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Dayspring Academy For Education And Arts, Florida; Charter Schools

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Dayspring Aca for Ed and Arts ICR		
Long Term Rating	BB/Stable	Rating Assigned

Rating Action

S&P Global Ratings assigned its 'BB' issuer credit rating (ICR) to Dayspring Academy for Education and the Arts, a Florida not-for-profit corporation. The outlook is stable.

An ICR reflects an obligor's general creditworthiness, focusing on its capacity and willingness to meet financial commitments when they come due. 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.

Dayspring Academy opened its first school in 2000 and has expanded to five schools on five separate campuses; its fifth campus opened on schedule and at the anticipated enrollment level in fall 2020. The schools are located in New Port Richey, near Tampa in Pasco County. Currently, all five schools operate under a single charter and are overseen by Pasco County School District, an authorizer serving 14 other charter schools within its boundaries as of the 2019-2020 school year. Dayspring's current 15-year charter contract expires in 2033. For fall 2019, Dayspring served 922 students in grades prekindergarten (PK)-12. As of fall 2020, it serves 1001 students. Annually, Dayspring has observed material growth with an 8.8% increase in headcount over the past three years. Each of its schools serves different grade levels with Minuet serving pre-kindergarten and kindergarten, Harmony with kindergarten through fifth grade, Symphony currently serving grades six through 10, and Odeon, serving grades 11 through 12. Its fifth campus, Jazz, currently serves kindergarten through second grade.

We assessed Dayspring's enterprise profile as adequate, with excellent academic performance, seasoned and effective management, solid demand, a robust wait list, growing enrollment, and sound academic performance, tempered by potential construction risk and future expansion plans. We assessed Dayspring's financial profile as vulnerable, with a small revenue base of less than $10 million, very low unrestricted reserves, a manageable debt burden, and solid pro forma lease-adjusted maximum annual debt service (MADS) coverage. We believe that, combined, these credit factors lead to an anchor for Dayspring of 'bb', and a final ICR of 'BB'.

In fiscal year 2021, Dayspring Academy entered into a $10 million loan from the Equitable Facilities Fund to refinance existing note payables (approximately $3.1 million outstanding as of June 30, 2019) and to finance the costs of renovating an elementary school facility and constructing a new high school facility. This refinancing is intended to achieve material annual debt service savings and create a level debt payment schedule. The loan security includes a first lien on gross revenues of Dayspring Academy (all schools) and a first lien mortgage on properties of the school.

All Dayspring schools transitioned to a remote learning curriculum starting at the end of March for remainder of the 2019-2020 school year. Dayspring utilized an app-based program along with textbook- and project-based learning for its course instruction. For fall 2020, Dayspring is offering a hybrid learning model with 29% of its students learning remotely in the virtual classroom setting. Management reports near perfect student participation and no disruptions in the delivery of its educational and performance arts curriculum. We understand Dayspring has so far successfully absorbed costs associated with the online transition and COVID-19-related costs with no meaningful impacts on enrollment, student retention, and finances. Dayspring management says that it is stress-testing for various scenarios and is currently budgeting for flat state per pupil student funding growth in fiscal 2021. In our opinion, while Dayspring has weak liquidity at approximately 30 days' cash on hand projected as of June 30, 2020 (ignoring $400,000 of paycheck protection plan (PPP) funds received), management is focused on improving liquidity and we believe that the additional PPP funding could provide some additional flexibility to offset any emerging expense pressures over the next year. We will continue to monitor any developments in state funding or any potential impacts of recessionary pressures and take actions as we deem appropriate, particularly if Dayspring's financials materially weaken from current assessment levels.

Established by the United States Small Business Administration under the recently passed Coronavirus Aid, Relief, and Economic Security (CARES) Act, the PPP provides liquidity to financial institutions which in turn provide loans that support small businesses in meeting payroll, debt service, rent, utilities, or health care-related expenses. An additional benefit is that PPP loans are eligible for forgiveness (in full or in part) by the lender. In our view, this could provide additional operating cash flow support to the school in the near term to cushion against the impact of state funding cuts. We have not included this loan in our debt-based metrics, as it is uncertain if the loan will need to be repaid.

Credit overview

The rating reflects our opinion of Dayspring's:

- Annually Increasing enrollment, at 1,001 students for fall 2020, supported by excellent academics, robust demand and a wait list exceeding 100% of headcount for fall 2019;
- 20-year charter operating history, and a track record of consecutive renewal for the maximum term with a perfect performance score on its most recent authorizer review, which demonstrates longevity and operational effectiveness.
- Decent 2.3x pro forma lease-adjusted MADS coverage in fiscal 2019, with an expectation of achieving acceptable coverage for the rating for fiscal 2020; and
- Seasoned and skilled management, and an effective board with diverse skills.

Partly offsetting the strengths, in our view, are Dayspring's:

- Weak liquidity, with approximately 30 days' cash on hand projected at June 30, 2020 (ignoring PPP loan funds), and historically thin levels resulting from internal reserve spenddowns associated with expansion, which management has worked to remedy;
- Moderate expansion plans, which inherently present some uncertainty and risk; and
- Risk, as with all charter schools, that the charter authorizer could close schools for nonperformance of charter contracts or financial distress.

The stable outlook reflects S&P Global Ratings' opinion that over our outlook period, we expect Dayspring to maintain financial metrics around current assessment levels despite any state funding cuts, preserve its stable market position, good academics, and improve unrestricted days' cash on hand to levels more commensurate with the rating.

Dayspring's campuses are located in the western part of Pasco County with 80%-100% of families classifying as economically disadvantaged. However, Dayspring draws students from across the county and maintains a free and reduced lunch population of 51%. Dayspring also provides transportation to 200 students annually. Supporting its demand position is its sound academic performance which continues to draw students. Its position as a high-performing charter school receiving an 'A' grade for all but one year since inception, niche as an arts focused curriculum, and its focus on educating students to successfully complete college and attain associates level degrees coterminous with their high school diplomas, differentiate Dayspring from peers. The school is targeting growing enrollment by 100 students each year to approximately 1,400 students in 2025. Ultimately, management indicated that it has long-term plans to expand to about 400 students at each campus, which would total 2,000 students. With COVID-19, it is uncertain if these long-term growth plans will be altered due to potentially smaller in-person class sizes under possible social distancing scenarios, and we are uncertain if enrollment and retention will suffer for our rated charter schools. However, we believe that Dayspring's consistently high waitlist of over 120% of headcount will likely help it meet its current enrollment projections over the next couple of years.

Environmental, social, and governance factors

In our view, Dayspring is exposed to elevated health and safety social risk, given the recession's impact on state funding and Dayspring's heavy dependence on state revenues to support operations. Despite the elevated social risk, we believe Dayspring'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 there is a significant enrollment decline, failure to improve unrestricted days' cash on hand from the approximately 30 days' projected by management for fiscal 2020, and if state funding is materially reduced from current levels. Although we think Dayspring has taken steps to address COVID-19 and understand the virus 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 Dayspring's demand, finances, or trajectory.

Upside scenario

We consider a positive rating action within our outlook period unlikely, given the current economic climate. We believe that financial and operational pressures caused by COVID-19, and the recession we are in, with the potential for steep state funding cuts constrain a positive rating action at this time. Beyond our outlook period, we could consider a positive rating action if Dayspring were to meaningfully improve unrestricted days' cash on hand, while continuing to grow enrollment consistent with a higher rating category, while maintaining demand, and impressive academic performance.

Credit Opinion

Enterprise Profile

Economic fundamentals

Day-spring draws its students from Pasco County. The county's minor population size is good at 149,000 with a healthy projected increase of 8% through 2025.

Industry risk

Industry risk addresses the charter school sector's overall cyclicality 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 Dayspring's enrollment and demand profile as sound, supported by significant enrollment increases in conjunction with a robust wait list. Total enrollment has grown by 8.8% since fall 2016 with the addition of new grades at existing schools. Dayspring added a new K-5 campus in fall 2020, also in the county. Dayspring's increase in enrollment amid maintenance of a wait list of 122.5% of fall 2019 enrollment reflects excellent demand, in our opinion. The wait list is particularly solid for the lower and middle school entry grades, but is what we consider healthy at every grade level. Student retention rates have been healthy, in our view, measuring 90.4% in fall 2019 and an estimated 97.4% for fall 2020. Dayspring faces competition from a number of nearby local public, private, and charter schools with varied grade offerings. Management reports that it is not aware of any new schools opening in its service area.

Dayspring broke ground on its new Early College High School facility in June, with an anticipated opening by August 2021. Though COVID-19 impacts may delay school usage, we anticipate the project to not interrupt enrollment or business operations. After Dayspring's construction is completed, it will move its lower high school grades, 9-10, to join the upper grades on the new high school campus. Construction and relocation risk are minimal in our view, since Dayspring already has sufficient student enrollment at each grade level and the individual facilities are located in close proximity to the others. If construction were delayed, we believe Dayspring has capacity in its current facilities to house students during the outlook. Management also indicates that there are many school site options in the New Port Richey area, and it would expect additional lease costs to be minor in the event that additional space was needed.

We believe Dayspring has an above-average academic profile. Dayspring has maintained an 'A' rating on its state academic rating for every year except one since the school's inception. Its academic performance meaningfully exceeds district and state averages. Dayspring's vision for academic performance is focused on six C's: content, creativity, collaboration, character, customization, and community. Management attributes much of its success to its focus in these areas, incorporating learning-through-arts education as well as its emphasis on preparing students for post-secondary success. As a result of its early college program, many of its high school students graduate with an Associate level degree upon graduation. Further reflecting its impact, Dayspring is one of 16 schools in Florida with a 100% high school graduation rate.

We view Dayspring's standing with the charter authorizer, Pasco County School District, as very good. The district has renewed its charter twice, with the most recent renewal in 2018, extending through 2033. Pasco County provides financial and academic oversight, which is typical for its role as a district authorizer. Based on our discussion with the authorizer, they report a good working relationship with Dayspring and view the charter school as exceptional in comparison to its other peers. The authorizer noted that it is not aware of any compliance issues in the school's history and that Dayspring was the only charter school under its authorization to received perfect scores on its grade framework. Pasco County does not report any concerns with governance, academics, compliance, and finances. The authorizer noted potential state funding cuts are a concern for state charter schools beyond fiscal 2020 where no cuts materialized, but this future remains uncertain. The authorizer has historically provided financial support for capital projects and equipment purchases in the form of millage levies. We view the authorizer's consistent and nominal financial support as a credit strength. The statutory framework assessment reflects our opinion that despite areas of risk, the framework is not likely to hamper Dayspring's future ability to pay debt service, unless state funding is materially impaired and weakens financial metrics.

Dayspring's primary revenue source is per-pupil revenue from the state, passed through to the school from Pasco County School District. State per-pupil funding has been relatively stable, in our view, since significant cuts in fiscal 2012. Per-pupil funding including equalization revenues for capital was $8,180 for school year 2019-2020 compared with $7,930 for school year 2018-2019. For fiscal 2021, per-pupil funding is uncertain due to potential effects recession effects on funding. Management indicated that in its fiscal 2021 budget planning, it is assuming zero growth in per-pupil funding, which is fiscally prudent in our view. We expect Dayspring to maintain positive operations and we will continue to monitor any potential impact on the state funding environment.

Management and governance

Dayspring is governed by a seven-member independent board of trustees, which is its maximum capacity. In its bylaws, the board size may range from five to seven members, and we view the diversity of the membership as sufficient. Board diversity spans across law enforcement, education, business, finance, religion, and, technology. The board members serve for four-year, overlapping non-consecutive terms. Many however, reapply for future terms once they sit out for a term. Reflecting the solid community ties of the school, all of the current board members are parents or grandparents of students that attend or have attended Dayspring Academy. Dayspring has a formal strategic plan that includes specific financial and operational goals. We believe the board has been successful in executing on the mission and vision of the school. It maintains sufficient independence from management, and has controls in place to mitigate key risks.

Senior management is competent, skilled, and sophisticated. Dayspring's chief financial officer (CFO) and chief executive officer (CEO) are married. John Legg (CFO) and Suzanne Legg (CEO) also co-founded the school and have led the leadership team in their respective roles since Dayspring's inception. While we view this relationship and the tenure as a potential risk, we believe that the board has appropriate controls, traditional conflict of interest policies, and sufficient independence from management that should not impact its ability to remain effective as a governing body. Moreover, in our view, key person risk associated with having a long-serving CEO and CFO is partly mitigated with the formalization of robust succession plans for each of Dayspring's leadership personnel. Overall management, has impressive credentials, depth of knowledge, and decades of professional experience. John Legg is a former state senator. Suzanne Legg is pursuing her PhD and has decades of experience in education, previously serving as vice president for a separate Florida charter school. Dayspring's Principals have each served at Dayspring for over 10 years in various roles reflecting management stability. In addition, Dayspring's director of operations, campus director, and human resource director each have sufficient experience in their respective service lines.

We believe leadership is effective in operating its educational practice. The rigorous standards for academic performance are reflected in the long trend of top-tier performance on state exams and closing the educational gap for the low income students. Operationally, leadership fosters the market position of the school and community connections that have resulted in the donation of three out of its five owned facilities. Leadership demonstrates competence in navigating multiple expansions while maintaining compliance standards with its authorizer. Financially, the performance history is choppy and there is a limited track record of managing to covenants given that the series 2020 debt is Dayspring's first loan of its kind. We expect that over time, leadership will meet its financial covenants, which are similar to industry norms in our view. We would view the formalization of financial standards for Days' cash on hand and coverage that are more rigorous than Daysprings' bond covenants as deepening the school's proactive approach to risk and financial management.

Financial Profile

Financial performance

Dayspring's financial performance can be characterized by positive, albeit variable, full-accrual operating margins with solid 2.3x pro forma lease-adjusted MADS coverage. In fiscal 2019, total revenues were about $7.9 million and expenses were about $6.8 million, resulting in a surplus of $1.04 million or a 13% margin. Fiscal years 2018 and 2017 resulted in surpluses of $12,000 (0.2% margin) and $45,000 (0.8%), respectively. The substantially larger fiscal 2019 surplus was the result of enrollment growth and increases in state per pupil and equalization funding. Also, historically, Dayspring used cash flows to fund its capital needs which ultimately resulted in thinner margins prior to 2019. Management anticipates achieving another sound full-accrual surplus for fiscal 2020 and thus maintaining its acceptable lease-adjusted MADS coverage. For fiscal 2020, we expect some softening in performance in comparison with fiscal 2019 given ongoing capital projects, but ultimately anticipate another full accrual surplus. For fiscal 2021, Dayspring adopted a balanced budget and expects to meet its 1.1x debt service coverage covenant that is in effect in 2021. If there were state funding cuts in the near term that materially weaken coverage to levels below Dayspring's covenant, it is likely to be viewed unfavorably. The fiscal 2020 budget only partially accounts for expenses related to COVID-19 (full effects are unknown) and state per-pupil funds are uninterrupted for the current school year. Additional material COVID-19-related expenses and potential for per-pupil funding cuts are likely to affect growth in operations over the outlook.

Liquidity and financial flexibility

We consider Dayspring's balance sheet a key credit weakness and a constraint on our current rating. Management has focused on improving unrestricted cash by realizing savings from tighter expense controls, reducing its debt service expense through refinancing, and savings related to school facility closures as a result of the current pandemic. Management does not anticipate drawing on its cash reserves over the outlook period. Management projects approximately $500,000 in unrestricted cash as of June 30, 2020, ignoring PPP loan funds, equating to about 30 days' cash on hand. This is meaningfully improved from a minimal 19.4 days' cash on hand as of June 30, 2019, and 15.8 days' cash on hand at June 30, 2018. Despite looming state funding cuts, we expect enrollment growth to support Dayspring's ability to grow liquidity beyond 30 days' to meet its days' cash on hand covenants (beginning in 2021) over the outlook period.

Debt burden

Dayspring's pro forma lease-adjusted MADS burden is what we consider manageable, at 7.1% of fiscal 2019 total revenues. Dayspring has minimal long-term debt and its pro forma debt per student is approximately $11,593 per student based on fall 2019 enrollment. The organization's pro forma debt-to-capitalization ratio is high at 100.7%. Lease adjusted MADS for existing debt is $1.46 million occurring in 2025. Management has no plans for additional new debt during the outlook.

Financial policies

Dayspring meets standard annual disclosure requirements. Its audits are timely and sufficiently transparent, with no material or significant deficiencies in auditor findings. No investment policy exists, typical for its charter peers, but the organization has no aggressive investments. The financial policies assessment reflects our opinion that, while there may be some areas of risk, the school's overall financial policies are not likely to negatively affect its future ability to pay debt service. Our analysis of financial policies includes a review of Dayspring's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure, and a comparison of these policies with similar providers.

Dayspring Academy for Education and Arts, Florida--Enterprise And Financial Statistics

	--Fiscal year ended June 30--				Medians for 'BB' rated charter schools
	2020	**2019**	**2018**	**2017**	**2018**
Enrollment					
Total headcount	922	854	798	717	956
Total waiting list	1,129	960	885	872	MNR
Waiting list as % of enrollment	122.5	112.4	110.9	121.6	22.6
Financial performance					
Accounting standard	GASB	GASB	GASB	GASB	N.A.
Total revenues ($000s)	N.A.	7,865	6,166	5,730	9,039
Total expenses ($000s)	N.A.	6,822	6,154	5,685	MNR
EBIDA ($000s)	N.A.	1,336	332	305	MNR
EBIDA margin (%)	N.A.	17.0	5.4	5.3	14.3
Excess revenues over expenses ($000s)	N.A.	1,043	12	45	MNR
Excess income margin (%)	N.A.	13.3	0.2	0.8	2.3
Operating lease expense ($000)	N.A.	22	41	N.A.	MNR
Pension/OPEB adjustments ($000)	N.A.	N.A.	N.A.	N.A.	MNR
Lease adjusted annual debt service ($000)	N.A.	302	380	447	MNR
Lease-adjusted annual debt service coverage (x)	N.A.	4.50	0.98	0.68	MNR
Lease-adjusted annual debt service burden (% total revenues)	N.A.	3.8	6.2	7.8	MNR

Dayspring Academy for Education and Arts, Florida--Enterprise And Financial Statistics (cont.)					
	--Fiscal year ended June 30--				Medians for 'BB' rated charter schools
	2020	**2019**	**2018**	**2017**	**2018**
Lease-adjusted MADS ($000s)	N.A.	1,460	1,460	1,460	1,324
Lease-adjusted MADS coverage (x)	N.A.	0.93	0.26	0.21	1.20
Lease-adjusted MADS burden (% total revenues)	N.A.	18.6	23.7	25.5	13.6
Pro forma MADS ($000s)	N.A.	560	N.A.	N.A.	MNR
Pro forma lease-adjusted MADS coverage (x)	N.A.	2.43	N.A.	N.A.	MNR
Pro forma lease-adjusted MADS burden (% total revenues)	N.A.	7.1	N.A.	N.A.	MNR
Total revenue per student ($)	N.A.	9,209.6	7,726.8	7,991.6	MNR
Balance sheet metrics					
Unrestricted reserves ($000s)	N.A.	354.0	259.0	235.0	MNR
Days' cash on hand	N.A.	19.4	15.8	15.4	72.00
Total long-term debt ($000s)	N.A.	3,133	3,281	3,413	MNR
Unrestricted reserves to debt (%)	N.A.	11.3	7.9	6.9	11.9
Unrestricted net assets as % of expenses	N.A.	(1)	(1.3)	(0.4)	17.2
Debt to capitalization (%)	N.A.	102.1	102.4	100.6	91
Debt per student ($)	N.A.	3,669	4,112	4,760	16,811
Pro forma metrics					
Pro forma unrestricted reserves ($000s)	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma days' cash on hand	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma long-term debt ($000s)	N.A.	9,900	3,281	3,413	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma debt to capitalization (%)	N.A.	100.7	102.4	100.6	MNR
Pro forma debt per student ($)	N.A.	11,593	4,112	4,760	MNR

N.A.--Not available. N/A--Not applicable. MNR--Median not reported. MADS--Maximum annual debt service. Operating lease expense--Annual amount paid in facilities/capital lease payments; excludes equipment/nonfacility lease payments and excludes payments related to principal and interest on bonds. Net revenue available for debt service = EBIDA+operating lease expense. Lease-adjusted MADS coverage = (Net revenue available for debt service + operating lease expense) / (Lease-adjusted MADS). Total expenses include pension and OPEB adjustments. Pension and OPEB adjustments= reconciling adjustments made to financial information to account for differences in GASB 68 and GASB75.

Related Criteria And Research

- U.S. Public Finance Charter Schools: Methodology And Assumptions, January 3, 2017
- Guidance: Lease-Adjusted MADS Coverage , December 20, 2019
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, Apr 28, 2020