S&P Global Ratings

Research

Delaware County Authority, Pennsylvania Villanova University; Private Coll/Univ - General Obligation

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Villanova Univ ICR		
Long Term Rating	AA-/Stable	Upgraded
Delaware Cnty Auth, Pennsylvania		
Villanova Univ, Pennsylvania		
Delaware Cnty Auth (Villanova University) 2010		
Long Term Rating	AA-/Stable	Upgraded

Rationale

S&P Global Ratings raised its long term rating and issuer credit rating on Delaware County Authority, Pa.'s bonds issued for Villanova University to 'AA-' from 'A+'. The outlook is stable.

The higher rating reflects the university's improvement of various demand metrics including selectivity and matriculation to levels comparable with peers along with the continued robust operating surpluses and successful fundraising which have improved financial resources over time. The endowment remains lower than similarly rated peers but we expect continued momentum from fundraising and operating surpluses to continue to prompt growth. The university also has no plans for additional debt at this time.

We assessed Villanova's enterprise profile as very strong with growing enrollment, high retention, increased applications, and improved selectivity and matriculation. We assessed Villanova's financial profile as very strong, with a history of robust operating surpluses, growing financial resources, and moderate maximum annual debt service (MADS) burden. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'aa-' and a final rating of 'AA-'.

The rating reflects our view of the university's following strengths:

- Solid enrollment and demand as evidenced by incremental growth in enrollment, increasing applications, and ongoing high retention with good student quality;
- Very healthy financial operations with consistently good operating surpluses on a full-accrual basis as a result of sound fiscal discipline and budgeting practices;
- Improving available resources relative to operations and debt for fiscal 2018, particularly with cash and investments that are in line with similarly rated peers; and
- Average maximum annual debt service (MADS) burden of 4.5% with a predictable, conservative, front-loaded fixed-rate debt structure.

The rating also reflects our view of the university's following weaknesses:

- Limited revenue diversity, with more than 84% of gross revenues in fiscal 2018 coming from student-generated revenues (tuition, fees, and auxiliaries); and
- Lower endowment per full-time equivalent (FTE) compared with similarly rated peers.

All bonds are secured by a general obligation of the university.

Villanova University is an independent, coeducational institution in Radnor Township, about 14 miles west of Philadelphia. Founded in 1842 by the Augustinian Order of the Roman Catholic Church, the well-maintained 260-acre campus encompasses 75 buildings on Philadelphia's affluent Main Line. Villanova offers a comprehensive array of undergraduate, graduate, and professional degrees, including law, business, engineering, and nursing.

Outlook

The stable outlook reflects the university's healthy operating margins, adequate financial resources which we expect to grow, and solid enrollment and demand profile. We do not expect additional debt without commensurate growth in resources.

Downside scenario

We would consider a negative rating action if financial resource ratios declined or if operations weakened significantly. We would also view a weakening of the demand profile, or additional debt issuance without proportionate growth in resources negatively.

Upside scenario

We would consider a higher rating in the next two years if financial resource ratios grew to levels consistent with 'AA' rating medians and 'AA' peers, margins remained solid and enrollment and demand metrics such as selectivity and matriculation continued to remain consistent with medians.

Enterprise Profile

Industry risk

Industry risk addresses the higher education 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 higher education sector represents a low credit risk when compared with other industries and sectors.

Economic fundamentals

In our view, the university has good geographic diversity, with only 34.9% of students coming from Pennsylvania. While we believe the draw is national, there is still a concentration in the Northeast, although not for a particular state, therefore, Villanova's economic fundamentals are still anchored by the U.S. GDP per capita.

Market position and demand

Overall enrollment continues to improve incrementally with FTEs growing 0.8% to 10,062 in fall 2017 from the prior year. Undergraduate enrollment remains the largest component of overall enrollment, while graduate enrollment, including the law school, accounts for about 34%. Graduate enrollments declined slightly from the prior year although the law school saw a robust increase to 796 students, up from 550 in prior years. In our opinion, the university continues to benefit from a steady enrollment base.

Applications continued to experience solid growth of 7.7% in fall 2018 to 22,731. The university cites the addition of the early decision option in fall 2018 along with the university's classification as a Doctoral University by the Carnegie Foundation as main contributors to the growth. As a result of the increase in applications, selectively improved to 29% in fall 2018 from 36% and 44% in fall 2017 and fall 2016, respectively, which we view positively. The university expects to continue to benefit from the early decision option in fall 2019, although management's goal is not to enroll the majority of students during the early decision process but rather to diversify its options. Matriculation remains very competitive given the market, but the university has seen a nice improvement to 25% from 21%-22% in prior years. In our opinion, demand factors have improved nicely and are now comparable to some 'AA-' peers. In addition, management notes that the senior housing dorms which were debt and equity financed and the performing arts building, which was completely fundraised will be coming online in fall 2019 and winter 2020, respectively. The new dorms will allow the university to house over 85% of its undergraduates, which management believes will enhance the student life experience. In our opinion, these projects along with enhancements made to the basketball facilities may contribute to the continual success in the enrollment and demand profile.

Student quality remains solid with an average incoming freshmen SAT scores of 1,375 for fall 2018, well above the national SAT average of 1012. The retention rate remains about 96%, which is consistent with 'AA' rating medians. The six-year graduation rate is also slightly improved at 91% for fall 2018, up from 90% in prior years. According to management, Villanova has expanded its peer group slightly after the national doctoral university designation and includes universities such as Northeastern University, American University, Texas Christian University, Washington University in Saint Louis and Southern Methodist University in addition to the historical peer group which included Lehigh University, Boston College, and Wake Forest University. In our view, student quality and graduation metrics are consistent with other 'AA-' peers.

Villanova's most recent campaign ended on May 31, 2018, and the university successfully raised $760 million, $160 over its initial $600 million goal, which we view positively. Over $320 million was raised for endowment, while $180 million was raised for capital and other academic purposes along with $80 million for the annual fund. Management notes that $490 million has been received in cash and $270 remains outstanding in pledges. Alumni participation is high at 30%. We believe that the university will continue the momentum of successful fundraising into the next campaign which will likely be more focused on financial aid and scholarships.

Management and governance

The management team has been quite stable in the past five years. The president and the finance team have been in place for over 10 years. There were minimal changes to senior management although there is currently a national search for a chief security officer. A new chief internal auditor who oversees the internal audit and information technology controls function was hired in January 2018 as the university continues to enhance its enterprise risk management. A new general counsel and dean of continuing studies were promoted from within along with a new dean of nursing and interim dean of engineering. The 32-member board of trustees governing the university has been stable, with only rotational changes. We view the stability of the management team as a strength.

The university operates under the direction of a strategic plan. According to management, key goals under the old strategic plan have already been met and viewed as a success; therefore, the university is currently in the process of developing a new strategic plan for 2020 and onwards that will continue to highlight Villanova's value proposition and focus on raising the status of the university at the national level.

We consider the university's financial management policies and practices to be conservative and on par with best practices, including budgeting on a full-accrual basis, producing multiyear projections, and contingencies to produce positive surpluses each year. Management allocates a portion of surpluses into cash reserves and the quasi-endowment annually, which we view positively. The university has investment and debt policies, which we also view favorably.

Financial Profile

Financial management policies

The college has formal policies for endowment, investments, and debt. It operates according to a 10-year strategic plan and has a formal reserve liquidity policy. It also 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 weaken its future 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 comparable organizations.

Financial performance

Villanova's financial profile remains very solid, with a continued operating margin of 8% in fiscal 2018. Management is expecting similar results for fiscal 2019. While we believe the university may allocate additional resources to various areas under the new strategic plan, management emphasizes that it will continue to budget for at least a 4% margin every year, including depreciation, which we view as a best practice. We believe that the university's consistent operating surpluses are a key credit strength.

As with most private universities of its size, Villanova is highly dependent on student-generated fees; tuition, fees and auxiliary revenue generated 84% of fiscal 20187 adjusted revenue. Tuition (including room and board) was in line with peer institutions, although plans to increase the discount rate slowly over time to improve the academic profile of the university and attract high-quality students are still underway. Management has already built in the increasing financial aid, but budgeted margins are expected to remain about 4%. Management also notes that a key aspect of the next strategic plan and future fundraising goals will be around financial aid and student scholarships so that there will be less reliance on the operating budget to meet that need, which we view positively.

Financial resources

Expendable resources relative to operating expenses have declined slightly to 114.6% from 124% in fiscal 2017 mainly due to some slight deflation as a result of an increase in net property, plant and equipment and decrease in long term debt as per the calculation. However, cash and investments relative to operating expenses and debt have grown to 173.8% and 372.4%, respectively, which is comparable with other 'AA-' peers. Expendable resources relative to debt have rebounded nicely to 245.5% in fiscal 2018. Because of the university's policy of investing approximately 50% of its annual operating surplus back into the endowment, we expect financial resources will continue to grow over the next few years.

The endowment, which had a market value of approximately $711 million as of May 31, 2018, reflects a diverse allocation of assets: 51% equities (domestic and global), 18% private investments, 22% diversifying assets, 5% bonds, and 4% cash. The portfolio remains highly liquid with 30% of the portfolio available on a daily basis, 63% on a monthly basis, and 78% on an annual basis. The endowment spending policy remains 5%, based on a three-year rolling-average market value, which we believe is sustainable.

Debt and contingent liabilities

As of May 31, 2018, the university had $258 million of debt outstanding. The university has no contingent liability risk exposures from financial instruments with payment provisions that change on the occurrence of certain events. MADS of approximately $25 million was equal to what we consider a moderate 4.5% of fiscal 2018 operating expenses. The projects associated with the series 2015 bonds are on time and on budget, according to management. We do not anticipate the university will issue additional debt in the near term as capital projects such as construction of the performing arts center, and basketball pavilion renovations have been completely donor funded.

Villanova University, Pennsylvania Enterprise And Financial Statistics

	--Fiscal year ended May 31--					Medians for 'AA' rated private colleges and universities
	2019	**2018**	**2017**	**2016**	**2015**	**2017**
Enrollment and demand						
Headcount	11,023	10,983	10,842	10,728	10,544	MNR
Full-time equivalent	10,204	10,127	9,942	9,827	9,677	6,335
Freshman acceptance rate (%)	29.2	36.0	43.5	47.9	49.3	25.3
Freshman matriculation rate (%)	25.4	22.5	22.3	21.9	21.6	MNR
Undergraduates as a % of total enrollment (%)	61.6	63.4	64.6	65.2	65.7	71.0
Freshman retention (%)	96.1	94.7	94.8	95.8	93.7	94.5
Graduation rates (six years) (%)	91.0	90.1	90.4	90.5	89.7	MNR
Income statement						
Adjusted operating revenue ($000s)	N.A.	596,934	558,201	532,133	508,657	MNR
Adjusted operating expense ($000s)	N.A.	552,694	513,360	496,968	484,185	MNR
Net operating income ($000s)	N.A.	44,240	44,841	35,165	24,472	MNR
Net operating margin (%)	N.A.	8.00	8.73	7.08	5.05	2.02

Villanova University, Pennsylvania Enterprise And Financial Statistics (cont.)

	--Fiscal year ended May 31--					Medians for 'AA' rated private colleges and universities
	2019	**2018**	**2017**	**2016**	**2015**	**2017**
Change in unrestricted net assets ($000s)	N.A.	75,201	68,183	11,502	18,709	MNR
Tuition discount (%)	N.A.	29.8	29.3	29.2	28.3	38.0
Tuition dependence (%)	N.A.	72.7	73.7	73.6	74.2	MNR
Student dependence (%)	N.A.	84.2	85.4	86.1	86.9	58.9
Research dependence (%)	N.A.	1.1	1.2	1.2	1.3	MNR
Endowment and investment income dependence (%)	N.A.	5.1	4.8	4.4	3.8	MNR
Debt						
Outstanding debt ($000s)	N.A.	258,000	268,878	282,970	151,848	356,370
Total pro forma debt ($000s)	N.A.	258,000	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	4.20	4.44	3.71	3.54	MNR
Current MADS burden (%)	N.A.	4.50	4.84	5.00	3.34	4.00
Financial resource ratios						
Endowment market value ($000s)	N.A.	710,592	640,428	552,701	563,866	1,461,237
Cash and investments ($000s)	N.A.	960,718	875,326	755,826	757,344	MNR
Unrestricted net assets ($000s)	N.A.	636,506	561,305	493,122	481,620	MNR
Expendable resources ($000s)	N.A.	633,383	636,000	581,148	475,239	MNR
Cash and investments to operations (%)	N.A.	173.8	170.5	152.1	156.4	351.2
Cash and investments to debt (%)	N.A.	372.4	325.5	267.1	498.8	480.4
Cash and investments to pro forma debt (%)	N.A.	372.4	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	114.6	123.9	116.9	98.2	226.0
Expendable resources to debt (%)	N.A.	245.5	236.5	205.4	313.0	317.0
Expendable resources to pro forma debt (%)	N.A.	245.5	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	15.7	16.2	16.5	15.9	13.7

N.A.--Not available. MNR--Median not reported. MADS--Maximum annual debt service. Total adjusted operating revenue = unrestricted revenue less realized and unrealized gains/losses and financial aid. Total adjusted operating expense = unrestricted expense plus financial aid expense. Net operating margin = 100*(net adjusted operating income/adjusted operating expense). Student dependence = 100*(gross tuition revenue + auxiliary revenue) / adjusted operating revenue. Current debt service burden = 100*(current debt service expense/adjusted operating expenses). Current MADS burden = 100*(maximum annual debt service expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Expendable resources = unrestricted net assets + temp. restricted net assets - (net PPE- outstanding debt). Average age of plant = accumulated depreciation/depreciation and amortization expense.