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

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

Credit Profile

US\$35.0 mil hgr ed fac rev bnds (Case Western Reserve Univ) ser 2021B due 10/01/2042

<i>Long Term Rating</i>	AA-/Stable	New
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US\$28.675 mil hgr ed fac rev bnds (Case Western Reserve Univ) ser 2021A due 10/01/2044

<i>Long Term Rating</i>	AA-/Stable	New
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Ohio Higher Ed Fac Comm, Ohio

Case Western Reserve Univ, Ohio

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

<i>Long Term Rating</i>	AA-/Stable	Affirmed
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Rating Action

S&P Global Ratings assigned its 'AA-' long-term rating to the Ohio Higher Educational Facility Commission's series 2021A (fixed rate) and 2021B (FRN) bonds issued for Case Western Reserve University (CWRU). At the same time, we affirmed our 'AA-' ratings outstanding. The outlook is stable.

As of June 30, 2021, the last audit, CWRU had \$470.2 million of long-term debt outstanding. The majority of the debt is public, fixed-rate debt except the series 2019A floating-rate note which is being refinanced with this issuance. The pro forma ratios incorporate the \$56 million series 2021 direct-purchase arrangement (which refunded the series 2013 and 2016 bonds) and \$28.7 million series 2021A and \$35 million 2021B bonds. CWRU's general obligation (GO) pledge to make rental payments under a lease agreement with the commission secures the bonds. The university's obligation to make rental payments is absolute and unconditional and not subject to abatement, setoff, or counterclaim. Included in the debt figures is the operating lease obligation of about \$10 million as of fiscal year-end 2021, which we view as manageable relative to the overall balance-sheet position.

Because of the COVID-19 pandemic, CWRU transitioned to virtual instruction for the second half of the spring 2020 semester. Management gave cash refunds for housing and board to its students while they worked quickly to contain costs to offset the loss in revenue. The university's operations improved in fiscal years 2020 and 2021 despite the COVID-19 crisis. CWRU received \$4.5 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 \$6.5 million in HEERF II funding, \$663,000 from Employee Retention Credit, and \$4.8 million from state funding for COVID-19-related issues in fiscal 2021. Management reports another \$11.8 million in HEERF III for fiscal 2022 (or beyond). 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 for faculty and senior staff, 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. Some of the expense efforts will be rolled back in fiscal 2022 (such as pension-related cuts), while others are structural changes to the expense base expected to be maintained.

For fall 2020, the university operated with a hybrid model with courses being offered in person, fully online, and blended courses and reduced on-campus housing for the fall 2020 semester, and occupancy was 40% compared with 92% the previous year. For fall 2021, applications and enrollment improved and for the full fiscal year, the university posted an improved operating margin despite COVID-19-related pressures. Management is projecting an operating surplus for fiscal 2022 similar to fiscal 2021 based on better-than-expected first-year enrollment and continued expense savings.

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 very strong, with improved positive operations on a full-accrual basis and improved available resources for the rating given recent investment gains and debt repayment in recent years. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'aa-' and final rating of 'AA-'.

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

- 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; and
- Pro forma maximum annual debt service (MADS) burden of about 2% at fiscal 2021 year-end, which we consider low.

The rating reflects our assessment of the following weaknesses, including its:

- Low freshman matriculation rate of about 16% in fall 2021 compared with that of peer research institutions, indicative of significant national competition for high-quality students; and
- Potential for additional debt as CWRU assesses strategic projects on campus.

The university has three bank lines of credit, totaling \$150 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 \$390 million in external research awards and indirect cost recovery revenue in fiscal 2021, 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 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. We understand that there is potential for additional debt related to strategic capital investments which could weaken balance-sheet ratios and would be assessed when more details about the amount and timing were available.

Environmental, social, and governance factors

Vaccine progress in the U.S. has helped alleviate some of the health and safety social risks stemming from the pandemic; however, the higher education sector remains at a greater risk from remaining uncertainties. 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 environmental and governance risks are in line with the sector standard.

Stable Outlook

Upside scenario

We could consider a positive rating action if the university's available resources continue to improve such that capital projects and additional debt could be absorbed and metrics are in line with a higher rating, and if it sees sustained robust full-accrual surpluses (excluding external, nonrecurring funding) 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.

Credit Profile

Enterprise Profile

Market position and demand

CWRU has a broad draw for students with about 27% coming from within Ohio. While the number of international students declined during the pandemic, it remains about 20% of total full-time equivalent (FTE) for fall 2021. Similar to many colleges and universities, CWRU's enrollment declined in fall 2020 as the pandemic continued, but then rebounded in fall 2021 with a 5.6% growth in FTE. As a comprehensive research institution, CWRU has a larger proportion of graduate and professional students (approximately 50% of FTEs for fall 2021) than many of its peers. Applications for fall 2021 increased significantly over 14% over the past year and the solid demand profile is characterized by increasing applications and selectivity offset by weak matriculation. The matriculation at 16% reflects a highly competitive landscape for the students. As expected, selectivity for fall 2021 was somewhat weaker than historical levels 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. The entering class in fall 2021 was the largest in the university history at 1,606. Student quality remained high as measured by average freshmen ACT and SAT scores. Retention and graduation rates have improved as well, reaching 94% 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 scholarships, strategic capital projects, and research in the next one-to-two years.

Financial Profile

Financial performance

CWRU typically produces operating surpluses on a full-accrual basis, with margins ranging from 1%-6% in recent years. Operating results on a full-accrual basis were improved in fiscal 2021, 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 fewer expenses. For fiscal 2021, the negative COVID-19 effect is estimated at about \$45.5 million, with the most significant factors being lost auxiliary revenues and expenses associated with testing. For the full fiscal year 2021, however, management posted a robust surplus given its expense management efforts. For fiscal 2022, many of the structural expense management changes will be retained and surpluses are still forecasted for the year's budget especially given above-target enrollment and full auxiliaries.

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 2021, gross tuition and student fees represented 46% 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, which should remain a significant focus and revenue diversifier.

Available resources

CWRU's financial resource ratios are improved with growth in cash and investments due to a 31.5% investment return for fiscal 2021 and amortization and repayment of debt. In our opinion, the ratios remain in line with the 'AA' category medians, which we expect to increase overall when it reflects the improvement seen broadly in fiscal 2021. 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, 2021, expendable resources totaled approximately \$1.4 billion, equal to 120% annual adjusted operating expenses and 306% of total pro forma debt. Total cash and investments, which includes restricted assets, were approximately \$2.35 billion as of fiscal year-end 2021 (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 improved over historical levels and should remain solid relative to operations and debt.

The university's private equity, real assets, and private credit investments have mandatory capital calls related to future investments. Unfunded calls remain manageable, in our opinion, at about \$311 million. The university reports that about \$321 million is available in same-day liquidity; it is our view that its liquidity profile mitigates its unfunded calls.

Debt and contingent liabilities

CWRU has approximately \$470 million of debt as of fiscal year-end 2021 (excluding premium and unamortized bond issuance costs). The debt includes:

- Approximately \$392 million in fixed-rate debt;
- \$68 million in floating rate notes; and
- \$10 million operating lease obligations.

The debt amount varied some from last year with the repayment of the line of credit. We calculate maximum annual debt service (MADS) as the total debt service averaged over the remaining 24 years, resulting in a smoothed MADS of about \$27 million. The pro forma figures include the \$56 million direct purchase, which alleviated balloon payments in 2023 and 2024. Following the series 2021A and B issuance, 8% of CWRU's debt will be variable rate (\$35 million series 2021B bonds will be floating-rate notes). Management notes that the variable-rate exposure is offset by CWRU's interest-rate swaps resulting in a synthetic fixed rate.

The university is considering capital investments (including a dormitory project and research building all totaling about \$300 million-\$400 million) and there is potential for additional debt, though no finalized plans are available. Given the recent significant growth in cash and investments, CWRU could likely absorb the additional debt at the current rating, but without clarification on timing and financing for these projects, we currently haven't factored in the debt.

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 \$13 million as of the end of fiscal 2021. 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 \$87 million at the end of fiscal 2021 and is about 70% 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
	2022	2021	2020	2019	2018	2020
Enrollment and demand						
Headcount	12,142	11,465	11,874	11,891	11,824	MNR
Full-time equivalent	11,397	10,792	11,076	11,072	10,917	8,288
Freshman acceptance rate (%)	30.2	30.3	27.4	29.3	33.1	18.0
Freshman matriculation rate (%)	16.0	14.8	17.2	17.9	15.6	MNR
Undergraduates as a % of total enrollment (%)	47.7	47.4	45.3	44.3	43.6	65.1
Freshman retention (%)	93.7	93.4	93.2	94.4	92.5	95.0
Graduation rates (six years) (%)	85.4	85.3	84.4	84.9	82.6	MNR
Income statement						
Adjusted operating revenue (\$000s)	N.A.	1,252,752	1,277,812	1,230,105	1,195,955	MNR
Adjusted operating expense (\$000s)	N.A.	1,177,230	1,227,899	1,197,534	1,163,479	MNR
Net operating income (\$000s)	N.A.	75,522	49,913	32,571	32,476	MNR
Net operating margin (%)	N.A.	6.42	4.06	2.72	2.79	1.20
Change in unrestricted net assets (\$000s)	N.A.	117,923	(33,787)	29,798	22,859	MNR
Tuition discount (%)	N.A.	39.7	40.6	38.8	38.6	39.4
Tuition dependence (%)	N.A.	42.2	39.9	39.9	39.4	MNR
Student dependence (%)	N.A.	45.6	45.0	46.1	45.4	59.4
Health care operations dependence (%)	N.A.	0.0	0.0	0.0	0.0	MNR
Research dependence (%)	N.A.	20.4	20.6	21.5	21.8	MNR
Endowment and investment income dependence (%)	N.A.	8.1	6.4	6.7	7.0	MNR
Debt						
Outstanding debt (\$000s)	N.A.	470,194	509,535	483,765	496,973	540,885
Proposed debt (\$000s)	N.A.	119,715	N.A.	N.A.	N.A.	MNR
Total pro forma debt (\$000s)	N.A.	469,659	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	27,299	N.A.	N.A.	N.A.	MNR

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

	--Fiscal year ended June 30--					Medians for 'AA' rated Private Colleges & Universities
	2022	2021	2020	2019	2018	2020
Current debt service burden (%)	N.A.	2.76	2.78	2.84	3.03	MNR
Current MADS burden (%)	N.A.	2.22	2.12	2.06	2.20	4.20
Pro forma MADS burden (%)	N.A.	2.32	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value (\$000s)	N.A.	2,004,374	1,570,559	1,568,311	1,539,302	1,922,226
Cash and investments (\$000s)	N.A.	2,348,690	1,876,188	1,847,534	1,808,068	MNR
Unrestricted net assets (\$000s)	N.A.	342,619	224,696	258,483	228,685	MNR
Expendable resources (\$000s)	N.A.	1,419,326	1,144,072	1,053,313	1,050,654	MNR
Cash and investments to operations (%)	N.A.	199.5	152.8	154.3	155.4	338.3
Cash and investments to debt (%)	N.A.	499.5	368.2	381.9	363.8	447.8
Cash and investments to pro forma debt (%)	N.A.	500.1	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	120.6	93.2	88.0	90.3	185.4
Expendable resources to debt (%)	N.A.	301.9	224.5	217.7	211.4	261.5
Expendable resources to pro forma debt (%)	N.A.	302.2	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	18.5	16.9	17.2	15.9	13.9

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 November 9, 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

Ratings Detail (As Of November 9, 2021) (cont.)

Many issues are enhanced by bond insurance.

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