

Blackstone Valley Prep, Rhode Island; Charter Schools

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ICR		
<i>Long Term Rating</i>	BB+/Stable	New

Rationale

S&P Global Ratings assigned its 'BB+' long-term issuer credit rating (ICR) to Rhode Island Mayoral Academy Blackstone Valley (Blackstone Valley Prep [BVP]). The outlook is stable.

We assessed Blackstone Valley Prep's enterprise profile as adequate, characterized by enrollment growth, a robust waitlist, and a sizable student base at 1977 students, as well as a capable management team that has driven the school to success in sustaining a good charter standing. We assessed Blackstone Valley Prep's financial profile as vulnerable, based on its moderately weak liquidity, risks associated with annual escalators of the leases with Civic Builders Inc., and future financing needs. We believe that combined, these credit factors lead to an indicative stand-alone credit profile of 'bb'. As our criteria indicate, the final rating can be adjusted above the indicative credit level due to a variety of overriding factors. In our opinion, the 'BB+' rating better reflects BVP's solid enrollment and demand profile that is more comparable with those of peers at the higher rating.

Blackstone Valley Prep is a mayoral academy; therefore, the chair of the board must be a mayor of one of the municipalities in Rhode Island at all times. This is a requirement for keeping the school's mayoral academy charter versus the requirements of district and independent charter schools. We believe the mayoral requirement adds an additional risk factor to the school's charter not typically present in the sector. The composition of the academy's board mitigates this risk. BVP has three local chief executives on its board. The board also includes the state's lieutenant governor, who is a founding member. We expect the board's composition will continue to support the mayoral academy requirements.

More specifically, the rating reflects our view of the following:

- Growing enrollment, historically strong demand, and a solid market position, reflected by a robust and rising waiting list at over 100% of enrollment;
- History of operating surpluses generating good pro forma lease-adjusted maximum annual debt service (MADS) and similar results expected into fiscal 2019;
- History of good academic performance;
- Tenured management team with sound governance practices and thoughtful strategic planning; and
- Good working relationship with the chartering authority, the Rhode Island Department of Education (RIDE).

Partially offsetting the above strengths, in our view, are Blackstone Valley Prep's:

- Modest unrestricted reserves for the rating level, with 60 days' cash on hand at the end of fiscal 2018 and pro forma 68 days' cash on hand, reflecting BVP's cash contribution to the financing, calculated relative to fiscal 2019 results;
- Potential lease risk associated with several of BVP's facilities, because the leases have future escalator payments, although BVP expects to finance and purchase leases over the next few years prior to 2022; and
- In addition to the added risk of the mayoral requirement, the inherent uncertainty associated with charter renewals, given that the final maturity on the bonds exceeds the length of the existing charter.

An ICR reflects the 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 nature of and provisions of the obligation, its standing in bankruptcy or liquidation, statutory preferences, or the legality and enforceability of the obligation. BVP has two mortgage notes outstanding to a bank, due in monthly installments of \$23,041 and \$4,938, for Elementary School 1 located in Cumberland, R.I., with \$3.337 million and \$792,000 outstanding, respectively. The notes have final balloon payments of the unpaid principal balance and accrued interest is due Jan. 1, 2021. Management plans to refinance the notes prior to their maturity date with longer-term debt. These issuances financed the acquisition, expansion, and renovations of Elementary School 1. BVP's revenue, as defined in governing bond documents, primarily state per pupil funding, secures its debt.

BVP issued \$16 million of new debt, in the form of a loan from the Equitable School Revolving Fund. Blackstone Valley Prep used the loan proceeds to fund the acquisition of a 39,482-square-foot high school facility, which is which had previously been leased from Civic Builders, an organization known for financing, designing, and constructing charter school buildings. The loans are a general obligation of Blackstone Valley Prep secured by the school's revenues and a first-mortgage lien on the collateral property. We have taken into account this new debt and the elimination of lease payments for the high school when analyzing BVP's debt profile.

Blackstone Valley Prep operates a kindergarten through 12th grade (K-12), six-school network under one charter in the greater Providence County area. The six schools include three elementary schools, two middle schools, and one high school. The school was established as an economically diverse school, attracting students from two high-poverty urban districts. The school has enrolled a total of 1977 students, and is looking to continue expanding by adding more grades and increasing facility space.

Outlook

The stable outlook reflects our view that during the one-year outlook period, Blackstone Valley Prep will continue to meet its enrollment projections and maintain positive operations on a full-accrual basis, allowing it to sustain debt service coverage and improve cash levels to levels more consistent with the rating.

Downside scenario

We could lower the rating if the school were to fail to meet enrollment projections such that it generates notably weakened operating results, lease-adjusted MADS coverage, or liquidity below the historical position of about 60 days' cash on hand. In addition, any issues related to refinancing the new market tax credits obligations, which expire in 2020 and 2021, although not expected, could be viewed negatively.

Upside scenario

We are unlikely to raise the rating during the outlook period given BVP's leverage, modest unrestricted reserves, and expected expansion and future debt plans.

Enterprise Profile

Economic fundamentals

Blackstone Valley Prep is located in Providence County, about six miles north of the state's capital. The county's minor population is relatively small and its growth rate is slowly declining, trending downward at 1.2% over the next five years.

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, characterized by a growing student body, high student retention, and robust waitlist figures. Total enrollment has grown 12.4% over a three-year average, but is expected to drop to 8%-9% per year. BVP projects it will reach its charter cap of 2,360 students by 2021, and we believe this is a fair assessment, as the school has exceeded enrollment projections in the past, including fall 2018. The majority of students are in K-8, with a small, growing high school population. The school's waitlist in fall 2018 was about 100.4% of enrollment, which we view as large enough to sustain enrollment growth. We expect the waitlist to stabilize at that level over the coming years. Blackstone Valley Prep has high student retention, which we consider a positive factor, with little room to improve as the school has established itself well in its community.

Blackstone Valley Prep draws its students from two high-poverty urban districts, Pawtucket and Central Fall, as well as two higher-income suburban districts, Cumberland and Lincoln. Six public schools and three private schools also serve the area. We understand Blackstone Valley Prep outperforms the district by 13% in English Learning Acquisition and 15% in math on the Rhode Island Common Assessment System, giving it a competitive edge in its market position.

We view the school's standing with the authorizer as very good. Blackstone Valley Prep has held its charter with RIDE, the state's sole authorizer for charter schools, since 2011 and received a renewal in 2019 for the maximum term of five years through June 30, 2024. The authorizer has expressed a positive view of the school as a strong academic performer due to leaders who have laid a foundation for educational success. However, the charter terms may be adjusted after a pending renewal site visit of the high school, although this is not expected.

The statutory framework assessment reflects our opinion that, while there may be some areas of risk, the framework is not likely to negatively affect Blackstone Valley Prep's ability to pay debt service. State per-pupil funding has been flat over the past years: core instructional funding was \$8,831 per student for fiscal 2018 compared with \$8,806 for the previous school year. However, for fiscal 2019, the state plans to decrease per pupil funding by 0.66% to \$8,773 and

then increase it the following year drastically by 4.13% to \$9,135. Management reports that the funding environment in Rhode Island is dependent on the state's funding formula, which is now fully phased in.

Management and governance

The school is governed by a 13-member board of directors, which holds monthly meetings. There are no term limits, and the chair of the board must be a mayor of one of the municipalities in Rhode Island.

The management team is led by the chief executive officer, who led the growth of the school from 76 students to 1977. Other active administration positions include a chief academic officer, a chief operating officer, a chief financial officer, a chief schools officer, and heads for each of the six individual schools. KLR, a firm specializing in accounting, tax, and business advisory with a presence in New England, is the school's auditor.

In our view, the experienced management team is highly trusted by the governance board, which practices oversight but has shifted operational responsibilities to the executive director. The board has been self-sustaining throughout the school's history and the governance structure has been effective in producing steady financial results in most years and commendable academic results.

Financial Profile

Financial performance

Blackstone Valley Prep's operations have remained consistently positive since the start of operations. Fiscal 2018 financials show a \$1.68 million full-accrual surplus (a 6.18% excess margin), up from \$1.54 million in fiscal 2017. Blackstone Valley Prep's growth in revenues is certainly outpacing the school's growth in expenses over time, and we expect that to hold steady in the short term as the school is close to reaching its facility cap of 2,128 students. Management has conservatively budgeted for positive operations in fiscal 2019. EBIDA in fiscal 2018 was \$2 million or 7.55%, generating 1.39x MADS coverage. We anticipate MADS coverage to remain above 1x in fiscal 2019, albeit slightly lower, given the expectation of slimmer margins in fiscal 2019 due to the additional capital expenses associated with the expansion of the high school site and potential refunding costs of current leases.

Liquidity and financial flexibility

Blackstone Valley Prep's pro forma unrestricted reserves reached a high of \$4.1 million in fiscal 2018, equal to 59 days' cash on hand, which we view as a weakness in its financial profile relative to other financial metrics.

The pro forma MADS burden is moderately high, at 12% of expenses based on fiscal 2018 financials, along with other debt ratios that measure below rating medians, including pro forma debt per student of \$11,706, and pro forma unrestricted reserves to debt of 19.3%.

Debt burden

Pro forma MADS of \$3.254 million occurs in fiscal 2029. MADS of \$3.254 million assumes the school will be able refinance all existing leases subject to escalator payments prior to 2029. The school has a \$500,000 line of credit with the Bank of Rhode Island and does not plan to draw any of it in the future. We view the school's debt burden as high for the rating; we also understand that the school has multiple future financing needs, including the expansion of its high school facility and the purchase of its other facilities. Two leased facilities, which have new market tax credits

expiring within the next two years, are expected to be refinanced into longer-term debt.

As with many charter schools, the organization's pro forma debt-to-capitalization ratio shows significant leverage on the school's balance sheet. With the issuance of new debt and the anticipation of refunded leases, the ratio was 74.8%. We view the school's debt burden as a constraining factor to the rating.

Total pro forma debt is \$21.13 million. Proceeds from the loan will be used to acquire the leased high school facility. The transaction's legal structure is expected to be straightforward with a first lien on the organization's revenues as well as a first lien on the mortgaged property.

Financial policies

The school has formal policies for investment allocation, liquidity, and debt. Blackstone Valley Prep meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there may be some areas of risk, the organization's overall financial policies are not likely to negatively affect 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 similar providers.

Blackstone Valley Prep--Enterprise And Financial Statistics						
	--Fiscal year ended June 30--					--Medians for 'BB+' rated charter schools--
	2019	2018	2017	2016	2015	2017
Enrollment						
Total headcount	1,977	1,805	1,617	1,394	1,162	1,056
Total waiting list	1,984	1,787	1,800	1,975	1,741	MNR
Waiting list as % of enrollment	100.4	99.0	111.3	141.7	149.8	18.5
Financial performance						
Total revenues (\$000s)	N.A.	27,181	23,223	20,804	17,329	11,497
Total expenses (\$000s)	N.A.	25,500	21,681	20,363	17,192	MNR
EBIDA (\$000s)	N.A.	2,053	2,074	1,057	687	MNR
EBIDA margin (%)	N.A.	7.6	8.9	5.1	4.0	15.9
Excess revenues over expenses (\$000s)	N.A.	1,681	1,542	441	137	MNR
Excess income margin (%)	N.A.	6.2	6.6	2.1	0.8	3.8
Operating lease expense	N.A.	2,486	1,904	1,768	1,100	MNR
Lease-adjusted annual debt service coverage (x)	N.A.	1.83	2.09	1.56	1.53	MNR
Lease-adjusted annual debt service burden (% total revenues)	N.A.	9.1	8.2	8.7	6.7	MNR
Lease-adjusted annual debt service burden (% total expenses)	N.A.	9.7	8.8	8.9	6.8	MNR
MADS (\$000s)	N.A.	2,932	2,845	1,934	1,709	1,465
Lease-adjusted MADS coverage (x)	N.A.	1.55	1.40	1.46	1.05	1.40
Lease-adjusted MADS burden (% total revenues)	N.A.	10.8	12.3	9.3	9.9	13.1

Blackstone Valley Prep--Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					--Medians for 'BB+' rated charter schools--
	2019	2018	2017	2016	2015	2017
Lease-adjusted MADS burden (% total expenses)	N.A.	11.5	13.1	9.5	9.9	MNR
Pro forma MADS (\$000s)	N.A.	2,932	N.A.	N.A.	N.A.	MNR
Pro forma lease-adjusted MADS coverage (x)	N.A.	1.55	N.A.	N.A.	N.A.	MNR
Pro forma lease-adjusted MADS burden (% total revenues)	N.A.	10.8	N.A.	N.A.	N.A.	MNR
Pro forma lease-adjusted MADS burden (% total expenses)	N.A.	11.5	N.A.	N.A.	N.A.	MNR
Total revenue per student (\$)	N.A.	15,058.7	14,361.8	14,924.0	14,913.1	MNR
Balance sheet metrics						
Days' cash on hand	N.A.	59.10	69.47	40.02	40.79	102.50
Total long-term debt (\$000s)	N.A.	5,129	650	434	512	MNR
Unrestricted reserves to debt (%)	N.A.	81.7	619.2	499.1	363.5	17.0
Unrestricted net assets as % of expenses	N.A.	28.4	24.9	19.4	19.7	24.8
General fund balance (\$000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Debt to capitalization (%)	N.A.	41.1	11.0	9.6	12.6	87
Debt per student (\$)	N.A.	2,760	402	292	406	15,066
Pro forma metrics						
Pro forma unrestricted reserves (\$000s)	N.A.	4,069	N.A.	N.A.	N.A.	MNR
Pro forma days' cash on hand	N.A.	59	N.A.	N.A.	N.A.	MNR
Pro forma long-term debt (\$000s)	N.A.	21,129	650	434	512	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	19.3	N.A.	N.A.	N.A.	MNR
Pro forma debt to capitalization (%)	N.A.	75	11	10	13	MNR
Pro forma debt per student (\$)	N.A.	11,706	402	311	441	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. Lease-adjusted MADS coverage = (Net revenue available for debt service + operating lease expense) / (MADS + operating lease expense)

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