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Front Porch Communities and Services
California Statewide Communities Development Authority; Long Term Care

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Credit Profile		
US$196.3 mil rev bnds (Front Porch Communities and Services) ser 2021A due 04/01/2052		
Long Term Rating	A-/Stable	New
US$106.6 mil rev bnds (federally taxable) (Front Porch Communities and Services) ser 2021B due 04/01/2037		
Long Term Rating	A-/Stable	New
California Statewide Communities Dev Auth, California		
Front Porch Communities and Services, California		
California Statewide Comntys Dev Auth (Front Porch)		
Long Term Rating	A-/Stable	Outlook Revised

Rating Action

S&P Global Ratings revised its outlook to stable from negative and affirmed its 'A-' rating on California Statewide Communities Development Authority's series 2017A revenue bonds, issued on behalf of Front Porch Communities and Services (Front Porch). At the same time, S&P Global Ratings assigned its 'A-' rating to the California Statewide Communities Development Authority's approximately $196.3 million series 2021A tax exempt and $106.6 million series 2021B taxable bonds issued on behalf of Front Porch.

On April 1, 2021, Front Porch and Covia Communities officially affiliated. The series 2021 bond proceeds will be used to refinance existing Covia debt and Front Porch's HUD insured debt under one obligated group. A portion of the proceeds ($10 million) will go toward capital needs starting in fiscal 2023. Post issuance, Front Porch will have a streamlined debt profile with all debt under one obligated group (series 2021 and 2017 bonds will be outstanding post financing). In addition, refinancing of HUD-insured loans will eliminate compliance and reporting requirements.

The bonds are secured by gross revenues of the new obligated group.

Credit overview

The revised outlook is supported by our view that Front Porch's recent acquisition of Covia Communities (Covia) (effective April 1, 2021) has bolstered Front Porch's enterprise profile and expanded Front Porch's geographic reach, especially in Northern California. The affiliation also increases access to financial capital to support the modernization of Front Porch's facilities. Front Porch is now one of the largest not-for-profit senior living providers in the United States with 16 life plan communities, two active adult communities, and 34 affordable housing communities.

Additionally, while the acquisition is slightly dilutive to Front Porch's financial profile, we believe its ample liquidity, improved pro forma debt profile, and accretive influence of the acquisition on key balance sheet and debt metrics, provides Front Porch cushion to withstand near-term dilution.

Management attributes fiscal 2021 operating losses to the effect of COVID-19 on occupancy and demand. Operating losses have narrowed through the first quarter of fiscal 2022; however, we expect ebbs and flows in the resurgence of COVID-19 cases will likely affect occupancy and sales in the near to medium term. Nonetheless, management has indicated that occupancy and sales are trending positively, and they expect to end the year (fiscal 2022) ahead of budget with operations closer to breakeven. While we believe this is a reasonable target and supported by positive operating performance through June, we believe this will largely be dependent on a continued rebound in occupancy and execution of key savings initiatives.

On July 20, 2021, the board approved the consolidation and merger of Covia Foundation and Bethany Center Foundation into Front Porch Communities Foundation (this merger is expected end of 2021, following receipt of regulatory approval). Immediately following the series 2021 debt issuance, Covia will become a member of the obligated group, and following the refinancing of the HUD-insured loans, related Real Estate LLCs will be merged into the corporation. In November 2021, the organizations that own and operate the affordable housing communities, CARING Housing Ministries, Sunny View Lutheran Home and Covia Affordable Communities, will be consolidated into a single entity. Subsequently, Covia, plans to dissolve and its funds are expected to be transferred to Front Porch. Covia is expected to merge into the corporation by the end of 2021, which will result in there being a single obligated group member, the corporation.

The rating is also based on our assessment of Front Porch's:

- Expanded geographic reach and significant revenue diversity, including a wide range of geographic, pricing and service options;
- Effective and experienced management team that has demonstrated a willingness and ability to respond proactively to changing business conditions; and
- Improved pro forma debt profile, including improved leverage.

Partially offsetting credit factors include our view of Front Porch's:

- Softening demand, with occupancy rates that may not return to pre-pandemic levels until the end of fiscals 2022-2023;
- Continued execution and integration risk as Front Porch works through the recent acquisition of Covia; and
- Ongoing operating losses through the first quarter of fiscal 2022.

Other credit factors influencing the rating include a continued shift in the Care Center payor mix to more Medicaid-managed care and less private pay, which is driving lower average reimbursement rates; and management's willingness to review nonperforming assets and, if needed, exit a particular market, as it has demonstrated several times during the past decade.

Environmental, social and governance factors

The core mission of senior living communities like Front Porch is protecting the health and safety of its residents, which is further evidenced by its responsibilities as a continuing care retirement center (CCRC), as residents not only occupy a home, but receive additional services and care as they move through different stages of the continuum. While we note the temporary softening of demand due to the pandemic, for Front Porch, we deem those social risks to be in line with the sector. Furthermore, while we view Front Porch's governance risk as in line with the sector, we believe the recent acquisition underscores positive governance as we believe the affiliation with Covia will be beneficial from a size and scale perspective. Lastly, we view Front Porch's overall environmental risk as elevated relative to those of industry peers, given its location in markets that are historically prone to earthquakes and wildfires, particularly in recent years. This risk is somewhat mitigated as Front Porch has multiple transfer agreements with local skilled nursing facilities (SNFs) and hotels that can accommodate residents in the event of a wildfire. Deregulation of the electrical and natural gas industry in California as well as changes in the supply and sale of electricity and natural gas has resulted in increased costs of energy which could affect operations going forward.

Stable Outlook

Downside scenario

We would consider any material shifts in occupancy, operating results, or a significant decline in liquidity, credit risks that could result in a negative outlook or lower rating. In addition, we would consider a lower rating if the pandemic's financial and economic repercussions are too significant to absorb at the current rating level or if financial metrics in the outlook period are no longer appropriate for the rating. Lastly, we would view any negative pressure related to the acquisition unfavorably.

Upside scenario

It is unlikely that we would consider a positive outlook or higher rating within the two-year outlook horizon due in part to pandemic-related challenges and recent operating losses. We would consider a positive rating action in the longer term, if there are sustained gains in occupancy rates coupled with improved operating performance and maintenance of current balance sheet metrics. Lastly, we believe a positive rating action in the outlook period is unlikely due to inherent risks associated with the recent acquisition.

Credit Opinion

Enterprise Profile

We consider Front Porch's diverse portfolio of facilities a fundamental credit strength, with now sixteen life plan communities, two active adult communities and thirty five affordable housing communities, offering a wide variety of contract options, prices, and locations that provide a good hedge, in our view, against fluctuations in any one local market or service type. Most of Front Porch's obligated group communities are in California, except for England Oaks (Louisiana) and Cecil Pines (Florida).

Market position remains a credit strength further strengthened by Covia acquisition; although, occupancy and demand continue to be impacted by the COVID-19 pandemic

Front Porch currently operates 16 life plan communities; 34 affordable housing communities; 3,186 residential living and memory care units or RLUs, (independent and assisted living units as reported by Front Porch; ILU and ALU, respectively). Depending upon the community, Front Porch offers residents two different fee structures: month to month payments or entrance fees, with some communities offering both options. Ten of Front Porch's facilities are entrance fee continuing care retirement communities (CCRCs), while the others are rental multilevel retirement communities. Front Porch offers four basic entrance fee contracts and Covia Communities offers two basic types of entrance fee contracts. Prior to the acquisition, Front Porch's revenue mix was weighted more heavily toward rental revenue at 72% of total consolidated revenue as of fiscal year 2021, making it less reliant on entrance fees. However, post-acquisition, entrance fee as a percentage of residential and assisted living revenue has increased to 49% (from 28%).

Demand has historically been steady for Front Porch; however, like many senior living communities, the COVID-19 pandemic has depressed occupancy rates across all levels of service, starting in late fiscal 2020 and through 2021. Rental communities (88% occupancy across communities) and skilled nursing facilities (72% across communities) have been hit the hardest as management has been unable to show and fill open units due to the ebbs and flows in the resurgence of COVID-19 cases and as Front Porch relies on acute care referrals for skilled nursing facility (SNF) occupancy.

Front Porch communities with RLU occupancy below 90% are Claremont Manor at 81%, Fredericka Manor at 79%, Vista Del Monte at 88%, and Wesley Palms at 71%. In addition to the influence of COVID-19, the decline in occupancy at Fredericka Manor was driven by increased competition that is coming on board in the immediate area, and the decline in occupancy at Wesley Palms was expected, given the ongoing phased repositioning project. Also, while the Wesley Palms redevelopment project was completed on time and on budget; COVID-19 hindered management's ability to fill units as originally expected. Four of Covia's communities have RLU occupancy below 90%: Canterbury Woods (85%), El Sombroso Oaks (82%), Friends House (80%), and Spring Lake Village (89%). Front Porch's largest market is the La Jolla-San Diego region, with other key markets including Anaheim, Claremont, Pasadena, Cupertino, and Santa Barbara, Calif., and now other cities in Northern California. We expect occupancy will rebound to near historical levels by the end of fiscal 2022.

Consolidated management team and governance

Front Porch and Covia facilities are managed by a single management team. John Woodward, chief executive officer (CEO) since 2015, has responsibility for oversight of Front Porch including governance and board management, strategic facilitation, development and implementation, new business development, regulatory compliance, management oversight of affiliates and relationships with philanthropic organizations. Mr. Woodward's career includes over 35 years of investment banking and consulting experience assisting a wide range of not-for-profit and healthcare organizations. Eduardo Salvador joined Front Porch in 2017 as chief financial officer (CFO). Prior to joining Front Porch, Mr. Salvador served as CFO for St. Jude Medical Center for almost 10 years and as well as CFO for Tenet Healthcare and Vanguard Healthcare. According to management, there are a few positions open (due to various retirements), which allowed for rapid consolidation of the management team.

The new board comprises board members from both Front Porch (9 members) and Covia (6 members). All board members have an initial two-year term before beginning a three-year rotation.

Front Porch and its communities have been supported by four philanthropic partner organizations (three of which were consolidated into a single entity on April 1, 2021). In the past 10 years, philanthropic contributions have totaled in excess of $42 million.

Organizational changes expected by Dec. 31, 2021, following acquisition of Covia

Front Porch and Covia officially affiliated on April 1, 2021, creating a combined organization with 54 communities across four states. According to management, the impetus behind the acquisition was to achieve greater scale and expand their presence in Northern California. In addition, management anticipates the consolidation of the two organizations will bring favorable economies of scale and operational efficiencies.

Effective upon affiliation, Front Porch became the sole corporate member of Covia. Both communities maintained separate operations and debt structures; however, upon completion of the series 2021 debt issuance, Covia will also become a member of the obligated group.

On July 20, 2021, the board approved the consolidation and merger of Covia Foundation and Bethany Center Foundation into Front Porch Communities Foundation (merger expected end of 2021, following receipt of regulatory approval). Immediately following the series 2021 debt issuance, Covia will become a member of the obligated group, and following the refinancing of the HUD-insured loans, related Real Estate LLCs will be merged into the corporation. In November 2021, the organizations that own and operate the affordable housing communities, CARING Housing Ministries, Sunny View Lutheran Home and Covia Affordable Communities, will be consolidated into a single entity. Subsequently, Covia, plans to dissolve and its funds are expected to be transferred to Front Porch. Covia is expected to merge into the corporation by the end of 2021, which will result in there being a single obligated group member, the corporation.

Financial Profile

S&P Global Ratings' credit analysis and the numbers reported in this article, unless otherwise indicated, pertain to the consolidated system. The unaudited financial information was prepared by Front Porch management and combines the audited consolidated financial statements of Front Porch Communities and Services and audited consolidated financial statements for Covia for fiscal years 2019-2021.

Operating losses in fiscal 2021 and through the first quarter of fiscal 2022

In our view, the ongoing strength in demand at Front Porch's facilities and management's commitment to closely matching revenue and operating costs resulted in continued positive financial performance through fiscal 2020. Leadership attributes better than anticipated fiscal 2020 financial performance to various one-time benefits as well as ongoing expense management, with a particular focus on labor and supply costs. According to management, Front Porch received higher-than-expected developer fees from CARING Housing Ministries, as they manage 26 of Front Porch's affordable housing units (received $963,000 in fiscal 2020) and also received a favorable work compensation adjustment of around $3.3 million in fiscal 2020 and $1.2 million through Dec. 31, 2020. Management benefitted from another year of very strong non-operating revenue, driven in part by positive investment income and realized gains, (excluding unrealized gains on investments and derivative instruments) (contributed to ample fiscal 2020 adjusted MADS coverage in our view). Because some of Front Porch's communities are rental properties and not entry-fee CCRCs, the organization is not as reliant on cash flow from entry fees as other industry counterparts.

Operations declined materially in fiscal 2021 with Front Porch posting a year-end operating loss (negative 3% operating margin on a consolidated basis) driven by the effect of COVID-19 on occupancy across all communities, revenue, and labor. Management has budgeted around a negative 3% operating margin for fiscal 2022 but expect to exceed budget closer to breakeven operations. We view this as reasonable given recent performance trends; however, this will largely hinge on a continued rebound in occupancy, execution of various savings and revenue initiatives, and ongoing performance improvement. In addition, given Front Porch's stronger balance sheet metrics, particularly liquidity, we believe Front Porch has flexibility at the current rating level to absorb a near-term contraction in operations.

Ample and growing liquidity provides cushion to withstand near-term dilution

After several years of healthy operating performance and cash flow, coupled with favorable investment market returns and gains from the sale of assets, some of Front Porch's key metrics steadily improved, particularly unrestricted reserve levels.

Unrestricted reserves grew to almost $640 million (on a consolidated basis) as of June 30, 2021 and is expected to remain at this level in the outlook period. Unrestricted reserves to debt, which we consider a little light for the rating, has modestly improved as well. According to management, the material improvement in unrestricted reserves from fiscal 2020 to fiscal 2021 is attributed to favorable investment market performance.

Ongoing capital and repositioning projects

Management used series 2015 and 2017B bond proceeds to support the redevelopment of Front Porch's Wesley Palms campus in San Diego. Wesley Palms now includes 121 independent living units in the main building, 170 patio homes for independent living, and 22 Summer House units. Construction was carefully phased to allow current residents to remain in the community during construction. Construction through all phases and in all common areas was completed on time and on budget. Because the project followed a phased approach, occupancy levels filled up accordingly on a staggered basis so that the memory care unit and patio homes completed in earlier phases had reached over 90% occupancy; although, due to the pandemic, occupancy in later phases is below 90% because management has not been able to show and fill new units despite having a steady waitlist.

For fiscal 2022, management has budgeted approximately $62 million for routine capital spending with major investments at the Walnut Village ($10 million), Sunny View ($5 million), Fredericka Manor ($7.5 million), Spring Lake Village ($7.1 million) and San Francisco Towers ($4.7 million).

Series 2021 debt issuance will result in a streamlined debt structure and improved pro forma leverage

The impetus behind the series 2021 debt issuance is to streamline the debt profile under one obligated group, capture savings, and lock in long-term committed capital. Following the completion of the series 2021 debt issuance, Front Porch will have zero contingent liability exposure as defined in our criteria, thereby de-risking this attribute of the credit profile. In addition, proforma leverage will improve as only Front Porch's series 2021 and 2017 bonds will be outstanding post financing. Tax exempt proceeds will be used to refinance approximately $130 million of Covia fixed rate series 2011, 2012A, portion of series 2012B, and series 2015 JPM direct placement debt. Taxable proceeds will be used to refinance approximately $88.3 million in Front Porch HUD debt, $3.5 million of Covia series 2012B debt, and a $11.2 million Covia note payable. In addition, $10 million in proceeds will be used to finance various capital and renovation projects. Lastly, with the series 2021 debt issuance, Front Porch plans to amend and restate the original master indenture.

In accordance with the current legal documents, Front Porch must maintain certain financial covenants on its debt obligations--including maintaining a debt service coverage ratio of at least 1.20x . Failure to observe, perform, or comply with the covenants, unless corrective action has been commenced and diligently pursued within the applicable grace period of 30 days, could result in an event of default. However, Front Porch is currently in excess of the covenant levels, and we do not anticipate any covenant violation in the near term.

Front Porch Communities And Services And Affiliates: Selected Financial Statistics

	--Three month interim ended June 30--	--Fiscal year ended March 31--		
Financial performance	**2021**	**2021**	**2020**	**2019**
Total operating revenue ($000s)	94,850	360,668	373,927	374,698
Total operating expenses ($000s)	93,592	372,877	373,977	397,450
Operating income ($000s)	1,258	(12,209)	(50)	(22,752)
Operating margin (%)	1.3	(3.4)	(0.0)	(6.1)
Net nonoperating income ($000s)	33,940	45,009	14,309	18,574
Excess income ($000s)	35,198	32,800	14,259	(4,178)
Excess margin (%)	27.3	8.1	3.7	(1.1)
Net entrance fees and deposits received ($000s)	15,409	16,962	36,952	39,650
Net available for debt service ($000s)	46,626	78,279	57,844	41,256
Adjusted net revenue available for debt service ($000s)	62,035	95,241	94,796	80,906
Maximum annual debt service ($000s)	23,190	23,190	23,190	23,190
Adjusted MADS coverage (x)	10.7	4.1	4.1	3.5
Revenue only coverage (x)	8.0	3.4	2.5	1.8
Liquidity and financial flexibility				
Unrestricted reserves ($000s)	640,031	595,583	446,270	500,573
Unrestricted days' cash on hand	758.9	698.9	515.7	539.0
Unrestricted reserves/long-term debt (%)	136.8	127.8	92.3	103.5
Unrestricted reserves/contingent liabilities (%)	582.6	542.1	415.8	492.2
Average age of plant (years)	12.8	13.5	13.4	12.5
Capital expenditures/depreciation and amortization (%)	N.A.	74.7	108.5	119.8
Debt and liabilities				
Long-term debt ($000s)	467,784	466,170	483,398	483,734
Long-term debt/capitalization (%)	47.0	49.4	62.8	58.4
Contingent liabilities ($000s)	109,857	109,857	107,327	101,700
Contingent liabilities/long-term debt (%)	23.5	23.6	22.2	21.0
Debt burden (%)	6.2	6.2	6.2	6.2
Pension Funded Status (%)	N.A.	97.7	69.1	86.8
Deferred revenue from EF				

Front Porch Communities And Services And Affiliates: Selected Financial Statistics (cont.)

	--Three month interim ended June 30--	--Fiscal year ended March 31--		
Financial performance	**2021**	**2021**	**2020**	**2019**
Pro forma ratios				
Pro forma unrestricted reserves ($000s)	640,031	595,583	N/A	N/A
Pro forma long-term debt ($000s)	462,411	460,797	N/A	N/A
Pro forma unrestricted days' cash on hand	758.9	698.9	N/A	N/A
Pro forma unrestricted reserves/pro forma debt (%)	138.4	129.3	N/A	N/A
Pro forma debt/capitalization (%)	46.7	49.1	N/A	N/A
Pro forma adjusted debt/capitalization (%)	34.7	36.2	N/A	N/A
Proforma contingent liabilites	0			
Utilization				
# of ILU/ALU Units	3,301	3,228	3,228	3,366
# of Memory Care Units	166	159	153	145
# of SNF Units	674	716	816	855
ILU/ALU occupancy rate (%)	88.0	90.0	91.0	93.0
Memory Care occupancy rate (%)	89.0	88.0	91.0	88.0
SNF occupancy rate (%)	72.0	71.0	83.0	86.0

N/A--Not applicable. N.A.--Not available. MNR--Median not reported. * Please note, this unaudited financial information was prepared by Front Porch management and combines the audited consolidated financial statements of Front Porch Communities and Services and audited consolidated financial statements for Covia Group for the fiscal years FY 2019, 2020 and 2021.

Credit Profile

- Security: The bonds are secured by gross revenues of the new obligated group.
- Group rating methodology: Core.
- Credit Overview: Front Porch Communities and Services is a California nonprofit public benefit corporation that provides housing and services to residents of its senior living and active adult communities and that develops, owns, and manages affordable housing for seniors. As a result of the acquisition of Covia and its related entities, Front Porch is now one of the largest not for profit senior living providers in the United States and operates sixteen multi-level senior living and three active adult monthly rental communities containing 3,313 independent living and assisted living residential units, 166 memory support units, and 671 skilled nursing beds. All of the obligated group communities are located in California, except for two active adult communities in Louisiana (England Oaks) and Florida (Cecil Pines) as well as one affordable housing community in Arizona. Ten of the communities are CCRCs and six of the multi-level communities are monthly rental communities. Front Porch, through its subsidiaries, also develops, owns and manages 34 affordable housing communities. The corporation is the only member of the obligated group and upon issuance of the series 2021 bonds, Covia will also become a member of the obligated group.

Related Research

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