

## CREDIT OPINION

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# University of Idaho, ID

## Update to credit analysis

### Summary

The [University of Idaho's](#) (Aa3 stable) strong credit quality reflects the university's significance as the state's land-grant and leading research university, sizeable total wealth for the rating category and continued positive operating results. The credit profile is also strengthened by recent increases in state appropriations, the university's diverse revenue sources and positive cash flows providing good debt service coverage. However, market challenges are evident given declining enrollment and could become a more material credit challenge if the university is unable to maintain positive operating performance. Additional offsetting factors include comparatively thin liquidity at the current rating level and limited opportunity for revenue growth.

### Credit strengths

- » Land-grant university in the [State of Idaho](#) (Aa1 stable) with a statewide presence through instructional centers and agricultural research and extension centers
- » Positive operations resulting in good cash flows which provided 3.2x annual debt service coverage in fiscal 2017
- » Diversified revenues with solid government appropriations (37% of operating revenue) and research funding (25% of operating revenue) in fiscal 2017
- » Improved spendable cash and investments, covering operations by 0.5x and debt by 1.0x

### Credit challenges

- » Mounting student market pressure leading to declines in enrollment and limited opportunities for net tuition revenue growth
- » Thin liquidity at the current rating level with approximately \$110 million of monthly liquidity providing 113 monthly days cash on hand
- » A large pension obligation that will require increased funding over time

### Rating outlook

The stable outlook reflects our expectation that the university will continue to achieve positive operating performance despite enrollment pressures.

## Factors that could lead to an upgrade

- » Material growth in financial resources and liquidity
- » Strengthening of student demand demonstrated by stable or increasing enrollment and sustained growth in net tuition revenue
- » Sustained stronger operating performance

## Factors that could lead to a downgrade

- » Inability to maintain positive operating performance and good cash flow
- » Significant deterioration of liquidity
- » Substantial new debt without offsetting revenue growth

## Key indicators

Exhibit 1

UNIVERSITY OF IDAHO, ID

	2013	2014	2015	2016	2017	Median: Aa Rated Public Universities
Total FTE Enrollment	9,996	9,735	9,505	9,518	9,430	28,405
Operating Revenue (\$000)	351,916	355,839	370,078	378,096	386,391	1,104,854
Annual Change in Operating Revenue (%)	3.0	1.1	4.0	2.2	2.2	4.4
Total Cash & Investments (\$000)	333,540	380,430	390,840	397,408	421,585	1,201,140
Total Debt (\$000)	165,871	158,671	193,403	188,888	183,738	597,459
Spendable Cash & Investments to Total Debt (x)	0.8	1.1	0.9	1.0	1.0	1.3
Spendable Cash & Investments to Operating Expenses (x)	0.4	0.5	0.5	0.5	0.5	0.7
Monthly Days Cash on Hand (x)	94	101	114	120	113	162
Operating Cash Flow Margin (%)	10.1	11.0	12.6	12.9	9.7	12.0
Total Debt to Cash Flow (x)	4.7	4.0	4.2	3.9	4.9	4.4
Annual Debt Service Coverage (x)	2.6	2.7	3.1	3.9	3.3	3.0

Source: Moody's Investors Service

## Profile

The University of Idaho is the state's land-grant and leading research university, with mid-size enrollment and a statewide presence through instructional centers as well as agricultural research and extension centers. The university has a total FTE enrollment of 9,430 and has operating revenue over \$386 million.

## Detailed credit considerations

### Market profile: important role as Idaho's land grant and leading research university challenged by declining enrollment

The University of Idaho will continue to serve an important role as the state's land grant and leading research university. A statewide effort to increase participation in higher education has contributed to an increase in first-year student applications but has not yet translated into an overall increase in enrollment. Freshmen and transfer enrollment was down slightly for fall 2017 indicating the overall enrollment environment remains pressured for the university.

The most significant area of enrollment declines are non-resident undergraduate students, reflecting competition from neighboring states and a challenging international student environment. Declining resident graduate student enrollment is also impacted partially by the improving economy's countercyclical impact on graduate enrollment. The university has developed strategies to become more competitive for these students, and the success of these initiatives will be crucial to seeing growth in net tuition revenue, which has

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declined again in fiscal 2017 following a period of strong growth from fiscal 2011 to fiscal 2015. Although the overall number of high school graduates in the state is expected to grow over the medium term, this may not translate into increased enrollment due to Idaho's low college participation rate and an improving state economy.

The university continues to benefit from strong and growing donor support with three-year average gifts per student of \$2,542, significantly higher than the Aa3 median of \$807. The university recently announced a \$10 million gift for the Idaho Arena project with \$34 million now raised towards the \$45 million goal. The Center for Agriculture, Food and Environment (CAFE) is another fundraising priority for the university in fiscal 2018. Overall, management reported record \$38 million in fundraising in fiscal 2017 and expects to exceed this amount in the current fiscal year.

### **Operating performance: positive operations despite declining enrollment**

The university will continue to benefit from diverse revenue sources that support positive operating performance despite declining enrollment. Funding from the state of Idaho increased in fiscal 2017 and accounted for 37% of overall operating revenue, though the university does anticipate that appropriation growth will slow. The university's research profile continues to grow, reaching \$95 million (25% of revenues) in fiscal 2017.

As expected, enrollment declines led to a softening of operating margins in fiscal 2017, but the university was still able to deliver positive operating performance. The fiscal 2017 cash flow margin of 9.7% still provided a good 3.3x annual debt service coverage. Despite falling short of enrollment targets in fall 2017, we anticipate the university will be able maintain positive operating results due to expense control in fiscal 2018.

### **Wealth and liquidity: solid financial reserve growth though liquidity remains thin**

Favorably, overall financial resources will continue to grow due to fundraising and positive operations. Total cash and investments increased 26% since fiscal 2013, and the 6% growth from fiscal 2016 exceeded previous expectations. In fiscal 2017, spendable cash and investments covered debt by 1.0x and operations by 0.5x, appropriate at the current rating level.

The university's endowment, managed by the University of Idaho Foundation, achieved a 12.1% return in fiscal 2017 bringing the current value to \$283 million. Management reports a preliminary 6% rate of return so far in fiscal 2018. The university will again receive a projected distribution of \$11 million from the endowment in fiscal 2018 in accordance with the conservative 4.4% spending policy.

### **LIQUIDITY**

Liquidity declined slightly in fiscal 2017 due to capital investment and remains thin at the current rating level. Monthly liquidity was \$110 million, an increase of 31% since fiscal 2013, but provided only 113 monthly days cash on hand compared to the Aa3 median of 159 days.

### **Leverage: manageable debt levels with no plans for increased leverage**

Leverage will remain manageable even as the university continues to invest in capital projects due to significant donor and state capital support. The university has modest leverage relative to its revenues and size with \$184 million of outstanding debt. Softer operations in fiscal 2017 increased the total debt to cash flow to 4.9x, but this remains favorable at the current rating level. The university has no short term plans for any additional debt.

### **DEBT STRUCTURE**

Through the Series 2018A bonds, the university will defease the adjustable rate Series 2007B bonds and convert this debt to fixed rate. Series 2011 bonds will be the only adjustable rate debt outstanding, accounting for approximately 30% of total outstanding debt.

### **DEBT-RELATED DERIVATIVES**

Not applicable.

### **PENSIONS AND OPEB**

The university has a sizeable pension obligation that comprises approximately 45% of its \$335 million total adjusted debt and that will become an increasing credit challenge. This pension obligation is associated with participation in a cost-sharing multiple-employer defined benefit pension plan administered by Public Employee Retirement System of Idaho (PERSI), which covers substantially all state

employees. Moody's adjusted net pension liability is \$140 million for fiscal years 2015-2017, and the adjusted funded ratio was slightly below 60% in fiscal 2017. The pension expense was a manageable 2% of operating expenses in fiscal 2017.

Favorably, the university has a \$2.6 million asset for its OPEB plan. Employees hired after January 1, 2002, are not eligible to participate in the plan and the university has established a trust to help fund future costs and aims to contribute the full actuarially required contribution (ARC) annually.

#### **Management and governance: prudent fiscal management delivers continued positive results**

The university's very good strategic positioning reflects management's fiscal discipline, which has led to positive operating performance despite enrollment pressures. The current management team was largely put together after the current president joined in 2014 and utilizes the current strategic plan (launched in 2016) as a guide for benchmarking and utilizing the resources of the university.

The eight members of the university's Board of Regents also serve as the Idaho State Board of Education, which governs K-20 education in the state of Idaho. This can be a positive for the university as the state continues in its efforts to incentivize more high school graduates to enroll in Idaho's colleges and universities.

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