

RatingsDirect®

Summary:

Colorado; Note

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US\$500.0 mil TRANs ser 2023A due 06/28/2024

Short Term Rating

SP-1+

New

Credit Highlights

- S&P Global Ratings assigned its 'SP-1+' short-term rating to the State of Colorado's \$500 million series 2023A education tax and revenue anticipation notes loan program (E-TRANs).

Security

Securing the principal of the 2023A E-TRANs are repayments from the individual school districts in the pool on a several basis, as well as the state's pledge of other available investments should school loan repayments be delinquent. Colorado law provides for a direct deposit to the state treasurer by county treasurers of school district property taxes to the extent local school districts do not repay their obligations to the state. All school district cash-flow obligations must be repaid by June 25, 2024, although in practice, school loans in previous years have generally been repaid much earlier than their scheduled maturity. If school payments are insufficient, Colorado's backup liquidity is pledged to make up any shortfall on or after June 25, 2024.

Credit overview

The series 2023A notes mature on June 28, 2024. The proceeds will be used to fund the state's fiscal 2024 interest-free cash-flow loan program for local school district borrowers.

We consider the projected coverage level, based on the state's combined repayment sources, including the proposed series 2023A E-TRANs and a subsequent expected E-TRANs issuance in fiscal 2024 of about \$650 million, very strong at 7.34x, especially since it conservatively assumes no repayment by schools of their cash-flow loans. Despite our very strong assessment, we note the state, in practice, has never had to use its own alternate liquidity for E-TRANs, because there has never been a school cash-flow loan default in the program's 21-year history.

Colorado's outlook remains strong with upward revisions within its June 2023 forecast spurred by strong year-to-date fiscal 2023 revenue growth, resulting in projected historic Taxpayer Bill of Rights (TABOR) refunds. General fund revenues are projected to increase to \$17.8 billion in fiscal 2023, up 0.5% compared with \$17.7 billion in fiscal 2022, followed by a projected decline of 7.1% to \$16.5 billion in fiscal 2024 due to slowing wage growth and tighter lending conditions dragging economic growth. The state estimates it will end fiscal 2023 with a very strong general fund budgetary-basis balance equal to \$3.7 billion, or 18.5% of appropriations above its 15% target, and estimates a comparable very strong general fund balance of \$3.7 billion, or 21.2% at fiscal year-end 2024. Similar to fiscal years 2022 and 2023, Colorado's cash position is elevated to the point where the state does not expect to issue general fund cash flow notes in fiscal 2024, and revenues are expected to exceed the constitutional TABOR revenue cap in fiscal

2023 by \$3.38 billion, to be refunded to taxpayers in the following fiscal year.

If necessary for E-TRANs repayment, Colorado expects to first use alternate liquidity from its highway and education funds by purchasing the school notes as an investment in those funds, but if these two funds are not sufficient, the state pledges to use available general fund liquidity after payment of general fund notes (G-TRANs), if any are outstanding. As the state does not plan to issue fiscal 2024 G-TRANs, the full projected \$6.78 billion of general fund borrowable resources are available, if necessary, to repay the E-TRANs, and are factored into our calculation of projected note coverage.

The rating reflects our view of Colorado's:

- Very strong 1.45x projected cash coverage at note maturity by projected fiscal year-end 2024 cash from the state's education and highway funds, assuming no repayment on any of the underlying financed school district cash-flow loans pledged to the E-TRANs, and very strong 7.34x projected cash coverage based on the state's combined repayment sources; and
- Long history of the E-TRANs program, with no delinquent school district loan repayments.

For additional information on the long-term creditworthiness of the state, see our most recent full analysis on Colorado, published May 19, 2022, on RatingsDirect.

Environmental, social, and governance

In our view, environmental, social, and governance factors reflect those of the State of Colorado.

Credit Opinion

Flow of pledged revenues

Securing the principal of the 2023A E-TRANs are repayments from the individual school districts in the pool on a several basis, as well as the state's pledge of other available investments should school loan repayments be delinquent. Colorado law provides for a direct deposit to the state treasurer by county treasurers of school district property taxes if local school districts do not repay their obligations to the state. All school district cash-flow obligations must be repaid by June 25, 2024, although in practice, school loans have generally been repaid much earlier. If school payments are insufficient, Colorado's back-up liquidity is pledged to make up any shortfall on or after June 25, 2024.

School obligations repay only the E-TRANs principal. The state must pay the interest-cost component of the education loan TRANs out of its general fund. Colorado intends to pay in advance series 2023A note interest from a state general fund appropriation at the time of E-TRANs closing, pursuant to the notes' resolution, which is the same procedure followed for previous years' series of E-TRANs.

Each school district pledges to pay to the state treasurer, one business day after receipt, all ad valorem taxes credited to its general fund after March 1, 2024, until its respective cash-flow loans are repaid. District tax revenues are pledged on a first-lien basis. Over the long history of the state's E-TRANs program, no participating school district has ever defaulted on its E-TRANs cash-flow note. However, if a local school district defaults on its school obligation after June 25, 2024, Colorado covenants to purchase the defaulting school obligation at par from its restricted nongeneral fund

holdings as an eligible investment for the funds to pay the E-TRANs by their June 28, 2024, maturity date. Unexpended proceeds (which are deposited as working cash reserves) are also available for payment of any defaulting school obligations, although we do not include this in our coverage calculation.

The state's restricted highway and education funds are available as alternate liquidity for the E-TRANs apart from, and not available as, liquidity for Colorado's general fund or G-TRANs, if G-TRANs were unexpectedly to be issued later this fiscal year; the highway and education funds are available to be used to purchase any potentially defaulted school notes as an investment.

As a practical matter, the state expects it would first tap the education and highway funds, if needed, and then, if necessary, use other internally borrowable state general fund resources. Pledged E-TRANs money will be held in a segregated note-repayment account, the investments of which will be commingled within the state's general fund.

State alternate liquidity coverage

Colorado projects that the primary sources of backup liquidity, the state education and highway funds (not including other funds), will have a combined projected cash balance of \$1.66 billion at fiscal year-end June 30, 2024, down modestly but comparable with the estimated \$1.84 billion projected at fiscal year-end 2023.

In addition to the education and highway funds, the state projects to have extra borrowable resources of \$6.78 billion at fiscal year-end 2024 from its general cash pool, which would also be available for the E-TRANs.

The state estimates the highway fund will hold \$384.9 million at fiscal year-end June 30, 2024, and the education fund will have \$1.28 billion, for a combined total of \$1.66 billion. This would provide strong 3.33x cash coverage on the \$500 million series 2023A E-TRANs. However, the state plans to issue about \$650 million (estimated, subject to change) additional E-TRANs in January 2024, which will reduce projected cash coverage by highway and education funds alone to 1.45x on the combined \$1.15 billion of E-TRANs to be outstanding, assuming no school district repays any part of its cash-flow note. However, adding in the state's other projected available general and other funds' borrowable resources of \$6.78 billion, we calculate cash liquidity coverage by education fund, highway fund, and cash pool borrowable resources to be a very strong 7.34x on the combined fiscal 2023A E-TRANs and the projected additional 2023B E-TRANs.

The historical cash coverage on last fiscal year's \$775 million combined series 2022A&B E-TRANs (issued for fiscal 2023) by state education and highway funds (\$1.84 billion) alone at fiscal year-end 2023 was 2.38x. Including all other available state borrowable resources of \$7.04 billion at fiscal year-end 2023, combined E-TRAN actual coverage was a very strong 11.47x, slightly higher than originally projected.

Colorado expects to have sufficient liquidity to purchase a defaulted school loan on short notice, if necessary. State investment practices remain conservative, in our opinion. The state has two investment pools: one with short-term cash investments and the other with long-term ones. As of May 2023, the state's total portfolio mix of investments held \$20.86 billion, with 36.3% invested in corporate securities, 23.9% in commercial paper, 20.7% in U.S. Treasury notes, 6.6% in federal agencies, 6.4% in money market securities, 3.7% in agency CMOs, and 2.4% in asset backed securities.

Because the schools repay only principal, Colorado's obligation to repay the interest component on the education loan

TRANS is entirely a state general fund obligation, and restricted alternate liquidity available to purchase school obligations cannot be used to pay E-TRANS interest. However, because Colorado intends to fund full interest in advance at note closing, we believe state appropriation risk is mitigated. Note repayment account investments will be commingled with the general fund as a subaccount. As per the resolution, funds in this account are irrevocably pledged to, and are to be used solely for, repayment of the notes. This fund is not available for general fund expenditures or interfund transfers.

The E-TRANS program

The 2023A E-TRANS proceeds will fund a portion of the state's fiscal 2024 interest-free cash-flow loan program for local school district borrowers and to reduce the amount of separately secured state general fund TRANS borrowing. The fiscal 2023 E-TRANS program is expected to fund cash-flow needs for 24 participating school districts, up from 17 participants in last year's E-TRANS program. The school borrowing program for cash flow provides interest-free loans to local school district borrowers to meet yearly cash-flow needs.

Colorado projects that the largest individual school district borrowers in the fiscal (year ending) 2024 school cash-flow loan borrowing program will be Denver City & County School District No. 1 (AA+/Stable), which we expect to account for about 52.6% of the total program; Adams-Arapahoe School District 28J (AA-/Stable), which we expect to account for about 7.9%; Boulder Valley School District RE-2 (AA+/Stable), which we expect to account for about 5.8%; and Douglas County School District No. RE-1 (not rated) at about 5%.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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