STANDARD & POOR'S
RATINGS SERVICES
McGRAW HILL FINANCIAL

RatingsDirect®

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

Primary Credit Analyst:
Ashley Ramchandani, Chicago (1) 312-233-7071; ashley.ramchandani@standardandpoors.com

Secondary Contact:
Avani K Parikh, New York (1) 212-438-1133; avani.parikh@standardandpoors.com

Table Of Contents

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

Credit Profile		
Ohio Higher Ed Fac Comm, Ohio		
Case Western Reserve Univ, Ohio		
Case Western Reserve Univ, various rev bnds ser 1990B, ser 1994		
Long Term Rating	AA-/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services affirmed its 'AA-' long-term rating on various Ohio Higher Educational Facility Commission's revenue bonds issued on behalf of Case Western Reserve University (CWRU). At the same time, Standard & Poor's affirmed its:

- 'A-1' short-term rating on the university's commercial paper (CP) program, authorized at $90 million, based on liquidity support from JPMorgan Chase N.A. (A+/A-1) as well as Northern Trust (A+/A-1).
- 'AAA/A-1' rating on the series 2008A bonds, reflecting a letter of credit (LOC) from PNC Bank N.A. (A/A-1). We base our short-term rating solely on that of PNC. The LOC expires Jan. 1, 2017.

The outlook, where applicable, is stable.

We assessed CWRU's enterprise profile as very strong, characterized by consistent, but moderate, enrollment growth and a healthy demand profile, with improved selectivity though 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, with sufficient available resources for the rating, though somewhat weaker than peers. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'aa-'. 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 somewhat weak, are consistent with peer institutions.

The 'AA-' rating reflects our assessment of CWRU's strengths:

- Stable undergraduate and graduate enrollment due to the university's broad range of programs, research and community medical coalitions, and healthy demand metrics despite strong competition for CWRU's high-quality students;
- Consistently positive operating results on a full-accrual basis for the past five fiscal years;
- Sizable cash and investments of $1.7 billion at June 30, 2015; and
- A low debt burden of less than 3% at fiscal 2015 year end, which we consider low.

The 'AA-' rating reflects our assessment of the following weaknesses:

- Available resource ratios that while adequate are low for the 'AA' rating category, with June 30, 2015, expendable resources equal to 94% of operating expenses and a stronger 172% of total debt, and
- Weak freshman matriculation rate of 15% in fall 2015 compared with that of peer research institutions, indicative of significant national competition for high-quality students.

CWRU, located 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 was awarded approximately $292 million in research grant and indirect cost recovery revenue in fiscal 2015 principally related to health sciences and the medical school. We we note that the university received a total of $389 million 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.

Outlook

The stable outlook reflects our anticipation 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.

Upside scenario

While an upgrade is unlikely in the next two years, we could consider a higher rating if CWRU produces more robust full-accrual surpluses and if available resources were to increase significantly.

Downside scenario

We could consider a negative rating action in the next two years if enrollment were to decline, the university were to incur full-accrual deficits, or if available resources were to decrease from current levels

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 about 28% of students coming from the state of Ohio. As such, our assessment of CWRU's economic fundamentals is anchored by the national GDP per capita.

Market position and demand

The university's overall enrollment has consistently grown at a moderate rate, with average increases of approximately 4.2% for the past four years. Enrollment growth has occurred primarily at the undergraduate level, followed by stable to increasing enrollment at the graduate level. As a comprehensive research institution, CWRU has a larger proportion of graduate and professional students (approximately 52% of total enrollment) than many of its peers. Most undergraduate students enter as freshmen, and 97% attend as full-time residential students. Management reports that a concerted focus on recruitment and improved retention and student quality have supported enrollment growth. We understand that management expects total headcount to decrease slightly in fall 2016, given the upcoming graduation of a particularly large class; management further reports that it anticipates maintaining incoming freshman class sizes at current levels of 1,200 to 1,300.

Management reports that applications for fall 2016 are up slightly over last year. Demand flexibility is marked in our opinion, with the university experiencing increasing selectivity, somewhat mitigated by weak matriculation. Management reports that it has implemented an early decision component in its application process, which it anticipates will result in improved matriculation over time. The university is notably selective, accepting a low of 36% of undergraduate freshman applicants compared with 70% in fall 2009. Matriculation is limited at 15% for fall 2015, reflecting, in our view, a highly competitive market environment.

Student quality is also very high as measured by an average freshmen ACT score of 31. The freshman-to-sophomore retention rate has improved incrementally during the past few years to 94% for fall 2015, consistent with management's goal. The graduation rate has remained stable in the past few years and was at 80% for fall 2015. In our view, CWRU's enrollment and demand profile is healthy.

CWRU publicly announced a $1 billion comprehensive campaign in 2011. Management reports the university has met its original campaign goal ahead of schedule through a mix of cash and pledges. We understand that management has increased the campaign goal to $1.5 billion and is at 86% of its goal, having experienced another record year of fundraising. The campaign will benefit funding for programmatic support, scholarships, capital projects, faculty chairs, and the annual fund. The university's last comprehensive campaign in 1994 raised more than $400 million. We understand that the alumni participation rate for fiscal 2015 was approximately 20%, similar to that of the past four fiscal years.

Management and governance

CWRU's regulations and bylaws do not provide for a minimum or maximum size for its board of trustees; there are 45 regular (voting) members, including the president, who is an ex-officio member, and 90 members emeriti. Members are generally limited to four consecutive four-year terms, and at age 75 (once the term ends) may move to emeritus status. 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. Within the past year, the university has hired a new vice president of financial planning, and appointed on July 1, 2015, an associate vice president of planning and administration. No other changes in senior leadership are planned.

Financial Profile

Financial management policies

While the university has no formal debt policy, it does maintain formal policies for endowment and investments. In addition, the university budgets for depreciation expenses and an operating contingency, which we view as a positive credit factor. In our view, the university has good financial practices and manages in a proactive manner.

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 negatively affect 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 to peer universities.

Financial performance

CWRU typically produces small operating surpluses on a full-accrual basis, with margins ranging from 0.5% to 3.4% over the past four fiscal years. Operating results on a full-accrual basis were $16.3 million for the fiscal year ended June 30, 2015, compared with a high of $34 million a year earlier. We note that returns on operating investments were approximately $11.8 million in fiscal 2015 compared with approximately $20 million in fiscal 2014, excluding of endowment spending for operations. In fiscal 2015, the university was able to exceed expectations with respect to core operating results as a result of several expense control measures implemented in recent years. Management projects positive operating results on a full-accrual basis for fiscal 2016.

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. We understand that CWRU's board recently reduced the percentage for this component of the formula slightly; thus, while the specified percentage is 5% in the current fiscal year, for fiscal 2017 it likely will be 4.5%. In addition, the board has approved an additional draw amount between fiscal years 2009 and 2015 for the comprehensive campaign. According to management, an additional $5.9 million went toward supporting the campaign in fiscal 2015. Management anticipates withdrawing $6 million during fiscal 2016 and expects to draw a similar amount in future years to support its development campaign. The fiscal 2015 endowment draw to support operations was approximately $67.8 million, not including the additional draw to support the campaign; at about 5.1% ($73.7 million total) of beginning market values, we consider both levels manageable.

Operating revenue streams are relatively diverse compared with peers; however, CWRU is increasingly dependent on student-related charges to fund operations. In fiscal 2015, gross tuition and student fees represented 44% of total revenue, with gifts, grants, and contracts providing another 22% of annual income and endowment spending another 8%. The university receives a concentration of National Institute of Health funding; we understand that management has concentrated efforts 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 satisfactory, in our view, though lower than the average of other 'AA-' rated private universities. 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, 2015, expendable resources totaled approximately $970.6 million; we note that CWRU's expendable resources equated to 94% annual adjusted operating expenses of approximately $1 billion and 172% of total debt, compared with the 'AA' rating category medians of 250% and 323%, respectively. Total cash and investments were approximately $1.7 billion as of fiscal year-end 2015, excluding funds held by trusts, which the university does not manage, but are shown as assets on the financial statements, equaling

165% of annual adjusted expenses and 302% of total debt. We believe that a significant growth in additional debt without commensurate growth in financial resources could pressure the rating.

At June 30, 2015, the market value of long-term pooled investments (excluding outside trusts not under direct university control) was about $1.45 billion. The allocation was 40% equities, 24% alternative investments, 16% private equity, 13% real assets, 4% fixed income, and 3% cash. Management has structured its pooled endowment investment policy to focus on consistency of investment outcomes in a variety of economic and inflationary environments.

Many of the university's private equity and real assets investments have mandatory capital calls related to future investments. At the end of fiscal 2015, unfunded calls totaled approximately $143.8 million; at Feb. 4, 2016, unfunded calls were $164.3 million (about 11% of portfolio market value, which we consider somewhat aggressive). However, the university reports that approximately 40% ($600 million) of long-term investments could be liquidated in less than 30 days.

Debt and contingent liabilities

CWRU had approximately $565 million of debt as of fiscal year-end 2015. The debt includes:

- Approximately $272 million in long term debt;
- Approximately $135.5 million in VRDBs;
- $67.5 million in direct placement debt; and
- $69 million outstanding of $90 million authorized CP program. We understand that, in the event of an unremarketed rollover, liquidity for the program is provided by JPMorgan Chase ($60 million) and Northern Trust ($30 million).

The university also has two bank lines of credit, totaling $70 million, available for working capital. There is no outstanding balance on these lines at present.

On July 1, 2015, CWRU refinanced its series 2001 and 2002A bonds in the amount of $75.48 million with a three-year direct placement with Wells Fargo Bank N.A. Based on our review of documents, we understand that with respect to the series 2014 direct placement in the amount of $67.5 million, there are events that lead to acceleration of debt and cross-default and no additional financial-based covenants associated with the debt. We have reviewed documents associated with the series 2015A direct purchase debt and understand that while there are no additional financial-based covenants associated with the debt, there are provisions for acceleration and cross-default in the event of nonpayment. We consider the risk of nonpayment remote at this time given the university's current financial profile.

The debt profile of the university is uneven, in our opinion; as such we calculate MADS as the total debt service averaged over the life of the bonds, resulting MADS of about $22 million. About 17% (giving effect to interest-rate swaps) of the university's debt is variable rate. In addition, CWRU has contingent liquidity risk exposures that we consider manageable at the current rating level. The exposures come from approximately $143 million in series 2014 and 2015A direct purchase debt sold directly to refund a portion of the university's variable-rate debt. We understand that while the university is considering restructuring its debt, it does not have plans to issue any new-money debt at this time.

In addition, the university has five interest-rate swap contracts with a total notional amount of $175 million (one of the small swaps is amortizing, so this number declines slightly every year). The effect of the contracts, all of which are floating-to-fixed rate, is a net variable-rate exposure of about 17%. The contracts are all with Morgan Stanley as counterparty, and the mark-to-market value was negative $23.5 million on March 22, 2016. The university reports that its collateral threshold is $20 million, resulting in periodic collateral postings (currently $2 million-$5 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 (DB) plan. The DB plan had a funded status of negative $68 million at the end of fiscal 2015, compared with negative $56 million the previous year. We understand that DB contributions are made annually according to actuarial valuations. The university offers a retiree health care plan but reports no related liability on the university's balance sheet because the cost is paid entirely by retirees.

Case Western Reserve University, OH

	--Fiscal year ended June 30--					Medians
	2016	2015	2014	2013	2012	Private Colleges & Universities 'AA' 2014
Enrollment and demand						
Headcount	11,340	10,771	10,325	10,026	9,636	MNR
Full-time equivalent	10,587	10,130	9,622	9,259	8,815	3,749
Freshman acceptance rate (%)	36.3	38.3	41.9	54.3	51.3	26.5
Freshman matriculation rate (%)	15.2	15.4	16.2	17.1	13.0	34.3
Undergraduates as a % of total enrollment (%)	45.2	45.6	45.1	43.7	41.7	72.2
Freshman retention (%)	93.9	93.2	94.2	91.6	93.0	94.4
Graduation rates (five years) (%)	N.A.	N.A.	77.6	78.8	77.5	87.3
Income statement						
Adjusted operating revenue ($000s)	N.A.	1,051,428	1,045,840	1,008,434	988,577	MNR
Adjusted operating expense ($000s)	N.A.	1,035,105	1,011,695	1,003,498	977,883	MNR
Net operating income ($000s)	N.A.	16,323	34,145	4,936	10,694	MNR
Net operating margin (%)	N.A.	1.58	3.38	0.49	1.09	MNR
Change in unrestricted net assets ($000s)	N.A.	19,086	18,341	17,810	(69,185)	MNR
Tuition discount (%)	N.A.	40.8	40.7	39.7	37.2	36.4
Tuition dependence (%)	N.A.	37.5	35.3	34.4	32.2	MNR
Student dependence (%)	N.A.	43.7	41.2	40.2	37.3	MNR
Healthcare operations dependence (%)	N.A.	0.0	N.A.	0.0	0.0	MNR
Research dependence (%)	N.A.	22.3	23.8	25.1	26.9	MNR
Endowment and investment income dependence (%)	N.A.	7.6	8.0	7.4	7.1	MNR
Debt						
Outstanding debt ($000s)	N.A.	564,856	578,243	588,546	550,166	252,800
Proposed debt ($000s)	N.A.	75,480	N.A.	N.A.	N.A.	MNR

Case Western Reserve University, OH (cont.)						
	--Fiscal year ended June 30--					Medians
	2016	2015	2014	2013	2012	Private Colleges & Universities 'AA' 2014
Current debt service burden (%)	N.A.	2.78	2.51	3.09	2.81	4.00
Current MADS burden (%)	N.A.	2.12	3.62	4.13	3.07	MNR
Financial resource ratios						
Endowment market value ($000s)	N.A.	1,439,174	1,380,515	1,256,079	1,223,893	1,163,613
Cash and investments ($000s)	N.A.	1,708,388	1,694,480	1,530,379	1,450,226	MNR
Unrestricted net assets ($000s)	N.A.	201,953	182,867	164,526	146,716	MNR
Expendable resources ($000s)	N.A.	970,628	1,014,400	873,553	760,234	MNR
Cash and investments to operations (%)	N.A.	165.0	167.5	152.5	148.3	378.4
Cash and investments to debt (%)	N.A.	302.4	293.0	260.0	263.6	463.1
Expendable resources to operations (%)	N.A.	93.8	100.3	87.1	77.7	250.4
Expendable resources to debt (%)	N.A.	171.8	175.4	148.4	138.2	323.1
Average age of plant (years)	N.A.	14.2	13.8	13.0	12.2	13.0

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). Tuition dependence = 100*(gross tuition 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 & long-term investments. Expendable resources = unrestricted net assets + temp. restricted net assets - (net PPE- outstanding debt). Average age of plant = accumulated depreciation/depreciation & amortization expense.

Related Criteria And Research

Related Criteria

- General Criteria: Methodology: Not-For-Profit Public And Private Colleges And Universities, Jan. 6, 2016
- USPF Criteria: Contingent Liquidity Risks, March 5, 2012
- USPF Criteria: Commercial Paper, VRDO, And Self-Liquidity, July 3, 2007
- USPF Criteria: Municipal Applications For Joint Support Criteria, June 25, 2007

Ratings Detail (As Of March 25, 2016)		
Ohio Higher Ed Fac Comm, Ohio		
Case Western Reserve Univ, Ohio		
ser 1994		
Long Term Rating	AA-/Stable	Affirmed
Case Western Reserve Univ rev bnds ser 2006		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Ohio Hgr Ed Fac Auth (Case Western Reserve Univ) rev var rate dem bonds ser 2008A		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Long Term Rating	AAA/A-1	Affirmed

1603917 | 302418718

Ratings Detail (As Of March 25, 2016) (cont.)		
Ohio Hgr Ed Fac Auth (Case Western Reserve Univ) rev var rate dem bonds ser 2008C		
Long Term Rating	AA-/Stable	Affirmed
Ser 2012A & Ser 2013A		
Long Term Rating	AA-/Stable	Affirmed

Many issues are enhanced by bond insurance.