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Clovis Municipal S.D. 1 (Curry County), NM

Update to credit analysis

Summary

Clovis Municipal School District (MSD; Aa3), NM's credit profile is stable overall. The district's financial position is healthy, especially relative to state peers. Fiscal 2018 is expected to end with a surplus due to a one-time payout from the Public Education Department (PED), which was not budgeted. The tax base is moderately-sized, and is anchored by Cannon Air Force Base, which employs around 10,000. The direct debt burden is manageable, and principal amortization is rapid. We note the credit profile is challenged by an elevated pension burden, and annual contributions remain unfavorably below the tread water level.

Credit strengths

» Stable tax base anchored by Cannon Air Force Base (AFB)

» Manageable direct debt burden

Credit challenges

» Elevated pension burden and weak annual pension contributions

Rating outlook

Moody's generally does not assign outlooks to local government credits with this amount of debt outstanding.

Factors that could lead to an upgrade

» Trend of surplus operations, adding to fund balance and reserves

» Significant tax base expansion

» Material reductions to the pension and fixed cost burdens

Factors that could lead to a downgrade

» Fiscal 2018 audited results that are not in line with reported performance

» Deterioration of reserves and fund balances

» Sustained tax base contractions

» Increases to the pension and fixed cost burdens that are not comparable to peers

Key indicators

Exhibit 1

Clovis Municipal S.D. 1 (Curry County), NM	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$2,008,556	$2,109,391	$2,162,595	$2,283,528	$2,378,920
Population	46,104	46,104	47,233	47,233	40,000
Full Value Per Capita	$43,566	$45,753	$45,786	$48,346	$59,473
Median Family Income (% of US Median)	78.4%	78.4%	75.3%	75.3%	75.3%
Finances					
Operating Revenue ($000)	$61,190	$62,418	$63,853	$65,648	$63,554
Fund Balance ($000)	$11,842	$8,173	$12,712	$14,421	$9,634
Cash Balance ($000)	$9,567	$12,734	$13,724	$14,417	$13,076
Fund Balance as a % of Revenues	19.4%	13.1%	19.9%	22.0%	15.2%
Cash Balance as a % of Revenues	15.6%	20.4%	21.5%	22.0%	20.6%
Debt/Pensions					
Net Direct Debt ($000)	$32,146	$39,640	$41,385	$38,795	$41,170
3-Year Average of Moody's ANPL ($000)	$186,091	$206,577	$200,529	$206,749	$230,798
Net Direct Debt / Full Value (%)	1.6%	1.9%	1.9%	1.7%	1.7%
Net Direct Debt / Operating Revenues (x)	0.5x	0.6x	0.6x	0.6x	0.6x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	9.3%	9.8%	9.3%	9.1%	9.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	3.0x	3.3x	3.1x	3.1x	3.6x

Source: District's audits; Moody's; US Census (MFI)

Profile

The district is located in Clovis (issuer rating Aa3), 100 miles northwest of Lubbock, 106 miles southwest of Amarillo, and 220 miles east of Albuquerque (Aa2 negative), and serves approximately 8,000 students.

Detailed credit considerations

Economy and tax base: moderately sized base anchored by Cannon AFB

The district's tax base will likely continue expanding over the mid-term driven by ongoing residential and commercial development. The district is located in Curry County (Aa3), the state's agricultural center, approximately 220 miles east of Albuquerque (Aa2 negative) and 100 miles northwest of the city of Lubbock, Texas (Aa2 stable). The district serves Clovis (Aa3), which is the county seat. The local economy benefits from the presence of Cannon Air Force Base (AFB), which employs around 9,800 military and civilian personnel. The district's assessed value (AV) has grown steadily since 2004, resulting in a fiscal 2018 AV of $807.1 million, derived from a full value (FV) of $2.42 billion. Preliminary values for fiscal 2019 indicate further expansion to $838 million, derived from a moderately-sized full value of $2.52 billion.

Officials report that development continues in the local area: several single-family homes are going up near the district's new elementary school; two new hotels are under construction; and, Southwest Cheese and BNSF Railway are expanding, adding many new jobs. There is possibility that a race track and casino will be built in Clovis, which would attract tourists from nearby Lubbock and Amarillo. New Mexico's Racing Commission will make a decision in early October 2018.

Resident incomes are below national average, with median family income of 71.8% of the US (2016 ACS). Resident incomes may be artificially low due to the significant presence of military personnel.

Enrollment has declined modestly since fiscal 2012. Per the New Mexico Public Education Department, fiscal 2018 enrollment was 8,026, or a 2.43% reduction from prior year. Officials attribute enrollment fluctuations to the Cannon Airforce Base: young families relocate to Clovis for a short amount of time, enrolling their students in elementary school, only to leave a few years later. Regardless, the district has successfully managed their finances despite enrollment loss. Management has budgeted for flat enrollment over the next several years.

Financial operations and reserves: stable financial position, with surplus expected in fiscal 2018

The district's financial position will likely remain stable given conservative budgeting practices, and a management team focused on retaining cash. The district was negatively impacted by the state's mid-year cuts, which was the main driver of fiscal 2017's $1.3 million deficit, reducing General Fund balance to $10.4 million, or 17.5% of revenues.

Fiscal 2018 is a reportedly positive year, with the district increasing its General Fund balance by around $850,000 (unaudited, cash basis), to $10.1 million. Officials explain that the Public Education Department (PED) implemented two mid-year funding adjustments, awarding the district an additional $1 million in funding, which was not budgeted. Further, around 15 to 18 positions were vacant by year-end, resulting in cost savings.

The fiscal 2019 budget is balanced with cash reserves, a practice required by the Public Education Department. Despite slight enrollment declines, revenues will increase given tenure and education of teaching staff (a variable in the funding formula). Officials report that they shifted around $500,000 in maintenance costs out of the General Fund to their capital fund. All up, the General Fund is expected to remain flat year over year.

LIQUIDITY

General Fund cash is stable. At fiscal 2017 year-end, cash was $9.2 million, or 15.5% of revenues. Based on unaudited fiscal 2018 results, operational cash increased by approximately $850,000.

Debt and pensions: manageable direct debt burden, but elevated pension burden

Despite plans to issue additional debt in the near-term, the district's debt burden will remain manageable because it is capped by statute at 2% of full value. At 1.9% of fiscal 2018 full value, the district's debt burden is slightly above state and national medians. Principal payout is above average, with 89.3% retired in ten years. The district plans to issue $8 million in new money in 2019 and 2020. Debt is structured so as to allow the layering in of additional bonds without adjustment to tax rates.

DEBT STRUCTURE

The district has $47.3 million in outstanding, fixed-rate obligations. The debt service schedule is flat, with all debt retired by 2034.

DEBT-RELATED DERIVATIVES

The district is not party to any derivative agreements.

PENSIONS AND OPEB

The district has a high employee pension burden, based on unfunded liabilities for its share of the Educational Retirement Board (ERB), a cost sharing plan administered by the state. Clovis' annual contributions into the plan have been at the statutorily required amount, which is well below the actuarially required amount, a situation which has driven the large unfunded liability. Moody's fiscal 2017 adjusted net pension liability (ANPL) for the district, under our methodology for adjusting reported pension data, is $274 million, or an elevated 4.07x operating revenues.

In addition to a steadily increasing ANPL, the district's tread water gap has widened over the last two years from 2.44% in fiscal 2015 to 4.99% in fiscal 2017. The “tread water” indicator measures the annual contributions required to prevent the reported net pension liability from increasing. That is, it is the amount that the district would have to pay on an annual basis to ensure the unfunded liability does not increase. In fiscal 2017, pension contributions of $5.6 million were below the tread water indicator of $8.9 million, a credit negative. Currently, the district is able to pay the statutorily-required contribution without impairing operations. Further, unlike many of its New Mexican peers, the district has a sizeable General Fund balance, which helps to mitigate the gap between contributions and tread water. However, the district's reserve position is not so ample as to mitigate multiple years of underfunding.

Going forward, in order for ERB to meet its obligations, contributions will have to increase, which would place pressure on the district's reserves. Given New Mexico school districts' reliance on the state for its operating revenue, it is possible that the legislature would appropriate additional funds to cover increased pension costs; however, the state's response to reform is unclear at this time.

The district's fiscal 2017 fixed costs, including debt service, pension and OPEB contributions, were a manageable 14.2% of operating revenues. Inclusive of the treadwater payment, fixed costs increase to a still manageable 19.2%.

Management and governance: institutional framework score of Baa

The district is governed by a five-member board. Members serve without compensation for four-year terms. The Superintendent is selected by and serves at the discretion of the board. Of note, the district is committed to maintaining a cash reserve of at least 10% of budgeted operating expenditures.

New Mexico School Districts have an Institutional Framework score of Baa, which is low. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenue source, state aid or SEG, is subject to a cap, which cannot be overridden (in that, the State determines annual appropriations based primarily on student enrollment). Reliance on state funding limits revenue-raising ability; school districts do not collect property taxes for operation. 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, New Mexico School Districts enter into annual teaching contracts, which can limit the ability to cut expenditures over the near-term. Unpredictable expenditure fluctuations tend to be moderate, between 5-10% annually.

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