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San Juan Junior College District, NM

Update to credit analysis

Summary

San Juan Junior College District, NM (SJJC, GOLT Aa2) has a stable credit profile. The tax base is large and stable, despite exposure to the energy sector. The future of two large coal-fired power plants in the county is uncertain; however, the City of Farmington provides economic diversity, and the college has revenue-raising flexibility in the event of tax base volatility. The college's financial position is strong, with an addition to fund balance expected for fiscal 2018. SJJC's direct debt burden is modest, and management has no plans to issue again in the near-term. Moody's notes that the district has entered into a P3 agreement for student housing; if we consider the developer's financing costs to be an “on-balance sheet” liability, the college's debt burden does increase, but remains very modest. The credit profile also reflects a recent trend of enrollment declines and an above average pension burden, reflective of the district’s participation in a state-wide, cost-sharing plan (ERB).

Credit strengths

» Large tax base anchored by City of Farmington

» Low direct debt burden

Credit challenges

» Above average pension burden

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

» Substantial tax base expansion;

» Enrollment stabilization

» Reductions to the pension burden and fixed costs

Factors that could lead to a downgrade

» Sustained depletion of financial reserves

» Significant tax base contraction

» Further increases to the pension burden and fixed costs

Key indicators

Exhibit 1

San Juan Junior College, NM	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$12,347,119	$11,088,124	$11,211,157	$12,079,212	$10,912,865
Population	128,476	127,358	125,133	122,537	122,537
Full Value Per Capita	$96,104	$74,056	$89,594	$98,576	$89,058
Median Family Income (% of US Median)	89.2%	88.9%	89.0%	85.1%	85.1%
Finances					
Operating Revenue ($000)	$72,680	$76,779	$81,801	$72,817	$70,553
Fund Balance ($000)	$70,555	$73,333	$21,245	$20,702	($2,819)
Cash Balance ($000)	$17,073	$13,508	$14,834	$16,979	$21,315
Fund Balance as a % of Revenues	97.1%	95.5%	26.0%	28.4%	-4.0%
Cash Balance as a % of Revenues	23.5%	17.6%	18.1%	23.3%	30.2%
Debt/Pensions					
Net Direct Debt ($000)	$14,779	$13,100	$10,941	$15,850	$12,110
3-Year Average of Moody's ANPL ($000)	$0	$0	$141,970	$155,112	$196,899
Net Direct Debt / Operating Revenues (x)	0.2x	0.2x	0.1x	0.2x	0.2x
Net Direct Debt / Full Value (%)	0.1%	0.1%	0.1%	0.1%	0.1%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.0x	0.0x	1.7x	2.1x	2.8x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.0%	0.0%	1.3%	1.3%	1.8%

The net asset position is used as a proxy for fund balance
Source: District's audits; Moody's; US Census (MFI)

Profile

The college is a political subdivision of the State of New Mexico organized for the purpose of operating and maintaining a program of postsecondary education which provides coursework leading to certificates and associate degrees. The district's tax base is coterminous with San Juan County. For the 2017-2018 academic year, the unduplicated headcount enrollment was 10,678 and full-time equivalent enrollment was 4,592.

Detailed credit considerations

Economy and tax base: sizeable base serving the Four Corners region

San Juan College is located in San Juan County (Aa3 issuer rating), and serves the City of Farmington and the broader Four Corners region. The county is the largest producer of natural gas and fourth largest producer of oil in the state. Given the concentration, the district's tax base, which is coterminous with the county's, has been volatile due to swings in commodity prices. For example, sizeable assessed value (AV) contractions of 21.2% and 10.2% were incurred in fiscal 2011 and fiscal 2014, respectively. During the most recent decline in oil and gas prices, the district saw contractions of 8.8% and 2.6% in fiscal 2017 and fiscal 2018, respectively, although AV remained sizeable at above $3 billion (derived from a full value of over $10 billion). In fiscal 2019 full value expanded by 3.9% to $11.1 billion. With natural gas values on the upswing, officials do not anticipate further tax base declines in the near-term. Moody's notes the district has endured assessed valuation fluctuations in the past, and has responded with tax rate adjustments and/or tuition increases. Concentration in oil and gas is somewhat offset by Farmington's local economy, which is diverse, and boasts a range of retail businesses and restaurants. Additionally, San Juan Regional Medical Center (A3 STA) is a major employer with nominal competition.

The district's top ten taxpayers make up a moderate 21.7% of fiscal 2019 assessed value. The top two, Arizona Public Service Company (APS; A2 stable) and Public Service Company of New Mexico (PNM; Baa2 stable), each manage coal-fired power plants: Four Corners Power Plant and San Juan Generating Station, respectively. APS has already closed three of its five units, and invested $350 million to make the remaining plants EPA compliant. In April 2017, PNM announced plans to pull out of the San Juan Generating Station by 2022. If the Station were to close, around 700 jobs would be lost, as well as $750 million in AV.

Per our March 2018 San Juan County report, other businesses are investing in the region. Western Energy Partners is currently in the process of developing a 774 megawatt (MW) combined cycle gas fired power plant, an estimated $1.2 billion investment. The facility, known as the Clean Path Energy Center, has a projected starting date of operations in 2021. Furthermore, BP PLC (A1 stable) announced in August 2017 the discovery of a highly productive natural gas field in the Mancos Shale, part of the larger San Juan Basin. This discovery could add significantly to the tax base. Hilcorp Energy I, L.P. (Ba1 stable) has also acquired assets in the San Juan Basin in recent years and has indicated plans to increase drilling activity. If fully realized, these opportunities will provide tax base stability despite downward pressure relating to the potential closure of the San Juan Generating Station.

The district's median family income is below average at 85.1% of the US (2016 ACS). Unemployment levels were slightly elevated at 5.3% compared to the nation's 3.9% (August 2018).

SJJC is the fifth largest community college district in New Mexico based on headcount of approximately 11,000. The college has minimal competition in the immediate region. Since fiscal 2015, enrollment has declined by 11% (headcount) or 3.6% (annual FTEs), which is not atypical for community colleges where enrollment is inversely correlated with the economy. Officials anticipate an additional 2.5% decline in FTEs for fiscal 2019. The district has recently focused on making education more accessible by forming seven career pathways; building partnerships with businesses to create a job pipeline; and investing in student housing. Based on these initiatives, the college anticipates enrollment to stabilize in fiscal 2020 and fiscal 2021.

Financial operations and reserves: stable financial position despite declines in net asset position

Despite recent declines to the net asset position, driven by GASB 68 and 74, the college's operating position remains healthy.

Fiscal 2017 and fiscal 2018 saw declines to the net asset position. This was driven in large part by state aid cuts (approximately one-third of the budget) and recognition of pension and OPEB liabilities. As the state struggled to balance its own budget, it made a 5% mid-year cut to higher education in fiscal 2017, and reduced aid by another 5% in fiscal 2018. Further, due to changes in accounting standards, the district recognized a $59 million pension liability in fiscal 2015, which has subsequently grown to $111 million as of fiscal 2018 (unaudited), and an OPEB liability of $20 million in fiscal 2017, which declined slightly to $18.3 million in fiscal 2018 (unaudited). As such, the net asset position was negative $2.8 million in fiscal 2017, and fell again to negative $13.1 million in fiscal 2018 (unaudited).

In practice, management relies on fund accounting (rather than full accrual). The primary operating fund of the college is the instruction and general (I&G) fund. Fiscal 2018 ended with $18.4 million in fund balance, up $3 million from the prior year. Management attributes the increase to several factors, specifically vacancy savings, more adjunct contracts (which are less expensive than FTEs) and changes to the college's healthcare plan. Since fiscal 2014, the district has added $7.2 million to its I&G fund balance.

The fiscal 2019 budget is balanced with no appropriation of reserves. The college has assumed state aid will increase by $600,000 and property taxes by 1%. Although enrollment is projected to decline by 2.5%, the college increased tuition, effective Fall 2018. In light of recent volatility in state revenues, the college adopted a new tuition policy in April 2018 pursuant to which tuition will increase every other year per formula with the goal of providing revenues sufficient for college operations. In effect, management hopes to use tuition to reduce the impact of fluctuations in aid and property taxes. Currently, tuition represents approximately 10% of the operating budget.

LIQUIDITY

The college's cash position is stable. Fiscal 2017 ended with $21.3 million in cash and investments representing 30.2% of operating revenues. Based on unaudited results, management reports that cash remained flat or increased modestly in fiscal 2018.

Debt and pensions: modest debt burden with no plans to issue in the near-term; average pension and fixed cost burdens

The district's direct debt burden will remain low given absence of plans to issue in the near-term. At 0.1% of fiscal 2019 full value, the burden is modest, and will decline based on rapid principal amortization. The district does not have any remaining authorized unissued debt, and does not plan to approach voters for additional authorization at this time.

In July 2018, the college's board of trustees entered into a P3 agreement to build on-campus student housing. Under the agreement, the college is leasing property to a developer who plans to issue approximately $23 million in bonds through a not for profit corporation to finance the project. The debt will be repaid from rental revenues over a 32-year period. Upon final maturity, the property will revert to the college. Per discussion with college officials, SJJC is not responsible for the debt in any way. However, given the mechanics of the agreement, and the strong affiliation between the college and the P3, there is an argument that this is an "on-balance sheet" liability: if included, the debt burden would increase to a still-manageable 0.34% of full value and 0.5 times operating revenues.

DEBT STRUCTURE

Inclusive of the series 2019 bonds, the district will have $14.6 million in outstanding GOLT obligations. Principal amortization is rapid with 81% retired in ten years.

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. The college's annual contributions into the plan have been at the statutorily required amount, which is below the actuarially required amounts, which has driven increases to the unfunded liability. Moody's fiscal 2017 adjusted net pension liability (ANPL) for the district, under our methodology for adjusting reported pension data, is $196.9 million, which is an above average 2.79 times operating revenues.

The district's treadwater gap has increased and represented an above average 3.6% of operating revenues in fiscal 2017. The "tread water" indicator measures the annual contributions required to prevent the reported net pension liability from increasing if plan assumptions are realized. 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 $3.9 million were below the tread water indicator of $6.4 million, a credit weakness. Currently, the district is able to pay the statutorily required contribution without impairing operations.

The district's fiscal 2017 fixed costs, including debt service, pension and OPEB contributions, were a manageable 8.9% of operating revenues. Including the treadwater payment, fixed costs increases to 12.5%, which is average for the sector.

Management and governance: institutional framework score of Aa

SJJC is governed by a seven member board that serve six-year terms. Administration is stable, with minimal turnover. The college is accredited by the Higher Learning Commission of the North Central Association of Colleges and Schools. The district received reaffirmation of accreditation through 2024.

New Mexico CCDs have an Institutional Framework score of Aa, which is high. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenue sources are state aid and property taxes, with the latter subject to a statutory cap $5.00 (per $1,000 AV) that cannot be overridden at the local level. If the CCD's operating levy is below the cap, they can increase it with voter approval. Property tax revenues are limited to an annual increase of 5%, which still provides for significant revenue-raising headroom. 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 has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

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