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Ratings

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Summary:

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

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Credit Profile		
US$89.67 mil unltd tax sch bldg bnds ser 2020A dtd 06/01/2020 due 08/15/2045		
Long Term Rating	AAA/Stable	New
Underlying Rating for Credit Program	AA/Stable	New
US$6.37 mil unltd tax rfdg bnds ser 2020B dtd 06/01/2020 due 08/15/2025		
Long Term Rating	AAA/Stable	New
Underlying Rating for Credit Program	AA/Stable	New
US$5.54 mil unltd tax rfdg bnds ser 2020C dtd 06/01/2020 due 08/15/2032		
Long Term Rating	AAA/Stable	New
Underlying Rating for Credit Program	AA/Stable	New
Mesquite Indpt Sch Dist PSF		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF / CRS		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating and 'AA' underlying rating to Mesquite Independent School District (ISD), Texas' $89.67 million series 2020A unlimited-tax school building bonds, $6.37 million series 2020B unlimited-tax refunding bonds, and $5.54 million series 2020C unlimited-tax refunding bonds. At the same time, S&P Global Ratings affirmed its 'AA' underlying rating on the district's existing GO debt. The outlook is stable.

The 'AAA' long-term rating reflects our view of the district's eligibility for the Texas Permanent School Fund (PSF) bond guarantee program, which provides the security of a permanent fund of assets that the district can use to meet debt service on bonds guaranteed by the program. (For more information, see our report, published June 7, 2019, on RatingsDirect.)

An unlimited-ad valorem-tax pledge secures the bonds. Officials intend to use bond proceeds from series 2020A for construction, renovation, acquisition, and equipment of school buildings. Proceeds from the series 2020B and 2020C bonds will be used to refund a portion of the district's outstanding bonds for debt service savings.

Credit Overview

Mesquite ISD is part of the Dallas-Fort Worth metropolitan statistical area (MSA) and the local economy continues to expand with residential and commercial development. Management is fiscally conservative and budgeting practices generally support a very strong general fund balance annually. Although recent debt issuances have increased the overall net debt, the tax base growth has kept ratios consistent with similarly rated peers and the debt service tax is expected to remain stable.

In regards to COVID-19 and the current recession, we believe the district has sufficient reserves to mitigate any short-term effects if any unexpected cuts in revenues or unanticipated expenditures occur. While the district is conducting distance learning for the remainder of the 2019-2020 academic year, it continues to receive state funding; therefore, we expect the district's key metrics will remain stable in the near future. The district's above-average reliance on state aid could cause financial challenges in the long-term if state funding were to change as a result of COVID-19 and the recession. We will continue to monitor impacts on district revenues, specifically any changes to state funding. For more information, see "An Already Historic U.S. Downturn Now Looks Even Worse," published on April 16, 2020.

Additional rating factors include our view of the district's:

- Expanding local economy and sizable enrollment that totaled 40,379 in fiscal 2019;
- Sustained very strong finances with available reserves averaging slightly more than 30% of expenditures during the past four fiscal years;
- Strong financial management practices; and
- Moderate-to-moderately high debt with slow amortization.

Environmental, social, and governance factors

We analyzed the city's environmental, social, and governance risks relative to its economy, management, financial measures, and debt and liability profile and determined that all are in line with our view of the sector standard.

Stable Outlook

The stable outlook on the 'AAA' rating reflects our view of the strength of the Texas PSF guarantee, based on the fund's assets and performance.

Downside scenario

We could lower the rating if the district exhibits materially weakened finances or if overall net debt increases to a level that is significantly higher than that of similarly rated peers.

Upside scenario

Assuming all other rating factors remain stable or improve, we could raise the rating if the local economy were to continue to expand and diversify, leading to stronger wealth and income levels more in line with that of higher-rated peers.

Credit Opinion

Economy

Mesquite ISD serves an estimated population of 185,177. In our opinion, median household effective buying income (EBI) is good at 92% of the national level, and per capita EBI is adequate at 71%. At $50,070 per capita, the 2020 market value totaling $9.3 billion is, in our opinion, adequate. The 10 largest taxpayers make up roughly 5.1% of net taxable assessed value, representing a very diverse tax base in our opinion.

The district is largely residential but also encompasses active retail, industrial, and healthcare industries. Its proximity to Dallas provides convenient access to the deep and diverse MSA employment base. Officials noted several large residential developments in various phases of construction and home values generally range from $200,000-$400,000 although there are some homes priced higher. Additionally, commercial development continues within the district, as construction has been deemed essential by the state during COVID-19 stay at home orders. Continuous residential and commercial development has led to consistent tax base growth in prior years, with net taxable assessed value (AV) increasing 40% from fiscal years 2016-2020, averaging 9.9% annual growth over that span. Preliminary assessed valuation for 2021 is expected to come in at $10.4 billon, which reflects a 10.6% increase from the prior year. There is a strong likelihood that future AV growth will not be as strong as historical trends, but will depend on the effect of COVID-19 and the current recession. However, we believe this will not materially affect our view of the district's economy.

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. In 2020, enrollment is expected to be 39,638 students. Although the district is experiencing strong tax base growth, enrollment growth has been less than 1% over the past three years. The district's demographer is projecting that enrollment will not reflect strong growth until 2025 when children from young families moving into the district will enter the school system.

The district's available fund balance of $118.0 million is very strong in our view, at 33% of general fund expenditures at fiscal year-end (Aug. 31) 2019. The district reported a surplus operating result of 2.0% of expenditures in 2019. The district depends primarily on state aid for general fund revenue (71.8%), followed by property taxes (26%).

The district's conservative budgeting approach evidenced by its strong management team has led to a maintenance of very strong finances with general fund surpluses in four of the past five audited years. Fiscal 2019 audited results reflect a $7.1 million general fund surplus due to conservative budgeting practices for both revenues and expenditures, and $3.1 million from a sale of property. While the district adopted a $3.7 million deficit budget for fiscal 2020, official anticipate ending the year with break-even results, which we view as realistic given the district's ability to outperform its budget in the past three fiscal years.

The tax rate is $1.45 per $100 of AV of which 97 cents is dedicated for M&O and the remaining 48 cents dedicated for debt service. Following the changes related to House Bill 3, the district will further compress its M&O tax rate;

however, state funding will increase to offset the tax rate decrease.

Given the strength of the district's finances and the district's policy to maintain 22% of expenditures in reserve we believe the available fund balance will remain very strong in the near term. Additionally, the district has no plans to drawdown fund balance; therefore, we believe the district has sufficient reserves to mitigate any short-term effects from COVID-19 and the recession. If state funding were to change as a result of COVID-19 and the current recession, the district's finances could be pressured; however, officials report there has not been any communication from the state that would negatively affect them.

Management

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

Key practices and policies include:

- Management prepares the budget using two-to-five years of historical data analysis and data gathered from external sources regarding local economic trends and state funding projections.
- Monthly budget-to-actual reports are provided to the board and budget amendments can be made as needed.
- While the district does not have a formal overall debt management policy, it does have a formal swap-management policy that governs the use of existing and future derivatives. It also manages debt issuances to minimize tax effect and maximize savings on refunding's.
- The rolling five-year capital improvement plan follows the district's planned bond election.
- The long-term financial plan includes revenue and expenditure projections in line with meaningful assumptions regarding AV growth, enrollment, and instructional costs.
- The formal investment policy follows state guidelines, and management provides investment earnings and holdings reports to the board quarterly.
- The district follows a formal reserve policy that requires the maintenance of reserves at a minimum of 22% of operating expenditures, which it is currently exceeding.

Debt

At 7.8% of market value, we consider overall net debt as moderately high, but at $2,962 on a per capita basis, we view it as moderate. Amortization is slow, with 32% of the district's direct debt scheduled to be retired within 10 years. Debt service carrying charges were 13.7% of total governmental fund expenditures excluding capital outlay in fiscal 2019, which we consider moderate.

The district issued series 2003A bonds as variable-rate debt, which accounts for approximately 3% of the district's total debt portfolio. A standby bond purchase agreement (SBPA) through JPMorgan Chase Bank N.A. (A+/Stable) that extends to Dec. 31, 2020, provides liquidity for these bonds. A swap at a synthetic fixed-rate liability with JPMorgan Chase Bank hedges the debt. The termination rating trigger for both parties is 'BBB', which we consider remote. At present, there are no plans to terminate the agreement.

In total, its direct debt burden is approximately $805.3 million. The district held a successful bond election in May

2018, authorizing a total of $325 million of debt. Following this issuance, the district will not have unissued debt that has been authorized and does not intend to approach voters for additional authorization in the near future.

Pension and other postemployment benefit liabilities

We do not view pension and OPEB liabilities as an immediate source of credit pressure for Mesquite ISD, as required contributions currently make up a small portion of total governmental expenditures, and are not expected to materially increase over the next few years. Under a special funding situation, the state contributes a sizeable share of the employer contribution and carries responsibility for the proportionate share of the unfunded liability.

The district participates in the following plans:

- Teacher Retirement System (TRS), 75.2% funded with a proportional share of the net pension liability equal to $126.2 million.
- Texas Public School Retired Employees Group Insurance Program (TRS-Care), which provides health insurance coverage to members of the TRS pension plan. TRS-Care is 2.7% funded and the district has a proportionate share of the net OPEB liability of $145 million.

In fiscal 2019, the district paid its full required contribution of $3.8 million, or 0.7% of total governmental expenditures, toward its pension obligations. Also the district paid $2.2 million, or 0.4% of total governmental expenditures, toward its other postemployment benefit (OPEB) obligation. Combined pension and OPEB carrying charges totaled 1.1% of total governmental fund expenditures.

Given that contributions are done on a statutory basis that is typically lower than the actuarially determined contribution (ADC), fiscal 2019 contributions were materially below both static funding and minimal funding progress. Furthermore, the plans' 30 year, level dollar, open amortization schedule will result in slow funding progress even if actual contributions meet the ADC. Also, the 7.25% discount rate could lead to some contribution volatility. For more information on recent reforms to improve TRS funding, see the report "Texas Funds Public Schools, Staving Off Expenditure Growth For Now," published June 13, 2019 on RatingsDirect.

Related Research

- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019

Ratings Detail (As Of June 1, 2020)		
Mesquite Indpt Sch Dist GO		
Long Term Rating	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF / CRS		
Long Term Rating	AAA/A-1/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed
Mesquite Indpt Sch Dist PSF/CRS		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed

Ratings Detail (As Of June 1, 2020) (cont.)		
Mesquite Indpt Sch Dist PSF/CRS		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed