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Ratings

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University of St. Thomas, Texas; Public Coll/Univ - Unlimited Student Fees

Primary Credit Analyst:
Laura A Kuffler-Macdonald, New York (1) 212-438-2519; laura.kuffler.macdonald@spglobal.com

Secondary Contact:
Steven Sather, Centennial; steven.sather@spglobal.com

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Credit Profile		
US$40.0 mil taxable bnds ser 2020 due 06/30/2060		
Long Term Rating	BBB+/Negative	New

Rationale

S&P Global Ratings assigned its 'BBB+' rating to the series 2020 taxable revenue bonds issued for the University of St. Thomas (UST), Texas. The outlook is negative.

We assess UST's enterprise profile as strong, with a growing undergraduate enrollment and solid matriculation rates, and despite continued declines on the graduate enrollment side. This has led to healthy increases in overall full-time equivalent (FTE) enrollment; however, the tuition discount has been rising and net tuition revenues remain pressured. We assess the university's financial profile as adequate, with a history of full-accrual deficit operations and solid available resource metrics relative to medians. Should UST not return to break-even operations by 2021, we could lower the rating. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'bbb+' and a long-term rating of 'BBB+'.

In particular, the rating reflects our view of the following credit weaknesses:

- A history of deficit operations on a full-accrual basis;
- Pressured net tuition revenues as a result of increasing tuition discount rates and declining graduate enrollment;
- A competitive market, with larger public universities offering lower tuition rates; and
- A narrow geographic draw, because a majority of the students come from the Houston region.

Somewhat offsetting the above weaknesses is our view of the university's:

- Modest pro forma maximum annual debt service (MADS) burden of 2.34% for fiscal 2019;
- No near-term additional debt plans beyond the current issue; and
- Increased FTE students totaling 2,520 for fall 2019, a 4.7% increase over the prior year.

Bond proceeds will be used to refund all debt outstanding and provide $8 million for various strategic capital projects. All bonds are a general obligation of the university.

UST is a co-educational Catholic university in the Museum District of Houston and was founded by the Basilian Fathers in 1947. It offers degrees in more than 39 subject areas; master's degrees in 22 subject areas; and doctorates in philosophy, education, and nursing.

Outlook

The negative outlook reflects that during our two-year outlook period we could lower the rating to 'BBB' if UST's operating deficits persist or available resources continue to decline.

Upside scenario

Should the university work to improve its full-accrual-based deficits and achieve break-even operations by fiscal 2021, and graduate enrollment stabilizes, while maintaining available resources, we could revise the outlook to stable.

Enterprise Profile

Industry risk

Industry risk addresses the higher education sector's overall cyclicality and competitive risk and growth by applying various stress scenarios and evaluating barriers to entry, levels and trends of profitability, substitution risk, and growth trends observed in the industry. We believe the higher education sector represents a low credit risk when compared with other industries and sectors.

Economic fundamentals

In our view, UST has limited geographic diversity, with approximately 89% of students coming from Texas. Therefore, the state of Texas' GDP per capita anchors our assessment of the university's economic fundamentals.

Market position and demand

Following a few years of lower enrollment (some of which management attributes to a decline in graduate programs), UST opened a few new programs, including the re-establishment of its school of nursing's bachelor's program, which have attracted additional students. Graduate enrollment remains stressed, with education and business programs seeing the most declines. Management actively evaluates the viability of the university's program mix and makes adjustments as necessary, which we view as a credit strength.

After several years of total headcount declines, the university has seen an increase during the past two years, driven by undergraduate admissions. Fall 2018 and 2019 headcount rose 2.4% and 6.3%, respectively. Total headcount for fall 2019 was 3,523. On an FTE basis, enrollment had been flat but also increased the past two years. FTE rose 4.7% to 2,520 students, compared with 2,408 in fiscal 2018. The undergraduate side of UST has seen steady enrollment growth on an FTE basis. For fall 2019, FTE undergraduate enrollment was 1,859, a 7.3% increase compared with the prior year, and we expect continued growth for fall 2020.

Graduate-level FTE enrollment fell in fall 2019 by 2.5% to 655 students, from 672 in fall 2018. Management has introduced new areas for its MBA program, expanded its nursing programs, and restructured some of the tuition for its master's of liberal arts to attract more students. We expect that graduate enrollment will stabilize.

Approximately 61.9% of students are undergraduates. While UST is not selective, with an acceptance rate of 89.1% (typical of schools with large commuter bases), students are somewhat self-selective with their applications, as the university's good 34.9% matriculation rate indicates. Student quality measures are mixed, with an above-average retention rate (84%) and ACT (23) but a six-year graduation rate of 68%, which is low for the rating category. Average tuition for fall 2019 decreased 6.7% to $30,800 due to a transition from a per credit hour tuition system to a banded tuition system. Overall, tuition is comparable with that of regional peers.

Fundraising

Management completed its capital campaign in 2017, which raised $145 million for a new science building. The alumni giving rate is low at less than 8.2%, but overall annual giving has been good, in our view, with $8.12 million raised in 2019.

Management and governance

A 35-member board of directors governs UST, led by Dr. Richard Ludwick as president. Other than normal rotations, there have been no recent changes to the board of directors. We expect no significant changes to the board other than normal rotations.

Dr. Ludwick began his term as president on July 1, 2017. With Dr. Ludwick's presidency, UST had some turnover in management, in finance, enrollment, institutional advancement, and marketing. All of these positions have been filled and we expect to see stability in the management team. Dr. Ludwick and his team presented the strategic plan's framework to the board, which approved it in June 2018. The plan calls for addressing UST's rising operating deficits by increasing investments in infrastructure and marketing to boost enrollment, and focusing on increasing retention and graduation rates. The plan includes a bridge plan to incorporate fundraising goals to fund the projected financial shortfalls and new initiatives to boost enrollment. We believe the plan presents challenges in terms of stabilizing the graduate student body, which is required to increase net tuition revenues.

Financial Profile

Financial management policies

UST has a formal policy for investments. It operates according to a five-year strategic plan. The university meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there may be some areas of risk, the organization's overall financial policies are not likely to negatively affect its future ability to pay debt service. Our analysis of financial policies includes a review of the organization's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure, and a comparison of these policies with those of similar providers.

Financial performance

As is typical for a private university, UST is highly student-dependent, with about 78.6% of total revenues coming from tuition and auxiliaries, 9.3% from gifts, 1.5% from grants and contracts, and 5.5% from investment and endowment income. Historically, operations were positive; however, beginning in fiscal 2013, the university reported break-even operations. Subsequently, it has had full-accrual deficit operations. For fiscal 2019, UST reported a full-accrual operating deficit of $3.5 million, or a negative 3.8% margin. While the operating deficit has continued to increase, management expects fiscal 2021 to result in break-even operating performance. Operations have always been positive on a cash basis. Management attributes the operating deterioration to graduate enrollment declines and greater faculty expenses due to the conversion of some of its faculty to full-time from part-time, because of a regional accreditation standard. The tuition discount rate, while in line with the median for the rating category, in our view, has been increasing, and reached 40.3% of tuition and fees in fiscal 2019. UST projects its operating budget for fiscal 2020 will result in a break-even performance on a cash basis. In 2017, the board approved a two-year restructuring plan for fiscal years 2019 and 2020, which resulted in full-accrual deficits and increased investments in new initiatives that the university expected to finance through fundraising. However, with a shortfall in fundraising, the board authorized a one-time endowment spend above 5% to 6.0% for fiscal 2019. In fiscal 2020, management has identified approximately $5 million in cost savings that is expected to impact fiscal 2021's financial performance, resulting in a return to break-even operations on a full-accrual basis. The endowment spend rate is also expected to decline to 5% for fiscal 2021 as a result of these initiatives. We expect that management will reduce its endowment draw and will work to improve operations over the medium term.

Available resources

In fiscal 2018's audited financial statements, management reclassified $5.0 million in permanently restricted assets as temporarily restricted assets. This accounting error resulted in available resources increasing in two of the past three years. Available resources, as measured by expendable resources, increased significantly in fiscal 2018 to $42.1 million from $37.8 million in fiscal 2017 as a result of this re-classification. For fiscal 2019, expendable resources were $42.7 million and equaled 45.2% of operations and 106.8% of pro forma debt. These ratios are in line with those of rating category medians. Absent growth in balance sheet metrics, additional debt could pressure the rating. We expect management to work to continue to improve its balance sheet metrics.

The endowment has increased due to positive fundraising results and positive investment performance in recent years. The endowment had a market value of approximately $106.6 million as of June 30, 2019, compared with $102.4 million as of fiscal 2018. Investments were 71% in equity, 15% in fixed income, and 14% in diversifying strategies, as of June 30, 2019. The endowment spending rate policy is 5% of a 12-quarter moving average of the endowment assets, but in fiscal 2019 the board authorized a 6% draw to fund strategic initiatives. In fiscal 2019, the endowment draw was $5.0 million, which was only 5.5% of total university revenues for the year.

Debt and contingent liabilities

The university plans to refinance its entire debt portfolio and incur approximately $8.0 million in additional debt. This would result in total pro forma debt increasing to $40 million. The $8 million in additional debt would be used to help fund strategic capital projects. The planned refinancing would result in extending the maturity of debt outstanding to 2060 as compared to 2028. This resulted in a lower debt burden with a modest pro forma debt burden of 2.34% of fiscal 2019's operating expenses. The various bonds and loans that are currently outstanding were collateralized by property and some debt had debt service and liquidity covenants and had some bullet maturities. The university has been in compliance with all of its covenants. However, with this issue, all debt will be a general unsecured obligation of the university and there are no specific liquidity or debt service covenants. Management does not have any other additional debt plans over the outlook period.

University Of St. Thomas, Texas -- Enterprise And Financial Statistics

	--Fiscal year ended June 30--					--Medians for 'BBB' rated private colleges and universities--
	2020	**2019**	**2018**	**2017**	**2016**	**2018**
Enrollment and demand						
Headcount	3,523	3,314	3,237	3,312	3,411	MNR
Full-time equivalent	2,520	2,408	2,277	2,271	2,255	2,700
Freshman acceptance rate (%)	89.1	82.2	80.9	77.4	78.0	71.4
Freshman matriculation rate (%)	34.9	35.5	34.4	38.0	35.6	MNR
Undergraduates as a % of total enrollment (%)	61.9	61.8	57.6	54.8	52.9	74.1
Freshman retention (%)	84.0	82.0	85.0	82.0	83.0	78.8
Graduation rates (six years) (%)	68.0	57.0	60.0	58.0	57.0	MNR
Income statement						
Adjusted operating revenue ($000s)	N.A.	90,896	85,079	82,611	79,656	MNR
Adjusted operating expense ($000s)	N.A.	94,433	86,787	84,110	81,912	MNR
Net operating income ($000s)	N.A.	(3,537)	(1,708)	(1,499)	(2,256)	MNR
Net operating margin (%)	N.A.	(3.75)	(1.97)	(1.78)	(2.75)	(0.60)
Change in unrestricted net assets ($000s)	N.A.	(689)	3,026	12,638	14,107	MNR
Tuition discount (%)	N.A.	40.3	35.9	33.1	29.1	40.8
Tuition dependence (%)	N.A.	73.7	75.8	76.7	77.4	MNR
Student dependence (%)	N.A.	78.6	80.5	81.3	82.1	89.4
Health care operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	N.A.	1.5	2.0	2.2	2.6	MNR
Endowment and investment income dependence (%)	N.A.	5.5	4.2	4.3	4.3	MNR
Debt						
Outstanding debt ($000s)	N.A.	31,220	32,565	34,986	26,893	57,739
Proposed debt ($000s)	N.A.	40,000	N.A.	N.A.	N.A.	MNR
Total pro forma debt ($000s)	N.A.	40,000	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	2,207	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	8.05	7.05	8.13	3.15	MNR
Current MADS burden (%)	N.A.	8.20	10.20	3.35	3.46	4.00
Pro forma MADS burden (%)	N.A.	2.34	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value ($000s)	N.A.	106,589	102,369	93,315	81,789	77,239
Cash and investments ($000s)	N.A.	113,544	112,434	103,728	91,359	MNR
Unrestricted net assets ($000s)	N.A.	92,822	93,511	90,485	77,847	MNR
Expendable resources ($000s)	N.A.	42,707	42,146	37,821	42,980	MNR
Cash and investments to operations (%)	N.A.	120.2	129.6	123.3	111.5	82.6

University Of St. Thomas, Texas -- Enterprise And Financial Statistics (cont.)						
	--Fiscal year ended June 30--					--Medians for 'BBB' rated private colleges and universities--
	2020	2019	2018	2017	2016	2018
Cash and investments to debt (%)	N.A.	363.7	345.3	296.5	339.7	166.5
Cash and investments to pro forma debt (%)	N.A.	283.9	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	45.2	48.6	45.0	52.5	49.7
Expendable resources to debt (%)	N.A.	136.8	129.4	108.1	159.8	89.4
Expendable resources to pro forma debt (%)	N.A.	106.8	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	16.5	15.6	18.5	17.2	15.0

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.