MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns A1 rating to Villanova University's (PA) $22 million of Series 2012 revenue bonds; outlook is stable

Global Credit Research - 05 Oct 2012

University will have $175 million of pro-forma rated debt

DELAWARE COUNTY AUTHORITY, PA
Private Colleges & Universities
PA

Moody's Rating

ISSUE	RATING
Villanova University Revenue Bonds, Series 2012	A1
Sale Amount $22,000,000	
Expected Sale Date 10/09/12	
Rating Description Revenue: 501c3 Unsecured General Obligation	

Moody's Outlook STA

Opinion

NEW YORK, October 05, 2012 --Moody's Investors Service has assigned an A1 rating to Villanova University's $22.0 million of fixed-rate Series 2012 revenue bonds expected to be issued through the Delaware County Authority and has affirmed the ratings on the university's outstanding bonds detailed in the RATED DEBT section of the report. The rating outlook is stable.

SUMMARY RATING RATIONALE

The A1 rating reflects Villanova University's solid market position and niche as a relatively large Catholic university with diverse program offerings, strong management team with sound fiscal management practices, healthy operating performance and cash flow providing good debt service coverage, and fixed rate debt structure. Counterbalancing these strengths are heavy reliance on student charges and strong competition from both private and public universities, as well as limited financial resources relative to A1-rated peers.

STRENGTHS

*Comprehensive private Catholic university located in suburban Philadelphia with a nationally recognized brand and notable programs. The university's market strength is demonstrated by commanding a high net tuition per student of $27,526 in FY 2012.

*Senior leadership team with strong management and governance practices evidenced through a comprehensive strategic planning process that includes integrating goals and metrics with realistic financial modeling, capital needs, and resources.

*Healthy operating performance with a cash flow margins averaging 10.1% from FY 2010-FY 2012 leading to healthy annual average debt service coverage of 3.5 times over the same period.

*Healthy unrestricted liquidity evidenced by $308.8 million of monthly liquidity providing 328.5 monthly days cash, or almost 11 months coverage of operating expenses and the university has all fixed rate debt.

*Favorable philanthropic support, raising an average of $26 million in gift revenue from FY 2010-FY 2012 compared to the Moody's FY 2011 median of $13 million for A-rated private universities colleges over FY 2009-FY 2011. The university is in the silent phase of a comprehensive campaign.

CHALLENGES

*Highly competitive student market, evidenced by moderate pressure on the freshmen yield, down to 24% in fall 2012 from 27% in fall 2009 and net tuition per student growth is flat from FY 2009 to FY 2012, indicating increased price sensitivity of families during the slow economic recovery.

*High dependence on student charges, which represent 83% of operating revenue, highlighting the importance for the university to grow net tuition revenue, which has slowed in recent years growing just 1.6% in FY 2012 from FY 2011.

*Moderate balance sheet relative to A1-rated peers with FY 2012 expendable financial resources of $257.4 million cushioning debt 1.39 times and operations 0.71 times.

*Growing postretirement benefit and pension costs which will continue to depress the university's net assets. The liability was $20.2 million as of May 31, 2009, growing to $32.2 million as of May 31, 2012.

DETAILED CREDIT DISCUSSION

USE OF PROCEEDS: Proceeds from the 2012 bonds will be used to refinance a portion of the Series 2003 bonds and pay costs of issuance for level net present value savings. There will be no extension of maturity.

LEGAL SECURITY: Unsecured general obligation pledge of the university. There is no debt service reserve fund.

DEBT STRUCTURE: Including the Series 2012 bonds, all of the university's debt will be fixed-rate.

DEBT-RELATED DERIVATIVES: None.

MARKET POSITION/COMPETITIVE STRATEGY: SOLID REPUTATION AS A LARGE COMPREHENSIVE CATHOLIC UNIVERSITY; LOCATED IN A HIGHLY COMPETITIVE GEOGRAPHIC REGION

Villanova, a Catholic university located in suburban Philadelphia on the "Main Line", offers a traditional liberal arts education as well as professional programs in engineering, business, nursing, and law. The university will continue to have a healthy market position given its diverse and well-regarded array of undergraduate and graduate programs. Management reports fall 2012 enrollment of 9,381 full-time equivalent (FTE) students, of which 70% are undergraduate.

The university's high net tuition per student, which measured $27,526 in FY 2012 reflects its solid position in a very competitive market, as well as the presence of professional graduate programs typically offering little to no tuition discount. We note, however, growth of net tuition per student has slowed and is essentially flat from its FY 2009 peak of $27,548, following average annual growth of approximately 7% from FY 2007- FY 2009.

Management expects stable enrollment in its undergraduate programs and modest growth in its graduate programs. The university added an on-line human resources graduate degree beginning in fall 2010 and an online masters of public administration in fall 2012, which has since bolstered total graduate enrollment despite enrollment declines at its law school. The law school represents just 9% of total enrollment and 30% of graduate enrollment in fall 2012. The declining trend of law students reflects the national trend among law schools. The university also plans to add an online nursing program for practitioners with associates degrees to earn their bachelors degree.

Despite slight weakening of demand indicators, we believe the university maintains a strong market and relatively stable enrollment management. First-year applications of 14,901 for fall 2012 were 3% below the peak in fall 2011, yet remain above prior years. The selectivity rate has remained relativity consistent over the past several years (45.6% in fall 2012) and along with general industry trends, the university's matriculation of admitted students has declined somewhat, yielding 27% in fall 2008 compared to 24% in fall 2012. However, first-time-freshmen enrollment has been consistent enrolling approximately 1,640 first-time freshmen each fall. Villanova competes with other strong institutions primarily in the northeast, including Boston College (rated Aa3, stable), Bucknell (rated Aa2, stable), Lehigh (rated Aa2, stable), and University of Richmond (rated Aa1, stable), which contributes to a lower yield rate given the university's selectivity. The university has a national profile, due largely to its successful athletic (basketball and football) programs. However, while approximately 85% of Villanova's student body are out-of-state students, its geographic draw remains concentrated, with 65% of undergraduate students from Pennsylvania, New Jersey, and New York. The university reports an increase in the percent of students from outside the northeastern states and in addition to a recruiter on the west coast has added a new recruiter in the southwest. The university's ability to increase its draw from states outside of the northeast, given declines in high school graduation rates, and into more demographically vibrant states would be credit positive.

OPERATING PERFORMANCE: OPERATING PERFORMANCE EXPECTED TO NARROW, BUT REMAIN HEALTHY; SOUND FINANCIAL STEWARDSHIP HAS DRIVEN POSITIVE OPERATING PERFORMANCE

Management's strong fiscal oversight and engrained conservative budgeting and planning practices have produced healthy operating performance, although this has narrowed in recent years given slower net tuition revenue growth. The university generated an 8.2% operating margin in FY 2012 (ended May 31) and has a robust average operating margin of 10.1% from FY 2010 to 2012. Operating cash flow margin was 14.8% in FY 2012, which produced healthy debt service coverage of 3.3 times. Although the FY 2013 budget includes a thinner operating surplus compared to the FY 2012 budget by approximately $4 million, management reports that 2013 FYTD operations already reflect a $2 million positive variance for net tuition revenue compared to the FY 2013 budget by exceeding its enrollment target and budgeted financial aid.

Villanova continues to be highly reliant on student charges, comprising 83% of the university's Moody's adjusted operating revenue, followed by 6% investment income, 5% gifts, 4% other revenue, and 2% grants and contracts. While the university has strong dependence on tuition and fees, Villanova benefits from some diversity within tuition revenue because of its mix of undergraduate, graduate, and continuing education students. At this time, the university's slower growth in net tuition per student and high dependence on tuition represents a vulnerability; however, management maintains flexibility to adjust spending and grow revenue that will enable the university to continue generating healthy operating results. We expect the university to continue generating operating surpluses exceeding budget. Management follows conservative budgeting practices, in line with what we consider best practices, including conservative enrollment assumptions, 4.5% endowment spend rate, fully budgeting for depreciation and debt service, as well as contingency reserves.

BALANCE SHEET POSITION: MODERATE BALANCE SHEET CUSHION TO DEBT AND OPERATIONS; LIMITED CAPACITY IN THE NEAR TERM FOR DEBT ISSUANCE ABSENT GROWTH IN FINANCIAL RESOURCES

Villanova's FY 2012 expendable financial resources of $257.4 million provide a modest but adequate cushion to debt and operations of 1.39 times and 0.71 times, respectively. The university's expendable financial resources declined nearly 12% from $292.2 million in FY 2011 to its current level through a combination of investment losses and drawdown on reserves for capital investment. While the university has built up its resources overtime through reinvestment of strong operating surpluses and fundraising, management has a practice of spending from reserves rather than issuing debt for capital projects. By Moody's calculation, unrestricted cash and investments which could be liquidated in one month were $308.8 million in FY 2012, which could cover a solid 328.5 days of the university's cash expenses.

While relatively modest compared to its asset base, we note that the university's financial resources are depressed by a postretirement benefit and pension liability, which grew from $20.2 million as of May 31, 2009 to $32.2 million as of May 31, 2012 . The defined benefit plan has been closed since 1999. For the postretirement benefit cost the university pays a fixed $1,300 per participant annually.

At May 31, 2012, the university's FY 2012 investment return was negative 6.0% with an endowment of $357.2 million allocated as follows: 25% domestic equity, 22% hedge and opportunistic funds, 20% international equity, 12% fixed income, 11% commodities, 8% private equity, 7% opportunistic, 2% cash, and 1% real estate. The university's investment advisor is Cambridge & Associates. For FY 2013, the investment return as of June 30, 2012 investment return was negative 2.5%.

The university is in the silent phase of a comprehensive campaign with the last comprehensive campaign concluding in 2007, which achieved its $300 million goal. The goal has not yet been established for the next campaign. Gift revenue has grown each year from $20 million in FY 2009 to $28 million in FY 2012. Funds raised from the campaign will finance the broad initiatives set forth in the university's 10-year strategic plan adopted for FY 2010 to elevate the university's stature nationally with a focus on raising funds for the endowment and facilities. Growth in the university's endowment is an important credit factor. Total financial resources per student were $47,356 in FY 2011 ($44,987 in FY 2012) compared to a FY 2011 median of $59,145.

The university has invested considerably in the campus since its $50 million debt issuance in 2006 reflected in averaging a relatively high capital spending ratio of 2.5 times over FY 2007-2012. While capital spending has tapered off since 2009 after completing construction of buildings for the college of nursing and school of law, recent capital projects include renovation of dining facilities and residence halls, as well as construction of a pedestrian friendly campus. The bulk of these more recent projects have been funded through reserves from retained operating surpluses.

Potential future debt plans include a significant capital project with a project cost estimated at $250 million with a potential borrowing currently contemplated at approximately $150 million. The project includes construction of residence halls adding approximately 1,100 beds and a retail component, a parking structure, and a performing arts center on land adjacent to campus. The land is currently occupied by parking lots used for campus parking. There has been community resistance to the project, which must receive approval from the township. Given the uncertainty of approval for the project, as well as timing, size, and scope, we have not incorporated the potential debt issuance into the current rating. However, a sizeable debt issuance would likely pressure the rating or the outlook without compensating revenue and balance sheet growth, as well as continued strong operating performance.

MANAGEMENT AND GOVERNANCE: STRONG SENIOR LEADERSHIP TEAM

The university's healthy financial standing are attributable to management's strong oversight and multi-year planning. The university's conservative budget assumptions and multi-year financial plans have allowed the university to consistently exceed internal financial forecasts, as well as produce healthy operating performance amid challenges experienced in the private higher education institutions since the most recent economic downturn. Management's ability to consistently produce healthy and consistent operating surpluses demonstrates conservative budgeting practices, which is credit positive, but has been key to investing in campus facilities with a manageable use of debt. Investing in facilities is one important component in maintaining a healthy market position in a highly competitive market environment.

The university is governed by a board of trustees, consisting of not less than 20 nor more than 40 members elected for staggered terms with no fewer than nine members of the Augustinian Order. Board membership terms are five years and board members serving two successive terms may be reelected after at least a one year hiatus from the board. The board meets a minimum of five times per year. The board is currently composed of 34 voting members with various professional experiences to serve the university.

OUTLOOK

The stable outlook reflects our expectation of ongoing positive operating performance and strong debt service coverage, stable enrollment with continued growth in net tuition revenue, and that there would be growth in balance sheet resources with any significant additional debt.

WHAT COULD CHANGE THE RATING UP

Maintaining a solid market position accompanied by substantial increase in financial resources; continued healthy operating performance and strong debt service coverage; increased gift revenue; improved revenue diversity

WHAT COULD CHANGE THE RATING DOWN

Deterioration in operating performance, particularly if accompanied by weakening of student demand; decline in financial resources; additional borrowing absent commensurate growth in financial resources

KEY INDICATORS (FY 2012 financial data, fall 2012 enrollment data)

Full-Time Equivalent Enrollment: 9,381 students

Primary Selectivity: 45.6%

Primary Matriculation: 24.2%

Net Tuition per Student: $27,526

Educational Expenses per Student: $30,363

Average Gifts per Student: $2,728

Total Cash and Investments: $512.6 million

Total Direct Debt: $185.1 million

Total Comprehensive Debt*: $231.8 million

Expendable Financial Resources to Direct Debt: 1.39 times

Expendable Financial Resources to Operations: 0.71 times

Monthly Days Cash on Hand: 328.5 days

Monthly Liquidity to Demand Debt: Not applicable

Operating Revenue: $393.1 million

Operating Cash Flow Margin: 14.8%

Three-Year Average Debt Service Coverage: 3.48 times

Reliance on Tuition and Auxiliaries Revenue (% of Moody's Adjusted Operating Revenue): 83.1%

* Comprehensive Debt includes direct debt, operating leases, and pension obligation.

RATED DEBT:

Series 1998A and Series 2005: A1; Insured by National Public Finance Guarantee Corp (Formerly MBIA)

Series 2003: A1; Insured by FGIC

Series 2006: A1; Insured by AMBAC

Series 2010 and 2012: A1

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PRINCIPAL RATING METHODOLOGY

The principal methodology used in this rating was U.S. Not-for-Profit Private and Public Higher Education published in August 2011. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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