MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns underlying Aa2 rating to Snohomish County School District 2 (Everett), WA's G.O. bonds

Global Credit Research - 11 Oct 2013

$215 million of debt affected; Aa1 enhanced rating also assigned

SNOHOMISH COUNTY SCHOOL DISTRICT 2 (EVERETT), WA
Public K-12 School Districts
WA

Moody's Rating

ISSUE		RATING
Unlimited Tax General Obligation Refunding Bonds, Series 2013		Aa2
Sale Amount	$38,200,000	
Expected Sale Date	10/22/13	
Rating Description	General Obligation	
Unlimited Tax General Obligation Refunding Bonds, Series 2013		Aa1
Sale Amount	$38,200,000	
Expected Sale Date	10/22/13	
Rating Description	General Obligation	

Moody's Outlook NOO

Opinion

NEW YORK, October 11, 2013 --Moody's Investors Service has assigned an underlying Aa2 rating to Snohomish County School District 2 (Everett), WA's Unlimited Tax General Obligation Refunding Bonds, Series 2013. Concurrently, Moody's has affirmed the Aa2 rating on the district's outstanding general obligation debt. The newly issued bonds are secured by the district's full faith and credit and unlimited property tax pledge. The current offering will also receive the Aa1 enhancement rating of the Washington State School Bond Guarantee Program. The district is refunding portions of its outstanding bonds to realize debt service savings.

SUMMARY RATING RATIONALE

The Aa2 underlying rating reflects the district's improving, Seattle area local economy that includes the strong presence of The Boeing Company (A2/STA Senior Unsecured Rating), above average socioeconomic indicators, and narrow yet stable financial position. The district has drawn its reserves down to the lowest level in recent years, but expects them to remain above its 5% policy level. With additional revenues expected in the coming fiscal year as a result of the McCLeary decision in Washington State, the district's financial position and reserves should improve over the coming years.

The Aa1 enhancement rating is based upon the assumption that the bonds will qualify for, and be backed by, the Washington State School Bond Guarantee Program. Under this program, the state pledges its full faith, credit, and taxing power to guarantee debt service when due on qualified school districts' voter-approved general obligation bonds. The program rating reflects the pledge of the State of Washington (Aa1 GO rating with stable outlook), strong state oversight of local school districts, and strong program mechanics. For more detailed information on the state guarantee program, please refer to Moody's Global Credit Research Rating Update dated January 4, 2010.

STRENGTHS

- Large tax base beginning to show improvement after years of decline

- Above average socioeconomic profile, and participation in the greater Seattle metro area economy

- Relatively stable financial position

CHALLENGES

- Narrow General Fund financial position

- Relatively aggressive capital plan and somewhat high debt level, though with rapid principal amortization

DETAILED CREDIT DISCUSSION

LOCAL ECONOMY ANCHORED BY PRESENCE OF BOEING; TAX BASE SHOWING SIGNS OF IMPROVEMENT

The district is located in southwest Snohomish County (Aa1 Issuer Rating), and encompasses most of the cities of Everett (Aa3 limited tax general obligation rating) and Mill Creek, as well as some unincorporated portions of the county. The Everett area is an integral part of the greater Seattle metro area, and is home to significant Boeing Company (A2 senior unsecured rating) manufacturing facilities. Boeing is the world's largest commercial aircraft manufacturer, and is the largest employer in the area, with more than 30,000 local workers. Naval Station Everett and the State of Washington are also large employers in the area. Along with numerous business parks located in the area, the aerospace and related industry that exists in the Everett area provide a robust local economy upon which the district can draw.

Although the district's tax base declined significantly in recent years, losing roughly 30% of its value between 2009 and 2013, preliminary estimates of assessed value (AV) for 2014 indicate this trend has turned around. The district expects AV to grow more than 10% in 2014 to $13.2 billion. If this growth comes to fruition, it would represent a significant turnaround in the local economic growth picture. This new trend is also supported by the latest employment numbers. As of July 2013, unemployment in Snohomish County was 5.6%. This figure is well below both the national (7.7%) and state (6.8%) levels, and is greatly improved compared with recent years. Snohomish County saw unemployment above 10% as recently as 2010.

Largely as a result of the aerospace industry presence, which requires a highly educated workforce, the district's socioeconomic indicators are above the national average. According to the American Community Survey's 2010 estimates, median family income in the district is approximately 121% of the national level. Per capita income is estimated to be 109% of the national level.

NARROW GENERAL FUND POSITION IS A RELATIVE CREDIT WEAKNESS; CONSERVATIVE FINANCIAL MANAGEMENT EXPECTS RESERVES TO IMPROVE

As with many school districts in Washington State, Everett School District No. 2 has typically maintained a somewhat low level of reserves. Over the five years through fiscal 2012 the district's General Fund balance has averaged 6.2% of General Fund revenues, and has fluctuated within a relatively small band. Based on unaudited results for fiscal 2013, the district believes the General Fund ended with a balance of $9.6 million (5% of revenues) after a planned drawdown. The district has a formal fund balance policy of maintaining at least 5% of annual expenditures in the General Fund. The district's demonstrated ability to operate within a narrow band of fluctuation in fund balance, albeit at a relatively low level, and to stay above the adopted policy level is indicative of a strong management team. Additionally, the district has indicated that it expects reserves to increase beginning in fiscal 2015. Future reviews of this rating will likely focus on management's ability to build reserves up from the minimum policy level, a level that is much lower than similarly rated districts nationally, and currently a credit weakness. If the district fails to keep up with its rated peers in terms of reserve growth, there could be future negative rating pressure.

Similar to most Washington school districts, the district's primary revenue source is state funding at roughly 65% of General Fund revenues in fiscal 2012. While the state has limited funding for schools in recent years, the recent decision by the Washington Supreme Court ("McCLeary Decision," see Moody's US Public Finance Weekly Credit Outlook of July 11, 2013) to require full funding of education by the state will have a positive effect on the district. The district believes state and local revenues will increase by nearly $5 million for fiscal 2014.

District voters have demonstrated significant support of local funding of education represented by consistent approval rates above 60% historically for maintenance and operation (M&O) levies. Current such levies expire in

2014. The district expects to return to voters to seek approval for four year extensions for these levies. These local sources of funding comprise more than 20% of General Fund revenues. The district currently also has a capital projects levy that helps support its significant capital requirements, and is in place through fiscal 2015.

MODERATELY HIGH LEVEL OF OUTSTANDING DEBT A RESULT OF A SIGNIFICANT CAPITAL IMPROVEMENT PLAN; RELATIVELY RAPID DEBT REPAYMENT

The district is one of the largest in Washington State, and has a significant capital program characterized by periodic bond issues. With the current offering, the district has approximately $215 million in outstanding general obligation debt. At 1.8% of assessed value, this level of outstanding debt is moderately elevated. Additionally, there is the potential that the district will seek significant new approval in the near future to support its capital plan. Positively, the currently outstanding debt has a relatively rapid payout, with 92% repaid within 10 years, and 100% repaid within 10.5 years. However, significant near-term bond issuance plans would likely result in an increase in the level of outstanding debt as a percentage of assessed value.

WHAT COULD MAKE THE RATING GO UP

- Significant and sustained improvement in the General Fund balance

- Significant increase in resident wealth levels

WHAT COULD MAKE THE RATING GO DOWN

- Material decline in General Fund balance

- A return to significant deterioration in the local economy

KEY STATISTICS

Estimated population: 131,214

Median family income as % of US: 121%

Per capita income as % of US: 109%

2013 full value: $11.9 billion

Estimated 2014 full value: $13.2 billion

Full value per capita: $90,700

Direct debt as % of full value: 1.8%

10 year principal payout: 92%

General Fund balance as a % of revenues: 5%

The principal methodology used in the enhanced rating was US States Rating Methodology published in April 2013. The principal methodology used in the underlying rating was General Obligation Bonds Issued by US Local Governments published in April 2013. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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