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Washington Higher Education Facilities Authority University of Puget Sound; Private Coll/Univ - General Obligation

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Table Of Contents

Credit Highlights

Outlook

Credit Opinion

Enterprise Risk Profile--Strong

Financial Risk Profile--Strong

Related Research

Washington Higher Education Facilities Authority University of Puget Sound; Private Coll/Univ - General Obligation

Credit Profile

US\$26.8 mil rev and rfdg bnds (University of Puget Sound) ser 2023 due 06/30/2037

Long Term Rating

A+/Stable

New

Washington Higher Education Facilities Authority, Washington

University of Puget Sound, Washington

Washington Ed Fac Auth (University of Puget Sound) PCU_GO

Long Term Rating

A+/A-1/Stable

Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'A+' long-term rating to the Washington Higher Education Facilities Authority's \$26.8 million series 2023 revenue refunding bonds issued on behalf of the University of Puget Sound.
- At the same time, S&P Global Ratings affirmed its 'A+/A-1' rating on the university's series 2001 weekly rate demand revenue bonds issued by the authority. The rating's short-term component reflects our opinion of the university's self-liquidity.
- The outlook on the long-term rating is stable.

Security

The University of Puget Sound had approximately \$65.4 million in debt outstanding as of June 30, 2022, which included \$30.2 million of variable-rate debt and a small amount of capital leases. The \$26.8 million series 2023 bonds will refinance the university's series 2001 and 2021A variable-rate debt with fixed-rate bonds. The university currently has two interest rate swap agreements that synthetically fix its variable-rate debt, both of which will be terminated as part of this transaction. The swaps had a negative mark-to-market value of \$2.4 million as of June 30, 2023. The university also provides self-liquidity for its \$7.4 million of variable-rate demand bonds with \$62.5 million available in same- and next-day liquidity as of June 30, 2022. A broad pledge of unrestricted revenue, gains, and other support secures the bonds, which we view as equivalent to a general obligation pledge of the university. The university's pro forma maximum annual debt service (MADS) is a low 2.8% of fiscal 2022 adjusted operating expenses. We do not expect the university will issue any new debt in the two-year outlook period.

Credit overview

We assessed the University of Puget Sound's enterprise risk profile as strong, characterized by good geographic diversity and consistent student quality, offset by weak acceptance and matriculation rates. We assessed the university's financial risk profile as strong, reflecting solid financial resources and robust financial policies. We believe these credit factors, combined, lead to an anchor of 'a'. As our criteria indicate, the final rating can be within one notch of the indicative credit level. In our opinion, the 'A+' rating better reflects the University of Puget Sound's robust level

of cash and investments relative to debt.

The long-term rating reflects what we view as the university's strengths:

- A strong cash and investment position that has grown over time, particularly relative to debt;
- A manageable debt burden, with a modest pro forma MADS and no additional debt expected in the outlook period; and
- A solid endowment relative to those of peers on a per-full-time-equivalent (FTE) basis.

The long-term rating also reflects our assessment of the university's weaknesses:

- Weaker demand metrics than peers, particularly selectivity and matriculation rates;
- Limited revenue diversity, with student-derived revenue making up 82% of adjusted operating revenues; and
- Pressured operations in recent years, with deficits expected to continue through fiscal 2025.

The University of Puget Sound, founded in 1888 in Tacoma, is a private residential liberal arts and science institution with an emphasis on undergraduate education. The university offers more than 50 areas of study, including a school of music and a school of business and leadership.

Environmental, social, and governance

We analyzed the university's environmental, social, and governance factors pertaining to its market position and financial performance. Health and safety risks related to the pandemic, which we consider a social factor, have largely abated and are neutral in our credit rating analysis. We also view the university's environmental and governance factors as neutral in our analysis.

Outlook

The stable outlook reflects our view that the University of Puget Sound's balance sheet and lack of additional debt plans provide sufficient cushion for the current rating, despite deficits that are expected to continue through fiscal 2025. We also expect improved matriculation in fall 2023 will support stabilized enrollment in the outlook period.

Downside scenario

We could consider a negative rating action if deficits are larger than projected and cause a substantial decline in financial resources. We would also view weakening of demand metrics, such as enrollment and retention, negatively.

Upside scenario

We could consider a positive rating action if the university significantly strengthened its demand profile, primarily selectivity and matriculation, while maintaining or improving student quality. We would also expect the university to return to positive operations and further grow cash and investments.

Credit Opinion

Enterprise Risk Profile--Strong

Market position and demand

The University of Puget Sound has faced enrollment pressure in recent years. Most recently, FTE enrollment fell by 7% in fall 2022, to 1,968 students. The drop was driven by lower undergraduate enrollment as first-year class sizes have stabilized at around 400 students but are smaller than pre-pandemic classes. As a result, we expect FTE will likely drop further in fall 2023 before stabilizing. Deposits are up for first-year students, and selectivity and matriculation rates are improved, which we view positively. In fall 2022, selectivity was weak compared to peers at 83%, and matriculation was reflective of a highly competitive environment at under 10%. We would view improvement in selectivity and matriculation rates as well as continued enrollment stability as positive credit factors. Despite enrollment pressure, student quality remains stable and higher than rating category medians. Undergraduates make up 86% of the student body. The university has good geographic diversity, with only 36% of students from Washington state.

Management is targeting modest enrollment growth over the next several years under a strategic enrollment plan. The plan includes refreshing marketing materials and expanding video content. Additionally, the enrollment plan seeks to improve the use of analytics, increase application volumes, diversify enrollment channels, launch new graduate programs, and improve retention.

Management and governance

The University of Puget Sound has a stable and experienced management team. The university's president, Dr. Isiaah Crawford, has been in his role since 2016. Recently, the university gained a new chief financial officer following a retirement. There have also been transitions in the provost and vice president for university relations roles. The board has been stable, with primarily rotational changes.

The university operates according to a 2018-2028 strategic plan, "Leadership for a Changing World," with goals to advance institutional excellence, academic distinction, and student success; enrich campus learning through increased diversity, inclusion, and access; support and inspire faculty and staff members; enhance engagement with the community; and expand institutional assets by pursuing entrepreneurial opportunities. Management has updated the strategic plan to adapt to changing demand. In particular, management seeks to improve the university's financial health by right-sizing operations for a target enrollment size of 2,300 students.

Financial Risk Profile--Strong

Financial performance

Until fiscal 2020, the University of Puget Sound had a track record of positive margins on a full-accrual basis. Demand pressure, increased discounting, and impacts of the pandemic have weakened operations in recent years. The university ended fiscal 2022 with an operating loss of \$3.7 million, equal to -2.2% of adjusted operating expenses.

Management projects continued deficits through fiscal 2025 before a return to break-even operations in 2026. While we view these deficits negatively, we believe management has a commitment to financial discipline, including efforts to right-size operations. The series 2023 refinancing transaction will also provide some budget relief through fiscal 2026 by restructuring principal payments without extending the final maturity of the bonds.

Like many private universities of its size, the University of Puget Sound is dependent on student tuition and fees, which account for approximately 82% of adjusted revenue. After four years of declines, net tuition revenue increased in fiscal 2022. The university's discount rate is 48%, stable compared to fiscal 2021 and similar to the discount rates of peer institutions. Tuition typically increases 3%-4% per year and remains in line with peers at \$59,340 for the 2023-2024 school year.

Financial resources

The University of Puget Sound's financial resources remain a credit strength. Like peers, the university saw cash and investments decline in fiscal 2022 following robust growth in fiscal 2021. Cash and investments measured \$493.0 million as of June 30, 2022, equal to 300% of adjusted operating expenses and 796% of pro forma debt. Even with projected deficits in the outlook period, we expect the university's resources will remain solid for the current rating.

As of fiscal 2022, the University of Puget Sound's endowment had a market value of \$428.0 million. The asset allocation was moderately conservative, primarily invested in global equities, absolute return, real assets, and private capital. The university has an endowment spending policy of 5% of a trailing 36-month average market value with a two-year lag, which we view as sustainable. The university has a track record of successful fundraising efforts. In 2020, the university successfully met its internal five-year fundraising goal, raising \$51 million compared to a target of \$43 million. In January 2022, the university launched the silent phase of its current campaign, "Greater, We Ascend," with a working target of \$150 million. Management reports there was a significant increase in donations and donors in fiscal 2023.

University of Puget Sound, Washington--enterprise and financial statistics					
	--Fiscal year ended June 30--				
	2023	2022	2021	2020	2019
Enrollment and demand					
Full-time-equivalent enrollment	1,968	2,118	2,113	2,563	2,619
Undergraduates as a % of total enrollment	85.8	87.2	87.9	89.0	89.9
First-year acceptance rate (%)	82.7	88.3	86.9	83.8	88.3
First-year matriculation rate (%)	9.2	9.2	8.7	14.2	12.9
First-year retention rate (%)	78.7	88.0	76.3	80.9	80.6
Six-year graduation rate (%)	76.1	74.2	77.1	76.2	75.6
Income statement					
Adjusted operating revenue (\$000s)	N.A.	160,861	150,563	172,890	175,724
Adjusted operating expense (\$000s)	N.A.	164,535	154,487	172,953	170,761
Net operating margin (%)	N.A.	(2.2)	(2.5)	0.0	2.9
Change in unrestricted net assets (\$000s)	N.A.	(14,470)	24,306	(2,294)	5,129
Tuition discount (%)	N.A.	47.5	48.2	44.8	41.6

University of Puget Sound, Washington--enterprise and financial statistics (cont.)

	--Fiscal year ended June 30--				
	2023	2022	2021	2020	2019
Student dependence (%)	N.A.	82.0	77.0	86.1	85.8
Research dependence (%)	N.A.	0.1	0.1	0.1	0.1
Debt					
Outstanding debt (\$000s)	N.A.	65,358	67,484	68,647	70,551
Current MADS burden (%)	N.A.	2.7	3.0	2.9	3.0
Average age of plant (years)	N.A.	14.9	14.4	13.6	12.6
Financial resource ratios					
Endowment market value (\$000s)	N.A.	427,977	474,232	378,614	380,507
Cash and investments (\$000s)	N.A.	493,015	545,357	446,276	442,757
Cash and investments to operations (%)	N.A.	299.6	353.0	258.0	259.3
Cash and investments to debt (%)	N.A.	754.3	808.1	650.1	627.6

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 MADS burden = 100*(maximum annual debt service expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Average age of plant = accumulated depreciation/depreciation and amortization expense. N.A.--Not available. MNR--Median not reported. MADS--Maximum annual debt service.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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