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

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Table Of Contents

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Credit Profile		
Villanova Univ ICR		
Long Term Rating	A+/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has affirmed its 'A+' issuer credit rating (ICR) on Villanova University, Pa. Standard & Poor's also affirmed its 'A+' long-term rating and underlying rating (SPUR) on the series 2005, 2006, and 2010 revenue bonds issued for the university by the Delaware County Authority, Pa. The outlook is stable.

The rating was raised to 'A+' a year ago based on continued strong financial operating performance, prudent fiscal management, conservative debt structure, and improving demand trends. While the positive trends have continued, management states it now expects smaller surpluses due to a university-wide focus on affordability, which would increase its tuition discount rate and reduce margins below historical levels of 7%-9% annually. The university states it may issue approximately $150 million of debt over the next two to three years. This could pressure its financial resources, which are currently adequate for the rating. Given that the university expects weaker operating performance and balance sheet as a result of the future debt issuance, the rating could be pressured. Weaker margins, sustained below 5%, combined with expendable resources to debt ratio at or below 1.2x, would likely result in a negative rating action because the university will no longer be in line with its peers in the upper end of the 'A' rating category.

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

- Historically strong student demand, demonstrated by stable enrollment, growing applications over a long period of time, generally good selectivity, excellent freshmen retention rates, and very good student quality;
- Strong financial operations with consistently good operating surpluses on a full accrual basis and good growth in net tuition and fee income, as well as prudent fiscal management;
- Adequate financial resources for the rating category, with expendable resources of $331 million in fiscal year 2011 (May 31 year-end) equal to 77% of adjusted operating expenses and 163% of debt outstanding; and
- Manageable debt service burden, with maximum annual debt service (MADS) of approximately $16.6 million equal to 3.8% of fiscal 2011 adjusted operating expenses, and a predictable, conservative debt structure.

Partially offsetting factors include:

- Expected issuances of $150 million of debt in the next two to three years, which could pressure the university's financial resources;
- Slower growth in net tuition revenue for fiscal 2010 and 2011, with smaller surpluses expected due to an increased focus on affordability;

- Limited revenue diversity with more than 87% of gross revenues in fiscal 2011 coming from student-generated revenues (tuition, fees, and auxiliaries); and
- A relatively small endowment of approximately $376 million as of April 30, 2012, compared with many of its peers.

The university completed a debt restructuring in 2010 and refinanced both fixed- and variable-rate debt. Currently all of the university's bonded debt is fixed rate; it has never had interest-rate swaps associated with the bonds. As of May 31, 2011, Villanova recorded $202.6 million of total debt. Management states that it may issue $150 million of debt over the next two years to fund the construction of residential halls for undergraduate students. Although this debt will fund a self-supporting project, we expect it will pressure the university's financial resource ratios.

Villanova University is an independent, coeducational institution located in Radnor Township, about 14 miles west of Philadelphia. Founded in 1842 by the Augustinian Order of the Roman Catholic Church, today the well-maintained 260-acre campus encompasses 75 buildings on Philadelphia's affluent "Main Line" vicinity. Villanova offers a comprehensive array of undergraduate, graduate, and professional degrees, including law, business, engineering, and nursing. In fall 2011, total enrollment was 10,467, 66% of whom were undergraduates, and nearly all (92%) were full-time students.

Outlook

The stable outlook reflects Standard & Poor's expectation that over the next two years, the university will continue to produce good operating surpluses, albeit smaller than in the past, and will maintain a selective demand profile and financial resource ratios that are in line with the upper end of the 'A' category. The outlook further reflects our expectation that the additional $150 million of debt will be issued beyond our two-year horizon.

A negative rating action is likely if significant additional debt is issued and pressures financial resources to the point that expendable resources are equal to or below 60% operations and 1.2x debt – particularly with weaker operating margins of below 5%. Other factors that could lead to a negative rating action include deficit operating performance on a generally accepted accounting principles (GAAP) basis, significant deterioration of financial resources unrelated to debt issuance, or significant weakening of the demand profile. A positive rating action is unlikely during the outlook period given management's expectations for slimmer operating margins and a potential $150 million debt issuance.

Enterprise Profile

Enrollment and demand

The university has a strong demand profile, characterized by a growing applicant pool, a good level of selectivity, and high retention rates. Although year-to-year applications have been slightly variable, fluctuating between 13,000 and 15,000 over the past five years, the university has maintained steady acceptance rates at approximately 45%, which we view as selective. The freshmen matriculation rate has been pressured over the past five years, like many of its peers in a highly competitive regional market, and reached a low of 24% in fall 2011. Management states that demand indicators for fall 2012 are in line with historical trends.

Overall enrollment was flat at just under 10,500 in fall 2010 and 2011 (10,467 for fall 2011). Management indicates that its on-campus housing is close to capacity, and it plans to keep full-time undergraduate enrollment at the current level of 6,300 to 6,400 for the foreseeable future. Student retention continues to be very strong in our view, with approximately 94% of freshmen returning for their sophomore year in fall 2011. In our opinion, student quality, as measured by SAT scores, continues to be solid at approximately 1300 in fall 2011. The university draws approximately 67% of its students coming from mid-Atlantic states.

Management projects some change in its graduate enrollment with the launch of several online programs. The programs will boost enrollment without putting additional burden on the campus. Villanova's law school, like others across the country, has experienced a decline in applications. The school expects to recalibrate to a smaller size of approximately 650 students, from 719 currently, which would reduce expenses as well.

Management

The management team has been quite stable in the past five years. The president has been in place for six years and the finance team for over 10 years. 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 strong surpluses each year. The university has investment and debt policies, which we also view favorably.

Financial Profile

Operations

Villanova's financial profile is characterized by very good operating performance, a high level of dependence on student-generated income, and generally good financial resources. The university has maintained consistently strong financial operations on a full accrual basis over the past five fiscal years. For the fiscal year ended May 31, 2011, the university produced an operating surplus of $31.7 million (or 7.3% of fiscal 2011 adjusted operating expenses), similar to the previous year's results of $34.9 million. Management indicates that fiscal 2012 performance, on a GAAP basis, will likely show a slightly smaller surplus of approximately $20 million due to planned increases in financial aid as part of a new focus on student affordability. The long-term plan calls for slimmer, but still robust, margins of approximately 3%-5% over the next five years, down from historical levels of 7%-8%, while the school fulfills its strategic plan related to affordability.

Villanova consistently budgets for operating surpluses and planned savings for endowment and actual results generally exceed budgeted projections. Operating budgets routinely incorporate the full costs of depreciation, debt service, and other budgetary reserves. Beginning in fiscal 2009, management implemented various cost-saving measures, including hiring and salary freezes, to offset increases in financial aid and reduced investment income. Management states that over the next several years, it will slowly increase its financial aid to build the undergraduate demand profile and maintain high-quality students. We expect that the discount will increase to the mid-30% range, which will be more in line with its competitors, from about 28% currently. Given that management plans to continue to produce surpluses during this process of investment, we do not believe it will materially weaken operating performance, although surpluses will be smaller than before. The university's revenue base is fairly concentrated with tuition and other student-generated revenues accounting for 87% of total operating revenues.

Financial resources

As of May 31, 2011, expendable resources were $331 million, equal to 77% of adjusted operating expenses and 163% of debt outstanding of $203 million, which we consider consistent with the rating category. Cash and investments of $524.5 million were 121% of operating expenses and 259% of debt. All of the university's debt is fixed rate, and the university does not have any swaps related to its debt. MADS is, in our view, very manageable at $16.6 million, or 3.8% of fiscal 2011 adjusted operating expenses. In light of capital needs on campus, management may issue $150 million of debt to build student residence halls in the next two to three years. We believe that this is a significant amount of debt that could weigh on the rating if there is not commensurate growth in financial resources. Additional capital needs on campus will likely be funded through proceeds from a pending capital campaign or operating cash.

In addition to a significant cash position of $145 million as of May 31, 2011, the university's long-term investments of $375.6 million (as of April 30, 2012) reflect a diverse allocation of assets: 25% domestic equities, 21% global equity, 13% hedge funds, 13% inflation hedging, 8% opportunistic, 8% alternatives, 10% U.S. bonds, and 1% cash. Management states that 58% of the portfolio is liquid on a daily basis and 90% is liquid on an annual basis – which we view as highly liquid. As of May 31, 2011, a majority (66%) of invested assets were classified as levels 1 and 2, which we consider to be a proxy for the relative liquidity of assets. The spending policy continues to be 5%, based on a three-year-rolling average market value.

Fundraising

The university successfully concluded a $300 million campaign in December 2007, raising $304 million. Management expects to start another comprehensive campaign within the next year to support its endowment, scholarships, and capital projects. The goal and timing remain confidential through the campaign's silent phase, but the goal is likely to be larger than the previous campaign. The university's annual fund has been growing modestly over the past few years, raising $6.4 million in fiscal 2011, up from $5.8 million in fiscal 2010. The alumni participation rate rose slightly in fiscal 2011 to 21%, and management expects a further increase.

Related Criteria And Research

USPF Criteria: Higher Education, June 19, 2007

Ratings Detail (As Of June 15, 2012)		
Delaware Cnty Auth, Pennsylvania		
Villanova Univ, Pennsylvania		
Delaware Cnty Auth (Villanova Univ) rev bnds ser 2005 (MBIA)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Delaware Cnty Auth (Villanova Univ) ser 2006 (AMBAC)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Delaware Cnty Auth (Villanova Univ) univ rev bnds ser 2010		
Long Term Rating	A+/Stable	Affirmed

Many issues are enhanced by bond insurance.