FitchRatings

Public Finance
Tax-Supported
U.S.A.

Aledo Independent School District, Texas

Ratings

Long-Term Issuer Default Rating	AA

New Issue

$123,800,000 Unlimited Tax School Building Bonds, Series 2023[a]	AAA

[a]The 'AAA' rating on the Series 2023 bonds reflects a guaranty provided by the Texas Permanent School Fund (PSF), which carries a Fitch Insurer Financial Strength Rating of 'AAA'. The bonds' underlying Long-Term Issuer Default Rating, reflecting their credit quality before consideration of the guaranty, is 'AA'.

Outstanding Debt

Unlimited Tax School Building Bonds	AA
Unlimited Tax Refunding Bonds	AA

Rating Outlook

Stable

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (May 2021)

Related Research

Fitch Rates Aledo ISD, TX's $124MM ULT School Building Bonds 'AAA' PSF/'AA' Underlying (August 2023)

Aledo Independent School District (TX) ESG Navigator (May 2019)

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New Issue Summary

Sale Date: Early to mid-August via negotiation.

Series: $123,800,000, Unlimited Tax School Building Bonds, Taxable Series 2023.

Purpose: To refund a portion of Aledo Independent School District's (the district) outstanding debt for debt service savings.

Security: The bonds are payable from an unlimited ad valorem tax levied against all taxable property within the district and are further backed by the Texas PSF bond guaranty program.

The 'AA' Issuer Default Rating (IDR) and ULT ratings reflect the district's sound economic underpinnings supported by its location near the Dallas-Ft. Worth metroplex and the highest gap-closing capacity from a combination of adequate spending flexibility and robust reserves. The ratings also reflect the district's limited independent ability to raise revenue and its somewhat elevated fixed costs and long-term liability burden.

Economic Resource Base: Aledo ISD is located in northcentral Texas and is approximately 20 miles west of Fort Worth. The district, which encompasses about 132 square miles mostly within Parker County, serves a population that exceeds 30,000. According to U.S. Census data, the district's population has increased by more than 60% since 2010. The district's proximity to Dallas and its location in the broader DFW metro area provide residents with easy access to a large and diverse labor market. Wealth and income levels for the district exceed state and national levels by a sizable amount.

Key Rating Drivers

Revenue Framework: 'a': Revenue growth has been strong, in excess of the national GDP and CPI during the 10-year period ended in 2022. Growth over the next several years will likely mirror this trend given the expectation of a solid tax base and enrollment gains, a principal driver for state funding. As is the case with most school districts, Aledo ISD's independent legal ability to raise revenues is limited by state law.

Expenditure Framework: 'aa': The district maintains adequate expenditure flexibility with a strong ability to adjust salaries. The fixed-cost burden is 13%, which Fitch Ratings considers moderate. Spending growth is expected to trend in line with revenue growth.

Long-Term Liability Burden: 'a': The long-term liability burden on resident personal income is elevated but still in the moderate range. Fitch expects the burden to decline slowly, except for personal income growth, as the absence of additional debt in the medium term and below-average amortization of existing debt includes series 2023 bonds.

Operating Performance: 'aaa': The district's history of maintaining robust reserve levels leaves it well positioned to address the current slowdown caused by the pandemic and any future cyclical downturns. Strong financial management practices underpin the district's favorable operating performance.

Rating Sensitivities

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- A sustained long-term liability position at or below 20% of personal income.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Sizable and continual declines in operating reserves, weakening the district's financial flexibility; and
- A sizable increase in the long-term liability burden to 40% or more of personal income, which Fitch considers high.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AA	Affirmed	Stable	8/8/23
AA	Upgraded	Stable	9/16/10
AA–	Revised	Stable	4/30/10
A	Upgraded	Stable	7/7/08
A–	Assigned	Stable	4/15/05

Credit Profile

Roughly 65% of Aledo ISD's tax base is residential, with a small portion of oil and gas exposure due to its location over parts of the Barnett Shale natural gas field. Tax base gains over the past several years is the result of reappraisal gains and new construction. Fiscal 2023 taxable assessed valuation (TAV) at $5.4 billion reflects a 24% increase over fiscal 2021 TAV. Industry concentration has shifted downward from previous years. While four of the district's top 10 largest taxpayers are directly engaged in the oil and gas industry, they represent about 2.5% of TAV on a combined basis, down from over 10% in previous years, a shift aided by an increase in residential development. Management expects strong residential development to continue. Based on third-party demographer projections, the district is not slated to reach build out for several decades.

Given the district's fast population growth, it has experienced strong annual enrollment gains. The five-year compound average growth rate (CAGR) through 2022 was 6.7% for ADA. Management expects enrollment to continue to grow as the tax base continues to expand. Demographers expect enrollment to total about 45,000 students at build-out. Based on publicly available data, as of October 2022 (fiscal 2023), refined ADA totaled 7,116, a 5% increase over the prior year.

Revenue Framework

Funding for public schools in Texas is provided by a combination of local (property tax), state and federal resources. The vast majority of districts, including Aledo ISD, are funded using a target revenue approach, whereby the combination of local and state funding for operations meets a predetermined per-pupil amount, which varies from district to district.

The state budgets the majority of instructional activity through the Foundation School Program (FSP), which uses a statutory formula to allocate school aid considering each district's property taxes, projected enrollment and amounts appropriated by the Legislature in the biennial budget process. The Tier 1 component of the FSP provides districts a certain level of operational funding, and the basis for most Tier 1 allotments is called the basic allotment. The basic allotment is a per-pupil dollar amount that, when multiplied by average daily attendance and adjusted for specific district student characteristics, produces a district's Tier 1 allotment.

The primary revenue source for the district is its property tax, accounting for roughly 68% of fiscal 2022 general fund revenues while state support accounted for about 31%.

The district's revenues expanded at roughly 6.4% CAGR for the 10 years ended fiscal 2022 driven primarily by strong enrollment growth. Fitch anticipates robust enrollment and tax base growth will continue to drive revenue growth in excess of national economic performance.

Recent K-12 policy changes significantly increased Texas Education Agency (TEA) funding. The increase for the fiscal 2020–2021 biennium totaled $11.6 billion (roughly 20%) to $67 billion. House Bill 3, the 2019 funding legislation, included a number of changes to K-12 education. The increased state funding resulted in an increase in the per-student basic allotment to $6,160 from $5,140; this allotment has remained in place for the current biennium, through fiscal 2023. Subsequent legislative sessions have made only modest changes to state K-12 funding levels including the 2023 session that ended May 29.

In a special session subsequent to the passage of the fiscal 2024–2025 budget, the Legislature and governor approved a significant property tax reduction bill that would add more than $13.3 billion of tax relief to $5.3 billion that was previously in state law. This plan must also be approved by voters in November. The tax reduction would be provided by reducing (compressing) local property tax rates for school districts, increasing the state-mandated school homestead exemption, prohibiting school districts from raising homestead exemptions and capping appraisal increases for properties not subject to homestead exemptions. If approved by voters, the plan does not provide an increase to the per-student basic allotment, but changes the composition of total funding by reducing local property tax revenues and backfilling with additional state funding.

While the property tax pledge securing the district's bonds is unlimited, state law requires districts to demonstrate the ability to service outstanding and any proposed debt with a debt service rate of no more than $0.50 per $100 of TAV. The district's fiscal 2023 overall property tax rate at $1.3679 per $100 of TAV includes a $0.9429 M&O rate and a debt service rate of $0.4250. The district's fiscal 2023 debt service tax rate is comfortably below the state-mandated cap for new issuances.

Expenditure Framework

The district's main general fund expenditure item is instruction (57% of fiscal 2022 spending), which is typical for school districts. Adopted budgets generally include salary increases and additional staff to address growth, as well as some use of operating revenues for one-time spending.

District spending has generally kept pace with revenue growth to accommodate student body growth. This trend is likely to continue barring any changes in district policy.

The district retains a solid degree of expenditure flexibility in labor costs given a lack of collective bargaining and its use of individual, annual employment contracts for teachers. Fixed costs are moderate at 13% of fiscal 2022 governmental expenditures. Expenditure flexibility should remain adequate provided that any future debt is proportionate to growth in revenues.

The district participates in the Texas Teachers Retirement System (TRS), a cost-sharing multiple employer system. Actual contributions are fixed in statute, while the ADC measures contributions needed to eliminate the unfunded liability in 30 years. Statutory rates have often been below the ADC, with the resulting funding period slipping beyond the 31-year statutory maximum. Contributions, and the NPL, are shared by school districts and the state.

TRS lowered its discount rate to 7.25% from 8.00% in 2019 and to 7.00% in 2022. In 2019, the Legislature raised state, employer and employee rates over five years to bring the funding period within the legal maximum threshold; the funding period is 23 years as of the 2021 valuation. Like all Texas school districts, the district is vulnerable to future state policy changes that shift more of the contributions and liabilities onto districts, as well as to TRS' ability to achieve its funding assumptions over time.

Long-Term Liability Burden

Fitch estimates the long-term liability burden at roughly 20% of personal income. The debt portion of the long-term liability burden is comprised primarily of direct debt (71% of total) followed by overlapping debt (29%).

In May 2023, voters approved a $123.8 million bond program to finance the construction of a new elementary school, land acquisition, as well as the repurposing and expansion of pre-existing facilities. The current bond issuance will exhaust the district's voter-authorized debt. While the district does not expect to approach voters for additional bond authorization over the next year or so, continuing rapid enrollment growth trends may call for additional bond capacity in the medium term.

The district provides pension benefits exclusively through its participation in the TRS. Under GASB 67, TRS' assets covered 89% of liabilities as of the system's fiscal 2022 audit, a ratio that falls to 76% using Fitch's standard 6% return assumption, instead of the 7% used by TRS. Reported system figures are based on a lower discount rate implemented by TRS in 2018 and the statutory increase in contribution rates approved in 2019. Higher than expected contributions have eliminated the depletion date reported by TRS in fiscal 2018, which school districts reported in their fiscal 2019 audits, and have brought forecast amortization to 30 years.

Statutory contribution increases strengthen the likelihood of funding improvement, but future progress ultimately depends on whether actual TRS performance matches actuarial assumptions over time. At present, the state carries just over one-half of TRS' employer NPL on behalf of school districts and pays roughly one-half of the contribution.

Operating Performance

Given Aledo ISD's robust fund balance position and ability to adjust expenditures, Fitch believes that the district has the capacity to reasonably absorb potential financial pressure resulting from future economic downturns without impairing its strong financial resilience.

Officials adopted a $2.4 million general fund deficit for fiscal 2023. Management expects year-end results to be close to budgeted expectations. Fiscal 2024 will commence on Sept. 1, 2023 and officials are scheduled to adopt the budget on Aug. 28, 2023. According to representatives, preliminary budget projections reflect a slight drawdown; however, this is subject to change as the district has several days to present an official propose budget. Fitch expects the district will continue to prudently manage its costs in order to maintain operating performance that is consistent with the current rating.

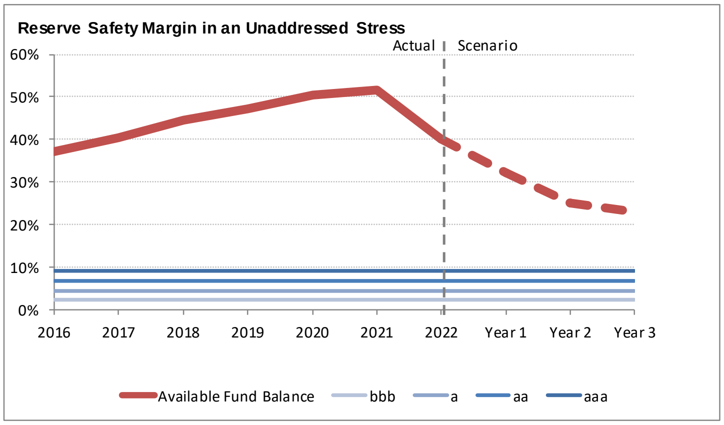
ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch’s ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Aledo Independent School District (TX)

Scenario Analysis

Ver 48



Analyst Interpretation of Scenario Results

Since at least fiscal year-end 2016, the district has maintained an unrestricted general fund balance of at least 37% of operating expenditures. Fiscal 2022 audited results reflect a general fund drawdown of about $2.5 million, due to lower-than-expected ADA and sizable increases to transportation and insurance costs. The district opened its second middle school campus and one-time costs related to the new school site also contributed to the drawdown. In spite of the deficit, the district's financial cushion remains solid with the fiscal 2022 unrestricted general fund balance totaling $29 million, net of transfers, and accounting for 40% of operating expenditures.

Scenario Parameters:			Year 1	Year 2	Year 3
GDP Assumption (% Change)			(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)			2.5%	2.5%	2.5%
Revenue Output (% Change)	*Min Y1 Stress:* **-1%**	*Case Used:* **Moderate**	(1.1%)	3.2%	7.6%
Inherent Budget Flexibility				Limited	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2016	2017	2018	2019	2020	2021	2022	Year 1	Year 2	Year 3
Total Revenues	43,013	43,052	50,474	53,685	60,998	64,631	69,870	69,078	71,313	76,739
% Change in Revenues	-	0.1%	17.2%	6.4%	13.6%	6.0%	8.1%	(1.1%)	3.2%	7.6%
Total Expenditures	41,408	41,634	46,497	50,580	56,206	60,503	72,300	74,108	75,961	77,860
% Change in Expenditures	-	0.5%	11.7%	8.8%	11.1%	7.6%	19.5%	2.5%	2.5%	2.5%
Transfers In and Other Sources	46	22	16	51	35	6	-	-	-	-
Transfers Out and Other Uses	-	-	-	71	100	600	102	105	107	110
Net Transfers	46	22	16	(20)	(65)	(594)	(102)	(105)	(107)	(110)
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus/(Deficit) After Transfers	1,650	1,440	3,993	3,085	4,726	3,534	(2,533)	(5,135)	(4,754)	(1,231)
Net Operating Surplus/(Deficit) (% of Expend. and Transfers Out)	4.0%	3.5%	8.6%	6.1%	8.4%	5.8%	(3.5%)	(6.9%)	(6.3%)	(1.6%)
Unrestricted/Unreserved Fund Balance (General Fund)	15,337	16,778	20,771	23,855	28,333	31,613	29,080	23,945	19,191	17,960
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	15,337	16,778	20,771	23,855	28,333	31,613	29,080	23,945	19,191	17,960
Combined Available Fund Bal. (% of Expend. and Transfers Out)	37.0%	40.3%	44.7%	47.1%	50.3%	51.7%	40.2%	32.3%	25.2%	23.0%

Reserve Safety Margins	Inherent Budget Flexibility				
Moderate	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	18.1%	9.1%	5.7%	3.4%	2.3%
Reserve Safety Margin (aa)	13.6%	6.8%	4.5%	2.8%	2.0%
Reserve Safety Margin (a)	9.1%	4.5%	2.8%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.4%	2.3%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's scenario analysis assumes the GDP and expenditure growth sequence shown in the 'Scenario Parameters' section. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

SOLICITATION & PARTICIPATION STATUS

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For information on the participation status in the rating process of an issuer listed in this report, please refer to the most recent rating action commentary for the relevant issuer, available on the Fitch Ratings website.