

New Issue: Laredo Independent School District, TX

MOODY'S ASSIGNS Aaa RATING TO LAREDO ISD (TX) \$57 MILLION UNLIMITED TAX SCHOOL BUILDING BONDS, SERIES 2006

A3 UNDERLYING RATING AFFECTS \$269 MILLION IN PARITY DEBT, INCLUDING CURRENT ISSUE

Primary & Secondary Education
TX

Moody's Rating

ISSUE	UNDERLYING RATING	RATING
Unlimited Tax School Building Bonds, Series 2006	A3	Aaa
Sale Amount \$57,000,000		
Expected Sale Date 08/15/06		
Rating Description TEXAS PSF GUARANTEE		

Opinion

NEW YORK, Aug 7, 2006 -- Moody's Investors Service has assigned a Aaa rating to Laredo Independent School District's \$57 million General Obligation Bonds, Series 2006. Prime credit quality is provided by a guarantee of the Texas Permanent School Fund (PSF) for timely payment of principal and interest in the event that the school district is unable to meet debt service requirements. Sizable PSF assets and conservative program regulations provide strong bondholder protection. Moody's believes the limitations placed upon the PSF's actual leverage remain conservative and consistent with this highest of ratings.

State statutes provide for the advancement of revenues by the PSF from their cash reserves, prior to default, sufficient to meet a school district's debt service obligations should the district be unable to make timely payment. These funds will, in turn, be intercepted from the District's next state aid allocation until full repayment, as either a lump sum or installment payment, to the PSF. For additional information on the PSF program please see Moody's Special Comment "Moody's Affirms The Aaa Rating for Texas Permanent School Fund Guarantee" dated August 2005.

At the same time, Moody's has assigned an A3 underlying rating to the current \$57 million sale. The District's outstanding debt was recently affirmed at A3 on July 10, 2006. The bonds are secured by an unlimited ad valorem tax levied against all taxable property within the District. The A3 rating takes into consideration the District's sizable and growing tax base, high debt levels that are somewhat supported by State aid, and satisfactory financial operations.

MODERATE GROWTH DRIVEN BY LOCATION IN SOUTH TEXAS

Located in Webb County (Moody's rated A2), the District is located in south Texas and serves the central part of the City of Laredo (Moody's rated A2). Although population in the City grew 44% between 1990 and 2000, the population of the District only grew 6.4% over this same period. The slower population growth represents the slower growth occurring in the District relative to the local area. The tax base is large, however, at \$1.7 billion for fiscal 2006 and has experienced healthy growth of 5.9% annually for the last five years. Growth is driven by an equal mix of new construction and reevaluations. New construction is occurring in residential and retail developments. In 2005, the tax base had a substantial increase of 18% due to a change in ownership of a medical center facility. Enrollment growth has been a moderate 1.5% annually over the last five years given that most of the new growth in the City is taking place in a neighboring school district. The District's wealth levels are low with a 2000 per capita income of \$9,046, which is a minimal 46.1% of the State and 41.9% of the Nation. Growth in the PCI has not kept pace with the State given that the State's PCI grew 52% relative to the District's 46% increase between 1990 and 2000. Moody's believes the tax base will continue to see moderate growth and that enrollment will follow historical trends.

DEBT BURDENS HIGH DESPITE SIGNIFICANT STATE AID

The District's debt burdens are substantially mitigated by State assistance which supports approximately 80% of total debt service requirements for unlimited tax debt and lease revenue bonds issued by the Laredo

ISD Public Facility Corporation. Including debt from the facility corporation and State assistance, the debt burdens are high at 4.6% on a direct basis and 10.1% on an overall basis. Without State assistance, the debt burdens increase to an elevated 17.2% direct and 23% overall. Debt is schedule for average retirement with 47% of principal repaid in ten years. After the current sale, the District will have no authorized but unissued debt remaining. Moody's believes the District's debt burdens will remain high; however, we also recognize the significant amount of State aid that helps to support annual debt service requirements.

SATISFACTORY GENERAL FUND RESERVE LEVEL

District officials were successful in building the General Fund balance over several years and then used the fund balance in 2005 for some one time capital needs. The total fund balance increased from \$14.2 million, or 10.7% of General Fund revenues in fiscal 2000 to \$35.2 million, or 19.9% of General Fund revenues in fiscal 2004. Annual surpluses were attributable to tightened expenditure controls and conservative budgeting. In 2005, the total fund balance decreased by \$6.4 million to \$28.7 million, or 16.8% of General Fund revenues. Given that the total fund balance has consistently held reserves for capital projects, Moody's notes that the unreserved portion of the fund balance has remained close to the \$12 million level and in fiscal 2005, the \$12.1 million unreserved balance equals 8.6% of General Fund revenues. Although the unreserved portion of the fund balance is relatively narrow, it still provides an adequate contingency reserve consistent with the A3 rating. Additionally, Moody's believes the fund balance is satisfactory given that the State supports a strong 80% of General Fund operations.

On February 1, 2003 the District secured additional financial flexibility when voters approved an increase in the tax rate limitation from \$13.50 per \$1,000 assessed valuation to the State maximum of \$15.00 per \$1,000 assessed valuation. Under the old State funding formula, the District had substantial tax margin and Moody's believes the new State funding program will continue to provide substantial support for the District's operations.

KEY STATISTICS:

Enrollment: 22,500

2006 Full valuation: \$1.7 billion

Full value per capita: \$16,736

2000 Per Capita Income: \$9,046 (46.1% of State)

Direct debt burden: 4.6%; without State assistance: 17.2%

Overall debt burden: 10.1%; without State assistance: 23.0%

Payout of Principal (10 years): 47.3%

2005 Undesignated General Fund balance: \$12.1 million (8.6% of General Fund revenues)

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RESEARCH

Summary: Laredo Independent School District, Texas; General Obligation; School State Program

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Credit Profile

US\$57. mil unlt'd tax sch bldg bnds ser 2006 dtd 08/15/2006
due 08/01/2036 AAA
Sale date: 14-AUG-2006

AFFIRMED

\$4.000 mil. Laredo Indpt Sch Dist GO (FSA) AAA/A(SPUR)
\$129.430 mil. Laredo Indpt Sch Dist PSF AAA

OUTLOOK: STABLE

Rationale

Standard & Poor's Ratings Services assigned its 'AAA' enhanced program rating and 'A' issuer credit rating (ICR), and stable outlook, to Laredo Independent School District, Texas' series 2006 unlimited-tax GO school building bonds and affirmed its 'AAA' enhanced program rating and 'A' ICR, and stable outlook, on the district's preexisting GO debt.

Standard & Poor's also affirmed its 'A' Standard & Poor's underlying rating (SPUR), and stable outlook, on the district's public property finance contractual obligations.

The enhanced rating reflects the security provided by the Texas Permanent School Fund.

The ICR and SPUR reflect the district's:

- Location in the Laredo MSA, which serves as a major international trade center;
- Strong state support for operations and debt service; and
- Sound financial position despite a high debt burden and additional capital needs.

These strengths are offset by the district's:

- Low wealth and income levels, and
- High overall debt burden.

An unlimited ad valorem property tax pledge secures the bonds. District officials will use bond proceeds to finance the construction of a new middle school, a new high school, and permanent K-3 classrooms that will replace portable classrooms.

The 14-square-mile Laredo Independent School District, with about 105,669 residents, is entirely within Laredo, Texas ('A+' SPUR, GO debt rating), which is located along the main trade corridor of the U.S.-Mexico border. The district serves an estimated student enrollment of 23,174 for fiscal 2006 at 20

elementary schools, four middle schools, and four high schools. Enrollment has grown by an average of almost 2% annually since fiscal 2000. Due to the district's relative maturity, management expects additional enrollment growth to remain a modest 1%-2% annually.

The city's 15.00% employment growth over the past five years outpaced labor force growth and reduced the historically above-average unemployment rate to 5.65% in 2005, which was just slightly higher than state and national rates. The district's \$1.94 billion fiscal 2007 property tax base is moderately concentrated with the 10 leading taxpayers accounting for 13% of total assessed value. Assessed value growth has historically averaged a modest 2.0%-3.0% annually since 2000 -- the exception was a 12.6% increase in fiscal 2005 due to some revaluations and strong commercial redevelopment in downtown Laredo. District wealth levels remain well below average: Market value is below \$20,000 per capita and the city's per capita effective buying income indicator is just 54% of the national average.

Laredo Independent School District's financial position is sound. Steady enrollment increases and strong property tax base growth in 2005 have helped the district build sound reserves. The \$19.8 million unreserved general fund balance at fiscal year-end 2005 equaled about 12% of operating expenditures; the total \$28.8 million fund balance was roughly 17% of expenditures. In fiscal 2006, district officials will draw down reserves with a planned \$5 million of onetime capital expenditures to supplement the construction and rehabilitation of school buildings. After the drawdown, they are projecting an adequate unreserved fund balance at 8.7% of expenditures, which management plans to increase in subsequent fiscal years given the board's policy to maintain a minimum of two months' operating expenditures in reserve. The adopted fiscal 2007 budget is balanced based on conservative revenue estimations and the use of the additional four cents of maintenance taxes permitted under House Bill 1 of the 2006 Texas school financing reform provisions.

Laredo Independent School District's management practices are considered good under Standard & Poor's financial management assessment (FMA) methodology, indicating practices are deemed currently good but not comprehensive. In addition to a formal fund balance policy, key items include monthly fiscal presentations to the board that track revenues, expenditures, and investment performance. Management, however, does not have a formal capital improvement plan or debt management policy that extends beyond state guidelines.

Outlook

The stable outlook on the enhanced program rating reflects the Texas Permanent School Fund's strength and stability. The stable outlook on the ICR and SPUR reflects the expectation that district officials have reasonably identified all major capital requirements and that continued prudent financial management and strong state support will allow the district to manage its high debt burden. Historically, stable economic and student enrollment growth also lend stability to the rating.

Debt

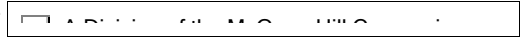
Laredo Independent School District is currently receiving instructional facilities allotment and Tier III funding, which pays for almost 80% of its GO debt service requirement, excluding public property finance contractual obligations. Despite the substantial state aid for GO debt service, the overall net debt burden, assuming the same state support, is still considered a high 9.5% of market value. Over the past six years, the district had undertaken an extensive rehabilitation and modernization of its school facilities, issuing more than \$200 million of debt before this issuance. According to management, this \$57 million authorization should complete its capital program; therefore, management does not plan to go back to the electorate for at least the next five years. Officials, however, intend to issue roughly \$12 million of TANs later this year to fund seasonal cash flow shortfalls.

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Tax Supported
New Issue

**Laredo Independent School
District, Texas**

Ratings

New Issue

Unlimited Tax School Building
Bonds, Series 2006* AAA

Outstanding Debt

Unlimited Tax Bonds..... A
Public Property Finance
Contractual Obligations..... A
Lease Revenue Bonds..... A

Rating Outlook Stable
(Revised from Positive on 7/7/06)

*The 'AAA' rating is based on the guaranty provided by the Texas Permanent School Fund, whose insurer financial strength is rated 'AAA' by Fitch Ratings. The underlying rating reflecting the credit quality without the guaranty is 'A'.

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New Issue Details

\$57,000,000 Unlimited Tax School Building Bonds, Series 2006, are scheduled to price the week of Aug. 14 via a syndicate led by JP Morgan. Dated Aug. 15, 2006, the bonds will be issued as a combination of current interest and capital appreciation bonds and are subject to optional redemption as prescribed in the offering statement.

Security: Bonds are secured by an unlimited tax pledge of the district as well as a guaranty provided by the Texas Permanent School Fund.

Purpose: Bond proceeds will be used for the construction, acquisition, and equipping of schools; to purchase school sites; and to pay costs of issuance

■ Outlook

The underlying 'A' rating reflects the Laredo Independent School District's (Laredo ISD, the district) adequate but narrowed financial position, substantial state support for operations and capital construction, and recent notable property tax base growth. The district's financial reserves have thinned as a result of planned capital outlays as well as past large salary increases and personnel additions for police and security functions, leading to a Rating Outlook revision for all district debt to Stable from Positive on July 7, 2006. Fitch Ratings believes that district trustees will adopt the administration's proposed balanced budget plan for fiscal 2007 as an initial step toward returning its general fund balance to compliance with its policy requiring reserves to equal two months of expenditures. The district's high direct debt burden as a ratio of taxable assessed valuation (TAV), even after adjusting for state support, is a credit concern, although sustained voter support is notable.

■ Rating Considerations

Strong growth returned to the district's tax base in recent fiscal periods, most notably in fiscal 2005, when TAV increased by 18% due to the purchase of the city's nonprofit hospital by a private company, making it a taxable entity. Preliminary fiscal 2007 estimates point to growth of over 8% due to equal parts new construction and reappraisal. Ongoing downtown development should spur additional TAV growth in the future. The district's top 10 taxpayers account for a moderate 14% of total TAV, led by the privately acquired hospital at over 5%. Current property tax collection rates are below average and typical for the border region but adequate on a total collections basis.

The district's financial position had shown dramatic improvement in recent years but narrowed beginning in fiscal 2005 due to a combination of one-time and recurring costs. As a result of planned capital outlays, the creation of a district police department, and large teacher pay raises (\$2,000), fiscal 2005 posted a \$6.4 million general fund operating deficit, decreasing the undesignated fund balance to \$12.2 million, or 6.8% of spending. Program expansions and capital outlays continued in fiscal 2006, resulting in a projected drawdown of \$13.6 million, although the undesignated portion of its reserves is projected to decline by less than \$5 million, leading to available reserves of \$7.5 million, or 4.4% of spending. Under the new school funding formula, the administration's proposed fiscal 2007 budget is balanced with the aid of the optional four-cent levy allowed by the new state law for general purposes. The proposed budget conservatively assumes a slight decline in average daily attendance (ADA), as well as year-round full employment, with no savings due to turnover or vacancies. Of long-term concern to Fitch is the district's ability to return to structural balance in the face of increasing payroll costs and reduced local control under the new school funding formula.

August 10, 2006

The Texas Legislature recently passed property tax relief measures that were subsequently signed by the governor. The legislation provides for mandatory reductions in the local operations and maintenance (O&M) property tax rate of 11% for fiscal 2007 and a cumulative 33% for fiscal 2008, based on the fiscal 2006 O&M tax rate. To offset the loss of local revenue, the state will increase its share of funding to local school districts, including Laredo ISD, so that the measures are expected to be revenue neutral.

Due to the district's very low property wealth per student, the state currently supports 80% of Laredo ISD's debt service for its unlimited tax bonds, including this issue, and lease revenue bonds. Adjusting for this substantial state support, direct debt as a percentage of TAV is still high at 5.5% due to the districtwide capital plan. Direct debt on a per capita basis is moderate at just under \$900. Overall debt to TAV is high at 8.1%, reflecting issuances by the city of Laredo (general obligation [GO] debt rated 'A+' by Fitch), Webb County (GO debt rated 'A+' by Fitch), and Laredo Community College District (GO debt rated 'A+' by Fitch). Overall debt per capita is more moderate at just over \$1,300. Principal payout for all debt is slightly below average at 41% in 10 years. Given the recent award for state support on the series 2006 bonds, the debt service tax impact for the 2006 bonds is projected to be about \$0.05 initially and decrease slightly thereafter upon receipt of existing debt allotment funds. In addition, because of declining cash reserves, as well as the large amount of grant funds awarded to the district, a tax anticipation note borrowing of approximately \$12 million is planned for later this month.

Located on the Rio Grande, the border city of Laredo serves as the principal port of entry into Mexico and the largest inland port in the U.S. Over the past decade, Laredo has undergone substantial population growth. However, the district's enrollment of approximately 23,000 has experienced only modest growth due to central Laredo's nearly complete development. Laredo's proximity to Mexico and an economic base focused on trade and transportation closely link its economic health to that of its southern neighbor. Trickle-down effects of fluctuations in the value of the peso and dependence on international policies can create some economic uncertainty for the area. Recent integration of the U.S. and Mexican economies through free trade agreements and Laredo's essential transportation network has added stability.

■ Strengths

- Sustained community support for the growing capital plan.
- Substantial state support for operations and capital-related program.
- Growing taxable values.

■ Risks

- Weakened financial margins.
- High debt levels.

For more information, see Fitch Research on "Laredo Independent School District, Texas," dated July 9, 2006, available on Fitch's web site at www.fitchratings.com.