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California School Finance Authority Aspire Public Schools; Charter Schools

Primary Credit Analyst:
Carolyn McLean, New York (1) 212-438-2383; carolyn.mclean@standardandpoors.com

Secondary Contact:
Laura A Kuffler-Macdonald, New York (1) 212-438-2519;
laura.kuffler.macdonald@standardandpoors.com

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Credit Profile		
US$23.1 mil rev bnds (Aspire Public Schools) ser 2015A dtd 12/17/2015 due 08/01/2045		
Long Term Rating	BBB/Stable	New

Rationale

Standard & Poor's Ratings Services assigned its 'BBB' long-term rating on the California School Finance Authority's series 2015A and B charter school revenue bonds, issued for the Aspire Pubic Schools--Obligated Group. The outlook is stable.

Operations from two of Aspire's 38 schools secure the bonds. These schools are each separate legal entities and operate under the parent organization, Aspire Public Schools. Based on our Group Rating Methodology, published Nov. 19, 2013, the rating analysis encompasses the entire Aspire organization as well as an obligated group, which includes the organization's two schools, as well as College for Certain II LLC, the borrower of the bonds.

The 'BBB' rating is based on our view of Aspire's group credit profile and the highly strategic status of the schools that are obligated to support the 2015 bonds. The rating only applies to the series 2015 bonds and does not apply to Aspire Public Schools as an organization.

Our rating reflects the obligated group's strong enterprise profile with good demand and strong academic performance. Its financial profile also supports the rating with strong and consistent margins, managing well through the significant delays in California state funding in the past. Its pro forma debt service coverage (DSC) is strong and does not require growth to meet coverage, even though additional growth is expected. Cash levels are also robust and expected to remain so. Strong connectivity with its charter management organization, Aspire Public Schools, and highly strategic link further support the rating.

Factors supporting the rating include our view of Aspire's:

- Established and experienced management team that operates its schools;
- Good demand demonstrated by enrollment increases during the past several years and significant waitlists;
- Solid academic performance at each of the obligated schools, with scores above local public school districts;
- Good DSC for the obligated group with 2x pro forma maximum annual debt service (MADS) coverage in fiscal 2015, which is in line with previous years;
- Solid cash levels with 187 days' cash on hand in fiscal 2015, which is expected to dip slightly in fiscal 2016 to about 100 days due to investment in its new building;
- A manageable pro forma MADS burden of 16% in fiscal 2015; and
- Strong connectivity with the parent and charter management organization, Aspire Schools.

Partially offsetting the rating is:

- Construction and expansion risk as the obligated group plans to open a third school building using proceeds of the bonds and cash reserves in fiscal 2016;
- Demonstrated appetite for expansion, which inherently presents some uncertainties and risks;
- The potential that Aspire's various charters could be revoked or not renewed due to Aspire's potential noncompliance with the terms of the charter (as with all charter schools) prior to the bonds' final maturity.

The series 2015A and B bonds will refinance existing 2005A certificates of participation (COPs) issued and secured by the Lodi Unified School District, as well as provide an additional $5 million of capital to partially fund the expansion of a third Aspire School in the district. The original debt service for the bonds was paid for in the form of lease payments from the Aspire Schools, although the charter school payments did not legally secure the bonds, the lease payments were approximately $1.3 million per year and the pro forma MADS is about $1.4 million. Given that the lease payments will only increase slightly, we believe that the school will be able to maintain current operating budgets and absorb the new debt service expense. The series 2015 bonds are secured by a gross revenue pledge of the three obligated schools, of which only two are currently operating. These bonds, in addition to Aspire's 2010 bonds (secured separately), will be the only series of bonds outstanding for all of Aspire's schools, although they do have other debt in their capital structure. Management states that it does not plan to issue additional debt secured by the revenues of the schools in the obligated group. Management will fund approximately $3 million of the new school with equity from the parent Aspire and the two existing schools on the site.

The bonds

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The borrower, College for Certain II LLC, is a limited liability company, which is a component unit of Aspire Public Schools. The sole member is a recently formed California nonprofit public benefit corporation formed as a support organization for charter schools that Aspire forms and controls. The borrower is a single-purpose entity with no assets other than the facilities. The borrower will enter into lease agreements with each of the schools in the obligated group. The covenants are in line with other charter school transactions and are listed below. Management is in compliance with these covenants currently and expects to remain well above these thresholds.

- Base rent coverage ratio for each school of at least 1.1x,
- Days' cash on hand of at least 30 days, and
- DSC of the obligated group of at least 1.0x.

Outlook

The stable outlook reflects our anticipation that Aspire will manage operations and attract sufficient students such that operations generate strong adjusted MADS coverage from the obligated group in the future. We also anticipate the school will maintain similar levels of days' cash on hand and its strong enterprise profile and good academic standing. We also expect construction and expansion of the third school will occur on time and on budget and will not weaken the credit quality.

We could consider a negative rating action in response to declines in enrollment, financial performance, debt service coverage, or days' cash on hand. A positive rating or outlook change, although not likely during the two-year outlook period, would be based on significant cash increases and sustained stronger MADS coverage at the obligated group, as well as continued strength at the parent.

Enterprise Profile

Organizational overview

Aspire Public Schools operate 38 schools and serves over 15,000 children in California and Tennessee. The system was founded in 1998 and was the nation's first charter management organization. Until 2013, all of its schools were in California, spread fairly evenly among the Central Valley, the Bay Area, and Los Angeles. In 2013, it opened its first three schools in Memphis to address the lack of school choice in Tennessee. The schools in California have a long history of strong academic performance, lean management, and serving low-income students.

The schools in the obligated group, River Oaks Charter School (ROCS) and Benjamin Holt College Preparatory Academy (Ben Holt) were opened in 2001 and 2003, respectively, and both are in the Central Valley. Aspire also plans to open a third school--currently called Ben Holt II--which will allow them to expand their middle and high school grades. The school expansion is pending authorizer approval, although management states that indicators are positive. The combined enrollment at the obligated schools is 1,124 and could grow to about 1,500 by 2022. All schools in the obligated group are authorized by Lodi Unified School District.

Management

Management of the Aspire Schools is quite centralized, with an executive team made up of the CEO, chief academic officer, chief people officer, and CFO. The CEO joined Aspire in September 2015 after a career working at other charter school networks. Other members of the management team have a long tenure with Aspire and we expect that the good financial policies and practices will continue.

A seven-member board governs all schools centrally, with parent and local boards supporting each school. The board is organized through committees and members have a mix of board tenure and career experience. The by-laws allow the board to grow up to 11 members and we expect that board membership will expand slowly over time.

Demand

Demand at the Aspire schools and at ROCS and Ben Holt, in particular, is strong. ROCS and Ben Holt have a waitlist that is over 100% of its current enrollment levels and plan to address the strong demand by opening the third school, Ben Holt II. Aspire's mission is to serve low-income populations and nearly all of its schools give priority to students who qualify for free and reduced lunch. While this has not been the case at ROCS and Ben Holt in the past, a change in policy beginning in the fall 2015 class is likely to increase that population from current levels of about 50% at ROCS and 35% at Ben Holt, to be in line with the local public districts, which are currently about 95% and 66%, respectively. ROCS and Ben Holt both outperform the district academically, which is true of many of the other Aspire schools across California as well. Although there are other local charter schools, the strong waitlist and ability to grow enrollment consistently over time demonstrates a strong market position, which we believe will be able to support the planned growth to the third school.

Financial Profile

State funding

- Prior to the enactment of the state's 2013-2014 budget, charter schools were funded through general-purpose entitlement and categorical block grants. The Local Control Funding Formula (LCFF) was approved in 2013, giving local educational agencies funding based on the demographic profile of the students they serve. The LCFF creates three funding mechanisms:
- A base grant for all students;
- Supplemental grants equal to 25% of the base grants for each English-learning student; and
- Supplemental grants for economically disadvantaged and foster youth enrollment in excess of 55% of total enrollment equal to 50% of the base grant provided for each student above the 55% threshold.

Funding under the new formula began in 2013-2014. Although it is estimated that full implementation will not be complete until 2020, the funding outlook is positive given its high portion of English language learning and economically disadvantaged students. State deferrals were significant in fiscal years 2012 and 2013 and have since diminished. Aspire has experienced growth in per-pupil funding since and has been able to grow its balance sheet with the additional funding. We expect this will continue in the near term.

Operating performance

The obligated schools financial performance has also been solid, with consistent margins and strong coverage of historical leases and pro forma debt service. The schools have produced excess margins of close to 10% in the last three years with pro forma MADS coverage of 2.0x in fiscal 2015, 2.2x in 2014, and 1.8x in fiscal 2013. We expect that coverage will be in line with previous levels, and if the expansion to Ben Holt II is successful, coverage will likely increase substantially in the medium term. The pro forma MADS burden is somewhat high, but in line with previous lease expense at about 16% of operating expenses in 2015. We expect this will decline over time given the flat amortization of the debt and the expectation for a growing expense base.

Liquidity and financial flexibility

Cash levels at the obligated schools have been strong in the past two years, but were much weaker prior to fiscal 2014, given the delays in state payments in California. In fiscal years 2015 and 2014, the schools had a combined 187 and 135 days' cash on hand, respectively. Prior cash levels were very low, below 10 days, but including receivables, they were more robust. Aspire, the parent, centrally manages the cash and notes that through all of the delayed payments and hold-backs in fiscal years 2012 and 2013, it did not require cash flow borrowing. We view this historical strong management of cash positively and believe that it demonstrates that financial management outperformed many of its peers. We expect cash levels to decline to about 90-100 days' cash on hand after investing about $2 million into the new building in fiscal 2016.

Aspire Charter School (River Oaks & Benjamin Holt) - Obligated Group, CA -- Selected Financial Statistics

	Fiscal year ended June 30					Medians
	2016	2015	2014	2013	2012	Charter schools 'BBB' 2014
Enrollment						
Total headcount	1,124	1,114	1,092	1,073	1,024	1,962
Total waiting list	1,351	1,018	816	762	N.A.	MNR
Waiting list as % of enrollment	120.2	91.4	74.7	71.0	N.A.	MNR
Financial performance						
Total revenues ($000s)	N.A.	9,479	8,962	8,354	8,070	MNR
Total expenses ($000s)	N.A.	8,593	7,890	7,844	8,000	MNR
EBIDA ($000s)	N.A.	2,875	3,060	2,502	680	MNR
EBIDA margin (%)	N.A.	30.33	34.14	29.95	8.43	15.90
Excess revenues over expenses ($000s)	N.A.	886	1,072	510	70	MNR
Excess income margin (%)	N.A.	9.35	11.96	6.10	0.87	4.5
Lease adjusted annual debt service coverage (x)	N.A.	2.08	2.22	1.82	N.A.	1.7
Lease adjusted annual debt service burden (% total revenues)	N.A.	14.5	15.4	16.5	N.A.	MNR
Lease adjusted annual debt service burden (% total expenses)	N.A.	16.0	17.4	17.6	N.A.	MNR
MADS ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	2,194
Lease adjusted MADS coverage (x)	N.A.	N.A.	N.A.	N.A.	N.A.	1.5
Lease adjusted MADS burden (% total revenues)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Lease adjusted MADS burden (% total expenses)	N.A.	N.A.	N.A.	N.A.	N.A.	11.10
Pro forma MADS ($000s)	N.A.	1,412	1,412	1,412	N.A.	MNR
Pro forma lease adjusted MADS coverage (x)	N.A.	2.04	2.17	1.77	N.A.	MNR
Pro forma lease adjusted MADS burden (% total revenues)	N.A.	14.9	15.8	16.9	N.A.	MNR
Pro forma lease adjusted MADS burden (% total expenses)	N.A.	16.4	17.9	18.0	N.A.	MNR
Total revenue per student ($)	N.A.	8,509	8,207	7,786	7,881	MNR
Balance Sheet Metrics						
Days' cash on hand	N.A.	187.3	135.2	9.8	30.3	134.00
Total long-term debt ($000s)	N.A.	14,043	14,601	15,137	15,654	MNR
Unrestricted reserves to debt (%)	N.A.	29.2	18.5	1.3	3.9	35.9
Unrestricted net assets as % of expenses	N.A.	56.7	47.9	36.9	29.1	36.2
General fund balance ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Debt to capitalization (%)	N.A.	74.8	80.1	84.6	87.6	MNR

Aspire Charter School (River Oaks & Benjamin Holt) - Obligated Group, CA -- Selected Financial Statistics (cont.)						
Debt per student ($)	N.A.	12,606	13,371	14,107	15,287	MNR
Pro forma Metrics						
Pro forma unrestricted reserves ($000s)	N.A.	2,450	N.A.	N.A.	N.A.	MNR
Pro forma days' cash on hand	N.A.	112.02	N.A.	N.A.	N.A.	MNR
Pro forma long-term debt ($000s)	N.A.	23,523	14,601	15,137	15,654	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	10.4	N.A.	N.A.	N.A.	MNR
Pro forma debt to capitalization (%)	N.A.	130.71	83.28	87.66	90.56	MNR
Pro forma debt per student ($)	N.A.	21,116	13,371	14,107	15,287	MNR

MNR--Median not reported. N.A.--Not available. MADS--Maximum annual debt service.

Related Criteria And Research

Related Criteria

- USPF Criteria: Charter Schools, June 14, 2007
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009