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FitchRatings

Public Finance
Tax-Supported
U.S.A.

Nebo School District, Utah

Ratings

Long Term Issuer Default Rating	AAA

New Issue

$99,895,000 Nebo School District Local Building Authority (UT) Lease Revenue Bonds, Series 2023	AA+

Outstanding Debt

Nebo School District Local Building Authority (UT) Lease Revenue Bonds	AA+

Rating Outlook

Stable

Applicable Criteria

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

Related Research

Fitch Rates Nebo School District, UT's Lease Revenue Bonds 2023 'AA+'; Outlook Stable (February 2023)

New Issue Summary

Sale Date: March 9, 2023

Series: Series 2023

Purpose: Bond proceeds will be used to fund construction and purchase of buildings and school sites.

Security: The series 2023 lease revenue bonds are supported by a covenant to budget and appropriate lease payments. The leased assets are school facilities.

The 'AA+' lease revenue rating reflects the slightly higher degree of optionality associated with appropriation backed debt. However, the district's projected lease burden from this issuance is low at 3.2% of 2022 spending and, given the appropriation nature of this obligation, Fitch notes that the district's liquidity position is good with days cash equal to 211 days in fiscal 2022 and averaging 169 days in each of the prior three fiscal years.

The district's 'AAA' IDR and GO ratings reflect its strong revenue growth prospects within the state school funding framework, solid expenditure control, low long-term liability burden including well-funded pensions, and its superior gap-closing capacity. Its revenue framework is supported by a growing tax base and protected by automatic tax levy adjustments during periods of taxable assessed valuation (TAV) decline. While the growing student population generates capital and operational cost pressures, it also results in increased state funding.

Economic Resource Base: Nebo School District is the state's sixth-largest district by enrollment with more than 36,000 students. It serves a rapidly developing suburban area at the southern edge of Utah's economically dynamic Wasatch Front region. The district's growth has been largely driven by the availability of land and relatively affordable housing within commuting distance of very strong job markets in northern Utah County and farther north in Salt Lake County.

Key Rating Drivers

Revenue Framework: 'aaa': Long-term general fund revenue growth is expected to outpace U.S. economic growth, reflecting a strong tax base, steady enrollment gains and increasing state per pupil funding. The district has substantial independent legal ability to raise revenues if needed with local property tax rates well below the legal limit.

Expenditure Framework: 'aa': The rate of spending growth is expected to be in line with to marginally above strong revenue growth, as rising enrollment drives increases to teaching staff. The district enjoys solid expenditure flexibility, with moderate carrying costs and a flexible labor environment.

Long-Term Liability Burden: 'aaa': The district's debt and net pension liabilities are low relative to its resource base. Future debt plans are manageable.

Operating Performance: 'aaa': The district has superior gap-closing capacity, with limited historical revenue volatility and superior inherent budget flexibility, accompanied by sizable reserves. Budget management in times of recovery is also strong, with rapid rebuilding of financial flexibility after downturns and conservative budgeting to maintain structural balance.

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Rating Sensitivities

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

- Both the IDR and lease obligations are at their highest rating levels/not able to be upgraded.

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

- For the IDR and lease obligation a sustained slowdown in revenue growth to less than the rate of nominal U.S. GDP.
- A sustained increase in the long-term liability ratio to above 10% of personal income.
- Material erosion of fund balance, resulting in weakened financial resilience.
- For the enhanced rating, a weakening of the credit quality of the state of Utah that leads to a downgrade of the Utah School Bond Default Avoidance Program rating.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	2/28/23
AAA	Upgraded	Stable	3/2/17
AA	Assigned	Stable	3/6/13

Credit Profile

The district's economic resource base provides strong fundamental support for operations. Utah County's unemployment rate runs well below that of the nation, and employment growth has been strong. Utah County is regularly among the fastest job creators among U.S. counties.

The district's TAV equaled $13.2 billion in 2022, and strong TAV growth is expected over the near term; TAV has risen by more than 10% in each of the last three years.

Revenue Framework

Funding for schools in Utah is a shared responsibility between the state, which has a constitutional responsibility for public education, and local school districts. Funding is provided from a combination of property taxes imposed by the local school district, state-imposed personal income taxes and corporate franchise taxes and federal sources. The weighted pupil unit (WPU) is the statutory allocation methodology for equalized school funding across the state. The state provides close to three quarters of Nebo's general fund revenues, and local property taxes provide about 19% of revenues.

The district has seen strong revenue gains over the past 10 years with the CAGR of 5.5% through fiscal 2021, which was higher than national GDP performance over the same period. State revenues have grown rapidly due to moderate increases in per pupil funding and strong enrollment growth, while property tax revenues have risen with robust development activity. For fiscal 2022, the Utah legislature provided an increase in WPU of about 5.92% over the previous year followed by a 6.01% increase in fiscal 2023.

The district has benefited from strong enrollment trends for many years. Enrollment has grown by almost 20% since 2010. Given healthy state per pupil funding growth and solid demographic trends, Fitch expects the district's revenue growth prospects to be strong over the near term. The district saw an increase of about 122 students in 2022, reflecting a 0.3% increase over the previous year. For the current fiscal year, the district experienced an increase of 756 students, however, only 385 students were in person students; the others participate in online education, which is managed by an independent third party. The 385 in person enrollment growth equates to a 1.09% increase over the previous year. Additionally, the district is able to retain a small portion of the per pupil student funding allocated by the state for the remote learning program operated by the independent third party. Overall, its medium range enrollment estimates place enrollment growth at about 200 to 300 students each year over the next three-five years. However, district officials will adjust staffing and capital plans as needed to accommodate actual growth.

The district has a high independent legal ability to raise revenues relative to its expected revenue volatility. The main operating levy (board levy) is well below the maximum level, providing the district with ample flexibility, and the district could raise approximately $21.9 million if the board levy were increased to the maximum rate of 0.25%. While the board has no

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plans to raise the board levy, it does plan to raise the voted discretionary levy through the truth in taxation process.

Expenditure Framework

The expenditure framework is typical for a school district, with a majority of general fund spending dominated by teacher and staff salaries and benefits.

Fitch expects the natural pace of expenditure growth to be in line with to marginally above revenue gains, absent policy action. Personnel and operational costs will increase with enrollment growth and opening of new schools.

The district has solid expenditure flexibility. The fixed carrying costs of debt service, pensions and other post-employment benefits (OPEB) are at the higher end of the moderate range (approximately 18.1% of governmental expenditures in fiscal 2022). In part, this reflects the moderate amortization of the district's direct debt over 10 years, which should help absorb any planned additional borrowings without materially increasing carrying costs. These revenue bonds currently being issued mature in 16 years. Total debt service is manageable and accounted for roughly 9.4% of governmental spending in fiscal 2022, with more volatile pensions contributions comprising about 8%.

The labor framework is also very manageable. About 55% of the district's workforce is subject to collective bargaining, but policymakers retain the authority to determine both staffing and compensation levels. The elected school board has the legal authority to impose terms in the rare instances when labor and management cannot agree to contract terms. While employees can strike, there is no recent history of strikes, and district officials characterize management/labor relations as very good. The district negotiates contracts annually to maintain the flexibility to adjust costs to changes in state funding levels. The district provided labor with a salary increase of 6.25% for fiscal 2023.

The district received close to $8 million in ESSER II and about $19 million in ESSER III funding and has used a portion of the funds to hire teachers to help students overcome learning gaps caused by the pandemic. The district has plans to convert the positions to permanent teaching positions once the one-time federal funds are expended, the cost of which is expected to be covered through attrition.

The district also has the ability to adjust class sizes and the number of paid teacher days if needed in a period of financial stress. Given growth in enrollment, adjustments to class sizes can typically be achieved by slowing hiring without resorting to layoffs or other more disruptive means of expenditure control.

Long-Term Liability Burden

The long-term liability burden is low relative to the economic resource base at about 6.8% of personal income. Principal amortization is moderate with approximately 55% of principal repaid in 10 years. Overlapping debt is minimal. Net Fitch adjusted pension liabilities of $163 million are equivalent to less than 2% of total personal income. Pensions are provided through the Utah Retirement System, which is adequately funded.

Following the issuance of GO bonds in July 2022, the district has approximately $121 million remaining bonding capacity under its 2018 GO bond authorization of $298 million, which it expects to issue over the next few years. The needs to issue these revenue bonds stem from the sharp increase in inflation, which has increased the actual cost of the district's capital program. The district has tentative plans to seek a new GO bond authorization in fiscal 2028 for capital projects, given rapid enrollment growth and the need for additional schools for about $400 - $500 million. Further increases in debt are likely to be paired with growth in the tax base and personal income and moderate debt amortization, muting the impact on the long-term liability metric.

Operating Performance

The district has superior gap closing capacity as compared with its revenue volatility. Fitch expects the district's unrestricted fund balance to remain considerably above levels supporting the 'aaa' operating performance assessment even as the district uses some of its reserves for

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planned purposes such as opening of new schools and implementation of its new employee benefit plan.

The district usually budgets conservatively and tends to beat its projections, and its last net operating deficit was in fiscal 2010 (equal to less than $1 million or 1% of spending at the time). The district's unrestricted general fund balance for fiscal 2022 totaled $88.9 million or 31% of spending. District management anticipates drawing down a portion of its fund balance to accommodate start-up costs associated with the opening of new schools. Projections for fiscal 2023 show unrestricted ending fund balance at 24% of spending.

The district had committed $15 million of its unrestricted general fund balance for economic stabilization (5% of general fund budgeted revenues) in fiscal 2022 and plans to increase this amount to reach $16 million under the proposed budget for fiscal 2023. Federal and state one-time funding received by the district accounted for close to $32 million, which it plans to spend within the required timeframe strictly on one-time expenses.

Budget management in times of recovery is strong, with rapid rebuilding of financial flexibility when needed, conservative budget planning and full funding of required spending such as pensions. The district has increased its financial cushion significantly since the Great Recession, adding to its unrestricted general fund balance each of the past several years. The district has strong financial practices and generally budgets conservatively.

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. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

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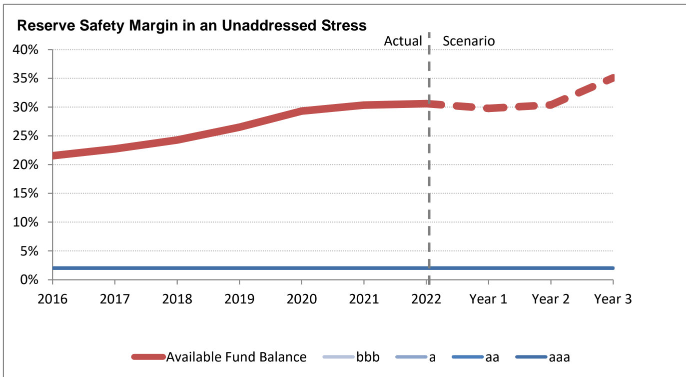
Nebo School District (UT)

Scenario Analysis

Ver 48



Analyst Interpretation of Scenario Results

The district has superior gap closing capacity as compared with its revenue volatility. Fitch expects the district's unrestricted fund balance to remain considerably above levels supporting the 'aaa' operating performance assessment even as the district uses some of its reserves for planned purposes such as opening of new schools and implementation of its new employee benefit plan.

Scenario Parameters:					Year 1	Year 2	Year 3
GDP Assumption (% Change)					(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)					2.0%	2.0%	2.0%
Revenue Output (% Change)	*Min Y1 Stress:*	**-1%**	*Case Used:*	**Moderate**	(1.0%)	3.5%	6.1%
Inherent Budget Flexibility						Superior	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2016	2017	2018	2019	2020	2021	2022	Year 1	Year 2	Year 3
Total Revenues	197,721	210,772	222,800	237,357	245,958	275,695	298,514	295,528	305,809	324,592
% Change in Revenues	-	6.6%	5.7%	6.5%	3.6%	12.1%	8.3%	(1.0%)	3.5%	6.1%
Total Expenditures	192,405	205,697	216,217	228,555	236,736	266,075	290,482	296,292	302,218	308,262
% Change in Expenditures	-	6.9%	5.1%	5.7%	3.6%	12.4%	9.2%	2.0%	2.0%	2.0%
Transfers In and Other Sources	41	96	71	168	22	1,677	46	45	47	50
Transfers Out and Other Uses	-	259	369	597	409	-	4	4	4	4
Net Transfers	41	(163)	(298)	(429)	(387)	1,677	42	41	43	46
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus/(Deficit) After Transfers	5,356	4,912	6,284	8,373	8,835	11,297	8,073	(722)	3,634	16,376
Net Operating Surplus/(Deficit) (% of Expend. and Transfers Out)	2.8%	2.4%	2.9%	3.7%	3.7%	4.2%	2.8%	(0.2%)	1.2%	5.3%
Unrestricted/Unreserved Fund Balance (General Fund)	41,441	46,823	52,597	60,787	69,547	80,757	88,937	88,215	91,849	108,225
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	41,441	46,823	52,597	60,787	69,547	80,757	88,937	88,215	91,849	108,225
Combined Available Fund Bal. (% of Expend. and Transfers Out)	21.5%	22.7%	24.3%	26.5%	29.3%	30.4%	30.6%	29.8%	30.4%	35.1%

Reserve Safety Margins	Inherent Budget Flexibility				
Moderate	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	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.

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