MOODY'S INVESTORS SERVICE

CREDIT OPINION
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Pima County Community College District, AZ

Update to credit analysis

Summary

Pima County Community College District's (PCC; Aa2 stable) credit quality reflects its very good brand and strategic position as the main provider of low-cost two-year higher education and vocational training in the Tucson, Arizona (Aa3 stable GO) metropolitan area. The college's strong wealth and liquidity, with approximately $192 million in total cash and investments and over 300 monthly days cash on hand in fiscal 2023, continue to provide good financial flexibility and strong coverage of expenses and debt. Enrollment remains well below pre-pandemic levels, but enrollment growth in fall 2023 and the expansion of in-demand vocational programs will continue to support the college's market position. PCC's operating performance weakened significantly in fiscal 2023 because of substantial expense inflation growth, but net tuition revenue growth, growing tax revenue and expense control measures instituted by the college's disciplined financial management team provide good prospects for improved EBIDA margins and debt service coverage over the next two fiscal years. PCC's leverage profile remains manageable, as the college maintains a low direct debt burden and continues to fund ongoing capital projects with financial reserves and existing bond proceeds.

Credit strengths

» Very good brand and strategic positioning as the provider of two-year and vocational education for the Tucson, AZ metropolitan area

» Strong monthly liquidity of $172 million in fiscal 2023 provides for over 300 monthly days cash on hand

» Disciplined and experienced financial management team with a track record of managing through enrollment headwinds and producing generally strong operating performance

Credit challenges

» Highly competitive market for students from a strong local economy and numerous other low-cost in-state higher education providers

» Enrollment declines and rising expenses have contributed to weakened operating performance in recent fiscal years

» Planned use of financial reserves on capital projects will limit wealth growth over the coming fiscal years

Rating outlook

The stable outlook reflects Moody's expectation that PCC's operating performance will improve in fiscal years 2024 and 2025 as the college grows net tuition revenue and enacts expense control measures, with improved EBIDA margins and annual debt service coverage above 2x. It also incorporates expectations that the college's leverage profile will remain manageable, with no additional issuance of revenue backed debt.

Factors that could lead to an upgrade

- Notable increase in operating scale and market share, reflected in material operating revenue growth and sustained increases in FTE enrollment beyond current level of 16,585
- Material increase in total cash and investments that outpaces peers and provides greater coverage of debt and expenses

Factors that could lead to a downgrade

- Continued deterioration of operating performance with low single-digit EBIDA margins and annual debt service coverage well below 2x.
- Notable increase in leverage from additional debt issuance without accompanying financial reserve, tax revenue and/or operating scale growth
- Significant reduction in unrestricted liquidity below 200 monthly days cash on hand

Key indicators

Exhibit 1
PIMA COUNTY COMMUNITY COLLEGE DISTRICT, AZ

	2019	2020	2021	2022	2023	Median: Aa Rated Public Universities
Total FTE Enrollment	19,512	15,544	15,000	15,293	16,585	30,783
Operating Revenue ($000)	183,441	191,630	197,486	224,841	209,562	1,505,466
Annual Change in Operating Revenue (%)	2.7	4.5	3.1	13.9	-6.8	8.8
Total Cash & Investments ($000)	150,166	181,970	193,329	210,249	191,531	1,947,594
Total Adjusted Debt ($000)	345,612	332,561	356,428	377,420	359,178	1,862,165
Total Cash & Investments to Total Adjusted Debt (x)	0.4	0.5	0.5	0.6	0.5	1.0
Total Cash & Investments to Operating Expenses (x)	0.9	1.0	1.1	1.1	0.9	1.3
Monthly Days Cash on Hand (x)	323	354	387	376	301	191
EBIDA Margin (%)	15.9	9.9	17.7	18.3	1.6	14.4
Total Debt to EBIDA (x)	2.0	3.0	1.6	1.3	15.4	3.4
Annual Debt Service Coverage (x)	25.5	3.3	7.8	8.9	0.7	4.1

Source: Moody's Ratings

Profile

Pima County Community College District is the main provider of two-year education and vocational training across five campuses in Pima County, Arizona. The district served fall 2023 enrollment of 16,585 full-time equivalent students and had operating revenue of approximately $210 million in fiscal 2023.

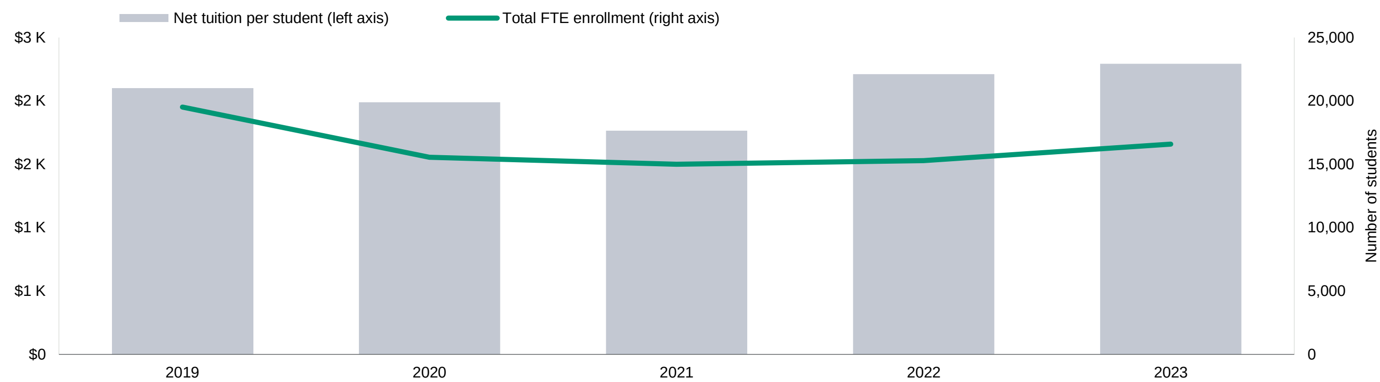
Detailed credit considerations

Market position

PCC maintains a very good market position given its important role as the two-year provider of higher education and vocational training in the economically diverse and growing Tucson area. The college continues to invest in new programs and tailor both its credit and noncredit offerings to student demand and local workforce needs. Enrollment has grown modestly in each of the past two academic years, with the college reporting continued growth in spring 2024. Enrollment growth in general education programs presently lags the college's vocational programs, given fierce competition from Arizona's four-year institutions. The colleges continues to invest in new capital facilities to expand its academic offerings under its Centers of Excellence model. Construction is now complete on new advanced manufacturing and aviation technology buildings and class size capacity in those programs will greatly expand as a result. The college is now working to renovate older facilities to expand its health sciences professions center and HVAC training program to meet growing demand in those fields of study.

Exhibit 2

Modest enrollment growth over the past two years has supported growing net tuition revenue



FTE enrollment is for the fall of each academic year. Net tuition per student is for each fiscal year
Source: Moody's Ratings

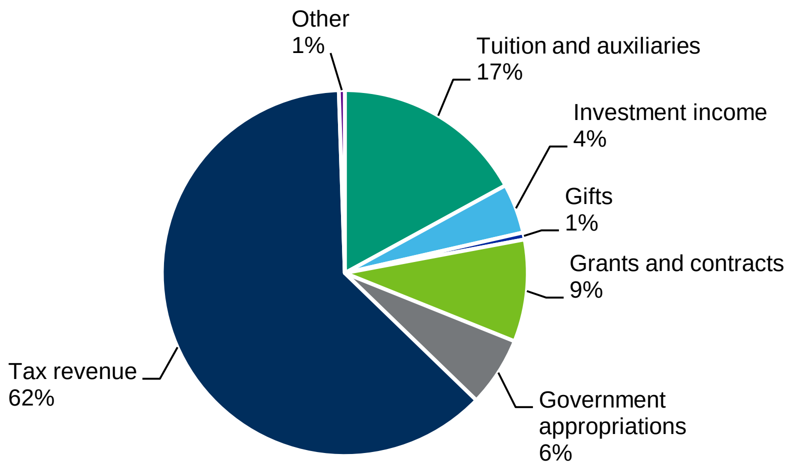
Operating performance

Operating performance will improve in fiscal 2024 after a year of deficit operations in fiscal 2023. PCC's EBIDA margin weakened notably as a result of the expiration of HEERF funding, modest net tuition revenue growth and substantial expense increases from inflation and a large wage and salary adjustment for college faculty and staff. Enrollment growth and planned increases in tuition and the property tax levy rate will support stronger operating revenue in fiscal 2024 and fiscal 2025. The college's experienced and disciplined financial management team is also planning a number of budget control measures such as eliminating vacant positions and centralizing spending to reduce annual operating expenses by $7.5 million over the next three fiscal years. If EBIDA margins and annual debt service coverage do not strengthen over the next two fiscal years, PCC's credit quality could weaken as a result.

Exhibit 3

Dedicated property tax revenue from Pima County's growing tax base will continue to support operating revenue growth

Fiscal 2023 operating revenue by source



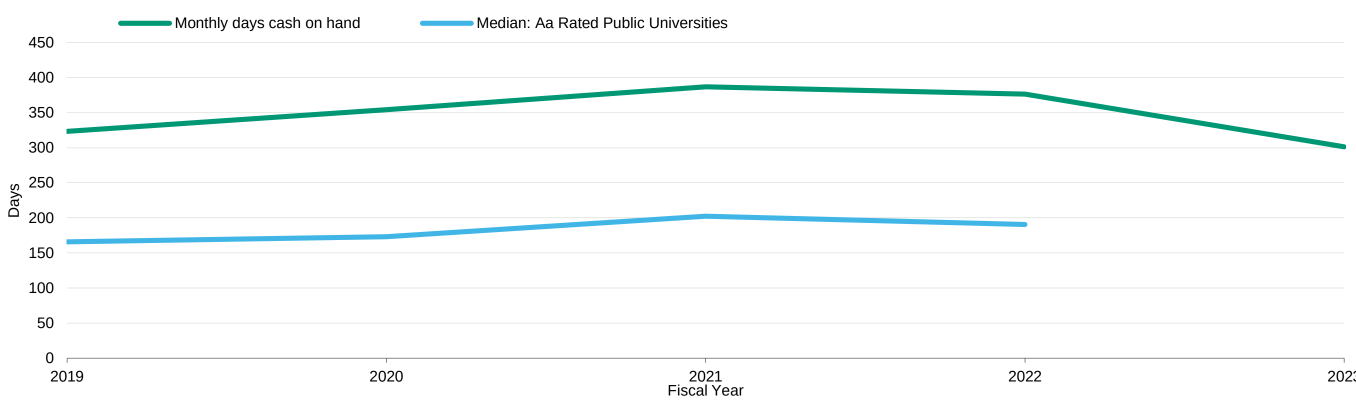
Source: Moody's Ratings

Financial resources and liquidity

PCC's wealth will remain stable or decline modestly over the next two fiscal years as the college continues to spend down reserves on planned capital projects. Favorably, the college's total cash and investments has grown 28% over the last five fiscal years, providing greater resources for the college to invest in strategic program initiatives and capital projects. Liquidity will remain excellent as the college maintains a very conservative policy to maintain at least 75% of annual operating expenses in liquid reserves, a threshold it has exceeded for several years.

Exhibit 4

PCC's liquidity remains well above similarly rated peer institutions

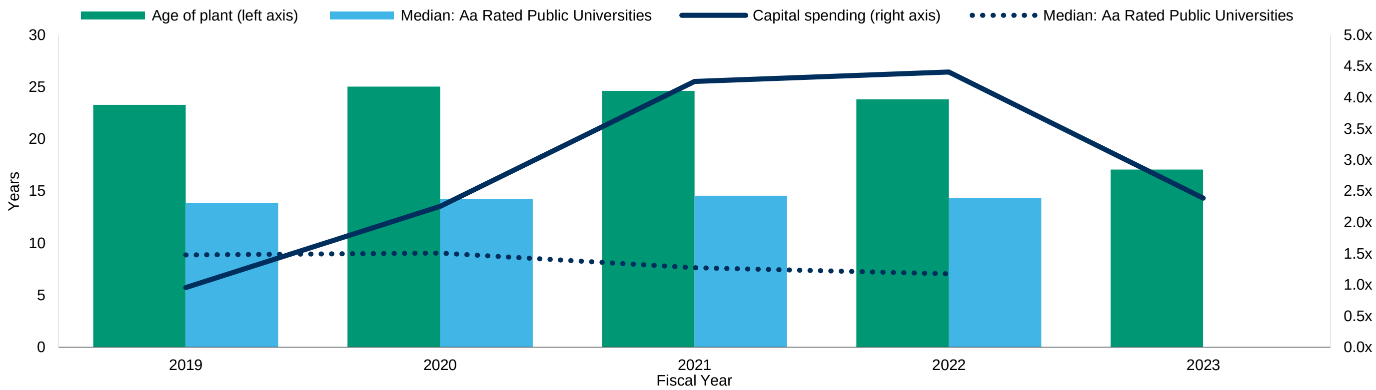


Source: Moody's Ratings

Leverage and coverage

PCC's leverage profile will remain manageable as the college maintains a low level of outstanding debt and has no additional borrowing plans. Financial reserves continue to provide good coverage of outstanding debt. Inclusive of its outstanding pension obligation, total cash and investments covered total outstanding debt by 0.53x in fiscal 2023, solid but below the public Aa median of 0.99x. Ongoing capital projects on the college's Centers of Excellence will be financed with unspent bond proceeds and existing financial reserves. PCC is in the process of exploring future capital plans once its Centers of Excellence projects are completed and is examining how to best use its real estate portfolio to provide services across Pima County.

Exhibit 5
Elevated capital spending in recent fiscal years continues to reduce the college's age of plant

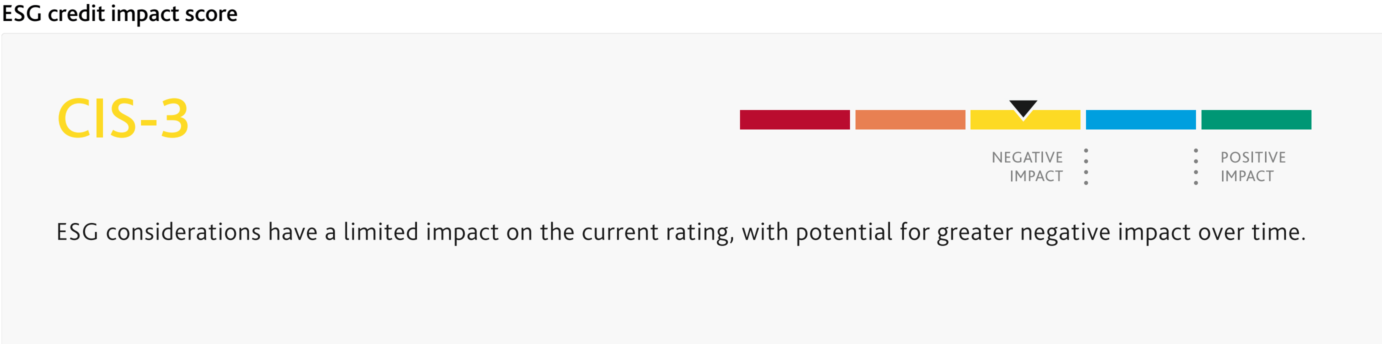


Source: Moody's Ratings

ESG considerations

Pima County Community College District, AZ's ESG credit impact score is CIS-3

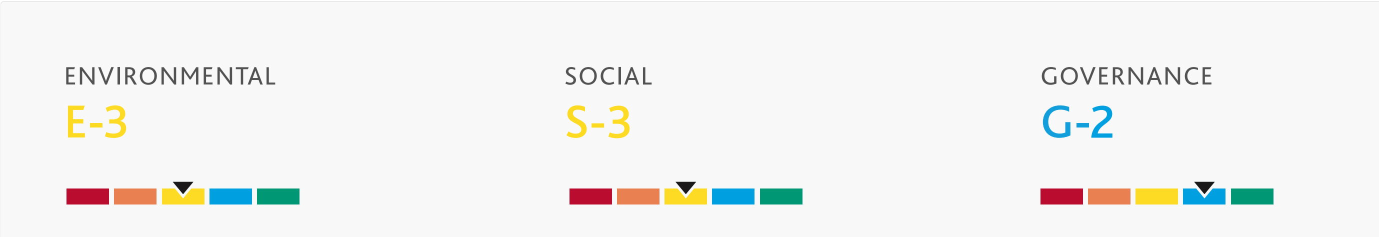
Exhibit 6
ESG credit impact score



Source: Moody's Ratings

Pima County Community College District's **CIS-3** indicates that ESG considerations have a limited impact on the current rating with potential for greater negative impact over time. Environmental and social risks, particularly demographic and societal trends, provide for this elevated risk. The college's strong role as a provider of two-year education in a growing metropolitan region partially mitigates its ESG risk exposures.

Exhibit 7
ESG issuer profile scores



Source: Moody's Ratings

Environmental

Pima County CCD's exposure to environmental risks is (**E-3**). This incorporates physical climate risks stemming from high heat and water stress. With its campus locations in Tucson, the college benefits from both the state and local government's long history of successfully managing its water resources and consumption.

Social

Pima County CCD's exposure to social risks is (**S-3**). While demographic trends in the state, especially the Tucson metropolitan area, are favorable, a robust local economy and highly competitive higher education market provides enrollment headwinds. Favorably, Pima County CCD's role as the sole provider of two-year education and provides a high value proposition for traditional and nontraditional students as well as employers looking for workforce development programs. Like many community colleges, Pima County CCD benefits from a flexible faculty structure, limiting fixed costs and providing budgetary relief, if needed, limiting human capital risks.

Governance

Pima County CCD's exposure to governance risk is (**G-2**). The college has a track record of generating solid and stable operating margins, growing financial reserves and limiting it use of debt. Like most community colleges, Pima County CCD benefits from diverse revenue streams that include tuition, property taxes and state aid. This revenue mix helps to insulate it from funding volatility at the state level, as well as countercyclical enrollment trends. The college is governed by a small, five member board of elected officials. While the current board operates effectively, this structure adds exposure to potential political considerations which could create misalignment with institutional priorities.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The principal methodology used in this rating was Higher Education Methodology published in August 2021. The Higher Education Methodology includes a scorecard that summarizes the factors that are generally most important to higher education credit profiles. Because the scorecard is a summary and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not match an assigned rating. We assess brand and strategic positioning, financial policy and strategy and operating environment on a qualitative basis.

The four- notch distinction between the scorecard-indicated outcome and the assigned rating reflects expectations that operating performance will materially improve in fiscal years 2024 and 2025 because of budget stabilization measures, resulting in stronger EBIDA margins and annual debt service coverage.

Exhibit 8

Pima County Community College District, AZ

Scorecard Factors and Sub-factors		Value	Score
Factor 1:	**Scale (15%)**		
	Adjusted Operating Revenue (USD Million)	210	A
Factor 2:	**Market Profile (20%)**		
	Brand and Strategic Positioning	A	A
	Operating Environment	Aa	Aa
Factor 3:	**Operating Performance (10%)**		
	EBIDA Margin	2%	Ba
Factor 4:	**Financial Resources and Liquidity (25%)**		
	Total Cash and Investments (USD Million)	192	Aa
	Total Cash and Investments to Operating Expenses	0.9	Aa
Factor 5:	**Leverage and coverage (20%)**		
	Total Cash and Investments to Total Adjusted Debt	0.5	A
	Annual Debt Service Coverage	0.7	Ba
Factor 6:	**Financial Policy and Strategy (10%)**		
	Financial Policy and Strategy	A	A
	Scorecard-Indicated Outcome		A3
	Assigned Rating		Aa2

Data is based on most recent fiscal year available. Debt may include pro forma data for new debt issued or proposed to be issued after the close of the fiscal year.

For non-US issuers, nominal figures are in US dollars consistent with the Higher Education Methodology.

Source: Moody's Ratings

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