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California School Finance Authority Aspire Public Schools; Charter Schools

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California Sch Fin Auth (Aspire Public Schools)		
Long Term Rating	BBB/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'BBB' rating on the California School Finance Authority's series 2015 and series 2016 charter school revenue bonds, issued for the Aspire Public Schools-Obligated Group. The outlook is stable.

Operations from 13 of Aspire's 40 schools secure the bonds. These schools 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. The 'BBB' rating is based on our view of Aspire's group credit profile (GCP) of 'bbb+' and the highly strategic status of the obligated schools, given that several of these schools are some of the oldest and most successful schools. We view the obligated group as important to the organization, with parent support of the obligated group as likely in the event of operating difficulties, but the obligated group as limited to a highly strategic status, given that it represents only 36% of total organization headcount. Under the methodology, a highly strategic group is rated one notch lower than the GCP, unless the standalone credit profile (SACP) of the obligated group is equal to, or higher than, the GCP. In this case, the 'bbb' SACP of the obligated group is one notch lower than the GCP. The rating applies only to the series 2015 and 2016 bonds--not to Aspire Public Schools as an organization. Financial metrics cited in this report (unless otherwise indicated) reflect those of the entire Aspire organization.

We assessed Aspire Public Schools' enterprise profile as strong, characterized by healthy demand; a diverse network, with 40 schools operating under 14 different authorizer jurisdictions spread out across California and Tennessee; and a solid management team that has demonstrated successful maneuvering of the challenges involved with the charter authorization process. We assessed Aspire Schools' financial profile as adequate, with an abundant revenue base, robust operating margins generating substantial maximum annual debt service (MADS) coverage, and a debt profile that we view as in line with the rating level. We believe that these combined credit factors lead to an indicative group credit profile of 'bbb' for Aspire Public Schools.

In our opinion, the 'bbb+' GCP (and final rating of 'BBB' on the bonds) better reflects Aspire's very large enrollment--over 15,000 students are enrolled at 40 individually chartered campuses under 14 separate authorizers--which limits exposure to any one charter.

More specifically, factors supporting the rating include:

- The sophisticated and experienced management team that operates the schools;
- Aspire's good demand, demonstrated by enrollment increases during the past several years; and
- The school's respectable MADS coverage of 3.13x in fiscal 2016.

Partially offsetting the rating are:

- Aspire's demonstrated appetite for expansion, which inherently presents some uncertainties and risks, though management expects to focus on building out existing schools instead of opening new schools in new regions;
- The school's modest cash position for the rating, with 103 days' cash on hand in fiscal 2016; and
- The potential that various charters could be revoked or not be renewed due to potential noncompliance with the terms of the charter (as with all charter schools) prior to the bonds' final maturity.

The series 2015 and 2016 bonds are secured by revenues of the 13 schools in the obligated group. The series 2015 and 2016 bonds make up the majority of Aspire's debt, although there are other short-term and state-funded facilities debt outstanding. Management does not plan to issue additional debt secured by the revenues of the schools in the obligated group in the near term. The borrower, College for Certain Inc., is a limited liability company and a component unit of Aspire Public Schools. The sole member is a California nonprofit public benefit corporation that was formed as a support organization for Aspire charter schools. The borrower is a single-purpose entity with no assets other than the facilities. The borrower has entered into lease agreements with each of the schools in the obligated group. The debt service coverage (DSC) and days' cash covenants are in line with those of other charter school transactions and are listed below. The base rent coverage calculation is more unique to the series 2015 and 2016 bonds. 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, allowing for some support from the parent if necessary;
- Days' cash on hand of at least 30; and
- DSC of the obligated group of at least 1x.

Aspire Public Schools operate 40 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.

Within the obligated group, River Oaks Charter School and Benjamin Holt College Preparatory Academy (Ben Holt) opened in 2001 and 2003, respectively, in the Central Valley. Aspire also opened a third school near those campuses--Ben Holt Middle School--to enable the schools to expand their middle and high school grades. The other obligated schools include Aspire Golden State College Prep Academy, Aspire Junior Collegiate, Aspire Titan Academy, Aspire Pacific Academy, Aspire Langston Hughes, Aspire Port City Academy, Aspire Alexander Twilight College Preparatory and Secondary Academy, Aspire East Palo Alto Phoenix Academy, and Aspire Lionel Wilson College Preparatory Academy. There are several schools in three regions--Central Valley, Los Angeles, and the Bay Area--which opened between 2006 and 2015. The combined enrollment at the obligated schools is about 5,695 currently and could grow to about 6,300 by 2022.

Outlook

The stable outlook reflects our view that Aspire will continue to perform at a healthy operational level and attract sufficient students such that it continues to generate substantial lease-adjusted MADS coverage in the next two years. We also anticipate the organization will at least maintain its current level of days' cash on hand and its strong enterprise profile.

Downside scenario

We could consider a negative rating action in response to concerns with charter standings or academic performance, or if there are declines in enrollment, charter standing, financial performance, or days' cash on hand.

Upside scenario

A positive rating or outlook change 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

Economic fundamentals

Aspire has 36 schools located across California and four schools located in Tennessee. Eleven schools are in Los Angeles County, which is the most populous county in the U.S. The county's minor population is very healthy, at about 3,571,000, and is expected to remain fairly stable, with projections indicating a modest decline of 2% through 2020.

Industry risk

Industry risk addresses our view of the charter school sector's overall cyclicality and competitive risk and growth through application of various stress scenarios and evaluating barriers to entry, levels and trends of profitability, substitution risk, and growth trends observed in the industry. We believe the charter school sector represents a moderately high credit risk when compared with other industries and sectors.

Market position

We view Aspire's enrollment and demand profile as sound, supported by its large enrollment, steady growth, and modest wait lists. 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-price lunch. Most of the schools outperform their local districts in state tests, and those that don't have scores close to the state average. The Aspire schools have a good reputation for academic quality, having earned state-level awards as well as a U.S. Department of Education award for educator effectiveness in 2012, which came with $27.8 million in grant funding. Although there are other local charter schools, Aspire's ability to increase enrollment consistently demonstrates a solid demand position, which we do not expect to change despite the competitive environment in California.

The schools in the obligated group have six charter school authorizers: Lodi Unified School District, San Juan Unified School District, Oakland Unified School District, Ravenswood City School District, Stockton Unified School District and Los Angeles Unified School District (LAUSD). Aspire schools outside of the obligated group are additionally authorized by six other local education agencies throughout California, and the Achievement School District and

Shelby County Schools in Tennessee. Management reports positive relationships with each authorizer and expects the renewal of each school's charter upon expiration. We view the overall organization's charter standings with its authorizers as sufficient, and based on our contact with a portion of the authorizers, there are no known concerns at this time. Aspire Schools has held its charter with the Lodi Unified School District for over 15 years and its charter with the Oakland Unified school district for over 14 years, representing the two longest-standing charters in the obligated group.

In our view, the statutory framework could negatively affect Aspire's ability to meet debt service due to its dependence on LAUSD as an authorizer for several of its schools. In 2014, LAUSD rejected renewal of two Aspire schools not within the obligated group; following a successful appeal by Aspire, these two schools were then chartered by the Los Angeles County Office of Education. Despite the good outcome, the risks of the authorization process remains, and in our view, there is a critical mass of students still under LAUSD's jurisdiction that could impact the overall credit profile should those charters face issues. Our concerns are somewhat offset by the staggered renewal terms.

Funding under the Local Control Funding Formula began in 2013-2014 and has been favorable since, with large jumps in per-pupil funding due to gap funding along with a robust state economy that has generated high revenues and local property taxes that dictate minimum funding level increases. However, we anticipate that the significant one-time state funds received in the past two fiscal years will cease, moderating per-pupil revenue growth in the near term.

Management and governance

Management of the Aspire Schools is quite centralized, with an executive team made up of the CEO, the chief financial officer, the chief operating officer, general counsel, and four area superintendents. The CEO joined Aspire in September 2015 after 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. In our view, the board is also well diversified. A 10-member board governs all schools centrally, and parent councils support each school. The board is organized through committees, and members have a mix of board tenure and career experience.

Financial Profile

Financial performance

Aspire's financial performance has generated consistently robust operating margins between 11%-12% in the past three fiscal years, with solid lease-adjusted MADS coverage ranging from 2.57x in fiscal 2014 to 3.13x in fiscal 2016. The obligated group's coverage of the series 2015 and 2016 bonds is 2.26x in fiscal 2016.

Liquidity and financial flexibility

Cash levels have been acceptable in the past three years but were much weaker prior to fiscal 2014, given the delays in state payments in California. In fiscal years 2016 and 2015, Aspire had 103 and 97 days' cash on hand with approximately $49 million and $39 million unrestricted reserves, respectively. The cash level for the obligated schools was 111 days' cash on hand in fiscal 2016. We expect cash levels to increase moderately as Aspire continues to build out the newer schools.

Debt burden

Aspire's lease-adjusted MADS burden is moderate for the rating, at 6.3% of operating revenues in fiscal 2016. We expect this will remain roughly the same as the organization expands, adding on additional debt or leases, offset by expectation of a growing revenue base.

Total series 2015 and 2016 bonds outstanding is $112 million. In addition, there is roughly $26 million in additional loans held by Aspire Public Schools. Based on past two years of monthly cash flows provided by management, liquidity is sufficient to cover an acceleration on these loans.

Financial policies

Aspire Public Schools meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, despite areas of risk, the organizations' overall financial policies are not likely to hamper their ability to pay debt service. Our analysis of financial policies includes a review of the organizations' financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure and a comparison of these policies with those of comparable providers.

Aspire Charter Schools - Consolidated, California

	Fiscal year ended June 30					Medians
	2017	**2016**	**2015**	**2014**	**2013**	**Charter Schools 'BBB' & 'BBB+' 2015**
Enrollment						
Total headcount	15,830	15,365	14,728	13,005	12,559	2,371
Total waiting list	8,838	5,605	6,392	4,928	3,774	MNR
Waiting list as % of enrollment	55.8	36.5	43.4	37.9	30.1	90.2
Financial performance						
Total revenues ($000s)	N.A.	205,734	174,377	150,900	125,801	MNR
Total expenses ($000s)	N.A.	180,746	154,403	132,698	105,546	MNR
EBIDA ($000s)	N.A.	37,250	32,355	30,047	31,030	MNR
EBIDA margin (%)	N.A.	18.11	18.55	19.91	24.67	17.10
Excess revenues over expenses ($000s)	N.A.	24,988	19,974	18,202	20,255	MNR
Excess income margin (%)	N.A.	12.15	11.45	12.06	16.10	6.4
Lease adjusted annual debt service coverage (x)	N.A.	2.54	2.23	2.21	3.42	1.9
Lease adjusted annual debt service burden (% total revenues)	N.A.	7.8	9.2	10.0	7.7	MNR
Lease adjusted annual debt service burden (% total expenses)	N.A.	8.9	10.4	11.4	9.1	MNR
MADS ($000s)	N.A.	13,013	13,013	13,013	13,013	2,142
Lease adjusted MADS coverage (x)	N.A.	3.13	2.75	2.57	2.54	1.8
Lease adjusted MADS burden (% total revenues)	N.A.	6.3	7.5	8.6	10.3	MNR
Lease adjusted MADS burden (% total expenses)	N.A.	7.2	8.4	9.8	12.3	10.90
Pro forma MADS ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma lease adjusted MADS coverage (x)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR

Aspire Charter Schools - Consolidated, California (cont.)

	Fiscal year ended June 30					Medians
	2017	**2016**	**2015**	**2014**	**2013**	**Charter Schools 'BBB' & 'BBB+' 2015**
Pro forma lease adjusted MADS burden (% total revenues)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma lease adjusted MADS burden (% total expenses)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Total revenue per student ($)	N.A.	13,390	11,840	11,603	10,017	MNR
Balance Sheet Metrics						
Days' cash on hand	N.A.	102.9	97.0	97.2	71.0	157.00
Total long-term debt ($000s)	N.A.	129,695	132,334	135,441	137,530	MNR
Unrestricted reserves to debt (%)	N.A.	35.0	29.9	25.0	14.3	32.1
Unrestricted net assets as % of expenses	N.A.	45.0	40.1	34.9	25.6	38.6
General fund balance ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Debt to capitalization (%)	N.A.	63.7	68.4	74.9	83.7	MNR
Debt per student ($)	N.A.	8,976	8,785	10,207	10,569	11,451
Pro forma Metrics						
Pro forma unrestricted reserves ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma days' cash on hand	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma long-term debt ($000s)	N.A.	129,695	135,494	135,441	137,530	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma debt to capitalization (%)	N.A.	59.93	71.64	76.46	86.69	MNR
Pro forma debt per student ($)	N.A.	8,441	9,200	10,415	10,951	MNR

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