S&P Global
Ratings

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Equitable School Revolving Fund, Delaware; State Revolving Funds/Pools

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Equitable School Revolving Fund, Delaware; State Revolving Funds/Pools

Credit Profile		
US$89.445 mil natl charter sch revolving loan fd rev bnds (Equitable Sch Revolving Fd) ser 2019A		
Long Term Rating	A/Stable	New
US$18.265 mil natl charter sch revolving loan fd rev bnds (Equitable School Revolving Fund) ser 2019B		
Long Term Rating	A/Stable	New

Rationale

S&P Global Ratings has assigned its 'A' rating to the Equitable School Revolving Fund (ESRF), Del.'s series 2019 A and B bonds, issued by the Arizona Industrial Development Authority and California Infrastructure and Economic Development Bank, respectively. Equitable Facilities Fund (EFF) as sole member of ESRF operates a pooled charter school loan program through ESRF. The purpose of the bonds is to capitalize the loan program.

Our 'A' rating reflects an adequate enterprise risk profile and a very strong financial risk profile. Details of our scoring methodology are below.

Bond provisions that we consider primarily relevant in our analysis include the following:

- The bonds are issued pursuant to a master trust indenture (MTI) and supplementals. Pledged to repayment of the bonds are school loan agreements and related repayments made with funds transferred to the MTI from bond proceeds and charitable contributions, all funds pledged under the MTI, and related fund interest earnings.
- Included in the pledge will initially be a $8 million debt service reserve fund (DSRF); the MTI provides flexibility to define the DSRF as needed under supplemental indentures, but in all cases the amount being no less than the amount that satisfies financial sufficiency tests for both debt service coverage (DSC; minimum pro forma maximum annual debt service coverage of 1.15x and 1.0x for parity and subordinate obligations, respectively) and leverage (minimum pledged assets to outstanding obligations no less than 1.2x and 1.0x for parity and subordinate obligations, respectively).
- The defined Obligated Group (OG) under the MTI that grants the trustee a security interest in the pledged funds currently consists of only ESRF. Additional members of the OG would not necessarily introduce credit risk, in our view, as long as the charitable purpose of EFF does not broaden or change in a fashion that significantly changes the composition or purpose of ESRF.
- To transfer out funds from the MTI to EFF for any legal purpose, all prior financial tests and required deposits must be made pursuant to the provisions of the MTI. We believe that any legal purpose is generally restricted to EFF's furtherance of its charitable purpose of making loans to charter schools and currently, this mission can be accomplished within ESRF. If there are transfers out of ESRF to make loans outside of the MTI, the rating could be negatively affected because our cash-flow analysis would then need to account for the release of funds. Given ESRF as currently being the sole vehicle for accomplishing the financial mission of EFF, our financial analysis assumes that surplus revenues from any year would be used by EFF to either make additional pledged loans or make up any

shortfalls as needed.

- Release of school loans from the pledged assets is conditioned on compliance with sufficiency tests (same as those related to the DSRF), and if the outstanding loan principal due represents more than 5% of pledged assets, then additional rating confirmation is needed.
- A limitation on issuing additional bonds, subject to the sufficiency tests mentioned under both the DSRF and release from pledge sections above.

ESRF is a Delaware charitable nonstock limited liability corporation (LLC). Its purpose is to further the charitable purpose of EFF of making loans and providing financial assistance to charter schools. EFF is the sole member of ESRF. ESRF is currently the only member of the OG under the MTI, and therefore is the entity that grants a security interest in the pledged assets to the trustee. The trustee then makes all required payments, including debt service payments, pursuant to the flow of funds in the MTI. We do not believe that the existence of the LLC introduces additional credit risk to bondholders, given our view of the following:

- Limitations on LLC overall activities that are related to furthering the charitable purpose of EFF, including the ability to undertake any lawful act in furtherance of that charitable purpose;
- Within the LLC's operating agreement, provisions that account for both the existence of at least one independent director and separateness from other legal entities, including EFF;
- All deposits of bond proceeds and charitable contributions deposited into the MTI's loan program fund are held in trust solely for the benefit of the LLC and this fund has only two purposes: to make pledged loans or replenish the DSRF; and
- Our review of a non-consolidation opinion that addresses consolidation of assets held in trust under the MTI if EFF becomes a debtor under Chapter 11 of the U.S. Bankruptcy Code.

Outlook

The stable outlook reflects our expectation that EFF will continue to use ESRF as the sole vehicle for accomplishing its mission of providing loans to charter schools. We base this expectation on EFF's current practice of directing both the bond proceeds and its charitable contributions to ESRF to make loans. As ESRF grows, the outlook also reflects management's representation that over-collateralization levels through both additional DSRF deposits and annual DSC will remain consistent with what is being contemplated as a result of the 2019 bonds being issued (i.e., a DSRF funded at about MADS and 1.3x annual DSC). Also supporting the outlook is EFF's mission to provide school loans to high-performing charter schools, which we believe is likely to be correlated with generally higher charter school ratings.

Downside scenario

We believe that the most immediate causes of any downside rating risk would be either one or a combination of the following: how ESRF's cash flows are structured to provide DSC, the composition of the pledged loan portfolio, or whether ESRF experiences any payment delinquencies or defaults. Key factors we would consider are the following:

- ESRF cash-flow projections that provide for DSC significantly less than the currently projected level of about 1.3x.

This level, in our view, provides a level of cushion to protect against potential defaults that is consistent with the current rating level; coverage of less than this could lead to downside rating risk.

- If the pledged loan portfolio begins to experience payment defaults or delinquencies, the rating could be lowered, even if there are funds sufficient to make all required bondholder payments because our view of the program's operating profile would likely be weaker. All else being equal, we generally consider programs that have not experienced any defaulted or delinquent payments as stronger than those that have.
- While a growing loan portfolio could help lower the overall default stress we apply to ESRF's projected cash flows, future loans that have characteristics such as the following could lead to the cash flows needing to withstand a higher default stress to maintain the rating just at its current level: loans with a longer weighted average maturity or deferred principal payments, loans to a portfolio of borrowers that are materially lower in credit quality, or loans that create undue portfolio concentration in one or several states. All of these characteristics serve as inputs to our default tolerance analysis, and all can have direct effects on our assessment of ESRF's financial risk profile and overall credit rating.

Upside scenario

We do not believe that in the near term there is any rating upside given the currently small size of the ESRF loan portfolio, the lack of any loan repayment history (since this is a new program), our uncertainty related to the future composition of the loan portfolio (e.g., credit ratings, amortization/repayment schedules) as it grows, and our expectation that over-collateralization arising from both the DSRF and annual DSC of about 1.3x should continue to provide default tolerance consistent with the current rating level but not a higher one. As ESRF grows, DSC levels significantly higher than the currently projected 1.3x could lead to a higher rating if we believe that level is sustainable for successive rounds of future bond issues. If the pledged loan portfolio improves significantly in credit quality, there also could be upside potential. We would note, however, that the need to withstand a significantly higher amount of default stress to achieve higher rating levels will likely preclude a higher rating for some time until the program matures.

EFF History And Mission

EFF's history and mission to support charter schools, as well as its nonprofit 501(c)(3) status, informs our view of ESRF's adequate enterprise risk profile. The EFF Board of Directors has ties to governmental entities that are charter authorizers, many of which are governmental institutions and public school districts. However, EFF is still a private nonprofit entity, and therefore our enterprise risk profile is scored as adequate instead of a stronger score.

EFF was formed to leverage a $200 million charitable contribution that will fund loans to charter schools. It is supported by two nationally recognized charter school nonprofit organizations: National Association of Charter School Authorizers and National Alliance for Public Charter Schools. EFF staff has broad expertise in all areas of the charter school sector, including lending, financial management, operations, staffing, and educational standards.

Philanthropic goals of EFF include:

- Reducing the cost of capital for charter schools
- Providing assistance to high-performing schools

- Sharing sector best practices in both educational and financial areas; and
- Partnering with schools participating in ESRF to facilitate ongoing financial success.

ESRF Loan Pool

ESRF has been capitalized through a prior charitable contribution and now through bond proceeds. The program benefits in our analysis from having both a pledged DSRF and a cash-flow structure that currently provides about 1.3x annual DSC. Both of these factors, along with our view of the program administration policies, help support the very strong financial risk profile.

The current cohort of 11 pledged loans with a total $158 million loan balance will be pledged to $111 million of outstanding bonds once the 2019 bonds are closed. Below is a listing of the current loan portfolio (totals may not be exact due to rounding):

- Alliance For College-Ready Public Schools, CA ($28.5 million, BBB group credit profile [GCP])
- Arlington Classics Academy, TX ($15.4 million, BBB-/Stable)
- Arizona School For The Arts, AZ ($10.5 million, BB+/Stable)
- Blackstone Valley Prep, RI ($15.9 million, BB+/Stable)
- Choices In Learning, FL ($9.1 million, BBB-/Stable issuer credit rating [ICR])
- James Irwin Charter Schools, CO ($26.1 million, BBB/Stable)
- KIPP Bay Area Schools, CA ($15.9 million, BBB ICR)
- KIPP Nashville, TN ($10.5 million, BBB-/Stable)
- Rocketship United, TN ($7.3 million, NR)
- Soulsville, TN ($10.2 million, NR)
- Village Tech Schools, TX ($8.4 million, BB/Stable ICR)

The over-collateralization of the annual debt service requirements consistent with a very strong financial risk profile reflects various criteria assumptions that are built into our default tolerance analysis. As stated above, our cash-flow analysis is supported by surplus revenues from any year that could be used by EFF to either make additional pledged loans or make up any shortfalls as needed. The reason for this is that ESRF is currently the sole vehicle for accomplishing the financial mission of EFF. On an aggregate basis, comparing all scheduled loan repayments and the $8 million DSRF to total debt service due, we calculate that loan revenues can withstand about a 26% reduction with 0% recovery and still achieve aggregate 1x DSC. However, in our methodology, we use a portfolio-wide recovery assumption of 46%, which corresponds to the recovery group for the charter school asset class that is consistent with a very strong financial risk profile. Because of this, our default tolerance analysis indicates a higher level of defaults possible than the 26% gross default rate (we consider it a gross default rate because we aren't incorporating recovery) to maintain the very strong financial risk profile.

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