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## Austin Achieve Public Schools, Texas; Charter Schools

**Primary Credit Analyst:**

David Holmes, Farmers Branch + 214 871 1427; david.holmes@spglobal.com

**Secondary Contact:**

Peter V Murphy, New York + 1 (212) 438 2065; peter.murphy@spglobal.com

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# Austin Achieve Public Schools, Texas; Charter Schools

## Credit Profile

ICR

*Long Term Rating*

BBB-/Stable

New

## Rating Action

S&P Global Ratings assigned its 'BBB-' issuer credit rating (ICR) to Austin Achieve Public Schools (AAPS), Texas. The outlook is stable.

An ICR reflects our view of an obligor's general creditworthiness, focusing on its capacity and willingness to meet financial commitments in a timely manner. It does not apply to any specific financial obligation because it does not take into account the obligation's nature and provision; standing in bankruptcy; or liquidation, statutory preferences, or legality and enforceability.

AAPS intends to enter into a maximum \$30 million loan from the Equitable Facilities Fund (EFF) to refund and refinance series 2017 bonds. The series 2017A bond proceeds were used to finance and refinance the acquisition, construction, renovation, and equipping of land and buildings for the school's elementary school building (AAE). The series 2017B bond proceeds were used to refinance a portion of the school's 2015 New Market Tax Credit deal to finance the acquisition, construction, and equipping of land and buildings for the school's middle school building (AAM). Additionally, proceeds in the amount of \$1.6 million would be used to convert purchased property into a bus yard. Based on current expectations, the EFF financing will be structured as a loan, with a par amount of approximately \$29.1 million and, when including a \$2.1 million debt service reserve fund series 2017 debt release, total proceeds of \$31.4 million.

The deal is intended to achieve material annual debt service savings and create a level debt payment schedule over the 30-year maturity. The EFF loan is a general obligation of AAPS, secured by the school's revenue and a first-mortgage lien on all of the financed properties.

Proceeds of the school's \$17.8 million series 2018 bonds, which we do not rate, were used to construct a new high school adjacent to its elementary school facility, including traditional classrooms, an athletic field, a cafeteria, and a gymnasium. The 2021 loan is on parity with the series 2018 bonds.

The EFF loan and 2018 educational revenue bonds are secured by all operating revenue of the charter school. Associated financial covenants include 45 days' cash on hand, annual debt service coverage of 1.1x, and an additional bonds test of 1.2x projected maximum annual debt service (MADS) coverage. Including the new debt issuance, the school has \$55.8 million in total pro forma debt.

Similar to its national peers, in response to the COVID-19 pandemic and broader safety concerns, AAPS moved to

virtual learning in March 2020 for the duration of the 2019-2020 school year. Management reports that the transition to online learning was smooth. Savings associated with closure of the campus largely offset expenses incurred as a result of the outbreak. In addition, AAPS secured \$2.5 million through the Payroll Protection Program (PPP) under the Coronavirus Aid, Relief, and Economic Security (CARES) Act that is not classified as a loan for accounting purposes and not expected to be paid back. The PPP funds are reflected in the schools' 2020 audits, with the audit recognizing the funds as cash and AAPS noting the loan as a liability. Our analysis mirrors the audited presentation, though we understand this skews performance given the one-time nature of these funds. In addition, AAPS received \$530,000 in CARES Act funding related to the COVID-19 pandemic. Despite high uncertainty regarding the duration and impact of the pandemic and the related effects on the performance of those charter schools in our rated universe, including the ability to resume classes and absorb unreimbursed additional costs, state per pupil funding in Texas continued as budgeted for fiscal 2020, and is expected to continue unabated for fiscal 2021 based on the most recent state reports; as well, the state has a biennium budget. We will monitor developments for any credit effects and take action as we deem appropriate. We believe the school has sufficient liquidity at the rating to withstand any potential moderate funding cuts over the outlook horizon, with 148 days' cash on hand, which includes the PPP loan.

For the 2020-21 school year, AAPS offered both in-person and remote learning options, in accordance with state and local recommendations. Officials will monitor local COVID-19 metrics and the efficacy of various modes of instruction and make the adjustments it deems necessary to its delivery during the pandemic. We expect no differential in state funding regardless of the mode of instruction.

### **Credit overview**

The 'BBB-' rating reflects our view of AAPS' adequate enterprise profile, characterized by the school's nearing its capacity of approximately 2,300 students, knowledgeable management team, and good charter standing. We assessed the school's financial profile as adequate, supported by the school's favorable pro forma lease-adjusted MADS coverage, improvement in fiscal 2020 liquidity to a level we consider solid for the rating, and a manageable debt burden supported by a history of positive and healthy operating margins. We believe that, combined, these credit factors lead to an anchor of 'bbb-' and a final issuer credit rating of 'BBB-'.

The rating reflects our view of AAPS':

- Solid 44% enrollment growth since fall 2017, though growth is expected to slow during the outlook period as school nears enrollment capacity;
- History of operating surpluses supporting healthy pro forma MADS coverage for the rating; and
- History of positive operating performance, with a \$2.1 million surplus in fiscal 2020.

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

- Substantial debt per student of more than \$29,000, which would remain at almost \$20,000 assuming full enrollment by 2023;
- Uneven academic performance in relation to peers, with a 'C' overall rating based on most recent state accountability standards; and
- Risk, as with all charter schools, that the school can be closed for nonperformance of its charter or for financial

distress before the final maturity of the bonds.

The stable outlook on the 'BBB-' rating reflects our view of the school's solid enterprise profile, large operating base, and acceptable MADS coverage for the rating, which will likely continue through the outlook period.

AAPS opened in 2012 and holds a mission to prepare the youth of East Austin to attend and excel at the nation's top colleges and universities. AAPS operates an elementary, middle, and high school on two campus sites in northeast Austin, serving about 2,190 students in pre-kindergarten through 12th grade. The elementary and high schools are located at the same campus, while the middle school stands alone. AAPS operates under a single contract with the Texas Education Agency (TEA) that was renewed in 2017 through 2027.

### **Environmental, social, and governance factors**

In our view, AAPS is exposed to elevated health and safety social risk given the COVID-19-related economic uncertainty's impact on state funding and the school's dependency on state revenue. Despite the elevated social risk, we believe the school's environmental and governance risk are in line with our view of the sector as a whole.

## **Stable Outlook**

### **Downside scenario**

We could consider a negative rating action if AAPS experiences material enrollment declines that lead to weaker margins, reserves declines, or lease-adjusted MADS coverage weakens. In addition, we could consider a negative rating action if AAPS' academic profile weakens compared with that of similarly rated peers. Although we believe the organization has taken steps to address COVID-19, and we understand the coronavirus to be a global risk, we could consider a negative rating action during the outlook period should unforeseen pressures related to the pandemic materially affect the school's reserves, demand, or trajectory.

### **Upside scenario**

We view a positive rating action over the outlook period as unlikely given AAPS' demand and financial metrics that are more reflective of those of 'BBB-' rated peers, including the school's debt per student metrics, which will likely prevent meaningful improvement of the school's financial profile.

## **Credit Opinion**

## **Enterprise Profile**

### **Economic fundamentals**

AAPS is located in Travis County and serves the Austin MSA. The county's school age population is significant at about 471,000, and is expected to grow rapidly, with projections to increase by a healthy 6.3% by 2025.

### **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**

We view the school's enrollment and demand profile as sound, reflecting stable enrollment in conjunction with a modest waitlist. Total enrollment has increased by 44% to more than 2,100 students for fall 2020 from 680 students in 2017, as the school added an elementary school in 2019 to the middle and high school levels. AAPS projects it will reach enrollment of approximately 2,300 students, its charter capacity, by 2023 and we believe this is a fair assessment given that the school has met budgeted enrollment projections in the past, including for fall 2020, and given the school's location in a rapidly growing market within the Austin MSA. While the market in the greater Austin area is not without competition, management believes that the school's unique learning system, which focuses on restorative learning practices, 1-to-1 technology resources, and a wide array of extracurricular activities, will support continued market demand. AAPS students are primarily Hispanic and about 93% of students qualify as economically disadvantaged. The school's goal is to provide college-ready instruction through academic rigor and innovation, restorative learning, and character development. AAPS has historically maintained solid year-to-year student retention that has averaged approximately 92% over the past two years.

For fiscal 2019, the school received an overall district rating of 'C', which we view as acceptable. Management reports that the school has continued to make academic progress, with returning students performing on average stronger than their local peers. The school also reports that high school performance standards, which have trended slightly stronger than the state average, will for the first time be fully accounted for in the next accountability rating. In addition, the school serves a free- and reduced-lunch population of 92%, which is higher than the majority of its local peers and well above the state average of 55%. As state testing and accountability have been postponed for both fiscal years 2020 and 2021 as a result of the COVID-19 pandemic, we will monitor the school's academic accountability performance. Given the school's increase in enrollment in recent years, we do not view academic accountability as having a significant impact on the school's market demand.

We view the school's standing with the authorizer as good. AAPS has held its charter with TEA for nine consecutive years, with the charter renewed once, on July 31, 2017, for a full 10-year extension through July 31, 2027. In addition, TEA approved an increase in the school's enrollment cap to 2,325 students in 2019.

The statutory framework assessment reflects our opinion that, despite areas of risk, the framework is not likely to hamper AAPS' ability to pay debt service.

### **Management and governance**

AAPS is governed by a board whose 12 members may each serve a maximum of three three-year terms. Board members have a diverse set of backgrounds, including real estate, finance, and education. The board's policies and internal controls utilize conservative investment practices and a goal of maintaining solid reserves to support operations. In our view, the management team is active in assessing the school's day-to-day and long-term financial and operational needs.

The school is self-managed, with what we consider a strong and dedicated senior management team, consisting of several long-tenured members. The CEO is the school's founder and has more than a decade of experience in

education management. He was also named a board representative of the Texas Charter School Assn, in 2019. The chief achievement officer and most of the school's principals have been part of the school for more than five years. We view the management team as a credit strength, demonstrated by its ability to significantly increase enrollment over the past five years while maintaining solid operations.

## **Financial Profile**

### **Financial performance**

AAPS has a history of solid operations with margins exceeding 7% for the past four years, including three years with more than 11% surplus operations. For fiscal 2020, AAPS posted an EIDA margin of 24.9%, or \$6.8 million, and a 2.32x pro forma lease-adjusted MADS coverage, which we view favorable. Management has budgeted for a \$3.2 million surplus for fiscal 2021 based on expected steady per pupil funding and slight enrollment growth toward capacity. We believe the school will be in a solid position to manage potential expenditure cuts in the event that state funding is reduced in fiscal 2021, which we view as unlikely based on state communication. AAPS attributes its consistently positive margins to consistent enrollment growth, a healthy state funding environment, and sound fiscal management. We view the organization's financial results and projections as indicative of steady financial performance and coverage metrics given the organization's strategic approach to operations and expansion, which incorporates the state funding environment and other pertinent assumptions. We expect lease-adjusted pro forma MADS coverage to remain at or above levels comparable to that of similarly rated peers in the near term given the school's historical operating performance and limited debt plans.

### **Liquidity and financial flexibility**

AAPS has held decent liquidity over the past several years, including ending fiscal 2020 with \$9.3 million in unrestricted reserves, or 147 days. The fiscal 2020 figures were an improvement compared with \$5.8 million, or 122 days, in fiscal 2019, a result of increased enrollment with school expansion, as well as receiving approximately \$2.5 million in PPP loan funding and approximately \$500,000 in CARES Act funds. Officials have no plans to draw down reserves and expect to build cash further in the outlook period as school expansion nears full enrollment. We believe AAPS will maintain liquidity commensurate with that of 'BBB'-rated peers given its solid revenue base and consistent enrollment trends.

### **Debt burden**

The school will have about \$55.3 million in debt after the 2021 loan is entered into with pro forma lease-adjusted MADS of \$2.9 million occurring in fiscal 2040. This translates into a moderately high pro forma debt burden of about 10.7% of fiscal 2019 revenue. Pro forma debt per student remains elevated at more than \$29,000, based on fiscal 2019 enrollment figures. Included in the pro forma debt is about \$15.1 million of New Market Tax Credit debt that will unwind by 2023 and that the school reports with expected minimal obligation to AAPS.

Pro forma debt per student remains elevated at more than \$29,000, based on fiscal 2020 enrollment figures. Although we view this as acceptable for the rating and not out of line with higher-rated issuers in the sector, we expect AAPS' debt burden to remain high over the outlook horizon. The school has no additional contingent liabilities or off-balance-sheet debt. We understand it does not anticipate issuing additional debt within the outlook period, but we

expect the overall burden to remain manageable as operations expand, given the stable increase in enrollment.

As with many charter schools, the organization's debt-to-capitalization ratio shows significant leverage on the balance sheet. Based on fiscal 2019 figures, the ratio was 95%. We view AAPS' debt burden as a constraining factor to the rating, but we expect these ratios to remain consistent with the rating.

### **Financial policies**

The financial policies assessment reflects our opinion that despite areas of risk, the organization's overall financial policies are not likely to hamper AAPS' 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 similar providers.

### **Related Research**

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

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