

Charter School Market Update

BAIRD



July 2016

HIGHLIGHTS:

- Interest rates (especially tax-exempt rates) continue to drop, hitting generational lows, yet again. See “**MARKET UPDATE**” section below for more information.
- Several Baird clients including Newark Charter School (a Delaware stand-alone charter school), King/Chavez Academy of Excellence (a California network charter school), Uplift Education (a Texas Charter School Management Organization), Great Hearts Academies (an Arizona Charter School Management Organization), Friendship Charter School (a District of Columbia network), and KIPP Philadelphia Charter School (a Pennsylvania Charter School Management Organization) took advantage of the favorable market environment to refinance existing debt and undertake new money borrowings. See “**RECENT DEAL IN FOCUS**” section below for more information.
- From January 2015 through June 2016, over \$3 billion of charter school bonds have been issued by 120 charter schools in 22 states (Source: Based on information derived from Bloomberg). See “**MATTERS OF INTEREST**” section below.

CONTACT US:

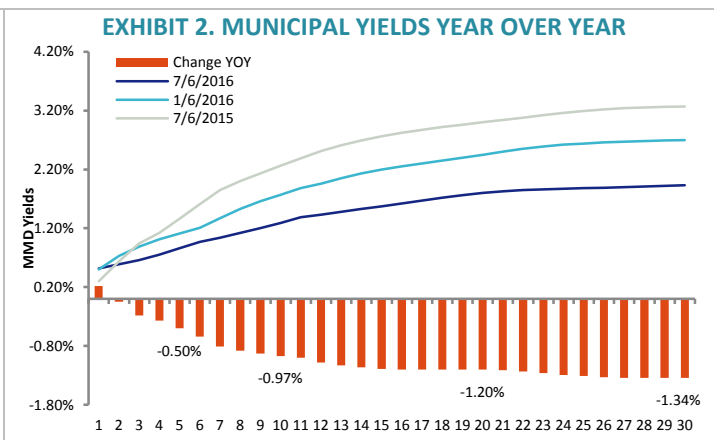
Robert W. Baird & Co.
Brian Colon, Manager
bcolon@rwbaird.com
 (303) 270-6335

National Charter School Finance Group
CharterSchoolFinance@rwbaird.com
www.rwbaird.com/charterschools
[Connect with us on LinkedIn!](#)

MARKET UPDATE: Interest Rates Hit Record Lows, Global Market Challenges Increase Muni Bond Demand

Record-low interest rates sink even lower: The all-time low interest rates from early June sank even lower after “Brexit,” Britain’s vote to leave the European Union. Results from the referendum vote were announced the night of June 23rd, and by the end of day on the 24th, the AAA municipal interest rate curve shifted down by 6–17 basis points or bps (0.60%-0.17%) (see Exhibit 1). The following week interest rates continued to tumble, reaching record lows, with the 10-, 20- and 30-year rates at 1.29%, 1.80% and 1.93%, respectively as of July 6. Short-term interest rates declined but not as dramatically, with the 2-year and 5-year landing at 0.59% and 0.86%, respectively as of July 6, seven bps lower than the 2016 low.

Looking back over the past six months to a year, the decline in interest rates has been significant (see Exhibit 2). The 20- and 30-year MMD¹ declined by 120 and 134 bps, respectively and the 20- and 30-year U.S. Treasury declined by 106 and 94 bps, respectively. With Brexit and economic numbers inconsistent, volatility week over week is anticipated to continue throughout the year, as market participants face uncertainty in how Brexit, among other global economies, will affect investments.

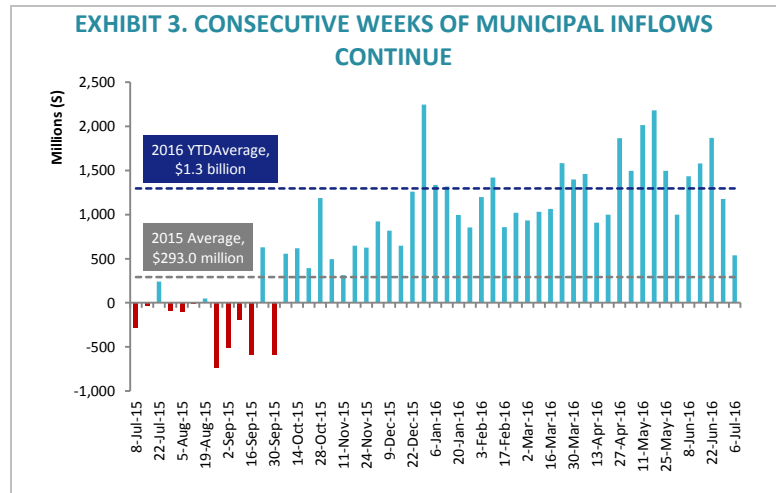


¹ Municipal Market Data Index (“MMD”), a daily index of “AAA” rated tax-exempt municipal bond interest rates. When pricing performance of any particular issue, a comparison is made based on the spread to MMD for transactions with similar credit ratings and final maturities. A bond marketed at a “lower spread” to MMD secured a lower interest rate given a particular market environment.

Supply: The trend of above-average municipal bond issuance has continued into July as issuers take advantage of the record-low interest rates (see “**RECENT DEAL IN FOCUS**” section below for an example of a refinancing Baird completed for Uplift Education).

Demand: The Brexit vote is not the only event driving investors to U.S. municipal bonds. While municipal bond rates are at record lows, they are far and away outshining the yields of other advanced economies. When banks from traditionally strong economies like Germany and Switzerland are paying negative interest rates, a 30-year yield of 1.93% (US MMD yield) starts to look pretty good. An indication of this demand can be seen in municipal in-flows, which continued for the 40th consecutive week (see Exhibit 3).

Economy: As interest rates reach (to some investors) “impossible” levels and countries overseas post negative yields, we are in unprecedented times. The U.S., however, posted strong employment June numbers, with nonfarm payroll employment increasing by 287,000 and the unemployment rate at 4.9%. Although these increases largely offset declines in May, inflation and the significant turmoil abroad make the chances of a Fed rate hike less probable in the near term. Read more about the “[2016 Midyear Fixed Income Market Outlook](#)” from Baird Senior Fixed Income Analyst Craig Elder.



MATTERS OF INTEREST: Charter School Bond Issuance Roundup

Issuance Volume by State: 2015 was a busy year for charter school bond market participants and 2016 continues to be on the same pace. Based upon information derived from market sources, from 2015 through June 2016, there were 133 publicly offered charter school bonds issued in 22 states, totaling over \$3 billion in par amount of bonds issued. Texas was the largest issuer, with 19 bond issues totaling over \$709 million, followed by Arizona with 26 bond issues totaling over \$556 million. California issued 21 bond issues with total par of more than \$500 million and Colorado had 16 issues with more than \$285 million. See Exhibit 4.

Issuance Volume by Rating: Of the 133 charter school bond issues, 24 (nearly \$650 million) had credit enhancement support in the form of a guaranty or moral obligation pledge from a third party, while 52 (approx. \$946 million) were non-rated. The remainder (approx. \$1.46 billion) were rated anywhere in the “BBB-” to “B” range. An unenhanced transaction² that priced at the lowest spread to MMD was one completed by Baird for **KIPP LA Schools** in August of 2015. Rated “BBB-” by Standard & Poor’s, for the 30 year final maturity, the spread to MMD was the lowest of any unenhanced charter school transaction priced from 2008 to 2015 at 129 basis points (1.29%) to the MMD, setting a new bar for the charter school sector. The transaction priced at lower spreads than other charter school issues that did not have credit enhancement support, even those transactions with a higher credit rating. In February 2016 this bar was raised once again when Great Hearts Academies came to market with a \$48.4 million “BBB-” rated financing. Baird priced the 30 year final maturity on those bonds at a 110 basis point spread to the MMD.

Exhibit 5 shows the number of transactions with credit enhancement (A or Higher) versus ratings of those transactions with no credit enhancement.

² A transaction that does not have any moral obligation or credit enhancement from a third party. As an example, the State of Texas has a Texas Permanent School Fund (“PSF”) Bond Guarantee Program which provides a permanent fund of assets that a charter school may tap if necessary to meet a debt service obligation. This guarantee provided by the PSF raises the credit rating of a charter school bond issue, typically from a low- or non-investment grade rating to AAA rating. As such, we do not include these transactions in the comparison of spread to MMD as the majority of charter school bonds are not investment grade.

EXHIBIT 4. CHARTER SCHOOL BOND ISSUANCE BY STATE 2015 TO JUNE 2016 (\$ IN MILLIONS)

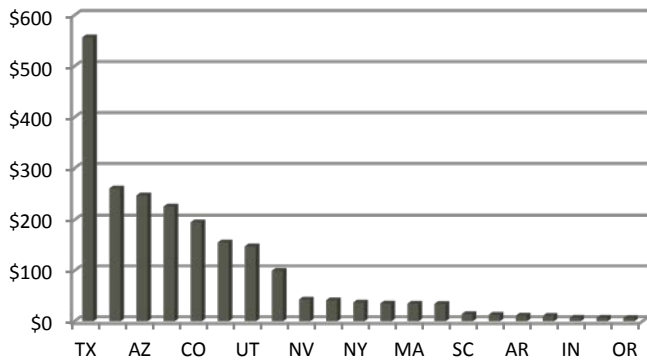
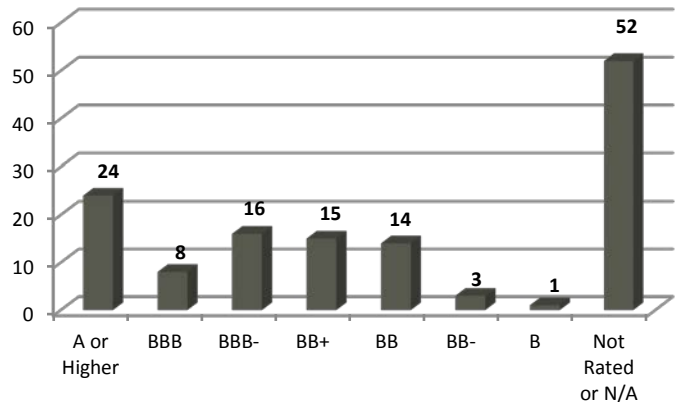



EXHIBIT 5. CHARTER SCHOOL BOND ISSUANCE BY RATING 2015 TO JUNE 2016




RECENT DEAL IN FOCUS: Uplift Education

Uplift Education (“Uplift”) is a client of Baird’s charter school team, having worked with our team members since 2007 and completing more than seven bond financings totaling over \$320 million. The latest successful transaction completed by Baird for Uplift was a \$42.98 million refunding and new money financing, sold on June 22, 2016. The Series 2016 bonds were issued to refinance \$8.735 million of Series 2007 bonds and to fund approximately \$33.7 million for improvements at Uplift’s existing educational facilities. The refinancing provided over \$1.592 million of total interest cost savings to Uplift, enabling more dollars to be spent in the classroom rather than paying interest cost. **This financing secured the lowest interest rate of any non-PSF guaranteed financing completed to date in Texas.**



Uplift Education

Dallas/Fort Worth Metro Area, Texas



\$42,980,000
 \$42,600,000 Education Revenue Bonds, Series 2016A
 \$380,000 Taxable Education Revenue Bonds, Taxable Series 2016B

June 2016

Baird served as **Sole Managing Underwriter**

Uplift Education




Mission: To create and sustain schools of excellence that empower students to reach their highest potential in college and the global marketplace and that inspire in students a life-long love of learning, achievement, and service in order to positively change their world. Each school provides free college preparatory education in a community that has limited high quality public education options. Our goal is to completely close the achievement gap between students, regardless of their ethnic or socio-economic background, while ensuring that 100% of our students graduate and enroll in college.

Financing Need:


- Finance and refinance the acquisition, improvement, construction and equipping of certain educational facilities
- Refund the outstanding Series 2007A bonds

Financing Results:

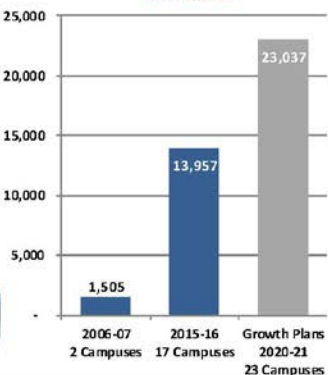
- Bond Rating of “BBB-” by S&P
- 35-year fixed rate financing
- Secured a TIC of 3.98% and 12.1% Present Value Savings on the refunding

Financing Purpose



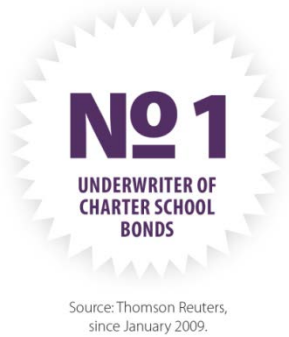
Enrollment



For additional information about this offering, please contact:

<p>Brian Colon Managing Director 303.270.6335 bcolon@rwbaird.com</p>	<p>Stacey Leigh Vice President 303.270.6338 sleigh@rwbaird.com</p>
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National Charter School Finance Group
 210 University Blvd, #460
 Denver, CO 80206
 303.270.6330
www.rwbaird.com/charterschools



ABOUT BAIRD:

Baird’s National Charter School Finance Group is the #1 ranked underwriter of charter school bonds since 2009 (Source: Thomson Financial, January 2009 – December 2015). In addition, Baird is the #1 ranked underwriter of charter school bonds since 2015 to date. Since 2003, members of the Baird Charter School Finance Group have completed over 140 charter school financings totalling over \$2.6 billion nationally. We have been in the forefront of providing innovative financing structures to charter schools utilizing tax-exempt bonds, New Markets Tax Credits, interim loans, Qualified Zone Academy Bonds and a combination of methods to finance construction, land purchase, renovations and other capital projects. We work with charter schools of all kinds, ranging from large and growing networks/CMO’s to single, stand-alone charters that are relatively early in their development cycles.

Baird’s National Charter School Finance Group has the knowledge and expertise to effectively address the challenges that are unique to charter schools during different cycles of their development and implement structures that provide maximum flexibility for future borrowings. A sample of recent charter school financings completed by Baird is below.

 <p>Arlington Higher Education Finance Corporation (Texas) (Uplift Education)</p> <p>\$42,600,000 Education Revenue Bonds, Series 2016A and Series 2016B (Taxable)</p> <p>S&P: BBB- June 2016</p>	 <p>The Delaware Economic Development Authority (Newark Charter School)</p> <p>\$12,240,000 Revenue Refunding Bonds Series of 2016A and Series of 2016B (Federally Taxable)</p> <p>S&P: BBB May 2016</p>	 <p>Philadelphia Authority for Industrial Development (KIPP Philadelphia Charter School)</p> <p>\$15,795,000 Revenue Bonds, Series of 2016A and Series of 2016B (Taxable)</p> <p>S&P: BB+ April 2016</p>	 <p>California Municipal Finance Authority (Palmdale Aerospace Academy)</p> <p>\$45,660,000 Charter School Revenue Bonds Series 2016A and Series 2016B (Federally Taxable)</p> <p>S&P: BB February 2016</p>	 <p>District of Columbia (Friendship Public Charter School)</p> <p>\$57,895,000 Revenue Bonds Series 2016A</p> <p>S&P: BBB March 2016</p>
 <p>Utah Charter School Finance Authority (Karl G. Maeser Preparatory Academies)</p> <p>\$12,450,000 Charter School Revenue Bonds Series 2016A and Series 2016B (Federally Taxable)</p> <p>S&P: BBB- February 2016</p>	 <p>The Industrial Development Authority of the City of Phoenix, AZ (Great Hearts Academies)</p> <p>\$48,465,000 Educational Facilities Revenue Bonds Series 2016A and Taxable Series 2016B</p> <p>S&P: BBB- February 2016</p>	 <p>Clifton Higher Education Finance Corporation (Texas) (IDEA Public Schools)</p> <p>\$70,885,000 Education Revenue Bonds Series 2015</p> <p>S&P: AAA (PSF)/BBB September 2015</p>	 <p>California School Finance Authority (Green Dot Public Schools)</p> <p>\$31,105,000 School Facility Revenue Bonds, Series 2015A (Tax-Exempt) and Series 2015B (Taxable)</p> <p>S&P: BBB- September 2015</p>	 <p>California School Finance Authority (KIPP LA Schools)</p> <p>\$27,790,000 School Facility Revenue Bonds, Series 2015A and Series 2015B (Taxable)</p> <p>S&P: BBB- August 2015</p>

SOURCES: Thomson Municipal Market Data Interactive; The Bond Buyer; Investment Company Institute Website; U.S. Department of Treasury; Bureau of Labor Statistics.

IMPORTANT DISCLOSURES

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