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# Case Western Reserve University, Ohio; CP; Joint Criteria; Private Coll/Univ - General Obligation

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# Case Western Reserve University, Ohio; CP; Joint Criteria; Private Coll/Univ - General Obligation

## Credit Profile

### Ohio Hgr Ed Fac Com, Ohio

Case Western Reserve Univ, Ohio

### Case Western Reserve Univ, various rev bnds

Long Term Rating

AA-/Stable

Outlook Revised

## Rationale

Standard & Poor's Ratings Services revised the outlook on Case Western Reserve University, Ohio's (CWRU) long-term rating and underlying rating (SPUR) to stable from negative based on significant financial progress, including achieving break-even operations in fiscal 2008 on a full accrual basis. Standard & Poor's also affirmed its 'AA-' long-term ratings and SPURs on various Ohio Higher Education Facilities Commission bonds issued on behalf of the university. The various 'A-1+' short-term ratings on outstanding variable-rate demand bonds reflect bank liquidity. We also affirmed our 'A-1+' rating on the university's commercial paper (CP) program, which is being increased to an authorized \$90 million from the existing \$63 million.

CWRU's senior management staff has worked hard to produce operating results that exceeded the university's financial plan goals, and in fiscal 2008 the university achieved budgetary balance earlier than planned. Management expects similar or better results in the current 2009 budget year. Outstanding debt at June 30, 2008, a mix of bonded debt and CP, was \$591 million.

In the event of any unremarketed CP roll-overs, the university's CP program is supported by a dedicated credit agreement with JP Morgan Chase Bank N.A. Liquidity on all of CWRU's variable-rate demand bonds is supported by various bank letters of credit and standby bond purchase agreements.

The long-term rating reflects CWRU's:

- Sizable \$1.78 billion endowment at June 30, 2008 (estimated at about \$1.4 billion at the end of October 2008);
- Growing undergraduate enrollment and adequate demand metrics given the strong competition for CWRU's high-quality student base;
- A broad range of undergraduate, graduate, and professional program offerings that, combined with research and community medical coalitions, support enrollment;
- Manageable pro forma debt burden of less than 5%, and no significant new debt planned at this time except for a small increase in the CP program authorization; and
- New management team in place, including a new president, provost, vice presidents of both admissions and advancement, dean of the school of medicine, and interim chief financial officer.

Offsetting credit factors include a stressful economic environment for the university as it continues to improve its

financial performance, initiate fundraising, and implement the strategic plan. In addition, financial resource ratios for CWRU remain low for the 'AA' rating category, even with a large endowment (\$1.78 billion market value at June 30, 2008). Unrestricted resources (UR) ratios at that time were equal to 124% of expenses and 182% of pro forma debt.

Located in Cleveland, CWRU is Ohio's largest private, independent research university, offers extensive graduate and professional degree programs, and has a large research base. Overall enrollment has stabilized in recent years, and undergraduate enrollment has increased in each of the last three years. Headcount for the fall 2008 semester was 9,814 students (8,144 full-time equivalent), up about 8% overall in the last six years. A new president began her tenure in July 2007, a new strategic planning initiative is entering the implementation stage, and the institution is focused on cost controls, fundraising, and strategic use of resources as they come available. Plans for a comprehensive capital campaign are currently under development. The university has no plans to issue new debt at this time, other than increasing its CP authorization to \$90 million from \$63 million.

## Outlook

The stable outlook reflects the university's significant progress in achieving balanced operating results on a full accrual basis, and our expectation of continuing positive operations on a budgetary basis. We also expect institutional stability in management, progress toward a successful capital campaign, fairly stable enrollment, and gradual improvement in freshman selectivity and matriculation rates. Capacity for additional debt (which is not currently expected) remains limited at this time as operating flexibility is being rebuilt.

## The University

CWRU offers a wide range of undergraduate, graduate, and professional degree programs, including arts and sciences, law, business, medicine, engineering, nursing, social sciences, and dentistry. The university received approximately \$400 million in both 2007 and 2008 in research grant and indirect cost recovery revenues from various funding sources, principally the National Institutes of Health and the National Science Foundation. The CWRU campus is one of the anchor institutions in University Circle, a 500-acre concentration of more than 40 educational, social, medical, cultural, and religious institutions at the eastern edge of Cleveland.

The university's overall enrollment has stabilized, and undergraduate enrollment has increased in each of the last five years. Headcount for the fall 2008 semester was 9,814 students. As a comprehensive research institution, CWRU has a larger proportion of graduate and professional students than its peers, currently about 56% of enrollment. The size of the entering undergraduate class was 1,026 for fall 2008, and is up from 836 in fall 2002. The student draw remains relatively broad, with about half of undergraduates coming from Ohio, and large numbers from Pennsylvania, New York, Michigan, and Illinois. In fall 2008, CWRU accepted about 73% of its freshman applicant pool. Of this, only 19% matriculated, a fairly weak level that indicates very strong competition from other institutions for the university's high-quality students. Student quality is demonstrated by fall 2008 entering-freshman SAT scores of over 1309 (the national average is about 1017) and average ACT scores of 29 (the national average is about 21). For the 2008-2009 academic year, total charges (tuition, fees, and room and board) for an undergraduate student are \$45,652, which is expensive but consistent with charges of peer private research institutions.

## Management And Strategic Planning

CWRU president, Barbara R. Snyder, began her tenure in July 2007, and started a new strategic planning initiative that is now in the implementation stage. The board and senior management have stated publicly that plan initiatives will be funded as resources become available. The university has filled many senior leadership positions in the past year and thus has a relatively new management team. In addition to a new president, CWRU has a new provost, senior appointments for admissions and advancement, various new deans including in the Weatherhead School of Management and the medical school, a new treasurer, and an interim CFO.

## Finances

### Adequate financial resources

Financial resource ratios for CWRU remain below average for the 'AA' rating category, but are not inconsistent with those of some peer research institutions. The university benefited from a substantial \$1.78 billion endowment at June 30, 2008, about \$214,000 per full-time-equivalent student. The current market value is roughly estimated at \$1.4 billion at Oct. 31, 2008, consistent with volatile general market conditions. Total cash and investments at the end of fiscal 2008 (including \$301 million of outside beneficial trusts) was nearly \$2.0 billion.

A more conservative measure of financial resources is UR, which adjusts audited unrestricted net assets (UNA) for fixed assets and long-term debt. This value remained substantial at June 30, 2008, at \$1.09 billion. Fiscal 2008 UR equaled an adequate 124% of operating expenses and 182% of pro forma debt (about \$600 million).

### Improving operating performance

Operating results on a full accrual basis were break-even for the fiscal year ended June 30, 2008, which compared with negative \$27 million in fiscal 2007, negative \$50 million in fiscal 2006, and negative \$44 million in fiscal 2005. Management reports that the 2009 budget is balanced when the presidential reserve is counted, that seven out of nine of the academic schools have achieved budgetary balance, and that the remaining two schools are on target to achieve balance within one to two years. Operations on a cash basis were positive in fiscal years 2008, 2007, and 2006, before depreciation expenses of \$55 million-\$60 million in each year.

The university's previous financial plan had targeted fiscal 2008 for budgetary balance. However, several added priorities, including prior research and faculty hiring commitments, resulted in a decision to take a more measured budgetary approach. This resulted in an initial budgeted \$10.5 million deficit in 2008, with a target of achieving break-even in fiscal 2011. The university exceeded the plan and hit balance in 2008. Standard & Poor's rating and outlook anticipate continued balanced operating performance, eventually returning to the university's strong historical operating margins prior to 2000.

The bottom-line changes in UNA for CWRU are driven by the market value of investment and are thus highly market driven. Between 2004 and 2007, bottom-line returns were positive due to realized and unrealized gains in CWRU's substantial endowment. That was not the case in 2008 due to the volatile market situation in fiscal 2008, which is expected to continue into fiscal 2009. The bottom-line change in the university's 2008 UNA was negative \$77 million, compared with positive \$173 million in 2007 and positive \$75 million in 2006.

The university's revenue base remains diverse and somewhat research driven. Funds from grants and contracts

accounted for 38% of 2008 unrestricted operating revenues. Gross student charges accounted for 35% of revenues, with endowment spending at 8.8%. Tuition discount on an institutional basis is manageable at around 39%. For fall 2008, the freshman discount rate was a still-high 55.7%, but an improvement from 60% levels seen in recent years.

### **Endowment and fundraising**

The university is supported by a sizable endowment with a market value of \$1.78 billion at June 30, 2008 (including outside trusts). The market value at the end of October 2008 is roughly estimated at around \$1.4 billion, consistent with volatile general market conditions. Endowment investments at June 30, 2008, continued a move toward a more aggressive asset mix, which is still comparable to that of peer institutions with similarly sized endowments. At fiscal year-end, the university-controlled endowment was a mix of 32% equities, 10% fixed income and cash, 17% hedge funds, 15% private equity, and 26% real assets. Many of the university's alternative and hedge fund investments have mandatory "capital calls" related to future investments; at June 30, 2008, those unfunded calls were about \$233 million. The asset mix in the university's directly invested "pooled" portfolio is not as liquid as other peer portfolios, as it had about 30.5% of daily-liquidity investments at June 30, 2008.

Investment returns on university-controlled assets at June 30, 2008, was a positive 0.5%, good considering market declines at the time. Returns for outside trusts, which tend to lag those of the university, were negative 5.3%. For university-held investments, the three- and five-year cumulative returns were positive 11.3% and 13.2%, respectively. The university's endowment spending policy has a complicated formula, but the net results are comparable to those of peer institutions and are roughly 5.0% of a three-year moving market value average.

CWRU's last comprehensive capital campaign took place in the early 1990s. While the university is not in a formal campaign, gifts and pledges received in fiscal 2008 totaled \$103 million, the largest amount received since 2001. Management is currently developing plans for a comprehensive capital campaign to support recently completed strategic planning.

### **Debt**

Outstanding debt at June 30, 2008, was \$591 million. This level is down from \$622 million in 2006 due to scheduled principal amortization as well as repayment of \$43 million in bank lines of credit. Outstanding debt includes about \$497 million of bonded debt, \$63 million of CP, and \$31 million of capital leases and notes. The university is increasing its CP program to \$90 million. The overall debt profile, including the effect of several floating-to-fixed rate swap contracts, is presently about 83% fixed rate and 17% floating rate. Debt burden, defined as estimated maximum annual debt service relative to operating expense, remains manageable at under 5% of 2008 expenses.

Management reports that except for the increased CP authorization, CWRU has no plans to issue new debt at this time and expects to fund strategic plan initiatives from gifts or internal resources, as such resources become available. Major projects could include improvements to the campus center, expansion of the "West Quad" research facilities, and various capital renewals and academic facility replacements.

## Debt Derivative Profile (DDP)

CWRU has been assigned a Standard & Poor's DDP overall score of '1.5' on a four-point scale where '1' represents the lowest risk. The overall score of '1.5' reflects Standard & Poor's view that CWRU's swap portfolio reflects very low risk credit risk at this time due to counterparty credit quality, the average economic viability of the swap portfolio over stressful economic cycles, and a sound debt and swap management internal procedures. Standard & Poor's is in the process of updating the university's DDP score to reflect the sixth and newest contract with a \$100 million notional amount.

CWRU has six swap contracts outstanding with a total swap notional amount of \$278 million. The effect of the swap contracts, all of which are floating-to-fixed rate, is a net variable-rate exposure of about 14%, with variable-rate exposure primarily from the CP program. The swap contracts are all with Morgan Stanley (A+/Negative) as counterparty.

## Contact

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Ratings Detail (As Of December 8, 2008)		
<b>Ohio Hgr Ed Fac Auth, Ohio</b>		
Case Western Reserve Univ, Ohio		
<b>Case Western Reserve Univ rev bnds ser 2006</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Outlook Revised
<b>Ohio Hgr Ed Fac Auth (Case Western Reserve Univ) rev var rate dem bonds ser 2008A</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Outlook Revised
<i>Long Term Rating</i>	AAA/A-1/Negative	Affirmed
<b>Ohio Hgr Ed Fac Auth (Case Western Reserve Univ) rev var rate dem bonds ser 2008C</b>		
<i>Long Term Rating</i>	AA-/Stable	Outlook Revised
<b>Ohio Hgr Ed Fac Auth (Case Western Reserve Univ) rev var rate dem bond ser 2008B</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Outlook Revised
<i>Long Term Rating</i>	AAA/A-1+/Watch Neg	Affirmed
<b>Ohio Hgr Ed Fac Com, Ohio</b>		
Case Western Reserve Univ, Ohio		
<b>Case Western Reserve Univ ser 2004A, 2004B1-4</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Outlook Revised
<b>Case Western Reserve Univ, CP</b>		
<i>Short Term Rating</i>	A-1+	Affirmed

**Ratings Detail** (As Of December 8, 2008) (cont.)

<b>Case Western Reserve Univ, VRDB ser 2001A</b>		
<i>Long Term Rating</i>	AA-/A-1+/Stable	Outlook Revised
Many issues are enhanced by bond insurance.		

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