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Case Western Reserve University, Ohio Ohio Higher Educational Facility Commission; Private Coll/Univ - General Obligation

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Table Of Contents

Rating Action

Stable Outlook

Enterprise Profile

Financial Profile

Related Research

Case Western Reserve University, Ohio Ohio Higher Educational Facility Commission; Private Coll/Univ - General Obligation

Credit Profile		
Ohio Higher Ed Fac Comm, Ohio		
Case Western Reserve Univ, Ohio		
Ohio Hgr Ed Fac Com (Case Western Reserve Univ) PCU-GO		
Long Term Rating	AA-/Stable	Affirmed

Rating Action

S&P Global Ratings affirmed its 'AA-' long-term on the Ohio Higher Educational Facility Commission's bonds issued for Case Western Reserve University (CWRU). The outlook is stable.

As of June 30, 2020, the last audit, CWRU had \$542.9 million of long-term debt outstanding. The majority of the debt is public, fixed-rate debt except the \$68.2 million series 2019A floating-rate note. On a pro-forma basis, we understand that CWRU is looking to refinance the series 2016 and a portion of the series 2013 with a \$56 million series 2021 direct-purchase arrangement. Securing the bonds is a general obligation of the college. The debt service on the bonds is paid under a lease agreement between the Ohio Higher Education Facility Commission and the university. The university had a total operating lease obligation of about \$9 million as of fiscal year-end 2020, which we view as manageable and modest relative to total debt outstanding.

Because of the COVID-19 pandemic, CWRU transitioned to virtual instruction for the second half of the spring 2020 semester. Management gave housing and board refunds to its students while they worked quickly to contain costs to offset the loss in revenue. The university's operations improved in fiscal 2020, despite the COVID-19 crisis. CWRU received \$4.4 million in CARES Act Funding in fiscal 2020; half of that amount was a pass-through for student emergency aid. The remaining funds helped offset the housing and dining refunds given in fiscal 2020. The university received another \$3.1 million of CARES Act funding (through Ohio) in fiscal 2021. Auxiliary revenue, which made up about 6% of adjusted operating revenue in fiscal 2019, decreased to 5% in fiscal 2020 given the refunds. To partially offset the loss in COVID-19-related revenue and increases in expenses, the university was able to make expense reductions, including suspension of retirement contributions, salary and hiring freezes, voluntary salary reductions, postponement of some capital projects, and travel restrictions. In addition, the management team added in a contingency to the budget given the ongoing uncertainty related to the pandemic.

For fall 2020, the university operated with a hybrid model with courses being offered in person, fully online, and blended courses. It reduced on-campus housing for the fall 2020 semester and occupancy was 40% compared with 92% the previous year. Freshmen and seniors were allowed to live on campus, along with those with research, clinical, or other hands-on requirements. The university took precautions to protect students and limit the spread of the virus while pursuing its testing, quarantine, and wellness plans. Full-time equivalent (FTE) enrollment declined 2.6% as the

university had a slightly smaller-than-typical freshman class, likely in part due to COVID-19. Management is hopeful freshman enrollment will improve in fall 2021, and applications and deposits were ahead of previous-year levels as of April 2021.

Despite the decline in enrollment and COVID-19-related expenses and revenue losses, management is projecting another full-accrual operating surplus in fiscal 2021. The fiscal 2021 budget does not include about \$11.2 million of federal funding. The university has no liquidity concerns.

Credit overview

We assessed CWRU's enterprise profile as very strong, characterized by relatively stable enrollment until the pandemic and a healthy demand profile, with improved selectivity, but mitigated by weak matriculation rates for the rating. We assessed CWRU's financial profile as strong, with consistently positive operations on a full-accrual basis and sufficient available resources for the rating, although somewhat weaker than category medians. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'a+'. As our criteria indicate, the final rating can be within one notch of the indicative credit level. In our opinion, the 'AA-' rating on the university's bonds better reflects CWRU's position as a comprehensive research institution with available resources that, while weaker than medians, are consistent with those of its peers and have increased in recent years.

The rating reflects our assessment of CWRU's following strengths:

- The university's broad range of programs, research, and community medical coalitions, which have historically led to healthy demand metrics despite strong competition for its high-quality students; Consistently positive operating results on a full-accrual basis for the past several fiscal years;
- Sizable cash and investments of \$1.9 billion as of June 30, 2020; and
- A pro forma maximum annual debt service (MADS) burden of about 2.1% at fiscal 2020 year-end, which we consider low.

The rating reflects our assessment of the following weaknesses:

- Available resource ratios that, while sufficient, are low compared with 'AA' category medians; and
- A low freshman matriculation rate of about 15% in fall 2020 compared with that of peer research institutions, indicative of significant national competition for high-quality students.

We have previously written about potential additional debt for housing, but the project and additional debt plans are on hold. Any additional debt other than the proposed direct-purchase arrangement will be factored in when more specific information is available.

The university has four bank lines of credit, totaling \$200 million, available for working capital. There is no balance on these lines at present.

CWRU, in Cleveland, is Ohio's largest private university. It offers a wide range of undergraduate, graduate, and professional degree programs, including arts and sciences, law, business, medicine, engineering, nursing, social work, and dentistry. The university's research base is extensive, in our view. CWRU received approximately \$343 million in

external research awards and indirect cost recovery revenue in fiscal 2020, principally related to health sciences and the medical school. It received more when including revenue passed through to the Cleveland Clinic. CWRU's campus is one of the anchor institutions in University Circle, a 500-acre concentration of more than 40 educational, social, medical, cultural, and religious institutions at the eastern edge of Cleveland.

CWRU and the Cleveland Clinic have an agreement for development and operation of a new Health Education Campus, which includes an academic building and dental clinic. Occupancy began in the spring of 2019 and we understand that the operations are as expected, with management reporting a solid working relationship and financial performance to date. Cleveland Clinic provided the interim financing for construction and the two organizations are jointly fundraising toward the project. Based on the agreement (\$50 million in five equal payments), CWRU paid \$10 million in January 2021 with another potential \$40 million liability over a four-year period beginning in 2021. We understand that funds are reserved for this potential liability.

The stable outlook reflects our expectation that CWRU will maintain relatively stable enrollment and demand; continue to produce positive operations on a generally accepted accounting principles basis; and, at minimum, maintain stable-to-improving available resources in the next few years.

Environmental, social, and governance factors

In our view, higher education entities face elevated social risk due to the uncertain duration of the COVID-19 pandemic. CWRU transitioned to remote learning in spring 2020 and adopted strategies this school year to protect the health and safety of students, faculty, and staff. We view the risks posed by COVID-19 to public health and safety as a social risk under our environmental, social, and governance (ESG) factors. Despite the elevated social risk, we believe the university's environment and governance risk are in line with our view of the sector.

Stable Outlook

Upside scenario

We could consider a positive rating action if the university's available resources increase materially such that measures are more in line with those of a higher rating, and if it sees more robust full-accrual surpluses as well as improvement in enterprise-profile characteristics such as matriculation that is more in line with those of a higher rating.

Downside scenario

We could consider a negative rating action if enrollment declines consistently, the university incurs full-accrual deficits, or additional debt plans yield balance-sheet ratios that are no longer commensurate with the current rating.

Enterprise Profile

Economic fundamentals

In our view, the university has good geographic diversity, with about 35% of all students coming from Ohio. Therefore, our assessment of CWRU's economic fundamentals is anchored by the national GDP per capita.

Market position and demand

Similar to many colleges and universities, CWRU's enrollment declined in fall 2020 as the pandemic continued. Total headcount was 11,465 (10,792 FTE students) in fall 2020, which was a decrease from levels in fall 2017. As a comprehensive research institution, CWRU has a larger proportion of graduate and professional students (approximately 51% of FTEs for fall 2020) than many of its peers. Applications for fall 2020 increased just under 1% over the past year and the solid demand profile is characterized by increasing applications and selectivity offset by weak matriculation. The recent decline in matriculation to 15% from over 17% the previous few years could be due to the pandemic and also a highly competitive landscape for the students. Management is reporting indicators for fall 2021 are solid with an increase in applications and deposits relative to last year, though some uncertainty remains regarding travel for international students, which is relevant as about 14% of undergrad FTE is international and the university has a broad geographic draw. We expect that the selectivity for fall 2021 could be weaker than previous years as management tried to offset some of the uncertainty in the current environment, although over the longer term, we expect selectivity and target class sizes to return to historical levels.

Student quality is also very high as measured by average freshmen ACT and SAT scores. Retention and graduation rates have improved as well, reaching 93% and 85%, respectively. In our view, CWRU's enrollment and demand profile is healthy with no material changes expected in the near term.

CWRU closed its most recent campaign in December 2018 where it raised \$1.8 billion (above the announced \$1 billion goal, which was revised to \$1.5 billion) in the comprehensive campaign started in 2011. The campaign benefits funding for programmatic support, scholarships, capital projects, faculty chairs, and the annual fund. In addition, the university does joint fundraising with the Cleveland Clinic to support that project. CWRU is raising funds for scholarships and could launch a campaign focused on them in the next year or so.

Management and governance

An interim president is currently in place at CWRU following the departure of Barbara Snyder, who left in early 2020. The board of trustees have selected the university's next president, Eric Kaler, the former University of Minnesota president and he will assume the role beginning on July 1, 2021. There are no other significant management changes that are anticipated at this time.

CWRU's regulations and bylaws do not provide for a maximum size for its board of trustees; there are 43 regular (voting) members, including the president, who is an ex officio member, and 89 member emeriti. Members are generally limited to four-consecutive, four-year terms, and may move to emeritus status once their term ends. Most board members are also alumni. We understand that board turnover has been routine. The full board meets formally three times a year and has a committee system.

Financial Profile

Financial policies

There have been no changes to the financial policies since the last review. In October 2018, the university adopted a formal debt policy, which did not exist previously. In addition, it budgets for debt service and an operating contingency, but not depreciation, which we consider a best practice. In our view, CWRU has good financial practices

and manages proactively.

It operates according to a five-year strategic plan, and has an informal reserve liquidity policy. The university meets standard annual disclosure requirements. The financial policies assessment is neutral, reflecting our opinion that, while there may be some areas of risk, the organization's overall financial policies are not likely to impair 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 peer universities.

Financial performance

CWRU typically produces small operating surpluses on a full-accrual basis, with margins ranging from 1%-4% in recent years. Operating results on a full-accrual basis were \$49.9 million (a 4.1% operating margin) for the fiscal year ended June 30, 2020, which was ahead of the previous year. The surplus reflected significant cost-saving measures in light of the COVID-19 pandemic and uncertainty, some support of federal funds, and fairly consistent research revenues with less expenses. Management estimates that the total negative COVID-19 effect was about \$58 million (including revenues lost and increased expenses). For fiscal 2021, the negative COVID-19 effect is estimated at about \$39 million with the most significant factors being lost auxiliary revenues and expenses associated with testing. For the full fiscal year 2021, however, management is still projecting a surplus given its expense management efforts. Not included in the budget is about \$11.2 million in federal support that would further bolster performance. For fiscal 2022, some of the savings measures will be reversed (such as the pension contribution and possible merit increases), but surpluses are still forecasted for that year's budget.

As of fiscal 2018, the university's endowment spending policy is based on a formula of 50% on an inflation index and 50% on 4.5% of the three-year average market value of long-term investments, resulting in an anticipated endowment draw of less than 5%. Beginning in fiscal 2019, CWRU adopted a new endowment payout policy, which compares the 10-year average of actual endowment activity and will adjust the annual distribution based on the comparison. The spending rate was maintained at 4.7% for fiscal years 2021 and 2022.

Operating revenue streams are relatively diverse compared with peers, although CWRU is primarily dependent on student-related charges to fund operations. In fiscal 2020, gross tuition and student fees represented 45% of total revenue. The university receives a concentration of National Institutes of Health funding; we understand that management has focused on remaining competitive for federal grants and is exploring efforts to bolster foundation and industry awards. In our opinion, management is positioned to adjust its research enterprise as project funding lessens, if necessary.

Available resources

CWRU's financial resource ratios are fairly consistent and sufficient for the rating, in our view, although they remain lower than 'AA' category medians. We calculate expendable resources as unrestricted plus temporarily restricted net assets minus net property, plant, and equipment plus long-term debt. As of June 30, 2020, expendable resources totaled approximately \$1.14 billion, equal to 93% annual adjusted operating expenses and 200% of total pro forma debt. Total cash and investments, which includes restricted assets, were approximately \$1.88 billion as of fiscal year-end 2020 (June 30), excluding funds held by trusts, which the university does not manage, but are shown as

assets on the financial statements. Cash and investments were equal to 153% of annual adjusted expenses and 332% of total pro forma debt. We believe that a significant growth in additional debt without commensurate growth in financial resources could pressure the rating.

The university's private equity, real assets, and private credit investments have mandatory capital calls related to future investments. As of February 2021, unfunded calls totaled approximately \$244 million; (about 15% of the investment pool value). The university reports that approximately 35% (about \$600 million) of long-term investments could be liquidated in less than 30 days; it is our view that the university's liquidity profile mitigates its unfunded calls.

Debt and contingent liabilities

CWRU had approximately \$511.9 million of debt including a line of credit as of fiscal year-end 2020 (excluding premium and unamortized bond issuance costs). The debt includes:

- Approximately \$410 million in fixed-rate debt;
- \$68.2 million in floating rate notes; and
- A \$34 million line of credit.

We calculate MADS as the total debt service averaged over the remaining 25 years, resulting in a smoothed MADS of about \$26 million. Approximately 13% of CWRU's debt is variable rate. Management notes that the variable-rate exposure is offset by CWRU's interest-rate swaps resulting in a synthetic fixed rate. The proposed \$56 million series 2021 direct purchase will alleviate the balloon payments in fiscal years 2023 and 2024.

The university has four interest-rate swap contracts with a total notional amount of \$70.2 million. Three of the four contracts terminate in 2022 and the fourth in 2034. The contracts are floating-to-fixed rate and all have Morgan Stanley as counterparty. The mark-to-market value was negative \$17.3 million as of the end of fiscal 2020. The university reports that its collateral threshold is \$20 million. In our view, CWRU's swap portfolio reflects low credit risk at this time due to counterparty credit quality, the average economic viability of the swap portfolio over stressful economic cycles, and sound debt and swap management internal procedures.

The university offers both a defined-contribution retirement plan to employees (which, by definition, is fully funded), and a defined-benefit plan. According to management, the latter is now closed to new entrants. It had a funded status of negative \$130 million at the end of fiscal 2020 and is about 60% funded. Defined-benefit contributions are made annually according to actuarial valuations. The university offers a retiree health care plan, but reports no related liability on its balance sheet because the cost is paid entirely by retirees.

Case Western Reserve University, OH -- Enterprise And Financial Statistics

	--Fiscal year ended June 30--					Medians for 'AA' rated Private Colleges & Universities
	2021	2020	2019	2018	2017	2019
Enrollment and demand						
Headcount	11,465	11,874	11,891	11,824	11,664	MNR
Full-time equivalent	10,792	11,076	11,072	10,917	10,820	7,338

Case Western Reserve University, OH -- Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					Medians for 'AA' rated Private Colleges & Universities
	2021	2020	2019	2018	2017	2019
Freshman acceptance rate (%)	30.3	27.4	29.3	33.1	35.4	19.8
Freshman matriculation rate (%)	14.8	17.2	17.9	15.6	15.4	MNR
Undergraduates as a % of total enrollment (%)	46.6	45.3	44.3	43.6	44.2	67.0
Freshman retention (%)	93.4	93.2	94.4	92.5	91.6	95.6
Graduation rates (six years) (%)	85.3	84.4	84.9	82.6	82.1	MNR
Income statement						
Adjusted operating revenue (\$000s)	N.A.	1,277,812	1,230,105	1,195,955	1,153,524	MNR
Adjusted operating expense (\$000s)	N.A.	1,227,899	1,197,534	1,163,479	1,132,070	MNR
Net operating income (\$000s)	N.A.	49,913	32,571	32,476	21,454	MNR
Net operating margin (%)	N.A.	4.06	2.72	2.79	1.90	2.20
Change in unrestricted net assets (\$000s)	N.A.	(33,787)	29,798	22,859	53,169	MNR
Tuition discount (%)	N.A.	40.6	38.8	38.6	38.4	38.5
Tuition dependence (%)	N.A.	39.9	39.9	39.4	39.2	MNR
Student dependence (%)	N.A.	45.0	46.1	45.4	45.4	60.5
Health care operations dependence (%)	N.A.	0.0	0.0	0.0	0.0	MNR
Research dependence (%)	N.A.	20.6	21.5	21.8	22.0	MNR
Endowment and investment income dependence (%)	N.A.	6.4	6.7	7.0	7.1	MNR
Debt						
Outstanding debt (\$000s)	N.A.	509,535	483,765	496,973	506,918	445,208
Proposed debt (\$000s)	N.A.	56,040	N.A.	N.A.	N.A.	MNR
Total pro forma debt (\$000s)	N.A.	565,575	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	26,126	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	2.78	2.84	3.03	2.92	MNR
Current MADS burden (%)	N.A.	2.12	2.06	2.20	2.16	3.70
Pro forma MADS burden (%)	N.A.	2.13	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value (\$000s)	N.A.	1,570,559	1,568,311	1,539,302	1,461,237	1,793,564
Cash and investments (\$000s)	N.A.	1,876,188	1,847,534	1,808,068	1,726,942	MNR
Unrestricted net assets (\$000s)	N.A.	224,696	258,483	228,685	205,826	MNR
Expendable resources (\$000s)	N.A.	1,144,072	1,053,313	1,050,654	968,498	MNR
Cash and investments to operations (%)	N.A.	152.8	154.3	155.4	152.5	304.8
Cash and investments to debt (%)	N.A.	368.2	381.9	363.8	340.7	484.3

Case Western Reserve University, OH -- Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					Medians for 'AA' rated Private Colleges & Universities
	2021	2020	2019	2018	2017	2019
Cash and investments to pro forma debt (%)	N.A.	331.7	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	93.2	88.0	90.3	85.6	189.9
Expendable resources to debt (%)	N.A.	224.5	217.7	211.4	191.1	303.6
Expendable resources to pro forma debt (%)	N.A.	202.3	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	16.9	17.2	15.9	14.9	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.

Related Research

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

Ratings Detail (As Of May 14, 2021)

Ohio Higher Ed Fac Comm, Ohio

Case Western Reserve Univ, Ohio

Ohio Hgr Ed Fac Com (Case Western Reserve Univ) PCU-GO

Long Term Rating AA-/Stable Affirmed

Ohio Hgr Ed Fac Com (Case Western Reserve Univ) PCU-GO

Long Term Rating AA-/Stable Affirmed

Ohio Hgr Ed Fac Com (Case Western Reserve Univ) PCU-GO (MBIA) (National)

Unenhanced Rating AA-(SPUR)/Stable Affirmed

Many issues are enhanced by bond insurance.

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