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CREDIT OPINION
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Contacts

Sam Feldman-Crough +1.415.274.1706
AVP-Analyst
samuel.feldman@moodys.com

Gregory W. Lipitz +1.212.553.7782
VP-Sr Credit Officer/Manager
gregory.lipitz@moodys.com

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Washoe County School District, NV

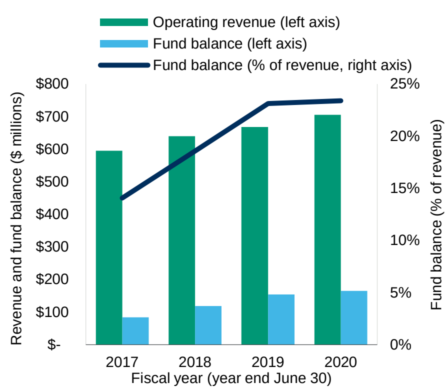
Update to credit analysis

Summary

Washoe County School District, Nevada (Aa3 stable) is supported by an exceptionally large, growing and diversifying tax base that is the second most populous county in the state of Nevada (Aa1 negative-multiple) and includes the city of Reno (A1 stable) as the major population center. The district's solid finances (Exhibit 1) will likely continue to improve, though they remain somewhat below national medians for similarly rated peers. Enrollment has decreased in fiscal 2021 by nearly 4% in year-over-year figures (Exhibit 2), driven by lower kindergarten enrollment and some modest loss to a new charter school.

Exhibit 1

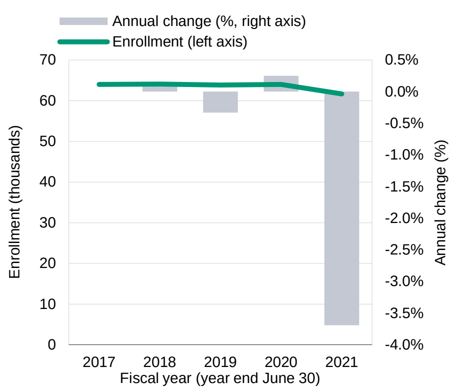
Revenue and fund balance continue to grow



Source: District audits and Moody's Investors Service

Exhibit 2

Enrollment declined nearly 4% in 2021



Fiscal 2021 figures based on year-to-date figures
Source: District audits and Moody's Investors Service

Economic exposure to tourism and gaming, as well as average resident income, pose long-term challenges to the district's otherwise strong credit profile. Favorably, the local economy has remained stable throughout the coronavirus pandemic, with year-over-year sales tax collections growing in most months through September 2020.

The district's increasing leverage and pension obligations are another challenge. Debt has more than doubled since 2016 with the addition of a new revenue source and is above average compared to similarly rated peers. Positively the district does not have plans to issue additional debt. Pension liabilities are also elevated and grew in fiscal 2020 after a few years of modest declines.

Credit strengths

» Voter approved sales tax (WC-1 tax) provides substantial funding for debt service and pay-go capital needs

» Large, growing and diversifying tax base spanning the Reno area

» Recent implementation of new reserve and budget policies in effort to bolster finances, especially for the general fund

» Notable reserves available to pay debt service

Credit challenges

» General fund reserves remain weak relative to peers

» Elevated combined debt and pension liabilities

» Economic exposure to gaming and tourism, thought the economy is diversifying

Rating outlook

The stable outlook reflects the likelihood that the material improvements to the district's financial position will be maintained, resulting in continued operating flexibility. The stable outlook also reflects the likelihood that the district's tax base will continue to grow and diversify.

Factors that could lead to an upgrade

» Material, sustained improvement in the district's reserves

» Significant continued economic diversification and improved income

» Material decrease in the district's fixed costs

Factors that could lead to a downgrade

» Material drawdown in reserves, especially if not met by subsequent expense reductions to return to a balanced budget

» Declines in the tax base that pressures tax rates for debt and operations

» Significant continued growth in leverage from either debt or net pension liabilities

Key indicators

Exhibit 3

Washoe County School District, NV	2016	2017	2018	2019	2020
Economy/Tax Base					
Total Full Value ($000)	$37,991,217	$41,525,917	$42,792,777	$47,002,243	$53,957,591
Population	439,914	445,551	450,486	--	--
Full Value Per Capita	$86,361	$93,201	$94,992	$104,337	$119,776
Median Family Income (% of US Median)	100.6%	102.4%	101.5%	--	--
Finances					
Operating Revenue ($000)	$570,298	$594,894	$640,264	$668,522	$705,165
Fund Balance ($000)	$80,925	$83,673	$118,904	$154,569	$164,965
Cash Balance ($000)	$71,595	$80,667	$98,242	$129,895	$136,496
Fund Balance as a % of Revenues	14.2%	14.1%	18.6%	23.1%	23.4%
Cash Balance as a % of Revenues	12.6%	13.6%	15.3%	19.4%	19.4%
Debt/Pensions					
Net Direct Debt ($000)	$464,161	$516,233	$709,722	$735,198	$1,035,502
3-Year Average of Moody's ANPL ($000)	$1,957,991	$2,193,641	$2,316,784	$2,400,956	$2,398,468
Net Direct Debt / Full Value (%)	1.2%	1.2%	1.7%	1.6%	1.9%
Net Direct Debt / Operating Revenues (x)	0.8x	0.9x	1.1x	1.1x	1.5x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	5.2%	5.3%	5.4%	5.1%	4.4%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	3.4x	3.7x	3.6x	3.6x	3.4x

2018 is most recent available data for population and median family income from the American Community Survey.
Sources: District audits, US Census Bureau and Moody's Investors Service

Profile

Washoe County School District is coterminous with Washoe County (Aa2 stable) and serves a population of approximately 450,486 (as of the 2018 American Community Survey) in northern Nevada, including the cities of Reno and Sparks (A2). The district serves approximately 62,000 students (as of fiscal 2021 estimates) and is the second largest in the state.

Detailed credit considerations

Economy and tax base: large and growing tax base that is diversifying away from a tourism-based economy

Recent investment from large tech companies is diversifying the tax base and economy and is reducing the area's traditional concentration in gaming and tourism. Within the last few years, Tesla (B2 stable) and Panasonic (Baa1 negative) began producing batteries in a so-called "Gigafactory" located just across the county border in Storey County. Additionally, Switch (Ba3 positive), Apple (Aa1 stable), Alphabet (Aa2 stable) and eBay (Baa1 stable) have also made investments in the area in manufacturing and distribution operations.

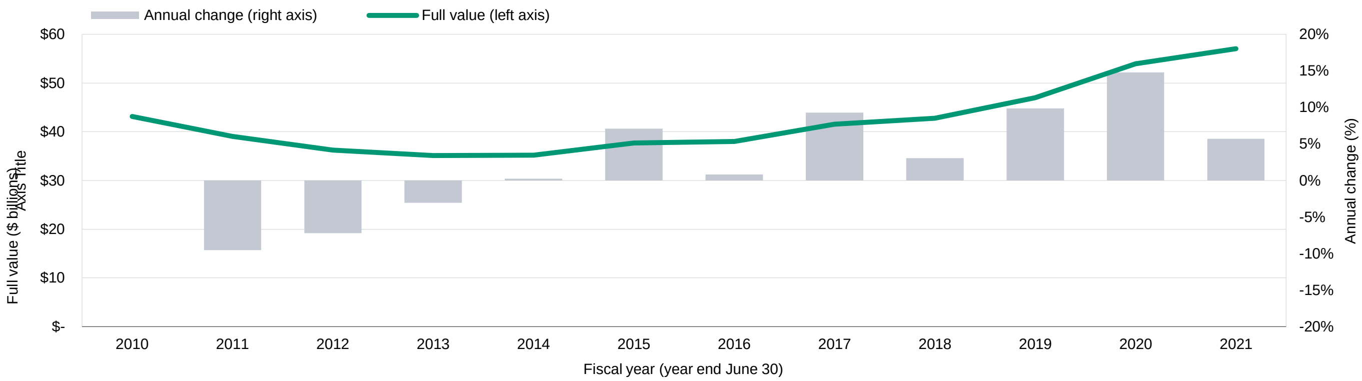
This diversification has supported a more stable economy through the coronavirus pandemic than in the state's major population center of Las Vegas (Aa2 negative) and Clark County, NV (Aa1 stable). October 2020 unemployment in Washoe County was 6.3%, which is just below the US average of 6.6% in the same survey. The state's unemployment rate, however, was a much higher 11.8% and Clark County's unemployment rate was higher still at 13.8%.

Property values will continue to grow, driven by continued commercial and manufacturing development, though the pace of growth will likely slow considerably from some of the recent exceptional single-year growth rates (Exhibit 4). At $57 billion in fiscal 2021, full value is nearly 20x larger than the median Aa3 school district tax base.

Exhibit 4

Exceptional recent property value growth will moderate

Washoe County SD, NV's full market values



Source: Financial disclosures and Moody's Investors Service

Despite these gains, resident income will remain just average compared to national medians considering tourism and hospitality still remain a component of the economy. Median family income is 101.5% as of the 2018 American Community Survey, just two percentage points below the national median for Aa3 school districts. Meanwhile, full value per capita has grown to $126,618 using fiscal 2021 full values and 2018 population; using more updated population estimates would only lower full value per capita slightly.

Financial operations and reserves: maintaining improved fund balance despite 4% enrollment loss

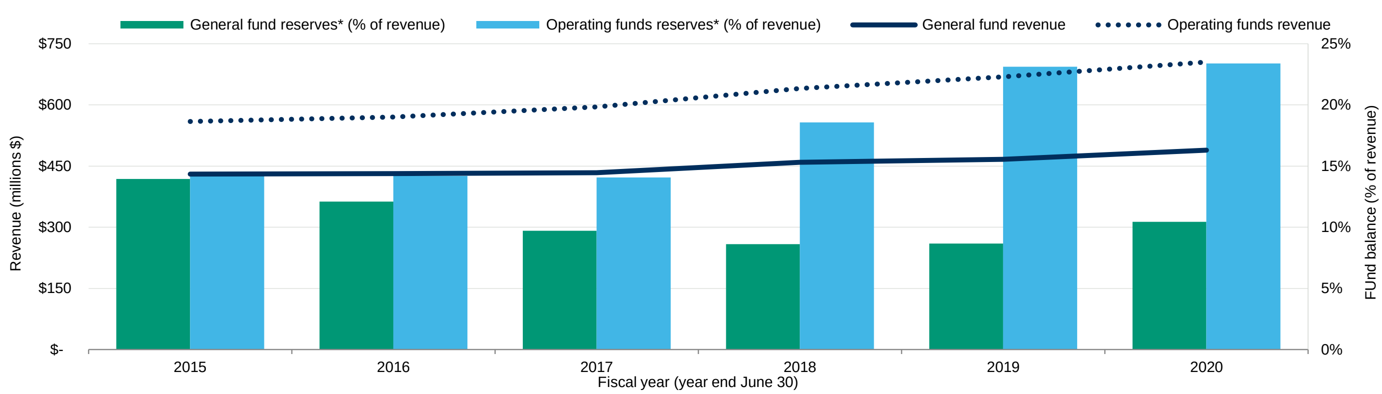
Fund balance will remain solid, if slightly below peers nationally, despite a large decline in enrollment in the current fiscal year, which is a national trend caused by the coronavirus pandemic. Fund balance in fiscal 2020 was $165 million, or 23% of revenue, across the operating funds[1], which is slightly above national medians. However, in the general fund alone, reserves are a weaker but still adequate $52 million, or 10% of revenue, which is about half of the national median for similarly rated districts. Despite this, general fund reserves are at the high end of the district's board-approved policy of 8-10% and these reserves are an improvement from prior balances that were declining through fiscal 2018 (Exhibit 5).

Continued improvement in fiscal 2020 reserves was driven primarily by continued careful expense management and increased local revenue from a sales tax for capital that had its first full year of collection in fiscal 2018. Overall, school closures in the last few months of the school year as a result of the coronavirus pandemic produced modest net savings and slightly increased revenue from state and federal sources, however the district primarily spent those funds on technology purchases, personal protective equipment and other pandemic-related expenses.

Exhibit 5

Fund balances have improved and are expected to be stable

Washoe County SD, NV's revenue and fund balances



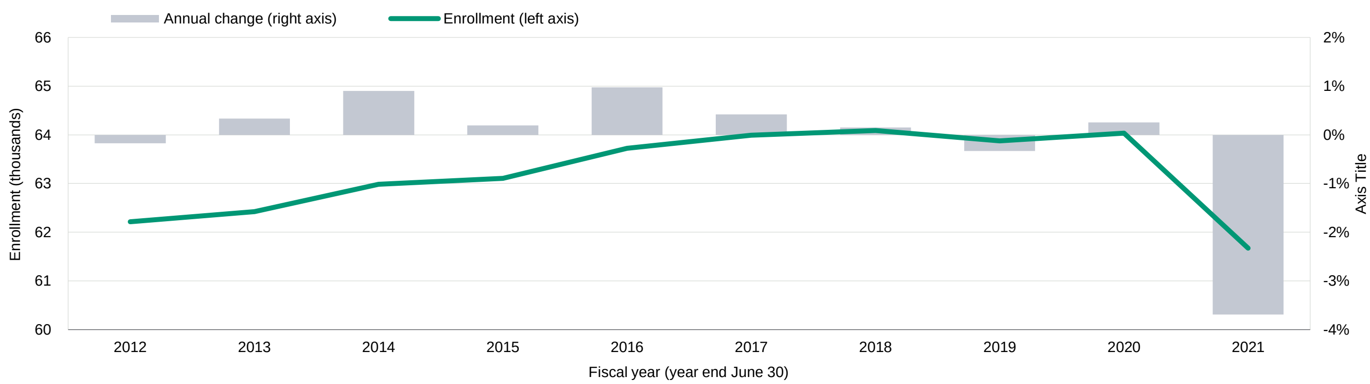
*Reserves are defined as available fund balance, as adjusted by Moody's.

Sources: District audits and Moody's Investors Service

Fiscal 2021 will see stability in reserves based on the district's budget and projections. The board approved a revised budget in December 2020 that incorporated state funding adjustments, revised enrollment projections and savings from vacant positions and other cost reductions. Despite that budget still projecting a modest deficit of $8 million in the general fund, we expect the district will be able to easily close the gap by fiscal year end, based on prior results and existing plans for savings.

Enrollment declined nearly 4% in year-to-date fiscal 2021 figures, leading to a modest reducting in state funding that was incorporated in the district's December revised budget. State funding also declined because of reductions in specific categorical grants for fiscal 2021. Enrollment had been largely stable for several years, with a slow trend of modest growing enrollment driven (Exhibit 6) by local economic growth. Charter schools remain a competitive pressure for the district, with a newly opened charter school drawing about 600 students in fiscal 2021.

Exhibit 6
Enrollment declining nearly 4% in 2021, but was otherwise growing modestly
Washoe County SD, NV's enrollment



Sources: District sources and Moody's Investors Service

Financial challenges remain in future years, starting in Fiscal 2022, but we expect the district will continue to capably manage these challenges using the improved budgeting tools and increased transparency implemented over the past few years. Among the future challenges to the district's finances are:

» Some state revenues have declined notably (particularly gaming revenue) and the state legislature will begin meeting in January to set new funding levels for education. If the legislature cuts state funding for education, it will reduce the district's second-largest revenue source (representing 31% of operating revenue in fiscal 2020) under the current funding model.

» Additionally, a new “pupil-centered funding plan” (SB 543) will be implemented statewide, which will make substantial changes to the way local and state sources are counted for funding education. The exact effect of these changes on total revenue available for the district remains uncertain, though the effects are not expected to be materially different to current funding levels at this time. Specific to fiscal 2022, SB 543 states general, special education and grant funding will be no less than actual fiscal 2020 revenue even under the new formulas, providing at least one year of stable revenue.

» If coronavirus transmission remains a sustained risk at the start of the school year, it may continue to increase district expenses and there may be limited additional stimulus to pay for required technology, distancing and cleaning expenses.

» Future property tax collections may be reduced over several years due to a judgement in a lawsuit about countywide assessment practices and Incline Village. The total size of the school district's portion of the judgment is about $20 million, though this may be reduced as the district is seeking to intervene in the settlement agreement. Even if the district's property taxes are reduced, it would likely be spread over multiple years and would result in a relatively limited annual revenue reduction.

Liquidity
Net cash in the general fund is a relatively weak $15.4 million, or just 3% of revenue in fiscal 2020, though this is improved from a ratio of 1% of revenue in fiscal 2019. The low cash position in the general fund compared to fund balance is due to large receivables from

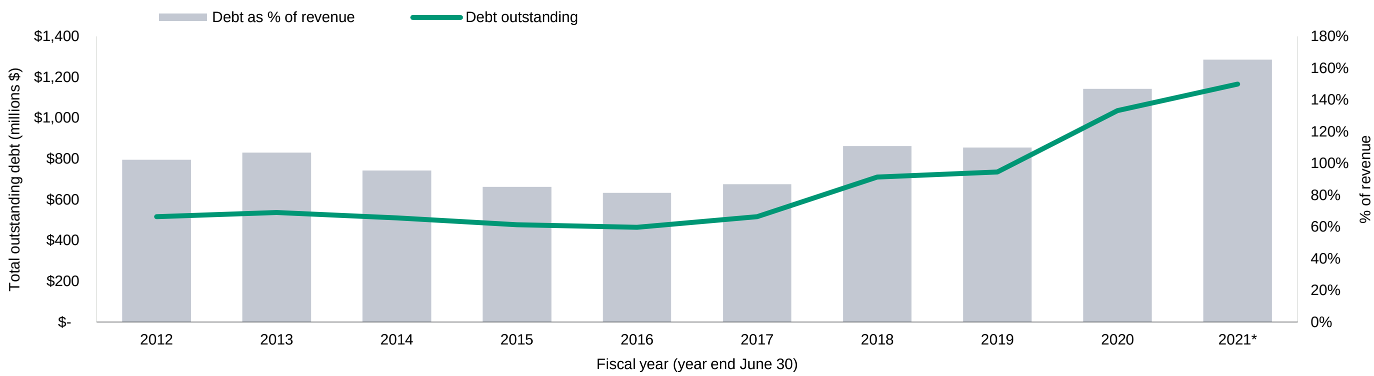
other governments, primarily the state. Across the operating funds, net cash is much stronger at $136 million, or 19% of revenue, as of fiscal 2020.

Debt and pensions: elevated liabilities will stabilize as debt issuance slows

Debt has more than doubled since fiscal 2016 (Exhibit 7) but it remains manageable given increased funding sources for the debt, including a sales tax that supports repayment of $547 million of the total (47%), which was also issued after fiscal 2017. After the issuance of $130.5 million in bonds in January 2021, the district will have about $1.2 billion in debt outstanding. This will represent about 3% of 2021 full value, which is slightly above national medians, and 165% of fiscal 2020 operating revenue, which is more than double national medians.

Exhibit 7

Debt has doubled since fiscal 2016 to meet ambitious capital plan
Washoe County SD, NV's debt outstanding



*Fiscal 2021 includes planned debt issuance in January 2021.
Source: Moody's Investors Service

After the upcoming issuance, the district is not expecting to have significant additional debt plans for the next few years. The district can continue to issue “rollover” bonds until March 4, 2025 as long as property values continue to grow, but it does not plan to do so at this time. The district also retains about $49 million in additional authorization for bonds backed by pledged revenues (sales taxes) but is also not expected to issue those bonds at this time.

Legal security

The 2021A bonds are secured by the full faith and credit of the district within the constitutional and statutory limitations for overlapping operating and debt service levies. Some of the district's bonds, though not the 2021A bonds, benefit from the additionally pledged revenue of the 0.54% county-wide WC-1 sales and use tax.

Debt structure

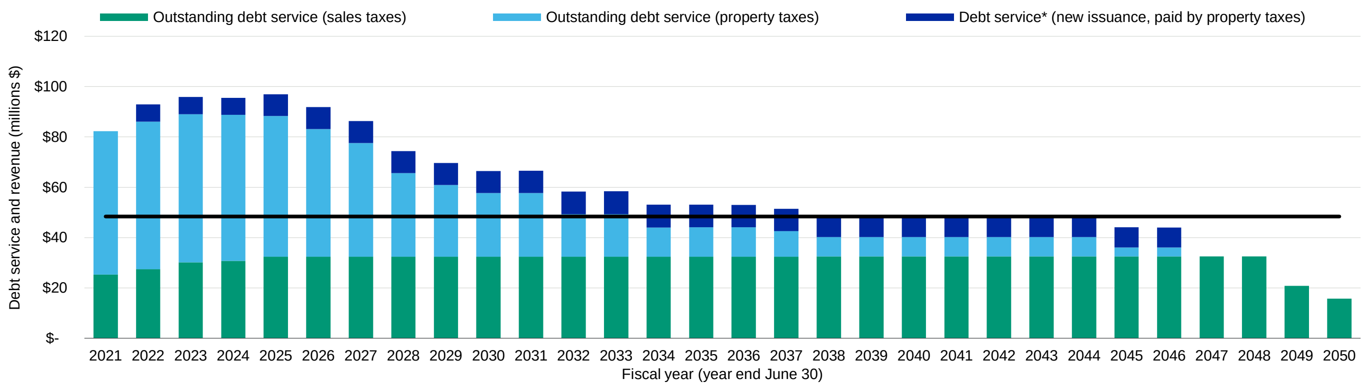
All of the district's debt is secured by the full faith and credit pledge of the district as well as a limited tax property pledge. About 47% of the district's debt also benefits from additional pledged revenues (sales taxes) which continue to pay debt service.

Debt service is generally declining over the life of the bonds after peaking in fiscal 2026 (Exhibit 8). Debt service paid by sales taxes (green bars) peaks at about 67% of 2020 sales tax revenues (black line in the exhibit, for comparison) starting in 2026, indicating sufficient coverage from sales taxes alone over the life of the outstanding bonds.

Exhibit 8

Debt service largely declines after peaking in 2026

Washoe County SD, NV's estimated debt service schedule



*Estimated debt service based on projected maturity schedule and estimated interest costs.
Source: District disclosures and Moody's Investors Service

Debt-related derivatives

The district does not have debt-related derivatives.

Pensions and OPEB

While pension liabilities are high, annual pension costs are not currently a source of pressure for the district, but a low funding rate at the plan level could lead future pressure. The plan's higher discount rate means the district is required by the state to underreport their pension liability and contributions are not keeping pace to amortize costs.

Moody's three-year adjusted net pension liability (ANPL) (2018-2020) is $2.6 billion, or 3.4x operating revenue and 4% of 2021 full value. In comparison, the district reported a GASB net pension liability of $716 million or only 1.01x 2020 operating revenue. We consider the district to be under reporting its liability based on the plan's 7.5% discount rate, which is higher than most local government pension systems around the country. We note this is a state plan and the discount rate is not controlled by the district.

The district's pension and OPEB liabilities add a significant amount of leverage to its balance sheet, and the district is moderately exposed to market volatility risk. Given the substantial size of the city's pension assets relative to revenue (330% as of fiscal 2020) and its pension system's allocation to volatile asset classes in support of an elevated 7.50% annual return target, the district has an elevated vulnerability to spikes in leverage from pension investment volatility. Moody's "pension asset shock indicator," which is our estimate of the one year probability of pension investment losses amounting to 25% of a government's operating revenue, was 16% in fiscal 2019, though it declined to 14% in fiscal 2020.

Total fixed costs including debt service and pension and OPEB contributions are average at 18.4% of fiscal 2020 operating revenue and do not appear as though they will create budgetary stress in the near term. Fixed costs, however, are slightly higher each year if the district were to make its full "tread water" payment, resulting in a small tread water gap of about 2% in most years. The tread water indicator measures the annual government contributions required to prevent reported net pension liabilities from growing, under reported plan assumptions.

ESG considerations

Environmental

Primary environmental considerations include water stress. According to data from Moody's affiliate Four Twenty Seven, the county has a "high" risk level for water stress. The area's primary water source is Lake Tahoe, which is expected to provide sufficient water to the area given it is the sixth largest lake (by volume) in the US, behind the five Great Lakes. However, as of December 15, 2020, most of Washoe County remains in extreme drought, though the Reno area is in a severe drought (one intensity lower) according to the U.S. Drought Monitor produced by the USDA, NOAA and University of Nebraska-Lincoln. Despite sufficient water supply for residents, exceptional droughts would not only reduce drinking water availability and quality but could also create additional wildfire-related hazards.

Social

Social considerations material to the rating include average income, average unemployment compared to national averages (but substantially better than statewide unemployment) and solid wealth as measured by full value per capita.

We regard the coronavirus pandemic as a social consideration in our ESG framework as it relates to "health & safety." The district has worked under state and local public health guidelines to maintain in-classroom learning whenever possible for the majority of students, especially for students in the youngest grades. The district continues to also provide at-home learning for students and has moved older students to exclusively distance learning during the current increase in community transmission. To enable this, the district has used pandemic-related funding (such as Federal, state and local distributions from the CARES Act) to fund new technology purchases as well as other necessary hardware and software.

Governance

Governance is a strength that supports recent improvements in the district's credit profile. Over the past few years, management worked to address the structural deficit in the general fund. The current board and administrative team set a multi-year goal to balance operations by fiscal 2021, however the district produced surpluses in fiscal years 2019 and 2020. As part of this work, in 2018 the management team successfully transitioned to a priority based budgeting system and improved accountability by implementing more detailed monthly expenditure tracking while seeing some improvements in revenue. Management credits the new budgeting process with allowing them to reach and just slightly exceed the board's 8-10% general fund reserve policy.

Nevada school districts have an Institutional Framework score of "A", which is moderate. Revenue predictability is moderate, with highly predictable property tax revenues offset by the state's ability to make unexpected funding and disbursement reductions. District's revenue raising ability is weak as the state legislature sets property tax rates and per pupil state aid revenue amounts. Operating expenditures are moderately stable and districts' ability to cut expenditures is moderate with fixed costs driven by debt service and pension contributions.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching adjustments dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 9

Washoe County School District, NV

Scorecard Factors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$57,039,609	Aaa
Full Value Per Capita	$126,618	Aa
Median Family Income (% of US Median)	101.5%	Aa
Notching Adjustments:[2]		
Economic Concentration		Down
Finances (30%)		
Fund Balance as a % of Revenues	23.4%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	11.9%	Aa
Cash Balance as a % of Revenues	19.4%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	8.9%	A
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x)	1.0x	Aa
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	2.0%	A
Net Direct Debt / Operating Revenues (x)	1.7x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	4.2%	A
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	3.4x	A
	Scorecard-Indicated Outcome	Aa3
	Assigned Rating	Aa3

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Sources: District audits, US Census Bureau and Moody's Investors Service

Endnotes

1 We define the operating funds as the general, debt service, special education, full-day kindergarten, special state appropriations, ERATE, government service tax, WC-1 sales tax and class size reductions funds.

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