Fitch Ratings - New York - 11 May 2020: Fitch Ratings has affirmed the long-term 'AAA' ratings on approximately $128 million of taxable revenue bonds, series 2016 issued by the Health and Educational Facilities Board of the Metropolitan Government of Nashville and Davidson County, Tennessee on behalf of Vanderbilt University (VU).

Fitch has also assigned VU a 'AAA' Issuer Default Rating (IDR).

In addition, Fitch has affirmed the 'F1+' Short-Term ratings on VU's $200 million taxable and tax-exempt commercial paper (CP) program.
The Rating Outlook is Stable.

SECURITY

The bonds are an unsecured general obligation of Vanderbilt, payable from all legally available funds.

ANALYTICAL CONCLUSION

The 'AAA' IDR and bond ratings reflect Vanderbilt's exceptionally strong resource base in context of its strong operating profile and low debt load. The university has very strong student demand and pricing flexibility, a well-diversified revenue base, consistently strong operating cash flow and robust fundraising to support strategic and capital investment needs.

The recent outbreak of coronavirus and related containment measures create an uncertain environment for the U.S. public finance higher education sector. Fitch's forward-looking analysis is informed by management expectations and by Fitch's common set of baseline and downside macroeconomic scenarios. Fitch's scenarios will evolve as needed during this dynamic period. Currently, Fitch's baseline scenario includes a sharp economic contraction in the second quarter, with sequential recovery starting in the third quarter. For higher education, the baseline case assumes that most residential campuses will reopen for fall 2020 following three to four months of closure.

The Stable Outlook reflects VU's resilience against expected revenue pressure under Fitch's baseline coronavirus scenario, including suspension of campus activity and a shift to online learning beginning in March. VU's financial profile is also resilient to more severe revenue stress under Fitch's downside case, which assumes a slower economic recovery and
prolonged or recurring coronavirus-related disruptions such as extended lockdowns and campus closures into 2021.

The 'F1+' Short-Term rating corresponds to VU's 'AAA' IDR and is consistent with VU's stronger revenue defensibility assessment, neutral debt structure and contingent liability assessment and coverage of maximum potential liquidity demands presented by its CP program from immediately available liquid resources.

KEY RATING DRIVERS

Revenue Defensibility: 'aaa'

Very Strong Demand and Well-Diversified Revenues

Vanderbilt has an excellent market position, with very selective admissions and a national draw resulting in very strong tuition price flexibility. Revenue sources are balanced between net student fees, research funding, contractual payments from Vanderbilt University Medical Center (VUMC), investment and endowment support and fundraising.

Operating Risk: 'aa'

Strong Cash Flow Margins; Robust Fundraising for Capex

The university has a track record of very strong cost management and financial performance, with cash flow margins averaging about 15% over the past three years. Sizable long-term capital plans, focused on
construction of residential colleges to replace traditional campus housing, are flexible as to timing and are mitigated by VU's resource base and very strong capital fundraising capacity.

Financial Profile: 'aaa'

Exceptional Resource Base with Low Leverage

VU's exceptionally strong resource base and low leverage support the 'aaa' financial profile assessment. Resources improved further in 2019 with $1.4 billion of proceeds from the securitization of certain VUMC-sourced revenues under a trademark license (TML) agreement. Available funds (cash and investments not permanently restricted) now exceed $6 billion, more than 10x the university's adjusted debt as of June 30, 2019, and a second TML securitization transaction in fiscal 2020 generated approximately $350 million in additional proceeds.

ASYMMETRIC ADDITIONAL RISK CONSIDERATIONS

No asymmetric factors affected the ratings.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Not applicable for 'AAA' ratings.
Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Significant unexpected resource deterioration more severe than Fitch's current downside assumptions, whether due to operating or investment stress or due to capital and debt plans, such that available funds-to-adjusted debt deteriorates sustainably from the current level in excess of 1,000% to approximately 400%-500% or less.

--Severe and continuing financial stress at VUMC or other VU operating challenges that weaken VU's operating cash flow margin sustainably to about 10% or worse, in conjunction with deterioration in the university's leverage position with available funds-to-adjusted debt falling precipitously toward approximately 500% or less, could pressure the rating.

**BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Public Finance issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/1011579](https://www.fitchratings.com/site/re/1011579).

**CREDIT PROFILE**

VU is a private comprehensive university located in Nashville, TN. The university serves a total headcount enrollment of 13,131 students as of fall 2019 including traditional undergraduates (52%) and graduate and professional students (48%). The previously consolidated VUMC became an independent and legally separate entity in April 2016; the reorganization materially reduced VU's leverage and healthcare exposure.

VUMC Relationship and TML Securitizations

VU and VUMC remain affiliated and strategically aligned, including through ongoing agreements and academic initiatives. Contractual payments from VUMC, including under the TML, still account for nearly 20% of VU's total operating revenue. VU has recently monetized certain payment streams due from VUMC under the perpetual TML. In July 2018, VU securitized the next 30 years of TML base payments (approx. $60 million per year and escalating 3% annually) for approximately $1.4 billion. VU completed a similar smaller transaction in December 2019, selling a portion of its 1%-of-VUMC-revenue royalty stream for 30 years for additional proceeds of approximately $350 million. The bulk of the proceeds from both transactions have been invested as quasi-endowment, largely for scholarship support. In both transactions, VU retained all its enforcement rights under the TML and other VUMC separation agreements.

Vanderbilt Well-Positioned to Weather Coronavirus

VU expects softer operating revenue and bottom line results potentially by $25 million for fiscal 2020 (year ended June 30) due to room and board adjustments, direct aid to students, maintenance of most payroll through May, and disruption of research activities especially in the medical school. Fiscal 2020 revenue pressures are mitigated by the pandemic's onset late in the academic and fiscal year, expense savings from both reduced activity and active cost management initiatives to offset revenue pressure, and federal stimulus funds.
Fitch's baseline expectation is that campus activity will resume for fall 2020, but that the pandemic and resulting economic stress will cause sector-wide pressure affecting most or all of VU's key revenue streams -- including net tuition revenue, research funding, VUMC contractual payments and endowment support -- at least into fiscal 2021. Fitch expects VU will continue making cost adjustments where necessary to maintain a sustainable budget, and the university has solid flexibility on the timing of major capital plans. Even in the event of sharper or prolonged revenue pressure in Fitch's downside case, Fitch expects Vanderbilt will maintain its very strong demand and operating profile, and that the university's robust financial profile will support continued exceptionally strong capacity, consistent with the current rating level, to meet financial commitments.

**REVENUE DEFENSIBILITY**

VU has a leading academic reputation with highly ranked undergraduate, graduate and professional programs. Enrollment has intentionally been held flat just below 6,900 at the undergraduate level, while combined graduate and professional enrollment has grown incrementally to approximately 6,245 in fall 2019 from 5,684 in fall 2015.

While fall 2020 enrollment remains uncertain, Fitch expects VU's strong market position will continue to support demand in the long run. The university had extremely competitive student demand indicators through fall 2019 with continued applications growth, an acceptance rate of 9% and a matriculation rate approaching 50%. VU has excellent student quality, with 97% freshman-to-sophomore retention and a 93% 6-year graduation rate, and a national draw. Approximately 90% of incoming freshmen are from out-of-state, including over 10% international, though Fitch expects this balance may shift toward in-state and regional students for fall 2020.
Strong fundamental pricing power is evident in steady net tuition per FTE growth averaging over 2%, as annual price increases are unlikely to affect enrollment levels. Despite strong underlying flexibility to raise prices, net tuition per FTE growth will be limited by substantial institutional aid. VU's relatively high discounting for its demand profile reflects VU's mission-driven choice to provide significant aid from endowments, annual fundraising and operations. Institutionally funded aid is likely to increase as a result of rising unemployment and lower family incomes driven by the pandemic. This may pressure net tuition revenue over the next one to two fiscal years due to VU's need-blind admissions and commitment to meet demonstrated need without loans. However, Fitch expects strong demand will continue to support pricing flexibility over time.

Endowment support increased sharply starting in 2019 as proceeds of the first TML securitization, invested as quasi-endowment for scholarships, phased into the endowment spending formula. The spending policy remains sustainable and lower than most peers with similarly large endowments, with an effective payout of generally 4%-5%. A policy spending target based on an average of the previous three calendar year-end market values, as well as substantial recent additions to the endowment, will mitigate effects to the operating budget of recent investment market volatility. The university also has flexibility to reduce its endowment spending rate if necessary to preserve long-term value against larger market swings.

Other sources help diversify VU's revenue base and -- despite across-the-board pressure in the current environment -- would typically help offset volatility in net tuition or investment income. Contractual payments from VUMC account for roughly 20% of VU's operating revenue. VUMC revenues consist of payments under several agreements and consist of approximately 40% purchased services (ground lease, utilities, security, etc.), 40% direct academic support (research and programmatic overlap) and ~20% TML payments not securitized by VU. Remaining TML payments include variable payments tied to VUMC's total revenue and profit, and
are likely to be lower for at least fiscal 2020 due to reduced health system volumes and higher expenses as a result of the pandemic. Research funding (~17%) and annual unrestricted fundraising (10% including net assets released from restriction) also help round out net student fees (31%) and investment returns (16%).

**OPERATING RISK**

The university has demonstrated good fundamental cost flexibility with a track record of strong operating performance. Operating margins and cash flow margins have averaged 7% and 15%, respectively, since fiscal 2017. Fitch expects VU will maintain sufficient cash flow margins around 10% or better through coronavirus-related pressure over the next one to two fiscal years, but that its strong cost flexibility will support a return to margins in line with recent historical results over time.

VU's sizeable capital plans and average age of plant around 13 years are offset by robust fundraising and a high level of recent capital investment that provides good flexibility. Sizeable capital plans are driven by continuing investment to expand its residential college model to all undergraduates. The current $500 million three-phase project has been underway since 2018 and is expected to be completed in 2023. VU's last comprehensive campaign ending in 2011 raised nearly $2 billion versus a $1.75 billion goal (about 40% for VUMC), and the university has continued robust fundraising for both endowment and capital uses.

**FINANCIAL PROFILE**

VU's exceptionally strong balance sheet resources and net leverage position are key credit strengths. Available funds totaled $6.3 billion at
June 30, 2019, up from approximately $43 billion the prior year due to the TML monetization, strong cash flow and investment gains over that period. Available funds exceed Fitch-adjusted debt by over 10x, significantly stronger than peer levels. Adjusted debt of $617 million includes $542 million of direct debt and $75 million of operating lease debt-equivalents, capitalized by Fitch at 5x annual expense.

The 'aaa' financial profile assessment also incorporates VU's resilience to severe portfolio and operating stresses using our global baseline and downside case assumptions. Assuming all previously planned additional debt, near-term investment losses approaching 40% fiscal YTD in the downside case, a slow and partial recovery in market values, and stressed cash flows not recovering substantially above 10% for several years, VU could still maintain available funds-to-adjusted debt solidly above 500% and stabilizing closer to 700%. There are no concerns about debt service coverage (over 10x in fiscal 2019) and liquidity (available funds equaled nearly 5x annual expenses), and VU has some additional debt capacity at the rating level through Fitch's downside case, including for a $100 million facility closed in 2019 to be funded in July 2020.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS
The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

**RATING ACTIONS**

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**VIEW ADDITIONAL RATING DETAILS**

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APPLICABLE CRITERIA

U.S. Public Finance College and University Rating Criteria (pub. 26 Mar 2020) (including rating assumption sensitivity)

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 27 Mar 2020) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Nashville & Davidson County Metropolitan Government Health & Educational Facilities
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Fitch Affirms Vanderbilt University (TN) Ratings at 'AAA'; Outlook Stable