

Research

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

Primary Credit Analyst:

Carolyn McLean, New York (1) 212-438-2383; carolyn.mclean@standardandpoors.com

Secondary Contact:

Stephanie Wang, New York (1) 212-438-3841; stephanie.wang@standardandpoors.com

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Credit Profile

US\$150.0 mil Villanova University Revenue Bonds (Villanova University) (Lancaster Avenue Project) ser 2015

Long Term Rating

A+/Stable

New

Villanova Univ ICR

Long Term Rating

A+/Stable

Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'A+' rating to Delaware County Authority, Pa.'s series 2015 bonds, issued on behalf of Villanova University. At the same time, we affirmed the 'A+' long-term rating, issuer credit rating (ICR), and underlying rating (SPUR) on the university's outstanding debt. The outlook on all ratings is stable.

The rating reflects the university's consistent operating surpluses and solid margins. The university's demand and enrollment are consistent, and financial resources are strong.

The university is issuing approximately \$138 million in new-money debt to construct several residence halls on campus. We believe that although the additional debt is significant, the university can absorb the debt at the current rating level.

The rating reflects our view of the university's:

- Historically strong student demand, as demonstrated by stable enrollment, good demand flexibility, and good student quality;
- Strong financial operations with consistently good operating surpluses on a full accrual basis, with a 5% margin in fiscal 2015 and good growth in net tuition and fee income, as well as prudent fiscal management;
- Solid financial resources for the rating category, with expendable resources of \$489 million in fiscal 2015 (May 31 year-end) equal to 101% of adjusted operating expenses and 163% of pro forma debt; and
- Average maximum annual debt service (MADS) burden of approximately \$25.3 million, equal to 5.2% of fiscal 2015 adjusted operating expenses, and predictable, conservative, front-loaded fixed-rate debt structure.

Partially offsetting factors include:

- Limited revenue diversity, with more than 87% of gross revenues in fiscal 2015 coming from student-generated revenues (tuition, fees, and auxiliaries); and
- Significant debt issuance associated with a residence-hall construction project.

The university is undertaking a project to construct residential halls for undergraduate students, a parking facility, a performing arts center, and a pedestrian bridge on the site of a surface parking lot on campus. The series 2015 bonds

are being issued to partially fund the construction of the residential halls and the parking facility, the rest of which will be funded with university equity. The pedestrian bridge is expected to be funded with a grant from the Commonwealth of Pennsylvania and the performing arts facility will be funded entirely with philanthropy. The new residence halls will add approximately 1,150 beds. Including existing residence halls, the facilities will be able to house about 85% of all undergraduate students. We believe that once the residence halls are completed, they will generate additional cash flow that will likely cover the debt service and operating expenses of the dorms starting in 2019.

The bonds are secured by a general obligation of the university and will amortize over 30 years. Postissuance, the total debt will be approximately \$300 million, all of which is fixed rate and a general obligation of the university. We do not anticipate that the university will issue additional debt beyond the series 2015.

Villanova University is an independent, coeducational institution in Radnor Township, about 14 miles west of Philadelphia. Founded in 1842 by the Augustinian Order of the Roman Catholic Church, 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 2014, total enrollment was 10,544, 66% of which 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 and 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 university will not issue additional debt beyond the series 2015 in the near term.

Downside scenario

Factors that could result in a negative rating action are weakened operating performance, significant deterioration of financial resource ratios, weakening of the demand profile, or debt issuance beyond the series 2015 bonds.

Upside scenario

A positive rating action over the two-year outlook period is unlikely due to the recent debt issuance, although factors that could result in a positive action are a significant improvement in financial resource ratios to the level of 'AA' category medians and continued strong operating performance with margins close to 5%. We also would expect enrollment and demand to remain stable.

Enterprise Profile

Enrollment and demand

The university has a strong demand profile, characterized by a stable applicant pool, a good level of selectivity, high retention rates, and good student quality. Selectivity was slightly weaker than the five-year average of 47%, at approximately 49% for fall 2014, and matriculation was also somewhat weak at 22%, although student quality improved with average SAT scores of approximately 1315. Management states that given improved student quality, some softening in selectivity and matriculation was expected. We do not believe this is a concern as the university

continues to demonstrate significant demand flexibility that supports the current rating. Preliminary fall 2015 metrics indicate higher applications and strong demand metrics, as well as a slightly higher enrollment. We expect demand to remain strong over the next few years.

Overall enrollment has been stable in the last few years, with enrollment of 10,544 in fall 2014, or 9,677 full-time equivalents. Undergraduate enrollment was 6,927 as of the same date and in line with historic levels. Management indicates that its on-campus housing is close to capacity, and that it plans to keep full-time undergraduate enrollment at the current level. Student retention continues to be very strong in our view, with approximately 94% of freshmen returning for their sophomore year in fall 2014.

Following the launch of several online programs in the last two years, graduate enrollment has increased, a trend management expects to continue over the next few years. At the same time, law school enrollment has declined, reflecting the reduced demand for law school programs nationally. Overall graduate and professional enrollment rose slightly in fall 2014 to 3,617 students, of whom 3,075 were graduate students and 542 were law students. The law school has contracted in size in the past few years as a result of the weakened law school market, but quality is unchanged, with the number of applications up slightly for fall 2015.

Management

The management team has been quite stable in the past five years. The president has been in place for nine years and the finance team for over 10 years. The university recently hired an investment manager who will oversee the endowment. 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. Management allocates a portion of surpluses into cash reserves and the quasi endowment annually, which we view positively. The university has investment and debt policies, which we also view favorably as a key credit strength.

Financial Profile

Operating performance

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 with surpluses of 5%-7% in the past five fiscal years. For the fiscal year ended May 31, 2015, the university produced an operating surplus of \$24.5 million (or 5% of fiscal 2015 adjusted operating expenses) compared with \$24.8 million surplus (5.7% margin) in fiscal 2014. The long-term plan calls for slimmer, but still robust, margins of approximately 5% over the next five years as the university fulfills its strategic plan related to affordability. We believe that the university's strong and consistent operating surpluses are key to the rating and expect them to continue for the next few years.

Villanova consistently budgets for operating surpluses and planned savings for endowment although actual results generally exceed budget. 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 review its financial aid strategy to build the undergraduate demand profile and maintain high-quality students. We expect that the discount rate may 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, 2015, expendable resources were \$489 million, up 8% from a year earlier, which is equal to 101% of adjusted operating expenses and 163% of pro forma debt, which we consider solid for the rating category. Cash and investments also increased 14%, to \$757 million, equal to 156% of operating expenses and 252% of pro forma debt. Due to the university's policy of investing approximately 50% of its annual operating surplus back into the endowment, financial resources will continue to grow over the next few years. Given the growth in resource ratios, we believe that the university will be able to absorb the additional debt.

In addition to a significant cash position of \$187 million as of May 31, 2015, the university's long-term investments of \$563 million reflect a diverse allocation of assets: 25% domestic equities, 27% global equity, 19% hedge funds, 7% inflation hedging, 3% opportunistic, 9% private capital-growth assets, 6% U.S. bonds, and 5% cash. Management states that 40% of the portfolio is liquid on a daily basis, 63% on a monthly basis, and 85% is liquid on an annual basis. We consider such a portfolio highly liquid. The spending policy continues to be 5%, based on a three-year-rolling-average market value. We believe that the endowment is invested conservatively and that the spending rate is sustainable.

Fundraising

The university recently announced a capital campaign to raise \$600 million; to date it has received approximately \$435 million in pledges, \$251 million of which has been collected in cash. The campaign aims to raise \$250 million for the endowment, including scholarships, \$125 for academic priorities, \$150 million for capital projects, and \$75 million for the annual fund. This campaign is approximately double the amount raised in the campaign that ended in 2007. We believe that the receipt of funds over the next few years will continue to buoy the university's balance sheet, and we expect the university to reach its goal.

Villanova University, PA						
	--Fiscal year ended May 31--					Medians
	2015	2014	2013	2012	2011	Private Colleges & Universities 'A' 2014
Enrollment and demand						
Headcount	10,544	10,492	10,380	10,467	10,482	MNR
Full-time equivalent	9,677	9,563	9,381	9,477	9,508	3,434
Freshman acceptance rate (%)	49.3	48.9	45.6	44.0	45.1	64.5
Freshman matriculation rate (%)	21.6	22.7	24.2	24.3	25.4	21.2
Undergraduates as a % of total enrollment (%)	65.7	65.2	66.0	66.1	66.7	80.9
Freshman retention (%)	93.7	94.0	94.0	94.2	94.8	86.3
Graduation rates (five years) (%)	N.A.	87.6	89.9	89.0	89.9	74.9

Villanova University, PA (cont.)

Income statement

Adjusted operating revenue (\$000s)	508,657	463,358	486,617	471,254	464,112	MNR
Adjusted operating expense (\$000s)	484,185	438,570	465,283	449,371	432,437	MNR
Net operating income (\$000s)	24,472	24,788	21,334	21,883	31,675	MNR
Net operating margin (%)	5.05	5.65	4.59	4.87	7.32	MNR
Change in unrestricted net assets (\$000s)	18,709	46,974	53,611	(6,138)	59,322	MNR
Tuition discount (%)	28.3	19.5	27.1	25.3	24.4	35.4
Tuition dependence (%)	74.2	71.5	73.7	74.1	73.1	MNR
Student dependence (%)	86.9	85.5	87.6	88.1	87.2	MNR
Healthcare operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	1.3	1.4	1.3	1.6	2.2	MNR
Endowment and investment income dependence (%)	3.8	3.8	3.3	1.8	1.9	MNR

Debt

Outstanding debt (\$000s)	165,662	173,544	183,866	193,597	202,601	90,765
Proposed debt (\$000s)	134,280	N.A.	N.A.	N.A.	N.A.	MNR
Total pro forma debt (\$000s)	299,942	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma MADS	25,283	N.A.	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	3.54	3.97	3.40	3.91	3.84	4.00
Current MADS burden (%)	3.34	3.68	3.57	3.70	3.85	MNR
Pro forma MADS burden (%)	5.22	N.A.	N.A.	N.A.	N.A.	MNR

Financial resource ratios

Endowment market value (\$000s)	563,866	501,483	425,793	357,022	375,061	218,129
Cash and investments (\$000s)	757,344	666,089	576,956	512,452	524,532	MNR
Unrestricted net assets (\$000s)	481,620	462,911	415,937	362,326	368,464	MNR
Expendable resources (\$000s)	489,053	454,634	371,457	294,731	330,813	MNR
Cash and investments to operations (%)	156.4	151.9	124.0	114.0	121.3	150.6
Cash and investments to debt (%)	457.2	383.8	313.8	264.7	258.9	266.7
Cash and investments to pro forma debt (%)	252.5	N.A.	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	101.0	103.7	79.8	65.6	76.5	97.9
Expendable resources to debt (%)	295.2	262.0	202.0	152.2	163.3	172.6
Expendable resources to pro forma debt (%)	163.0	N.A.	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	15.9	15.1	15.1	14.5	13.6	13.3

.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

USPF Criteria: Higher Education, June 19, 2007

Ratings Detail (As Of September 10, 2015)		
Delaware Cnty Auth, Pennsylvania		
Villanova Univ, Pennsylvania		
Delaware Cnty Auth (Villanova University) Series 2005		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Delaware Cnty Auth (Villanova University) Series 2006		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Delaware Cnty Auth (Villanova University) 2010		
<i>Long Term Rating</i>	A+/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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