

Changing Demographics: Impact on Debt and Capital Strategies

Susan Carlson

Director, Standard and Poor's

Susan Fitzgerald

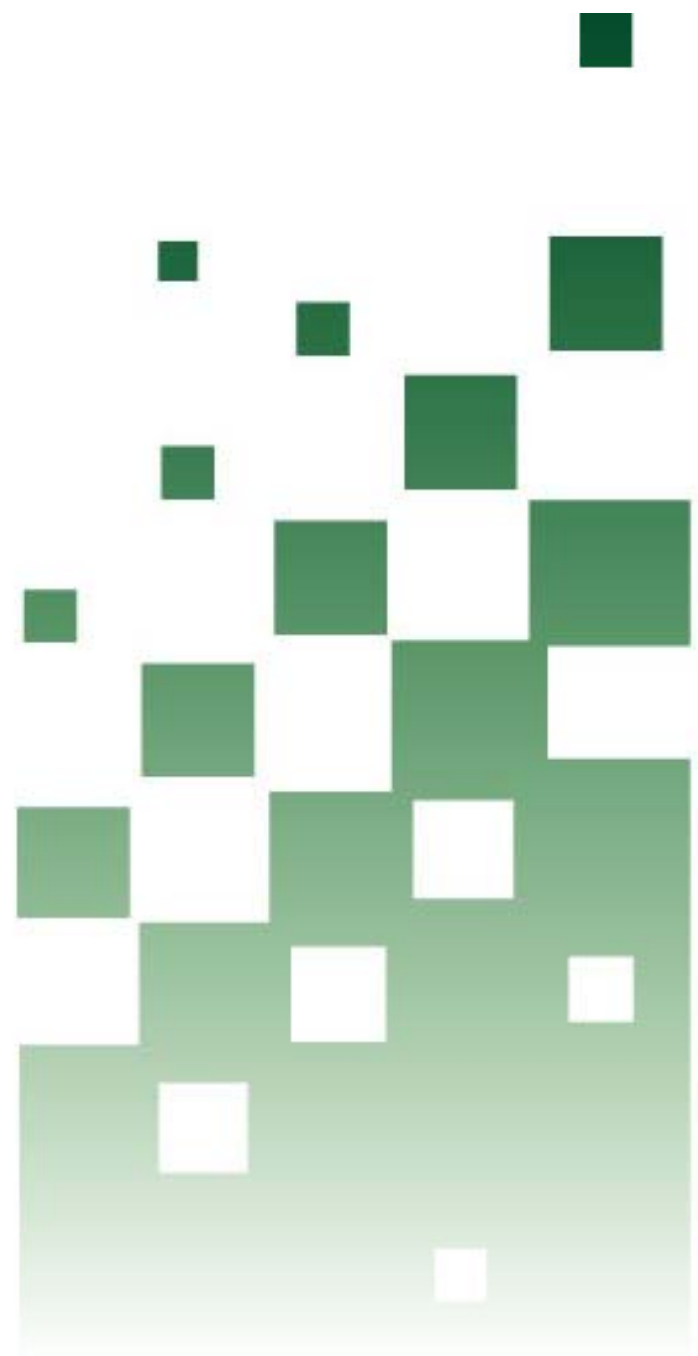
Sr. Vice President, Moody's Investor Service

Elissa Granick

Director, Fitch



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Ten Key Issues Affecting Higher Education Credit Quality



Moody's Investors Service

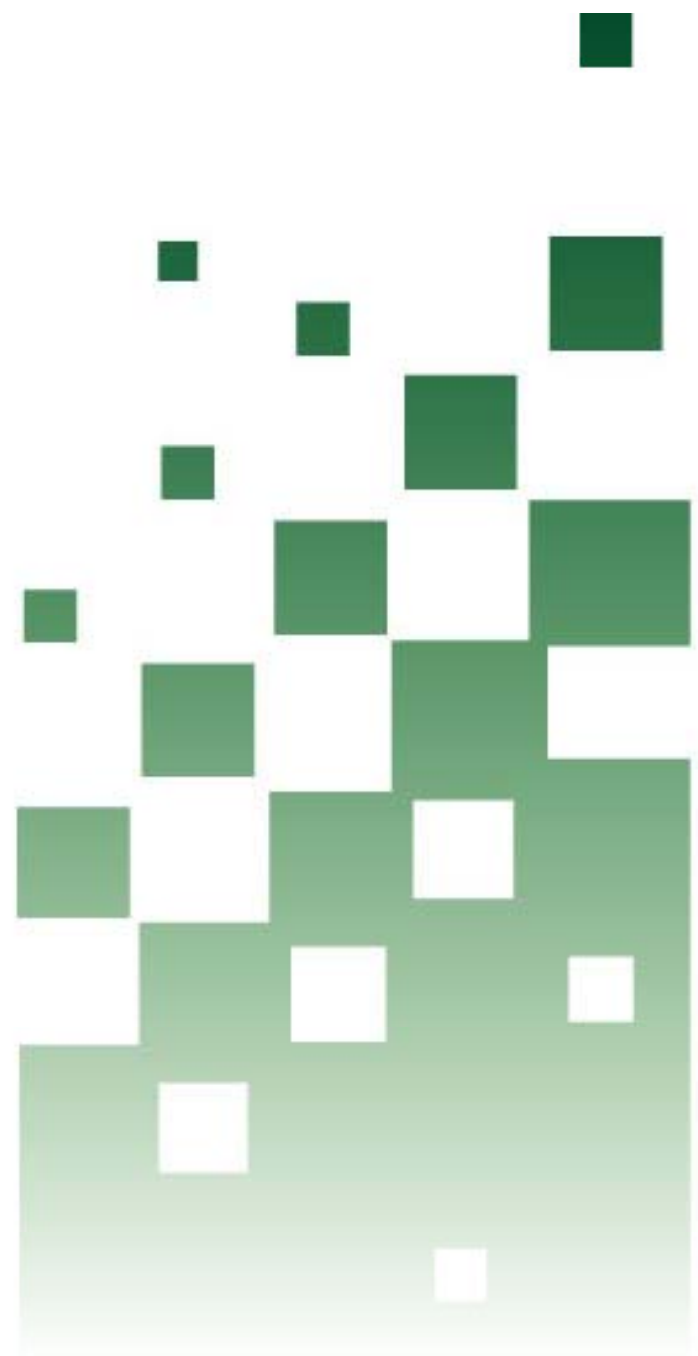
Susan Fitzgerald

Sr. Vice President

Susan.fitzgerald@moodys.com



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Moody's Investors Service

Stable Outlook for Higher Education Institutions

	Aaa	Aa	A	Baa	Below Baa3
Private Higher Education					
Number of Ratings	18	45	109	84	20
% of Private Higher Education Ratings	7%	16%	39%	30%	7%
Stable	100%	87%	79%	69%	60%
Positive	0%	4%	7%	13%	5%
Negative	0%	9%	14%	18%	35%
Four-Year Public Higher Education					
Number of Ratings	3	53	133	10	-
% of Public Higher Education Ratings	2%	27%	67%	5%	
Stable	100	94%	85%	60%	
Positive	0%	6%	9%	0%	
Negative	0%	0%	6%	40%	
Community College Districts (revenue bond ratings only)					
Number of Ratings	-	10	42	4	-
% of Community College Ratings		18%	75%	7%	
Stable		100%	95%	75%	
Positive		0%	0%	25%	
Negative		0%	5%	0%	



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Issue 1:

Evolving Student Demand and Customer Preferences

Traditional age demographics

Non-traditional age participation

Socio-economic profile of the student population

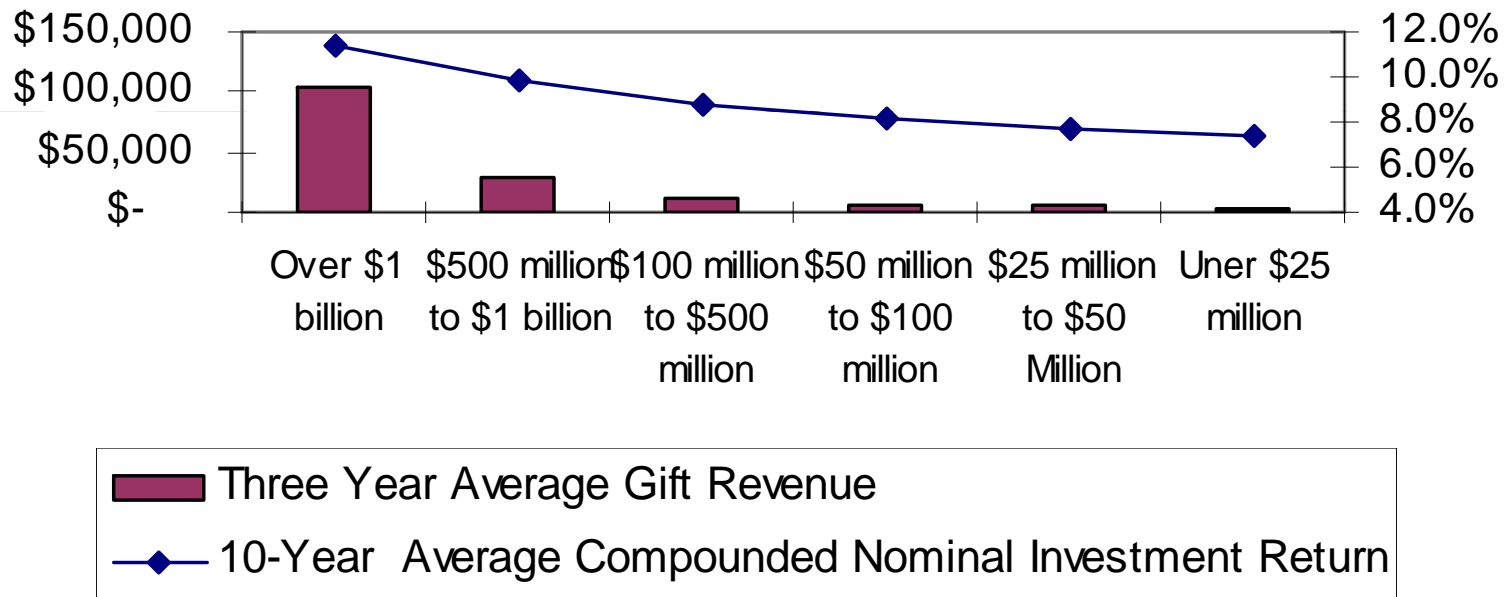
Evolving educational delivery methods

Increasing competition from new and existing providers

Rapid pace of change for programmatic and student life amenities

Issue 2: Increasing Sector Wealth Concentration

Wealthiest Have Higher Investment Returns and Stronger Fundraising



Implications for:

Tuition and Financial Aid Strategies, Operating Spending, Capital Spending, Sector Wide Philanthropy, External Scrutiny

Other External Industry Issues

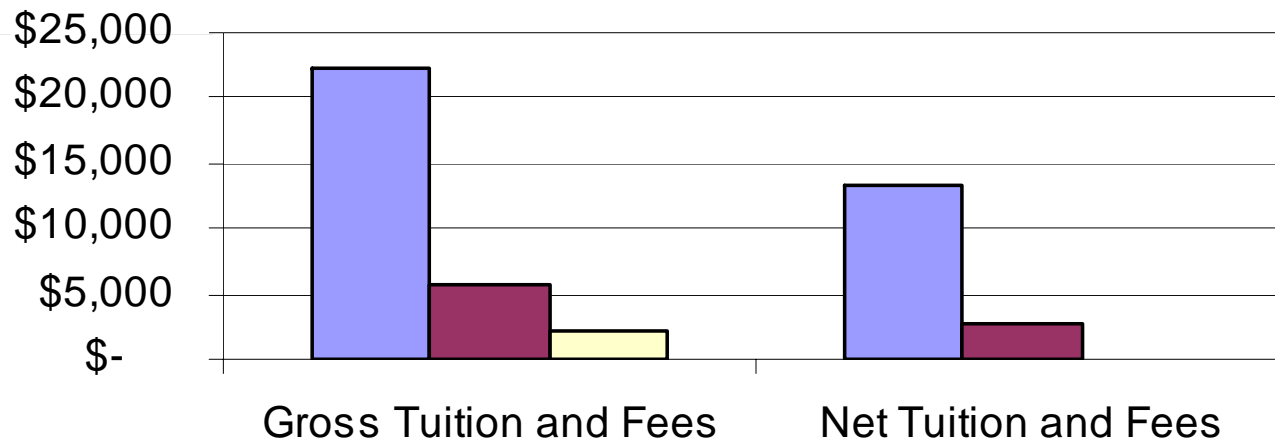
- ◆ **Issue 3:** Continuously Evolving Government Funding Paradigm
 - Federal funding for research
 - State and federal financial aid programs
 - State operating and capital funding
 - Tax support
 - Other direct and indirect support
- ◆ **Issue 4:** Increasing External Scrutiny and Demands for Transparency
 - Cost, compensation, provision of public benefit, and more...

Internal Responses

- ◆ **Issue 5:** Positioning of Mission
- ◆ **Issue 6:** Positioning of Pricing
- ◆ **Issue 7:** Determining the Right Levels of Spending: Both Programmatic and Capital
- ◆ **Issue 8:** Increasingly Sophisticated Balance Sheet Management Strategies
- ◆ **Issue 9:** Need for Improvement in Operational Management
- ◆ **Issue 10:** Evolving governance structures for a changing environment

Issue 6: Positioning of Pricing

Significant Difference Between Sticker Price and Paid Price (Projected FY2007)



Source: College Board

Private Public Community College

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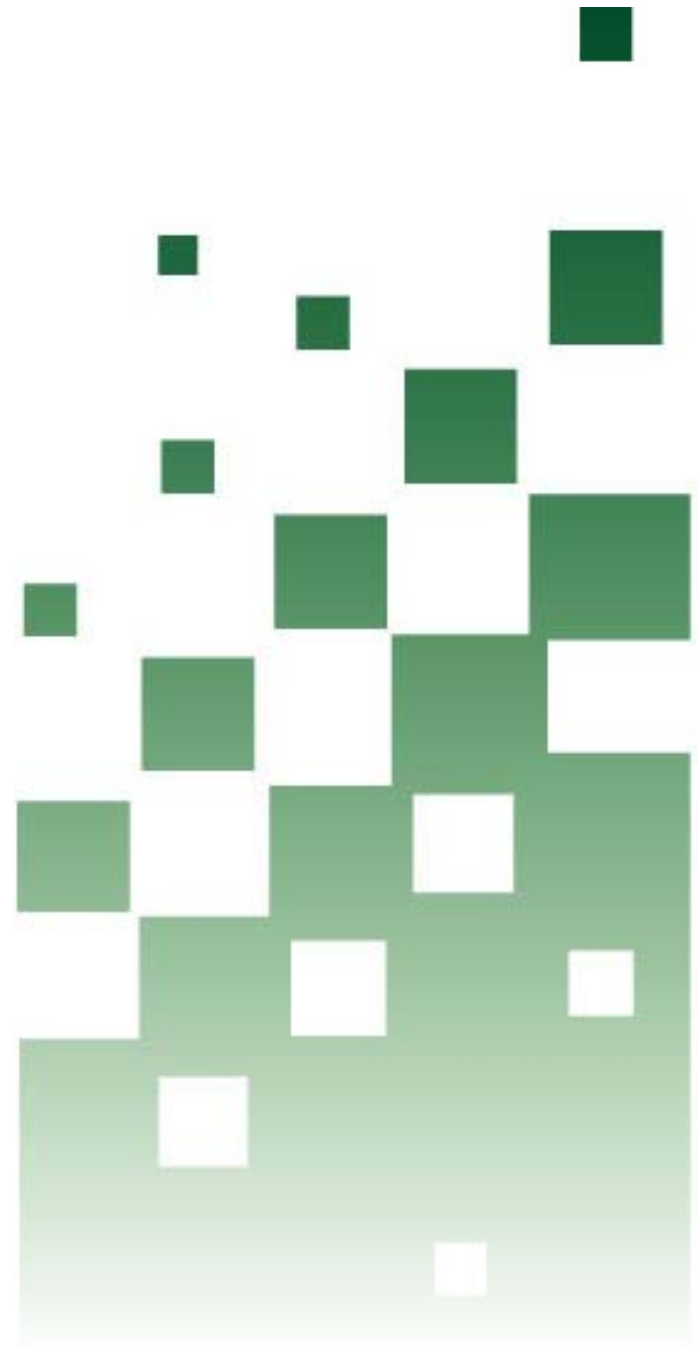
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Elissa Granick

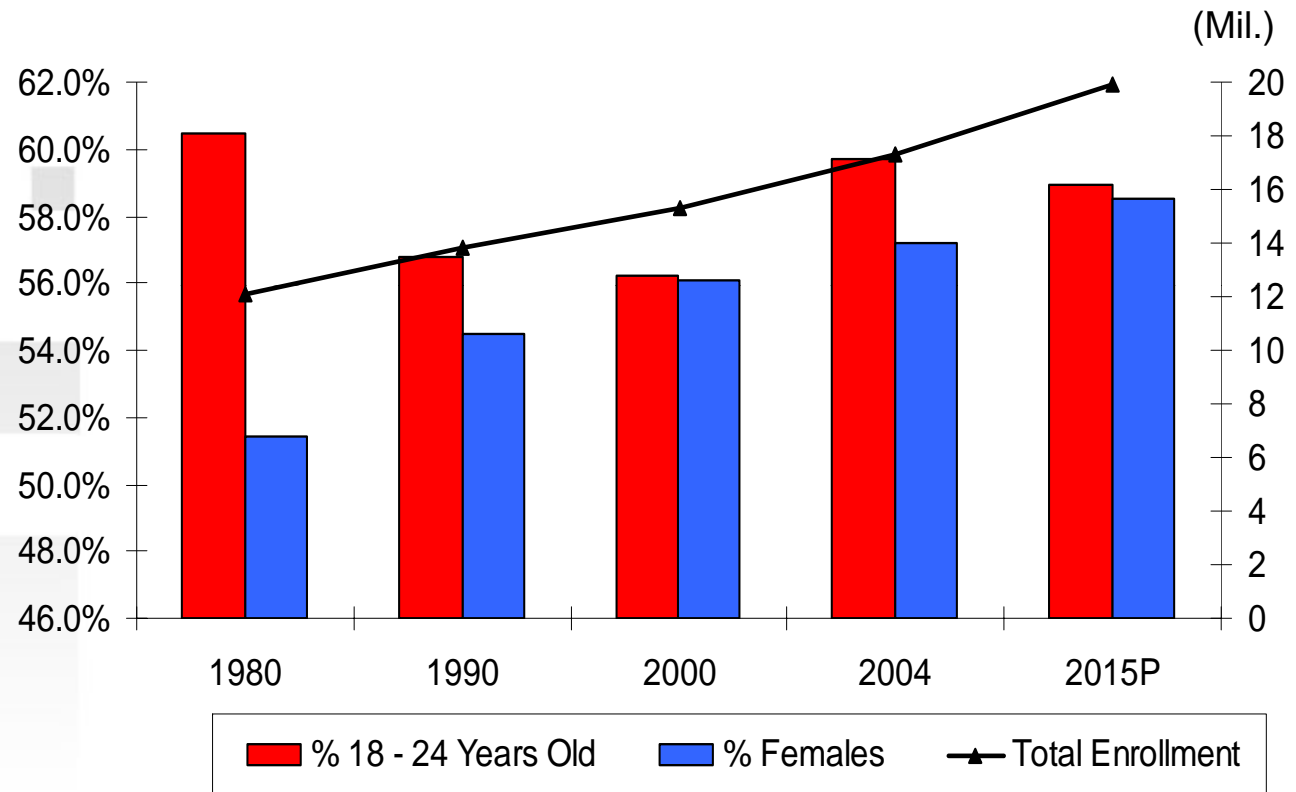
Director, Fitch

212 908 0658

elissa.granick@fitchratings.com

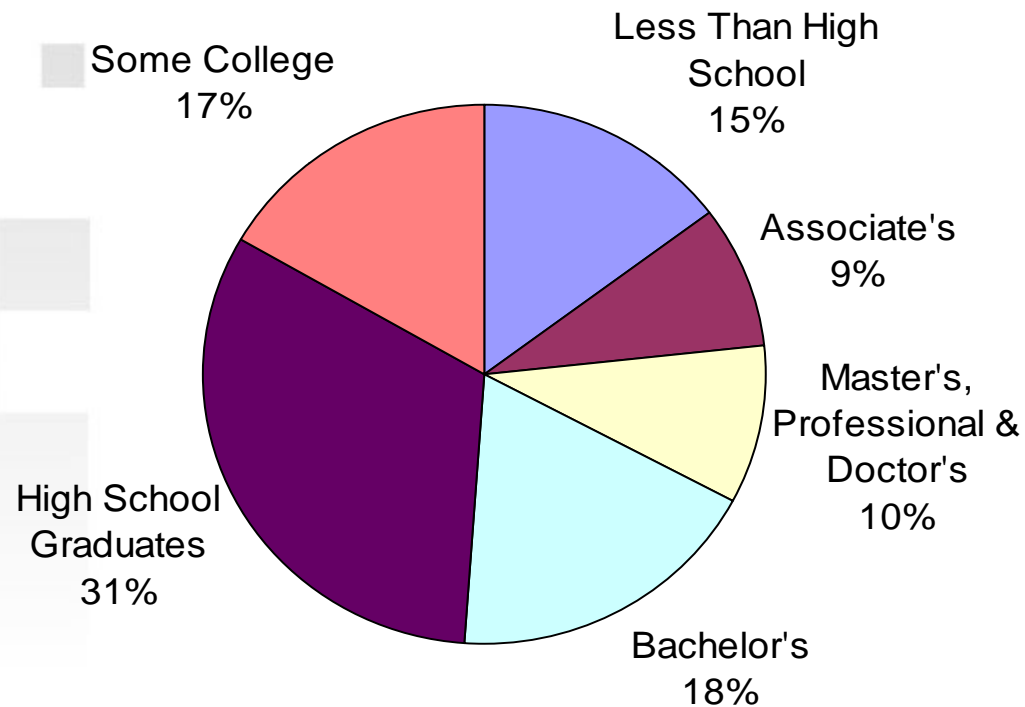


College Enrollment Trends — 1980–2015



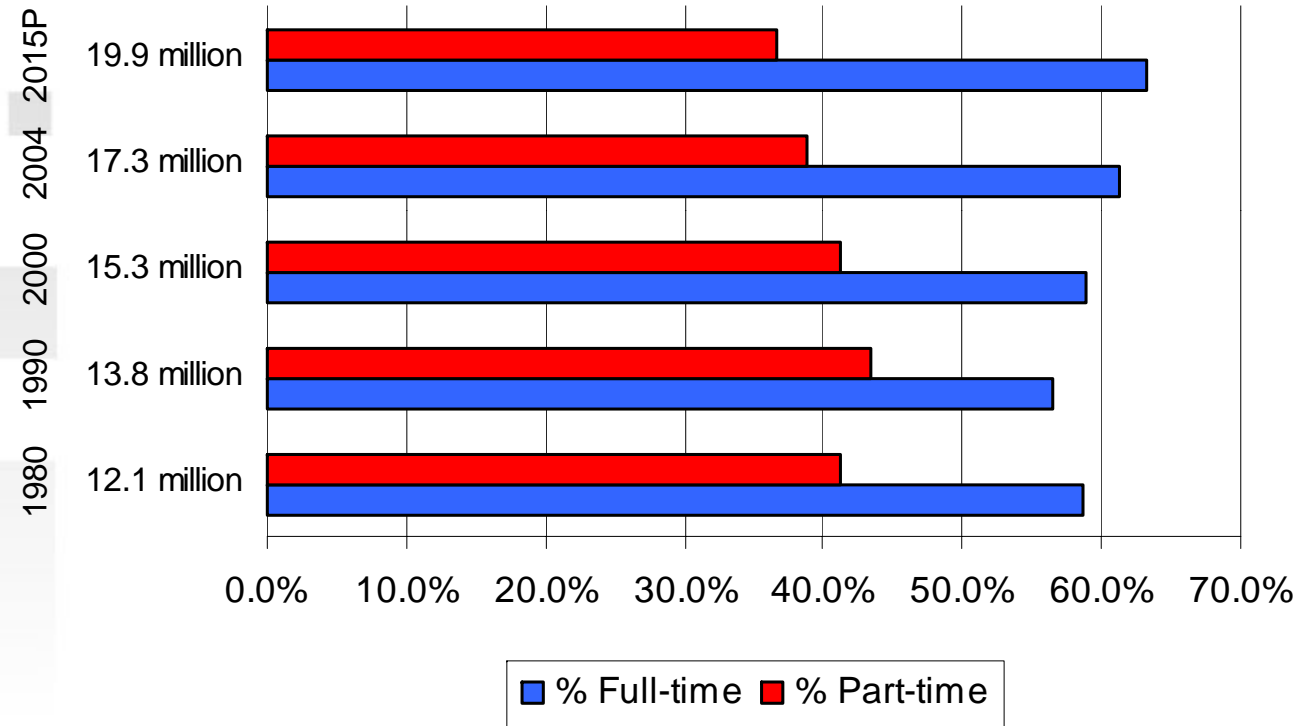
P – Projected. Source: U.S. Department of Education

Highest Level of Education Attainment — Persons 25 Years & over: March 2005



Source: Census Bureau

Trends in Attendance Status — 1980–2015



P – Projected. Source: U.S. Department of Education

College Enrollment Profile in the 25 Largest States

State	2005 Population	Fall 2004 Enrollment	% of Population with Bachelor's Degree	% Change in High-school Grad. 2002-03 - 2015-16	2004 High-school Dropout Rate
Alabama	4,557,808	255,826	13.7	-3.9	7.0
Arizona	5,939,292	490,925	15.5	71.5	11.0
California	36,132,147	2,374,045	19.0	10.9	6.0
Colorado	4,665,177	300,914	21.9	12.9	8.0
Florida	17,789,860	866,665	16.3	21.1	8.0
Georgia	9,072,576	434,283	17.0	20.4	12.0
Illinois	12,763,371	801,401	17.9	4.9	6.0
Indiana	6,271,973	356,801	13.6	7.6	13.0
Kentucky	4,173,105	240,097	11.2	-3.0	10.0
Louisiana	4,523,608	246,301	14.4	-10.8	10.0
Maryland	5,600,388	312,493	19.3	2.7	7.0
Massachusetts	6,398,743	439,245	21.8	-2.6	8.0
Michigan	10,120,860	620,980	15.1	-1.3	7.0
Minnesota	5,132,799	349,021	21.0	-11.7	5.0
Missouri	5,800,310	365,204	15.3	-3.6	7.0

College Enrollment Profile in the 25 Largest States (contd.)

State	2005 Population	Fall 2004 Enrollment	with Bachelor's Degree	High-school Grad. 2002-03 - 2015-16	High-school Dropout Rate
New Jersey	8,717,925	380,374	20.9	18.0	5.0
New York	19,254,630	1,141,525	17.3	-6.5	8.0
North Carolina	8,683,242	472,709	16.9	18.4	9.0
Ohio	11,464,042	614,234	15.0	-3.8	6.0
Pennsylvania	12,429,616	688,780	15.6	-4.8	5.0
Tennessee	5,962,959	278,055	14.4	3.4	11.0
Texas	22,859,968	1,229,197	17.4	15.5	9.0
Virginia	7,567,465	425,181	19.5	9.0	7.0
Washington	6,287,759	343,524	20.4	-0.4	7.0
Wisconsin	5,536,201	351,506	16.3	-10.4	7.0
<i>Total</i>	247,705,824	14,379,286	17.2		

*The 25 largest states represent 84% of the nation's population and 83% of national enrollment

Source: U.S. Dept of Commerce, Census Bureau, U.S. Department of Education, College Board's Annual Survey of Colleges,

Annie E. Casey Foundation, Kids Count Data Book, 2006



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Enrollment Trends by Control and Affiliation of Institution — 1980–2015

	1980	1990	2000	2004	2015 P
Total Enrollment (in millions)	12.1	13.8	15.3	17.3	19.9
Enrollment in Public Institutions	9.5	10.8	11.8	13.0	15.0
Enrollment in Private Institutions	2.6	3.0	3.5	4.3	4.9
% Independent private not-for-profit	57.2%	49.6%	44.3%	42.3%	
% Religiously affiliated private not-for-profit	38.1%	43.2%	43.1%	40.3%	
% Private for-profit	4.2%	7.2%	12.6%	17.4%	

P – Projected. Source: U.S. Department of Education

Industry Snapshot — Fall 2004

Distribution of Institutions and Enrollment by Control and Type of Institution

Number of Institutions = 4,216, Total Enrollment = 17.3 million

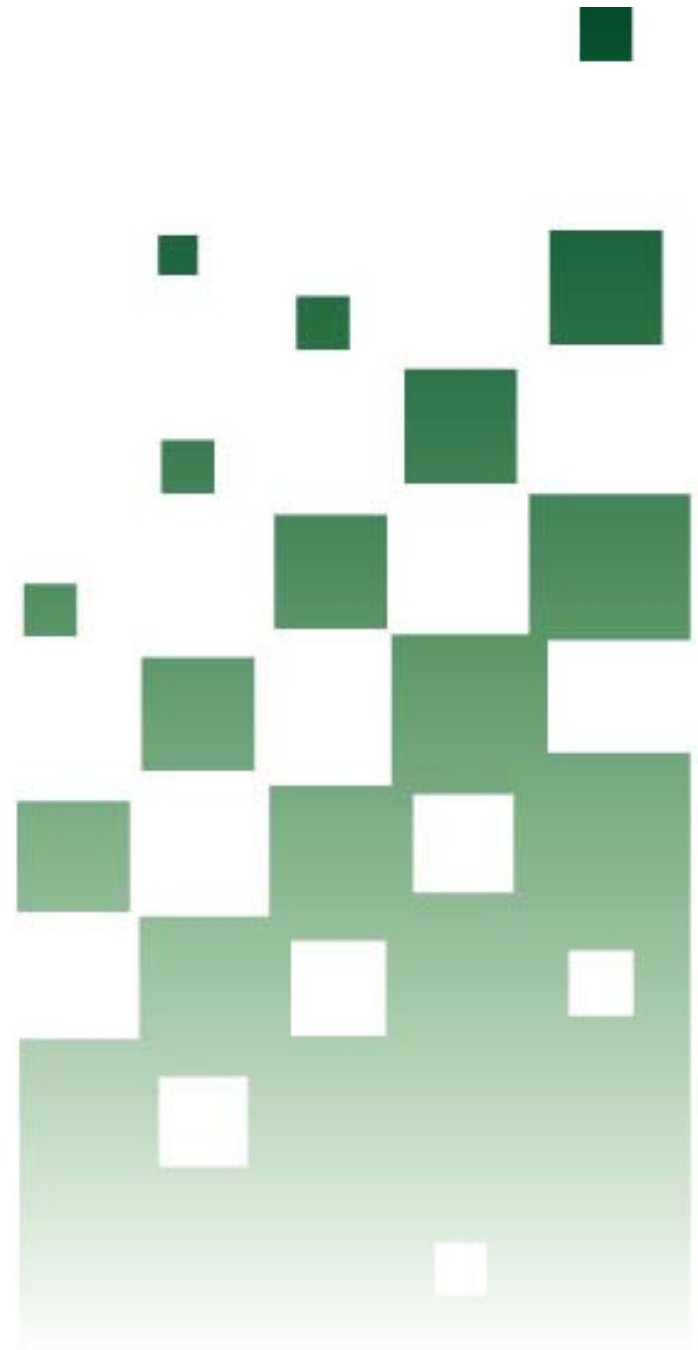
Control/Type of Institution	% of Students	% of Institutions	Avg Tuition	% of Students With Financial Aid
Public - 4 Year	39.0	15.2	\$5,128	70.0
Public - 2 Year	36.2	25.2	\$2,079	61.0
Private - 4 Year - not-for-profit	19.6	36.2	\$20,045	89.0
Private - 2 Year - not-for-profit	0.2	2.6	N/A	N/A
Private - for-profit	5.0	20.8	\$10,600	92.0
Total	100.0	100.0		76.0

Actual and Projected High School Graduates

Year	High School graduates (in millions)
1990-91	2.5
2006-07	3.1
2009-10	3.3
2015-16 (Projected)	3.2

Capital Decisions, Debt Capacity and Credit Ratings

Susan Carlson, Director
Standard & Poor's
312-233-7006
susan_carlson@sandp.com



Capital decision making

- ◆ Growth or “boom” states:
 - Building facilities to keep up with growth
 - Prioritizing projects
 - What is the funding mix? Gifts, student revenues, state capital grants,?
 - Knowing when to say ‘NO’
 - State capital grants: most growth states have large established public H.Ed systems

Capital decision making, continued

- ◆ Demographic loss states:
 - Renovate or replace facilities to stay competitive
 - Funding mixes
 - Publics: are state operating appropriations based on enrollment?
 - Privates: what's the market niche?
Where do students come from?

Capital decision making, continued

- ◆ States on the margin:
 - Slightly up, slightly down (Midwest)
 - More difficult to decide course of action
 - Harder to predict long-term enrollment
 - Demographic or enrollment projections can change with the national or regional economy (Michigan), or disasters (Rita/Katrina)

Capital decision making, continued

- ◆ Considerations for all:
 - Planning and prioritization
 - Borrowing too far ahead of the revenue stream(s)
 - Active monitoring of the capital plan
 - Fundraising capacity and staffing
 - Publics: availability of state capital support

Capital decision making, continued

◆ Management:

- Other options explored? (scheduling; distance learning; coordination with other institutions?)
- Admissions management
- Managing the student experience in either an up or down cycle
- Anticipating facility/capital needs for changing student profiles (more transfers, non-traditional, on-line students)
- Housing system impact can be more severe than overall institutional impact

Credit Factors: Debt

◆ Debt Capacity

- Debt burden (debt service as percent of expenses)
- Liquidity-to-debt ratios
- Is debt **revenue-producing**?
 - Gifts with bridge financing;
 - Future state capital grants;
 - New vs. replacement housing
 - Predictability of the pledged revenue source
- Avoid the “if we build it, they will come” syndrome. Show solid demand and revenue

Credit Factors: Debt

- ◆ There may be more credit flexibility regarding debt capacity if:
 - Financial position is stable and positive
 - Formal debt policy exists to force institutional prioritization
 - Auxiliary systems generate coverage and cash-flow for maintenance projects

Credit Factors: Finances

- ◆ We expect an institution to manage through enrollment and funding fluctuations
- ◆ Conservative budgets
- ◆ Budget flexibility

Credit Factors: Management

- ◆ Plan and monitor
- ◆ Prioritize capital
- ◆ Think 10-20 years out in facility needs, not just 5-years out
- ◆ Be smart (and strategic) in cuts, realignments and priorities

Credit Factors: Conclusion(s)

1. Avoid the 'perfect storm' from multiple factors weakening at the same time
2. Credit ratings should not guide strategic capital decisions
3. A rating down-grade may not be a bad thing it might provide short-term debt capacity