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Newark Higher Education Finance Corp. Orenda Education; Charter Schools

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Table Of Contents

Rationale

Outlook

Enterprise Profile

Financial Profile

Related Criteria And Research

Newark Higher Education Finance Corp. Orenda Education; Charter Schools

Credit Profile

US\$15.67 mil Ed Rev and Rfdg Bnds (Orenda Ed) ser 2015A due 08/15/2044

Long Term Rating AAA/Stable New

Underlying Rating for Credit Program BBB-/Positive New

US\$0.43 mil Ed Rev and Rfdg Bnds (Orenda Ed) ser 2015B due 08/15/2020

Long Term Rating AAA/Stable New

Underlying Rating for Credit Program BBB-/Positive New

Newark Higher Ed Fin Corp, Texas

Orenda Ed, Texas

Newark Higher Ed Fin Corp (Orenda Ed) Ed Rev and Rfdg Bnds (Orenda Ed) ser 2015A due 08/15/2044

Long Term Rating AAA/Stable Rating Assigned

Underlying Rating for Credit Program BBB-/Positive Rating Assigned

Newark Higher Ed Fin Corp (Orenda Ed) Ed Rev and Rfdg Bnds (Orenda Ed) ser 2015B due 08/15/2020

Long Term Rating AAA/Stable Rating Assigned

Underlying Rating for Credit Program BBB-/Positive Rating Assigned

Rationale

Standard & Poor's Ratings Services assigned its 'AAA' enhanced long-term (program) rating and 'BBB-' underlying rating to Newark Higher Education Finance Corp.'s series 2015A and 2015B education revenue refunding bonds issued for Orenda Education.

At the same time, Standard & Poor's affirmed its 'BBB-' underlying rating on Orenda's existing debt. The outlook on the 'AAA' enhanced rating is stable, and the outlook on the 'BBB-' underlying rating remains positive.

The 'AAA' enhanced program rating reflects our view of Orenda Education's participation in the Texas Permanent School Fund bond guarantee program. This program provides the security of a permanent fund asset that Orenda Education can access, if needed, to meet its debt service obligations on the 2015 bonds.

The underlying rating and outlook reflects our opinion of Orenda's consistently positive operations, good coverage, days' cash on hand that is well above rating medians, and continued stable and experienced management. The rating also reflects our opinion of possible growth and additional debt risks, and the unique nature of some of Orenda's students and programs.

The underlying rating further reflects our view of Orenda's:

- Very strong unrestricted cash reserves, as measured by 275 days' cash on hand at the end of fiscal 2014, though we understand management may draw down cash to help fund future capital projects;
- Long operating history, with a recent successful charter renewal for a 10-year term through 2025;

- Robust coverage ratios for the sector, with lease-adjusted maximum annual debt service (MADS; \$1.75 million) coverage of 1.6x for fiscal 2014;
- Consistent enrollment growth, as evidenced by an increase in students to 1,121 in fall 2014 from 36 in fall 2009, at its Gateway College Prep School (GCPS); and
- Sound management team that is focused on building headcount and the financial profile.

Partly offsetting the above strengths, in our view, are:

- The possibility of future growth and an additional debt issuance, whose timing and amount are uncertain;
- Potential competition from the Georgetown Independent School District (well rated by the Texas Education Agency, or TEA) and a newly opened kindergarten through ninth-grade charter school nearby;
- Relatively high leverage, with a pro forma debt burden (MADS compared to operating expenses) of 15.2% in fiscal 2014; and
- The inherent uncertainty associated with charter renewals because the final maturity of the bonds exceeds the time horizon of the existing charter.

Orenda expects proceeds from the 2015 issuance to be about \$15.7 million and to refund its 2011A, 2011B, 2013A, and 2013B bonds. In addition to the series 2015 issuance, the 2011Q bonds will be the only remaining bonds outstanding. According to management, the purpose of the bond issuance is for interest cost savings and there is no new money associated with the debt. The bonds are general obligations of the school secured by available revenues. Debt service is flat, with MADS anticipated to be \$1.28 in fiscal 2020. Pro-forma lease-adjusted MADS is estimated to be about \$1.75 million.

According to bond documents provided to Standard & Poor's, bond holders are provided operating and liquidity covenants. The liquidity covenant requires maintenance of 45 days' cash on hand, and the operating covenants require annual debt service coverage of 1.1x. If debt service falls below 1.1x but remained above 1.0x management may be required to engage a consultant acceptable to the issuer. If annual debt service coverage falls below 1.0x an event of default may be declared. Before the issuance of other long-term debt an additional bonds test requires 1.1x pro forma MADS coverage on a historical basis and 1.2x forward MADS coverage on existing and proposed debt.

Outlook

The positive outlook on the underlying rating reflects our expectation that Orenda will maintain its strong financial performance and liquidity position, in addition to continuing to meet its projected enrollment targets. A higher rating is possible if the school continues to execute its expansion plans. We would evaluate the effects of additional debt or program expansion at the time of implementation.

We could revise the outlook to stable or lower the rating if enrollment does not reach a level that generates sufficient debt service coverage or if the district's liquidity position weakens significantly. We also believe the district's relatively deep cash reserves will provide some cushion against revenue pressure from a potential slower-than-anticipated enrollment ramp.

Enterprise Profile

Enrollment

Orenda Education is an open-enrollment charter school founded in 2001 in Georgetown, Texas, about 30 miles north of Austin. The school currently operates out of five campuses throughout the state: two in Georgetown (GCPS, offering kindergarten through 12th grade, and Gateway Tech High School, offering grades nine through 12), one in Lubbock (offering grades six through 12), one in Lometa (offering kindergarten through 12th grade), and one in Goldthwaite (offering grades one through 12). As of fall 2014, total enrollment from all five campuses reached 1,320 students. This headcount represents nearly a 60% increase since fall 2011, when management operated with 831 total students.

Of the 1,320 students, 1,121 attend Orenda's newest campus, GCPS, in fall 2014. Phase I of Orenda's expansion plan for GCPS, which was funded from the 2011 bond proceeds, is complete, and the current facility is already near capacity. Phase II of Orenda's capital plan is also complete, and GCPS is now able to accommodate the designed maximum enrollment of 1,300. The contemplated Phase III could replace modular building with permanent classroom space keeping enrollment capacity at current levels. We understand management is also considering opening additional campuses in leased facilities but plans are still preliminary. We will evaluate the impact of expansion when more information is available. Orenda's other Georgetown campus, Gateway Tech High School, will operate at near capacity of 100 students in the next few years.

The Lometa and Goldthwaite campuses are about 86 and 106 miles northwest of Austin, respectively. The facilities in Lubbock, Lometa, and Goldthwaite operate within three separate, privately owned residential treatment/care facilities for young individuals who have been referred to the residential facility by Child Protective Services. The three hybrid facilities house about 130 total students, as of the fall 2014 headcount, and have operated at such levels throughout their history.

Orenda has only recently begun maintaining a wait list. The wait list for fall 2014 was 152 students, down from 249 students in fall 2013. School officials also report that retention rates are difficult to estimate given the fluctuations in the number of students attending the hybrid campuses, but management estimates the rate to be about 85% for the 2014-2015 school year.

Competition for Orenda's Gateway Tech and GCPS comes primarily from five well-rated Georgetown, Texas, independent school district facilities. The school's main charter competition in the area comes from a newly opened kindergarten through ninth-grade facility. School officials do not envision that this school will have a profound effect on operations, and they believe the Georgetown campuses are well positioned in that market.

Curriculum and academic performance

The school's curriculum focuses on core academic subject areas and state standards, while offering an abundance of extracurricular activities for a charter school. Although Orenda's academic performance has been somewhat volatile in the past, we view it as adequate and improving. As stated in previous reports, for the 2010-2011 school year the Gateway Tech High School was the only Orenda campus to receive an "academically unacceptable" rating; it has since improved this rating.

The official 2014 TEA accountability ratings for all school districts and charters indicate that both the Gateway Tech and GCPS campuses "met standards." This most recent rating demonstrates Orenda has successfully addressed the 2010-2011 academic issues at the Gateway Tech campus. In addition, GCPS also received five distinctions. Per a recent legislative action, the residential facility or hybrid campuses of Orenda are exempt from such assessments hereafter, and accountability ratings will be based only on the Gateway campuses.

Management and governance

The senior leadership is well seasoned and long serving. Orenda's founder and CEO, Richard Rickey, was a former hospital executive and incorporated Orenda in 1995 as a private not-for-profit shelter for abused or neglected children and has been with the district since its inception in 1999. Orenda's business manager has been with the district since 2009; she had worked previously for independent school district. The school has a stable board of directors that consists of six members from the community. The board is actively involved in the governance of the school and works closely with the school's management team and authorizer.

Financial Profile

State funding environment

In Texas, the majority of public school operating dollars come from the state rather than from local sources. Therefore, charter schools are almost entirely dependent on the state for operating revenue that is subject to annual appropriation by the state legislature. As a result, Texas' economic and financial situation has a direct impact on the school's operations, and funding will fluctuate along with the state economy. Recently, the Texas Legislature overwhelmingly approved legislation to increase the number of open-enrollment charter schools to 305 from 215 by 2019, and to give the TEA more flexibility to fast-track charter renewals for successful school as well as more authority to revoke academically failing charters after three years of unsatisfactory performance instead of four. State funding overall increased a little by 1.8% in fiscal 2015. We expect another modest increase in fiscal 2016.

Orenda's funding is calculated in two ways--schools functioning out of a residential facility receive state funding of about \$18,900 per pupil, while traditional per-pupil revenue accounts for about \$6,900 annually; thus we are mindful of the volatility the district may endure should enrollment dip slightly below expectations, especially at the RTFs.

Operations

Operations have been positive for at least the last four years, in part due to increases in enrollment as GCPS fills in grades. Orenda ended fiscal 2014 with a strong \$923,000 surplus, compared with fiscal 2013's very strong \$1.1 million surplus. The fiscal 2013 operations were aided by \$550,000 in one-time proceeds from a former hospital sale. On an EBIDA basis the school finished fiscal 2014 with a \$2.1 million surplus. Subsequently, pro forma lease-adjusted MADS coverage was good at 1.6x.

Based on unaudited fiscal 2015 results, the school anticipates ending this year with a sizable surplus of more than \$1 million. On an EBIDA basis, Orenda anticipates finishing fiscal 2015 with a very strong \$2.3 million surplus.

Balance sheet

The school's financial position has been positive and is improving. Orenda increased its ending unrestricted net assets

about 30% to \$3.2 million in fiscal 2014. As of Aug. 31, 2014, Orenda held about \$6.5 million in unrestricted cash and investments, or about 275 days' cash on hand, which we consider strong for a charter school. The significant growth in cash is due to strong operating results. We understand management may use some cash to help fund future capital projects, however; we anticipate levels will remain strong for the rating.

Orenda Education, Texas Financial Statistics

	--Fiscal year ended Aug. 31--			
	2015	2014	2013	2012
Enrollment				
Total headcount	1,322	1,206	999	819
Total waiting list	152	259	247	N.A.
Waiting list as % of enrollment	N.A.	31.6	24.7	N.A.
Financial performance				
Total revenues (\$000s)	N.A.	11,539	10,323	7,932
Total expenses (\$000s)	N.A.	10,613	8,646	7,517
EBIDA (\$000s)	N.A.	2,067	2,447	927
EBIDA margin (%)	N.A.	17.91	23.70	11.69
Excess revenues over expenses (\$000s)	N.A.	926	1,677	415
Excess income margin (%)	N.A.	8.02	16.25	5.23
Lease adjusted annual debt service coverage (x)	N.A.	1.78	1.89	1.33
Lease adjusted annual debt service burden (% total revenues)	N.A.	13.6	13.8	16.9
Lease adjusted annual debt service burden (% total expenses)	N.A.	14.8	16.5	17.8
MADS (\$000s)	N.A.	2,150	2,150	2,150
Lease adjusted MADS coverage (x)	N.A.	1.30	1.25	0.83
Lease adjusted MADS burden (% total revenues)	N.A.	18.6	20.8	27.1
Lease adjusted MADS burden (% total expenses)	N.A.	20.3	24.9	28.6
Pro forma MADS (\$000s)	N.A.	1,753	0	0
Pro forma lease adjusted MADS coverage (x)	N.A.	1.60	N.A.	N.A.
Pro forma lease adjusted MADS burden (% total revenues)	N.A.	15.2	0.0	0.0
Pro forma lease adjusted MADS burden (% total expenses)	N.A.	16.5	0.0	0.0
Total revenue per student (\$)	N.A.	9,568	10,333	9,685
Balance Sheet Metrics				
Days' cash on hand	N.A.	274.7	178.3	192.7
Total long-term debt (\$000s)	N.A.	21,103	10,471	10,623
Unrestricted reserves to debt (%)	N.A.	36.3	39.2	36.8
Unrestricted net assets as % of expenses	N.A.	31.8	30.0	18.5
Debt to capitalization (%)	N.A.	86.4	80.6	88.5
Debt per student (\$)	N.A.	17,498	10,481	12,971

N.A.--not available. N/A--not applicable. MADS--maximum annual debt service.

Related Criteria And Research

Related Criteria

- USPF Criteria: State Credit Enhancement Programs, Nov. 13, 2008
- USPF Criteria: Charter Schools, June 14, 2007

Ratings Detail (As Of July 24, 2015)		
Arlington Hgr Ed Fin Corp, Texas		
Orenda Ed, Texas		
Series 2013 A&B		
<i>Long Term Rating</i>	BBB-/Positive	Affirmed
Texas Pub Fin Auth Charter Sch Fin Corp, Texas		
Orenda Ed, Texas		
ser 2011A, B, Q		
<i>Long Term Rating</i>	BBB-/Positive	Affirmed

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