FitchRatings

FITCH RATES SAN ANTONIO ISD, TX GO BONDS 'AAA' PSF; 'AA' UNDERLYING; OUTLOOK REVISED TO STABLE

Fitch Ratings-Austin-07 December 2010: Fitch Ratings has assigned an 'AAA' rating to the following San Antonio Independent School District, TX bonds:

--$7.5 million unlimited tax school building bonds, series 2010A;
--$92.5 million unlimited tax school building bonds, taxable series 2010B (Direct Subsidy-Build America Bonds).

The 'AAA' long-term rating reflects the guarantee provided by the Texas Permanent School Fund (PSF), whose Insurer Financial Strength is rated 'AAA' by Fitch. Fitch also assigns an 'AA' underlying rating to the series 2010A and 2010B bonds.

In addition, Fitch affirms the following ratings on the district's outstanding bonds:

--$448.9 million unlimited tax bonds at 'AA'.

The Rating Outlook is revised to Stable from Negative.

RATING RATIONALE:
--The Outlook revision to Stable from Negative reflects the district's stabilized financial position, enabled by management's efforts to right-size its operations as its enrollment base continues to contract.
--The underlying rating reflects the district's solid financial position and management's notable efforts to maintain structural balance despite the challenges of shifting demographic patterns that have caused its enrollment base to stagnate.
--Stabilization of the enrollment base hinges on the successful implementation of the district's comprehensive plan to restructure and improve its aging schools. However, its demographic challenges are formidable given county-wide population growth patterns in the suburban areas beyond the district's boundaries.
--The recent voter approval of the district's large bond program is key to implementing its long-term plans but will further increase its already high debt burden.
--The service area has fared relatively well during the national recession, aided by its diverse economy, large and growing military presence, and stable home prices; however, overall wealth levels remain below average.

KEY RATING DRIVER:

--The district's continued progress in its restructuring efforts aimed at right-sizing its operations and capital plant is key to its long-term financial sustainability and maintenance of credit quality.

SECURITY:

The bonds are secured by an unlimited property tax levy and are secured further by the PSF guarantee.

CREDIT SUMMARY:

The district, which covers about 80 square miles, is located in Bexar County and primarily encompasses downtown San Antonio. Prominent industries in the local economy are domestic and international trade, convention and tourism, military and government employment, medical and health care, finance, and telecommunications. Due primarily to shifting demographic patterns, the district's average daily attendance (ADA) has declined by a total of 9.2% since fiscal 2000, despite

the district's efforts to reverse the trend through the expansion of early childhood programs, the implementation of alternative educational venues, such as internal charter schools, and previous bond-financed campus improvements.

The district's financial profile remains under pressure due to ongoing ADA declines. Notably, management avoided structural imbalances in fiscal years 2008 and 2009 through a combination of closing and re-purposing nine schools. School repurposing and closures, deferral of pay hikes in fiscal years 2008 and 2009, and leaner staffing levels enabled the district to cut over $36 million from fiscal 2008-2010, enabling the district to fund pay hikes in fiscal 2010. Fiscal 2009 posted a solid $9.9 million operating surplus, increasing the unreserved fund balance to $59.3 million or a strong 15.7% of spending. Unaudited fiscal 2010 results point to balanced operations which provided a 4.9% pay hike. The fiscal 2011 budget is balanced; despite a shortfall in expected ADA growth, ongoing cost controls are expected to maintain level reserves.

The current offering represents the first installment of the large $515 million GO authorization approved by a high 66% of voters in November 2010. As total facility needs were estimated at $1.2 billion, the authorization will fund the first phase of the district's 10-12 year facilities plan. This initial phase will fund extensive renovations to 22 campuses, allowing the district to consolidate five campuses within three years, generating an estimated $10 million in annual operating costs. The long-term plan, which will need additional voter authorization, calls for the consolidation of a total of 14 campuses, inclusive of these first five schools. Adjusted for 30% state support for debt service, the district's overall debt burden is moderate on a per capita basis at $3,085 but high as a percentage of market value at 7.2%. The planned issuance of the remaining $415 million in authorization by 2014 will further increase the debt burden and increase the debt service tax rate to a projected maximum of a high $0.41 per $100 taxable assessed valuation (TAV), up considerably from the current $0.23 rate. Principal amortization is slow at 35% principal retired within 10 years.

Considerations for Taxable/Build America Bonds Investors
This sector credit profile is provided as background for investors new to the municipal market.
Local Government General Obligation Bonds
The unlimited taxing power of most local government general obligation pledges is the broadest security a U.S. local government can provide to the repayment of its long-term borrowing and, therefore, is the best indicator of its overall credit quality. The average local government general obligation rating is 'AA', with approximately 85% rated at or above 'AA-' and 1% rated 'BBB+' or below. The relatively high ratings reflect local governments' inherent strengths: the authority to levy property taxes, nonpayment of which can result in property foreclosures; additional taxing power that can include sales, utility, and income taxes; and essentiality of and lack of competition for services provided by local governments. Those with low investment-grade or below-investment-grade ratings generally have a combination of a limited or highly volatile economic base, high levels of long-term liabilities, including debt and post-employment benefits, and/or unusually limited financial flexibility. For additional information on these ratings, see 'U.S. Local Government General Obligation Rating Guidelines,' dated Oct. 8, 2010 and available on Fitch's Web site at www.fitchratings.com.

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Additional information is available at 'www.fitchratings.com'.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, LoanPerformance, Inc., and IHS Global Insight.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria', dated Aug. 16, 2010;
--'U.S. Local Government Tax-Supported Rating Criteria', dated Dec. 21, 2009;
--'State Revolving Fund and Municipal Loan Pool Rating Guidelines', dated April 28, 2008.

For information on Build America Bonds, visit 'www.fitchratings.com/BABs'.

Applicable Criteria and Related Research:
State Revolving Fund and Municipal Loan Pool Rating Guidelines
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=384150
Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=548605
U.S. Local Government Tax-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=564566

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