</i>	AAA/Stable	Current
<i>Underlying Rating for Credit Program</i>	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF / CRS		
<i>Long Term Rating</i>	AAA/A-1/Stable	Current
<i>Underlying Rating for Credit Program</i>	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF/CRS		
<i>Long Term Rating</i>	AAA/Stable	Current
<i>Underlying Rating for Credit Program</i>	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF/CRS		
<i>Long Term Rating</i>	AAA/Stable	Current
<i>Underlying Rating for Credit Program</i>	AA/Stable	Affirmed

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