Gwynedd Mercy University, Pennsylvania; Private Coll/Univ - General Obligation

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Pennsylvania Higher Educl Facs Auth (Gwynedd Mercy Univ)		
Long Term Rating	BBB/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'BBB' rating on the Pennsylvania Higher Educational Facilities Authority's debt issued for the Gwynedd Mercy University (GMERCYU) and affirmed its 'BBB' rating on the series 2017PP2 Montgomery County Higher Education and Health Authority's revenue bonds issued on behalf of the Assn. of Independent Colleges and Universities of Pennsylvania Financing Program for GMERCYU. The outlook on all ratings is stable.

As of fiscal year-end 2018, the university had $22.3 million in fixed-rate debt and $18.7 million in weekly variable-rate debt that has an associated letter of credit (LOC). We understand that the university plans to convert its weekly rate 2017V1 bonds, currently rated 'AA-/A-1+' and backed by an LOC, to term mode bonds with no credit enhancement for periods of two to five years. Upon conversion to term mode, the rating on the bonds will be 'BBB'. The bonds will consist of subseries 2017V1A, 2017V1B, and 2017V1C and will comprise two series of $6 million and one series of $6.7 million, with no more than one subseries coming due in any one year, minimizing remarketing risk. Upon conversion to the term mode, the university intends to terminate its current LOC associated with the weekly rate mode. We believe the term conversions are manageable, given that no more than $6.7 million will be subject to tender in any year, and the university maintains access to liquid resources in excess of $27.3 million to cover any failed remarketing. The remarketed bonds will be secured solely by the pledged revenue of the university, which we consider equivalent to a general obligation of the university.

We assessed GMERCYU's enterprise profile as strong, characterized by growing full-time-equivalent (FTE) enrollment over the past five years and a generally improving demand profile, though we expect growth to flatten over time, with good growth in applications and an improving selectivity rate. We assessed the financial profile as adequate, characterized by improved operations with a full-accrual surplus recorded for fiscal 2018, as well as sufficient balance sheet resources for the rating category. Despite these strengths, we recognize that GMERCYU has a relatively high maximum annual debt service (MADS) burden that includes operating leases. Combined, we believe these credit factors lead to a 'bbb' indicative stand-alone credit profile and 'BBB' long-term rating.

The 'BBB' rating reflects our assessment of GMERCYU's strengths, including:

- Fifth consecutive year of FTE enrollment growth, with fall 2018 reaching a new peak of enrollment for the university;

- Sufficient available resources to operations and debt for the rating category, with $40.1 million in expendable resources equivalent to 52% of operations and 98% of debt; and
- History of positive operating performance, driven by robust growth in net tuition revenue, a lower tuition discount rate than those of peers, and decreased reliance on endowment draws.

The rating also reflects our assessment of GMERCYU's weaknesses, including its:

- Relatively high MADS burden of 6.1% of fiscal 2018 adjusted operating expenses when operating leases are considered;
- Very high dependence on student-generated revenue, with the university deriving nearly 95% of revenue from student-generated sources in fiscal 2018; and
- Softening matriculation rate, which has potential to pressure discount rate and net tuition revenue, despite strengthening of other demand metrics.

The Sisters of Mercy founded GMERCYU in 1948 as Gwynedd-Mercy Junior College. In 1963, the college amended its charter to grant bachelor's degrees in arts and science and changed its name to Gwynedd-Mercy College. It achieved university status in September 2013. Today, it is on a suburban campus in the Philadelphia metropolitan statistical area (MSA), where it operates as a coeducational, four-year Catholic institution that offers traditional undergraduate education, adult accelerated-learning programs, and several graduate programs.

Outlook

The stable outlook reflects our expectation that, over the two-year outlook period, GMERCYU's enrollment will continue to grow, though at a slower pace than in the recent past. We also expect the university will continue to improve its demand metrics, and will generate at least break-even operating results, while maintaining or growing available resources as measured by expendable resources. We also expect that the university will not issue any additional debt without commensurate growth in available resources.

Upside scenario

We could consider a positive rating action during the outlook period if GMERCYU continues to improve retention, selectivity, and matriculation while at least maintaining enrollment. At the same time we would expect continued full-accrual operating surpluses, continued growth of available resources, and decreases to the university's relatively high MADS burden.

Downside scenario

We could consider a negative rating action in the next two years if the university's enrollment declined or operations deteriorated, available resources were to weaken, or additional debt were issued without commensurate growth in resources.

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, GMERCYU has limited geographic diversity with approximately 87% of students coming from the local market. Although management indicates the university plans to expand its market reach beyond the Philadelphia MSA, we expect GMERCYU to remain a largely regional university. Therefore, the commonwealth of Pennsylvania GDP per capita anchors our assessment of the university's economic fundamentals.

Market position and demand

Nursing is GMERCYU's niche program, and its largest. Nursing accounts for 56% of the university's full-time undergraduate enrollment. However, the university has begun to diversify program offerings adding a bachelor in social work in 2017, a master's of science in occupational therapy in 2018, and programs in family nurse practitioner and digital communication to start later in 2019. We note that though nursing accounts for a majority of enrollment, GMERCYU is associated with 70 hospitals and more than 90 health care affiliates in the Delaware Valley, eastern Pennsylvania, and New Jersey with respect to its educational programs in the nursing and allied health fields.

FTE enrollment reached a new peak of 2,719 students in fall 2018. We note that in each year over the last five years FTE enrollment has grown, attributed in part to GMERCYU's niche nursing and health care programs. From fall 2014 to fall 2018, FTE enrollment grew an impressive 16%, though we note FTE enrollment growth of only 0.6% in one of those years. We expect that FTE enrollment at the university will continue to grow, but expect that any gains in enrollment will be smaller than those gains of the recent past.

Applications have increased by an impressive 53% from fall 2014 to fall 2018. Part of this growth is attributed to a decrease in applications during fall 2014 and 2015 coupled with significant increases in the three following years. Management reports the initial drop was due to a concerted effort to focus on students who are a better fit for the school rather than to raise the overall number of applications. Applications increased from fall 2016 due to GMERCYU purchasing additional names to increase the first-time full-time traditional student population, and in 2017 and 2018, they increased due to enhanced digital marketing. In our view, other demand metrics, such as selectivity and matriculation, are good for the rating category. Selectivity has improved over a five-year period to 60.9% in fall 2018 from 66.7% in fall 2014 due to an increasing applicant pool, and we would view further improvement in selectivity favorably. The matriculation rate has shown an overall trend of weakness over a five-year period, totaling 26.5% in fall 2014, peaking at 31.2% in fall 2015, and then dropping to 24.9% as of fall 2018. The matriculation rate indicates that GMERCYU faces competition with area schools. Student quality, measured by test scores, improved over five-year period, with the average SAT score increasing to 1010 from 953. These scores are now more in line with national averages.

GMERCYU completed a major capital campaign to raise $24 million in December 2014, surpassing its goal, receiving $27.3 million in pledges. GMERCYU reports it has started another miniature campaign, with a goal of $8 million within the next two years. As of Feb. 28, 2019, it reports it had surpassed this goal, having raised $8.3 million. The campaign supports academic excellence, student life, and other opportunities for students.

Management and governance

A stable and active board of trustees governs GMERCYU and supports its mostly long-tenured executive management team. We understand the board has not experienced turnover beyond normal rotations. The senior management team has historically been stable. Deanne Horner D'Emilio, JD, became the sixth president in August 2017. The recent opening in the vice president for academic affairs position was filled by Dr. Mary Van Brunt in July 2018. She brings experience in both education and corporate finance, which we view as a strength to the management team. Additionally, in July 2018, the vacant vice president for student services & campus life position was filled by Joshua Stern.

GMERCYU operates under the guidance of a strategic plan, which includes goals for the school year as well as projections for the following two. Management budgets on a full-accrual basis with several contingencies, which we consider best practice. The university typically outperforms its budget.

Financial Profile

Financial management policies

GMERCYU has formal policies for endowment and investments, debt, and liquidity. It operates according to a five-year strategic plan and is currently creating a three-year financial plan that will be linked to its 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 weaken its 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 comparable providers.

Financial performance

In fiscal 2018, GMERCYU achieved a full-accrual operating surplus of $2.1 million (2.7% operating margin) up from a fiscal 2017 surplus of $1.5 million (2.2% operating margin). We note that the university has reduced its reliance on endowment draws, drawing 4.5% in fiscal 2017 and fiscal 2018, down from the extraordinary 7% draws that characterized fiscal 2015 and fiscal 2016. We would view any increase above the 4.5% endowment draw negatively as extraordinary draws limit future financial flexibility. The improved operating margins over the past two fiscal years were driven by increased enrollment and increasing net tuition revenue. Net tuition revenue increased by 10% in fiscal 2018, 12% in fiscal 2017, and 16% in fiscal 2016, and we would view further increases favorably. For fiscal 2019, management has budgeted for slightly negative operations while maintaining an endowment spend of 4.5%, though we note that over the recent three years the university has conservatively budgeted for deficits or break-even operations but has achieved surpluses. GMERCYU budgets for deprecation that we view as a best practice.

GMERCYU is tuition dependent, with tuition and auxiliary revenue generating 95% of the total in fiscal 2018. The university also receives state appropriations for capital, which fluctuates each year. In fiscal 2018, state appropriations accounted for 0.6% of revenue. GMERCYU's tuition discount rate moderated to 30% in fiscal 2018, and overall it has declined from 33.1% in fiscal 2014. The discount rate compares favorably with discount rates at peer institutions. For fiscal 2019 (fall 2018), tuition and fees were set at $33,820 and room board at $12,840 for a total cost of $46,660, relatively stable from fall 2017 tuition of $47,090.

Available resources

In our opinion, available resources, as measured by expendable resources, are improved and good for the rating category at $40.1 million as of June 30, 2018, equivalent to 52% of adjusted operating expenses and 98% of debt. Cash and investments (including restricted assets) were $55.6 million, equivalent to 72% of operations and 136% of debt at fiscal year-end 2018. We believe the university will likely maintain its available resource ratios during the two-year outlook period, and would view improvement in available resources within the outlook period favorably.

Endowment market value was $38.4 million as of Fiscal 2018; while it has grown recently, we believe it is modest compared with those of peer institutions. GMERCYU has invested the majority of the endowment in pooled funds managed with the Sisters of Mercy, including a mix of public equity and fixed income. We view audited investment classification levels as a proxy for investment liquidity. At fiscal year-end 2018, investments were, in our view, highly liquid with 100% classified as levels 1 and 2.

The university has maintained an endowment spending policy based on the average value of its endowment assets over the most recent three-year period. For fiscal 2015 and 2016, the board authorized a 7% draw to cover operations knowing that it was budgeting a deficit in 2015. The endowment draw returned to 4.5% in fiscal 2017, and it is also budgeted at that level in fiscal years 2018 and 2019.

Debt and contingent liabilities

As of June 30, 2018, GMERCYU had about $41.0 million in debt. The debt as of fiscal year-end 2018 is blended with 53.2% fixed-rate debt and 46.8% weekly variable-rate debt. We recognize all current debt outstanding is parity debt, secured by a general obligation pledge of the university. TD Bank N.A. is the LOC provider for the current series 2017V1 weekly variable-rate revenue bonds. The LOC expires May 15, 2020. The university does not have any associated interest rate swaps but has an interest rate cap related to its variable-rate debt. The cap is in place for three years ending June 30, 2019, and has a strike price of 2%.

We note that the current weekly rate mode bonds are planned to be converted to a term mode within the next month. Upon the planned conversion to the term mode, the university intends to terminate its current LOC associated with the weekly rate mode. The remarketed bonds will be secured solely by the pledged revenue of the university, which we consider equivalent to a general obligation of the university. Additionally, rather than having one series of weekly rate mode bonds totaling $18.7 million, the university will remarket the bonds into term bonds with three subseries 2017V1A, 2017V1B, and 2017V1C, and with two series of $6 million and one series of $6.7 million, and with no more than one subseries coming due in any one year. Upon conversion of the bonds to term mode, total debt will comprise 54.2% fixed rate debt and 45.8% of term mode debt.

Upon conversion to term mode, MADS for all university debt will be $4.7 million in 2020, which we consider a relatively high 6.1% of fiscal 2018 operating expenses. Our calculation of the MADS burden includes operating lease payments. We include operating leases because they are medium term, cannot be cancelled, and are associated with buildings on satellite campuses for the adult-learning program; therefore, we consider these leases similar to debt. Management reports it does not have new debt plans for the next two years. A lien on and security interest in pledged revenue will secure all outstanding bonds; we consider this revenue stream a general obligation of the university, and the bonds remain on parity with previous debt. A debt service reserve fund, financed at the lowest of MADS, 10% of principal, or 125% of average annual debt service, provides additional bond security. GMERCYU agreed to maintain net revenue equal to 1.1x annual debt service.

Gwynedd-Mercy College, Pennsylvania

Enterprise And Financial Statistics

	--Fiscal year ended June 30--					Medians for 'BBB' rated Private Colleges & Universities
	2019	2018	2017	2016	2015	2017
Enrollment and demand						
Headcount	2,839	2,803	2,667	2,585	2,473	MNR
Full-time equivalent	2,716	2,700	2,521	2,461	2,340	2,463
Freshman acceptance rate (%)	60.9	62.6	67.6	67.8	66.7	70.5
Freshman matriculation rate (%)	24.9	27.1	27.4	31.2	26.5	MNR
Undergraduates as a % of total enrollment (%)	71.6	74.1	76.3	77.5	80.0	76.0
Freshman retention (%)	75.0	78.0	77.0	76.0	73.5	79.2
Graduation rates (six years) (%)	61.0	58.0	50.0	55.0	51.0	MNR
Income statement						
Adjusted operating revenue ($000s)	N.A.	79,413	71,836	66,394	60,348	MNR
Adjusted operating expense ($000s)	N.A.	77,356	70,308	65,788	61,526	MNR
Net operating income ($000s)	N.A.	2,057	1,528	606	(1,178)	MNR
Net operating margin (%)	N.A.	2.66	2.17	0.92	(1.91)	0.78
Change in unrestricted net assets ($000s)	N.A.	3,683	2,795	611	(1,047)	MNR
Tuition discount (%)	N.A.	30.0	29.4	31.4	33.1	39.5
Tuition dependence (%)	N.A.	88.0	87.7	87.2	84.4	MNR
Student dependence (%)	N.A.	94.6	94.2	94.4	92.5	88.3
Health care operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	N.A.	0.1	0.1	0.1	0.3	MNR
Endowment and investment income dependence (%)	N.A.	0.0	0.0	0.0	0.2	MNR
Debt						
Outstanding debt ($000s)	N.A.	41,035	42,750	42,645	43,600	59,055
Proposed debt ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Total pro forma debt ($000s)	N.A.	41,035	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	4,734	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	6.09	5.49	3.34	3.61	MNR
Current MADS burden (%)	N.A.	5.94	6.66	4.46	4.77	4.00

Gwynedd-Mercy College, Pennsylvania (cont.)

Enterprise And Financial Statistics

	--Fiscal year ended June 30--					Medians for 'BBB' rated Private Colleges & Universities
	2019	2018	2017	2016	2015	2017
Pro forma MADS burden (%)	N.A.	6.12	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value ($000s)	N.A.	38,398	34,244	29,563	29,112	75,273
Cash and investments ($000s)	N.A.	55,657	51,099	42,040	40,640	MNR
Unrestricted net assets ($000s)	N.A.	44,545	38,883	35,867	35,256	MNR
Expendable resources ($000s)	N.A.	40,067	38,340	33,762	33,393	MNR
Cash and investments to operations (%)	N.A.	71.9	72.7	63.9	66.1	83.6
Cash and investments to debt (%)	N.A.	135.6	119.5	98.6	93.2	157.7
Cash and investments to pro forma debt (%)	N.A.	135.6	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	51.8	54.5	51.3	54.3	48.0
Expendable resources to debt (%)	N.A.	97.6	89.7	79.2	76.6	87.7
Expendable resources to pro forma debt (%)	N.A.	97.6	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	14.5	14.9	15.4	15.6	14.4

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. Adjusted UNA = Unrestricted net assets + unrestricted net assets of the foundation. Average age of plant = accumulated depreciation/depreciation and amortization expense.

Ratings Detail (As Of April 15, 2019)

Gwynedd Mercy Univ variable rate rev bnds RMKT 5/1/19 ser 2017V1A dtd 05/01/2019 due 05/01/2036

Long Term Rating	BBB/Stable	Affirmed

Gwynedd Mercy Univ variable rate rev bnds RMKT 5/1/19 ser 2017V1B dtd 05/10/2019 due 05/01/2036

Long Term Rating	BBB/Stable	Affirmed

Gwynedd Mercy Univ variable rate rev bnds RMKT 5/1/19 ser 2017V1C dtd 05/01/2019 due 05/01/2036

Long Term Rating	BBB/Stable	Affirmed

Montgomery Cnty Hgr Ed & Hlth Auth, Pennsylvania

Gwynedd Mercy Univ, Pennsylvania

Montgomery Cnty Hgr Ed & Hlth Auth (Gwynedd Mercy Univ)

Long Term Rating	BBB/Stable	Affirmed