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CREDIT OPINION
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Grossmont-Cuyamaca Community College District, CA

Update to credit analysis

Summary

Grossmont-Cuyamaca Community College District (Aa2 Stable) continues to benefit from its participation in the strong and growing San Diego metropolitan economy, which is fueling ongoing property tax growth, adding to the district's large $48 billion tax base. The district also benefits from an improved financial profile and a positive enrollment trend as well as significant outside grant funding. These strengths are partly offset by an above average debt burden and future pension cost increases that are facing all community college district's in California.

Credit strengths

» Large and growing tax base

» Location within vibrant San Diego metropolitan economy

» Positive enrollment trend

Credit challenges

» Below average financial reserves for its rating level

» Rising pension costs common across all Californian Community Colleges

» Elevated debt levels compared to Community College district medians

Rating outlook

The stable outlook reflects our expectation that the district will continue to benefit from strong tax base growth and a solid financial profile. We also expect the district will benefit from continued enrollment growth.

Factors that could lead to an upgrade

» Sustained growth in financial reserves consistent with the higher rating category

» Successful management of future pension cost increases

» Material improvement in the district's socioeconomic indicators

Factors that could lead to a downgrade

» Protracted decline in the district's tax base

» Material weakening of the district's financial position, including a narrowing of reserves

Key indicators

Exhibit 1

Grossmont-Cuyamaca CCD, CA	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$38,077,068	$38,533,511	$40,159,459	$42,362,498	$44,518,597
Population	468,398	476,922	483,248	483,248	483,248
Full Value Per Capita	$81,292	$80,796	$83,103	$87,662	$92,124
Median Family Income (% of US Median)	106.1%	107.3%	107.0%	107.0%	107.0%
Finances					
Operating Revenue ($000)	$108,026	$114,170	$146,294	$175,537	$185,236
Fund Balance ($000)	$108,050	$116,815	$151,531	$158,444	$183,641
Cash Balance ($000)	$15,256	$25,887	$39,509	$56,155	$63,827
Fund Balance as a % of Revenues	21.3%	9.1%	66.2%	17.8%	15.9%
Cash Balance as a % of Revenues	14.1%	22.7%	27.0%	32.0%	34.5%
Debt/Pensions					
Net Direct Debt ($000)	$206,700	$257,409	$247,033	$264,372	$264,599
3-Year Average of Moody's ANPL ($000)	$179,428	$209,321	$198,896	$194,685	$228,412
Net Direct Debt / Full Value (%)	0.5%	0.5%	0.5%	0.5%	0.5%
Net Direct Debt / Operating Revenues (x)	1.9x	1.9x	1.9x	1.9x	1.9x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	1.0%	1.1%	1.2%	1.2%	1.3%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.5x	0.5x	0.5x	0.5x	0.5x

Source: Moody's Investors Service

Profile

Grossmont-Cuyamaca Community College District is located in the eastern half of San Diego County and serves a population of approximately 483,000 in the cities of El Cajon, La Lesa, Lemon Grove and Santee as well as unincorporated areas of the county. It operates two colleges, Grossmont College and Cuyamaca College with a combined resident FTES in fiscal 2017 of 19,948.

Detailed credit considerations

Economy and tax base: Substantial tax base poised for future growth

Grossmont-Cucyamaca CCD has a substantial $48 billion tax base that we expect will show solid growth in coming years as it continues to benefit from both the strong San Diego metropolitan economy and new property development in the cities of El Cajon, La Mesa and Santee. Fiscal 2018 saw assessed value grow by 6.2%, an improvement on the five year average annual growth of 4.8%. The district's tax base is very diverse, with the top 10 taxpayers comprising only 2.9% of the district's total AV. These taxpayers are a mix of apartments, shopping centers and commercial operations.

Socioeconomic indicators within the district are moderate for the rating category, with a Median Family Income of 107% of the US median and a full value per capita of just under $100,000, below the median of $107,000 for Aa2 rated Californian CCDs. Unemployment in San Diego county, a proxy for the district, is low at 3.2% compared to California at 4.2% and the nation as a whole at 4.1%.

Financial operations and reserves: solid and steady financial position, improved enrollment trend

The district's financial position is expected to remain steady as the district continues to benefit from enrollment growth and an improved state funding environment. Total general fund balance has increased from $11.9 million in 2012 to 32.7 million at the end of fiscal 2017. This equates to 19.8% of revenues, in line with the Aa2 national median for CCDs of 17.4%.

The district projects a $9.6 million spend down in reserves in fiscal 2018 (compared to a $25.0 million budgeted drawdown) as it spends accumulated state one time revenues and grant funds, which will leave it reserves of $23.0 million or a sufficient, if below the Aa2 median, 13.2% of revenue.

The district uses a fund allocation budgeting model in which it budgets to spend its reserves excluding 6.5% which is set aside as a contingency. Were the district to actually spend its reserves as budgeted, it would apply pressure to the rating since the remaining contingency would be well below the median for the sector. However, the district has historically outperformed budgeted expectations resulting in the maintenance of reserve balances that have averaged 15% over the last five years. We expect this trend to continue in fiscal 2018 and 2019 and produce a reserve in line with the recent average.

The enrollment in the district has been positive, with the district growing FTES by 11.8% or nearly 2,100 since its post recession low in 2013. While the district projects small declines in fiscal 2019, we expect that the district's diverse and growing list of program offerings as well as the implementation of the Grossmont-Cuyamaca College promise, a program offering a years free tuition to local high school seniors, will help stabilize enrollment. The district has yet to close salary negotiations for the 2018 fiscal year, but we do not expect the outcome of these negotiations will materially impact the districts credit profile.

LIQUIDITY

The district's liquidity position has improved significantly in recent years to $46.1 million on a general fund basis or 28% of revenue, compared to 4.2% in 2013. In addition, the district has over $7.8 million available in funds outside the general fund, including a capital outlay fund and funds held by the county for OPEB, that are usable by the general fund without repayment if required.

Debt and pensions: Elevated debt levels, moderate pensions compared to peers

The district's debt is manageable at 0.8% of assessed value after the most recent issuance, but elevated when compared to national Aa2 Community College District medians of 0.4%. Our expectation is that the continuation of the district's recent assessed valuation growth will keep the district's debt burden manageable even when incorporating the district's future debt plans. After the most recent issuance the district will have $192 million remaining authorization.

DEBT STRUCTURE

The district's debt is a mix of current interest and capital appreciation bonds with a final maturity, post the current issuance, of 2047.

DEBT-RELATED DERIVATIVES

The district has no debt-related derivatives.

PENSIONS AND OPEB

District employees participate in the California Public Employee Retirement System (CalPERS) and California State Teachers Retirement System (CalSTRS). The Moody's adjusted net pension liability (ANPL) for the district, under our methodology for adjusting reported pension data was $345.3 million in fiscal 2017. The three year average of adjusted net pension liability (ANPL) was moderate at 1.23 times operating revenue.

Moody's ANPL reflects certain adjustments we make to improve the comparability of reported pension liabilities. The adjustments are not intended to replace the district's reported liability information, but to improve the comparability with other rated entities.

The district's pension contribution in fiscal 2017 of $10.5 million falls somewhat short of our 'tread water' indicator of $12.5 million. The 'tread water' indicator measure the annual district contribution required to prevent the reported net pension liability from growing under reported assumptions. Contributions above this level cover all net pension liability interest and reduce a portion of the total outstanding liability; this is stronger from a credit perspective than contribution below the tread water level.

Similar to most Californian Community College Districts, pension costs will become an increasing budget pressure as rates increase over the next several years. As plan of its plan to address these increases, the district holds $8.1 million in a separate fund which is uses to offset the annual increases in CalPERS contribution requirements which lessens the pressure of these increases on the general fund. The district has also established an irrevocable trust for its OPEB liabilities, which has $8.1 million in it as of the end of fiscal 2017, or approximately 41% of the districts total OPEB liability.

Management and Governance

California CCDs have an Institutional Framework score of A, which is moderate. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. California CCDs' major revenue sources ar e determined by the state government or, for the most part, can only be raised with voter approval. Ad valorem property tax rates cannot be increased above 1% except to meet GO bond payments, and assessed valuation growth is also generally limited to 2% annually unless a property changes ownership. 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, California has strong public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be moderate, between 5-10% annually

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