FITCH RATES DALLAS COUNTY COMMUNITY COLLEGE DISTRICT, TEXAS' GOS AT 'AAA'; OUTLOOK STABLE

Fitch Ratings-Austin-30 May 2017: Fitch Ratings has assigned a 'AAA' rating to the following Dallas County Community College District (DCCCD), TX bonds:

--$62.3 million general obligation (GO) refunding bonds, series 2017.

The Rating Outlook is Stable.

SECURITY
The bonds are a direct obligation of the district, secured by an annual property tax levy limited to $0.50 per $100 of taxable assessed valuation (TAV) on all taxable property within the district.

KEY RATING DRIVERS

The 'AAA' rating reflects the district's significant independent ability to raise revenues, solid budgetary flexibility, ample reserve cushion, and limited historical revenue volatility. These provide the district with a high level of operating flexibility and anticipated financial resilience throughout the economic cycle. Fitch expects the long-term liability burden will remain moderate.

Economic Resource Base
Coterminous with Dallas County, the district serves a large and growing population base, currently estimated at 2.6 million. DCCCD is one of the largest community college systems in the state with numerous educational facilities throughout the county. The district derives support from state aid; however, revenues are primarily influenced by local trends, including enrollment and TAV. Enrollment typically runs counter-cyclical to local economic conditions, which adds a level of volatility to enrollment trends.

Revenue Framework: 'aaa' factor assessment
Fitch believes the district's natural revenue growth prospects are strong and will continue to equal or exceed U.S. GDP. The superior ability of the district to raise property tax and tuition/fee revenues in the event of normal cyclical decline supports the 'aaa' assessment.

Expenditure Framework: 'aa' factor assessment
The pace of spending growth should remain more or less aligned with revenues over time. Low carrying costs and the district's ability to adjust its labor costs, if needed, provide sound expenditure flexibility.

Long-Term Liability Burden: 'aa' factor assessment
The long-term liability burden is about 9% of local per capita personal income, and largely consists of overlapping debt. The assessment also considers the city of Dallas' unfunded pension liabilities on a resource base shared with the district. Fitch believes the burden will remain moderate given growth in liabilities should be offset by further population and income gains and the city's pension reform efforts.

Operating Performance: 'aaa' factor assessment
Fitch believes the district would maintain a high level of fundamental financial flexibility throughout the economic cycle given the various budgetary tools at its disposal. Modest expected revenue volatility as indicated in the Fitch Analytical Sensitivity Tool underpins the assessment.

RATING SENSITIVITIES

Shift in Profile: While not anticipated, a reversal of long-term economic growth trends and/or any material deterioration of the district's budgetary tools could apply downward pressure to the rating.

CREDIT PROFILE

The district benefits from its central location within the broad and growing Dallas-Fort Worth metropolitan economy and population base. Dallas is the third largest city in Texas and is a center for technology, trade, finance and major medical centers; it also ranks as the top visitor and leisure destination in the state. Top employers in the education, government and health services sectors lend stability to the employment base. The area exhibited good resiliency during the national recession and shifted into economic expansion earlier than many other parts of the country, and county unemployment remains low.

The tax base is without concentration and top taxpayers represent a mix of utility, air transportation, real estate, manufacturing and retail industries. Growth in the district's tax base has slightly outpaced enrollment performance historically. TAV grew by nearly 3.5% annually on average in the 10-year period over fiscals 2006-2016 while full-time equivalent students (FTE) enrollment expanded by roughly 2% during the same period.

Additional moderate TAV growth appears likely given the healthy regional economy; a strong 10% TAV gain was realized in fiscal 2017. This is balanced against Fitch's expectation of relatively modest change to enrollment trends in the near to intermediate term. A 3% gain in student FTE students (totaling nearly 51,000 in fiscal 2016) reversed a trend of steady enrollment decline since fiscal 2011, and management indicates enrollment trends are again up modestly in fiscal 2017.

Revenue Framework

Property taxes (for both operations and debt service) provide the largest portion of the district's total revenues (about 45% of total revenues in fiscal 2016), while state aid and tuition/fees each contributed about 22%. District operations have become more dependent on the local tax base in the past decade. Increasing tax revenue for operations has served to offset a portion of the declines in enrollment-related revenues, such as federal (largely Pell grant) revenue, state appropriations, and tuition, as well as some recessionary cuts to state funding. Third-party funding support stems from the long-standing commitment of the state and U.S. government to fund higher education. Nonetheless, these revenue streams remain susceptible to changes in enrollment trends, education policy and eligibility requirements, and recessionary funding pressure.

Revenues should continue to grow naturally in line with historical performance that equaled or exceeded U.S GDP. Average annual revenue growth of 4.7% in the 10-year period of fiscal 2006 - 2016 was well above U.S. GDP. This performance was due largely to the ability of district property taxes to capture solid TAV gains, but also a function of enrollment growth and additional enrollment-related revenues. Continued TAV and economic expansion in addition to some growth in student-related revenues should serve to offset an across-the-board, 4% state appropriation cut anticipated in the next biennium (fiscals 2018-2019).

The district's total tax rate is limited to $1.00 per $100 TAV according to state statute, of which no more than $0.50 per $100 TAV can be used for debt service. However, the district's operating property tax revenue is capped at a lower $0.16 per $100 TAV tax levy by locally voted limitation.

Moderate capacity exists under the local tax levy cap as the district presently levies slightly over $0.10 per $100 TAV or roughly 65% of its capacity. If a proposed tax rate results in an 8% year-over-year levy increase (based on the prior year's values), the rate increase may be subject to election if petitioned by voters. The district also retains full ability to independently raise its tuition and fee charges without any legal limit.

Instruction, student services, and administrative expenses consumed about 64% of total spending in fiscal 2016. Fitch expects the natural pace of spending growth should remain more or less aligned to revenues over time based on the district's current expenditure trends.

The district maintains sound flexibility to adjust employee headcount and compensation in response to changing enrollment trends. The district has demonstrated its ability to control key expenditure items in times of fiscal stress without affecting its educational goals. This is tempered by the district's need to maintain a competitive salary structure in the Dallas-Fort Worth MSA employment base in order to recruit and retain highly educated professionals for instructional and leadership purposes. Nonetheless, management's legal control of labor costs and headcount remains strong.

Fixed carrying costs - the combination of total annual tax-supported debt service, the contractually required annual pension funding amount, and the annual spending for other post-employment benefits (OPEB), net of state support - are low and consumed about 8% of total operating/non-operating expenses in fiscal 2016. Looking ahead, Fitch expects these fixed costs will remain low as a result of the district's rapidly amortizing tax-supported debt service schedule as well as manageable retiree costs that are shared with the state. Fitch assumes a continuation of shared state and district funding for the employer pension and OPEB contributions.

Long-Term Liability Burden

The long-term liability burden is estimated at 9% of 2015 Dallas County personal income, derived largely from overlapping debt. Fitch expects this burden will likely increase over time, but remain moderate given growth in liabilities should be offset by further population and income gains in conjunction with the city's pension reform efforts underway. (For more information, see "Fitch: Dallas Pension Bill Holds Reform Potential," March 15, 2017, available on Fitch's website at www.fitchratings.com).

The district's debt is supported by a separate tax levy of up to $0.50 per $100 TAV, and the current rate of roughly $0.02 provides significant taxing margin. Principal amortization of the district's tax-supported debt is rapid with 80% repaid in 10 years. Management presently anticipates funding its capital priorities, inclusive of expanding key, high-demand programs throughout its seven, separately accredited colleges, with the issuance of approximately $200 million in self-supporting revenue debt, backed by pledged tuition/fees. The district does not have any revenue debt currently outstanding.

The district participates in the Texas Teachers Retirement System (TRS), a cost-sharing, multiple-employer plan for which the state provides roughly half of the community college's (employer) annual pension contribution. Recent reforms have lowered benefits and increased statutory contributions in order to improve plan sustainability over time.

Under GASB 67 and 68, the district reported its share of the TRS net pension liability (NPL) at $66.4 million for fiscal 2016, with fiduciary assets covering approximately 78% of total pension liabilities at the plan's 8% investment rate assumption (approximately 71% based on a more conservative 7% investment rate assumption). The NPL remains small at less than 1% of personal income when adjusted for the 7% investment rate assumption.

Participants' required pension contributions are based on a statutory formula that consistently falls short of the actuarially-determined amount. Fitch therefore expects modest growth in the NPL even if investment returns meet assumed rates, although the overall long-term liability burden should remain within the current range given how small the pension liability is relative to overall debt. In addition, the district and all Texas community colleges remain vulnerable to future policy and funding changes by the state. The district also provides OPEB through the state-run, post-employment benefit healthcare plan, the obligation for which is small at less than 1% of personal income.

Operating Performance

Fitch believes the district's financial resilience is superior and expects it will be maintained throughout the economic cycle due to budget flexibility, modest revenue volatility, and history of maintaining high levels of unrestricted cash/investments. Fitch uses this measure as a proxy for unrestricted general fund balance as the district's enterprise accounting is likely to lead to variability in net asset reporting due primarily to the impact of GASB 68.

The district's high level of fundamental financial flexibility is a result of the various budgetary tools at its disposal, which include revenue-raising authority, the ability to use its historically strong reserve cushion in excess of Fitch's calculated reserve safety margin, and solid expenditure flexibility.

A trend of solidly positive operating margins stemming from revenue growth and expenditure control underpins the district's historically strong financial position. The district continued this trend in fiscal 2016 with a strong 9% margin as operating performance improved upon budget. The district's operating cushion of unrestricted cash/investments totaled a high $333.4 million or about 68% of spending at fiscal 2016 year-end, up by a modest $8 million (1.5% of spending) from the prior year.

Unrestricted reserves have been maintained well above the minimum four months of spending, consistent with the board's established policy. Management expects to keep unrestricted reserves closer to five months of spending in order to prioritize pay-go capital spending (about $86 million for the district's five-year facilities maintenance plan through fiscal 2017) rather than build higher levels of reserves.

The fiscal 2017 general unrestricted operating budget of approximately $422 million is up about 6% from the prior year and structurally balanced. Underpinning the year's finances is growth in property tax revenue, additional student enrollment assumed, as well as salary increases and further pay-go capital spending, balanced against targeted cost savings.

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In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478