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Orenda Education, Texas Newark Higher Education Finance Corp.; Charter Schools

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US\$23.09 mil ed rev bnds (Orenda Ed) ser 2017 due 08/15/2047

Long Term Rating AAA/Stable New

Underlying Rating for Credit Program BBB-/Stable 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 Current

Underlying Rating for Credit Program BBB-/Stable Downgraded

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 Current

Underlying Rating for Credit Program BBB-/Stable Downgraded

Texas Pub Fin Auth Charter Sch Fin Corp, Texas

Orenda Ed, Texas

Texas Pub Fin Auth Charter Sch Fin Corp (Orenda Education)

Long Term Rating BBB-/Stable Downgraded

Rationale

S&P Global Ratings lowered to 'BBB-' from 'BBB' its underlying ratings on Newark Higher Education Finance Corp., Texas' series 2015A and 2015B education revenue refunding bonds and its long-term rating on the series 2011B and 2011Q bonds. All bonds were issued for Orenda Education. At the same time, we assigned our 'AAA' enhanced program rating and 'BBB-' underlying rating to Newark Higher Education Finance Corp.'s series 2017 education revenue refunding bonds, also issued for Orenda Education. The series 2011B and 2011Q bonds are not part of the Texas Public School Fund (PSF) Guarantee program. The outlook on all ratings is stable.

We withdrew our ratings on the series 2011A, 2013A and 2013B as the bonds were defeased.

The 'AAA' enhanced program rating reflects our view of Orenda's participation in the Texas PSF bond guarantee program. This program provides the security of a permanent fund asset that Orenda can access, if needed, to meet its debt service obligations on the series 2017 and 2015 bonds. For more information on the program rating, please see the report "Texas Permanent School Fund; State Revolving Funds/Pools," published July 7, 2015, on RatingsDirect.

The downgrade reflects our view of Orenda's substantial increase in debt load to levels that are far above those of peer credits in the state and resulting deterioration in pro forma lease-adjusted maximum annual debt service (MADS) coverage.

We assessed Orenda Education's enterprise profile at strong, characterized by growing overall enrollment at its five campuses spread across four counties, good academic performance at its flagship school, and leadership by a stable and experienced management team. We assessed Orenda Education's financial profile as vulnerable, based on below-average pro forma lease-adjusted MADS coverage level for the rating and extremely high debt load relative to enrollment that is more than double most of its peers, though somewhat offset by an abundance of unrestricted reserves and a history of steady, positive operating performance which we expect will continue to generate good coverage to support the rating at the current level. We believe that combined, these credit factors lead to an indicative stand-alone credit profile of 'bbb-' and a final rating of 'BBB-.'

The rating further reflects our view of Orenda's:

- Exceptional level of unrestricted reserves, as measured by 288 days' cash on hand at the end of fiscal 2016;
- Long operating history, with a recent successful charter renewal for a 10-year term through 2025;
- Consistent enrollment growth, with an increase to 1,481 students in fall 2016 from only 185 in fall 2009; and
- Sound management team that is focused on building headcount and the financial profile.

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

- Extremely high leverage, with a pro forma lease-adjusted MADS burden of 22% of revenues in fiscal 2016;
- A shift in strategy with the opening of two new open-enrollment campuses in Belton and Kingsland, after closing two residential facility schools, resulting in startup expenses and risks of operating in new regions;
- Potential competition from the Georgetown Independent School District (ISD) and Roundrock ISD, with Georgetown ISD recently replacing older facilities; and
- The inherent uncertainty associated with charter renewals because the final maturity of the bonds exceeds the time horizon of the existing charter.

The \$23.09 million series 2017 bonds will be issued to finance the phase III construction of the Gateway College Preparatory School (GCPC), and to purchase land for and renovate the Kingsland School building. The bonds are general obligations of the school secured by available revenues.

Bond covenants include the maintenance of 45 days' cash on hand, and annual debt service coverage (DSC) of 1.1x. If debt service falls below 1.1x but remains above 1.0x, management may be required to engage a consultant acceptable to the issuer. If annual DSC 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.

Orenda Education, about 30 miles north of Austin, is an open-enrollment charter school founded in 2001 in Georgetown. The school currently operates out of five campuses: two in Georgetown (GCPS offering grades K-12, and Gateway Tech High School, offering grades 9-12), one in Kingsland (K-8), one in Belton (K-5), and one in Goldthwaite (K-12).

Outlook

The stable outlook on the underlying rating reflects our expectation that over the two-year outlook period, Orenda will

maintain its strong financial performance and liquidity position, in addition to continuing to meet its projected enrollment targets and complete its construction on time and within budget.

Downside scenario

We could consider a negative rating action should there be any weakening in enrollment growth or financial performance, or if liquidity falls significantly below current levels without an offsetting reduction in debt ratios.

Upside scenario

We do not expect a positive rating action over our outlook horizon given our view of the school's high leverage and future expansion plans.

Enterprise Profile

Economic fundamentals

Two Orenda charter schools are in Williamson County. The county's minor population is decently sized at about 187,000 and is expected to increase at an impressive 17.1% annually through 2020. Orenda also operates schools in Llano, Bell, and Mills counties.

Industry risk

Industry risk addresses the charter school sector's overall cyclical and competitive risk and growth by applying 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

As of fall 2016, total enrollment from all five campuses reached 1,522 compared with 1,377 in fall 2015. This fall 2016 headcount represents nearly an 86% increase since fall 2011, when management operated with 819 total students. Enrollment levels were relatively flat from fiscal years 2015 to 2016 as the school consolidated facilities; positive enrollment trends are evident following the completion of new updated facilities.

Of the more than 1,500 students, 1,300 attend Orenda's newest campus, GCPS, in fall 2016. 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. Phase III will replace a modular building with permanent classroom space keeping enrollment capacity at existing levels. Orenda's other Georgetown campus, Gateway Tech, operates at near capacity.

The new Kingsland and Belton campuses are about 60 and 30 miles west and north, respectively, of Austin. Both began their first year in fall 2016, a transition after Orenda decided to close two of its residential facility schools in 2016. Kingsland School started with 90 students in K-5, and Nolan Creek School in Belton started with just four students in kindergarten. We understand management expects to expand into middle and high school grades eventually for both schools, with the high school levels taking a hybrid instructional model in the same vein as Gateway Tech.

A facility in Goldthwaite is a privately owned residential treatment/care facility for young individuals who have been referred to the residential facility by Child Protective Services and has about 60 students and is not expected to grow. We understand Orenda has plans to open another residential facility school in the 2018-2019 school year.

The wait list for fall 2016 was 208 students, up from 146 in fall 2015. 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 87% for the 2015-2016 school year.

Competition for Orenda's Gateway Tech and GCPS comes primarily from Georgetown and Roundrock ISDs. Georgetown has recently renovated several of its facilities and there are plans for a new high school in Roundrock. School officials do not envision that local competition will have a profound effect on operations, and they believe the local school districts remain well-positioned in their respective markets given area growth projections following highway improvements.

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. According to the most recent 2016 State of Texas Assessments of Academic Readiness (STAAR) ratings, GCPS placed in the top 12% of all Texas public schools, "met standards," and earned distinctions in five of seven categories. We believe this achievement will allow Orenda to sustain its positive demand profile.

The Gateway Tech campus, which is not eligible to receive distinctions, met standards as well. As per a previous legislative action, Orenda's residential facility or hybrid campuses are exempt from such assessments hereafter, and the STAAR ratings for Nolan Creek School and Kingsland School are not yet available as they are currently in their first school year.

The statutory framework assessment reflects our opinion that despite areas of risk, the framework is not likely to hamper Orenda's ability to pay debt service. All campuses operate under a single charter authorized by the Texas Education Agency (TEA), which currently expires in 2025, lowering the chance of non-renewal. In Texas, the state rather than local sources provides the majority of public school operating dollars. Therefore, charter schools depend almost entirely on the state for operating revenue that is subject to annual appropriation by the legislature. As a result, Texas' economic and financial situation has a direct effect on a school's operations, and funding will fluctuate along with the state economy. We understand that for the next biennium, based on proposed bills by the state legislature, the state funding outlook is encouraging.

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; he has been with the district since its inception in 1999. Orenda's business manager has been with the district since 2009, having previously worked for an ISD. The school has a stable board of directors that consists of four members from the community out of total five board members. The board is actively involved in the governance of the school and works closely with the school's management team and authorizer.

Financial Profile

Financial performance

Operations have been positive for at least the past five years, in part due to increases in enrollment as GCPS filled in grades. Orenda ended fiscal 2016 with an operational surplus of \$1.1 million or an excess margin of 8.5%, roughly the same as fiscal 2015's surplus. Pro forma lease-adjusted MADS coverage is low for the rating at 1.2x.

Liquidity and financial flexibility

Orenda's unrestricted reserve position remains exceptionally healthy. As of Aug. 31, 2016, it held about \$8.6 million in unrestricted cash and investments, equal to 288 days' cash on hand. This is up from \$6.8 million at fiscal 2015 year-end, or about 228 days' cash on hand. The significant growth in cash is due to strong operating results.

Debt burden

Orenda's total pro forma debt is an estimated \$48.49 million in bonds, which comprise the series 2011B, 2011Q, 2015A, 2015B, and 2017. Aggregate lease-adjusted MADS, including leases for three of the campuses and a district office, is \$2.82 million, occurring in 2041. It represents an onerous 22.2% of total revenue. Debt per student also compares poorly at \$32,741 per student, an outlier among peers in the state, most of which have less than half that amount per student.

Financial policies

Orenda meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, despite areas of risk, the organization's overall financial policies are not likely to hamper its ability to pay debt service. Our analysis of financial policies includes a review of the organization's 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.

Orenda Education, TX -- Selected Financial Statistics

	Fiscal year ended Aug. 31					Medians: Charter schools 'BBB-'
	2017	2016	2015	2014	2013	2015
Enrollment						
Total headcount	1,481	1,377	1,326	1,206	999	806
Total waiting list	208	146	152	381	247	MNR
Waiting list as % of enrollment	14.0	10.6	11.5	31.6	24.7	39.8
Financial performance						
Total revenues (\$000s)	N.A.	12,682	12,932	11,539	10,323	MNR
Total expenses (\$000s)	N.A.	11,599	11,871	10,583	8,646	MNR
EBIDA (\$000s)	N.A.	2,810	2,807	2,097	2,447	MNR
EBIDA margin (%)	N.A.	22.16	21.71	18.17	23.70	17.50
Excess revenues over expenses (\$000s)	N.A.	1,083	1,061	956	1,677	MNR
Excess income margin (%)	N.A.	8.54	8.20	8.28	16.25	5.0
Lease adjusted annual debt service coverage (x)	N.A.	1.72	1.85	1.77	1.84	1.5

Orenda Education, TX -- Selected Financial Statistics (cont.)

	Fiscal year ended Aug. 31					Medians: Charter schools 'BBB-'
	2017	2016	2015	2014	2013	2015
Lease adjusted annual debt service burden (% total revenues)	N.A.	15.6	14.1	13.9	14.2	MNR
Lease adjusted annual debt service burden (% total expenses)	N.A.	17.1	15.4	15.1	16.9	MNR
MADS (\$000s)	N.A.	N.A.	1,819	2,150	2,150	999
Lease adjusted MADS coverage (x)	N.A.	N.A.	1.86	1.32	1.25	1.5
Lease adjusted MADS burden (% total revenues)	N.A.	N.A.	14.1	18.6	20.8	MNR
Lease adjusted MADS burden (% total expenses)	N.A.	N.A.	15.3	20.3	24.9	13.00
Pro forma MADS (\$000s)	N.A.	2,820	N.A.	N.A.	0	MNR
Pro forma lease adjusted MADS coverage (x)	N.A.	1.21	N.A.	N.A.	N.A.	MNR
Pro forma lease adjusted MADS burden (% total revenues)	N.A.	22.2	N.A.	N.A.	0.0	MNR
Pro forma lease adjusted MADS burden (% total expenses)	N.A.	24.3	N.A.	N.A.	0.0	MNR
Total revenue per student (\$)	N.A.	9,210	9,753	9,568	10,333	MNR
Balance Sheet Metrics						
Days' cash on hand	N.A.	287.8	228.4	275.5	178.3	123.00
Total long-term debt (\$000s)	N.A.	25,399	25,692	21,103	10,471	MNR
Unrestricted reserves to debt (%)	N.A.	34.0	26.7	36.3	39.2	19.1
Unrestricted net assets as % of expenses	N.A.	35.3	32.6	31.9	30.0	25.7
General fund balance (\$000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Debt to capitalization (%)	N.A.	86.6	87.7	86.4	80.6	MNR
Debt per student (\$)	N.A.	18,227	19,109	17,137	10,481	13,920
Pro forma Metrics						
Pro forma unrestricted reserves (\$000s)	N.A.	8,643	N.A.	N.A.	1,505	MNR
Pro forma days' cash on hand	N.A.	287.78	N.A.	N.A.	65.42	MNR
Pro forma long-term debt (\$000s)	48,489	48,489	25,692	21,103	10,471	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	17.8	N.A.	N.A.	14.4	MNR
Pro forma debt to capitalization (%)	N.A.	167.37	88.88	88.26	80.61	MNR
Pro forma debt per student (\$)	32,741	35,214	19,376	17,498	10,481	MNR

N.A.--Not available. MNR--Median not reported.

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