S&P Global
Ratings

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The Health & Educational Facilities Board of the Metro Government of Nashville & Davidson County, Tennessee
Vanderbilt University; CP; Private Coll/Univ - General Obligation

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Vanderbilt Univ, Tennessee		
Nashville & Davidson Cnty Metro Govt Hlth & Ed Fac Brd (Vanderbilt Univ)		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings has affirmed its 'AA+' long-term rating on Vanderbilt University (VU), Tenn.'s debt outstanding. The outlook is stable. At the same time, S&P Global Ratings affirmed its 'A-1+' short-term rating on VU's commercial paper (CP) programs. All debt is an unsecured general obligation (GO) of the university.

The long-term rating reflects our view of VU's extremely strong enterprise profile and very strong financial profile. We base the enterprise profile on the university's market position as well as its demand profile and impressive fundraising track record. The financial profile incorporates VU's healthy endowment, history of positive full-accrual operating results, and a reduction in exposure to its swap portfolio. Combined, these credit factors lead to an indicative stand-alone credit profile of 'aa+' and a long-term rating of 'AA+'.

The rating reflects our view of Vanderbilt's:

- Strong student demand, with an undergraduate selectivity rate of 9.6%, strong application volume, and strong student quality;
- Healthy endowment net assets of $4.6 billion as of June 30, 2018;
- Stable and strong management team;
- History of positive financial operations, with a $93.7 million surplus in fiscal 2018. We expect continued positive operating margins in fiscal 2019 and over the medium term; and
- History of strong fundraising, which includes the campaign that raised $1.94 billion when it wrapped up in 2011.

The university's short history of operations post separation, and selectivity and matriculation rates, as well as expendable resources to operations that would need to improve significantly for us to consider a higher rating partially offset these credit factors.

The short-term rating reflects our view of VU's adequate liquidity, sufficiency of the pledged assets, and unsecured GO pledge. The university committed several sources of funds to guarantee the full and timely purchase of any obligations tendered in the event of a failed remarketing. We believe the funds, which are held in high-quality, fixed-income securities, provide ample liquidity. To supplement cash and securities, VU also maintains a general-use line of credit with a maximum commitment of $250 million. Management has established clear and detailed procedures to meet liquidity demands as needed. We will monitor the credit quality, liquidity, and sufficiency of the assets that the university pledges monthly. As of Oct. 31, 2018, VU had $1.8 billion in same-day discounted assets to cover the $115 million in CP outstanding. In November 2018, VU entered into a private placement for $300 million. The university used a portion of the proceeds to refund all CP outstanding. Vanderbilt does not plan to draw on its CP over the medium term but does plan to draw as much as $90 million in 2021-2023.

In April 2016, the university separated its clinical operations from Vanderbilt University Medical Center (VUMC), a newly formed 501(c)(3). The transaction closed April 29, 2016, at which time VU defeased $849 million of debt. The university and the medical center now have an academic affiliation. The separation results in VU receiving substantially less of its total revenue from health care, which accounted for 69% of the university's total revenues in fiscal 2015. However, as a result of the reorganization, the university's associated operating expenses and debt also declined significantly. The university retained all but $79 million of its endowment. With the separation, the university reduced its debt substantially, going to $308 million in debt outstanding post-separation from $1.2 billion at fiscal year-end 2015. As of fiscal year-end 2018, the university had $359 million in debt, including $244 million fixed-rate, and $115 million taxable CP. With the additional debt that was incurred in fiscal 2019, the university has on a pro forma basis, a still modest $537 million in debt outstanding.

Outlook

The stable outlook reflects Vanderbilt's successful transition of its operations and cash flow, strong balance-sheet metrics relative to those of peers, and solid demand profile.

Upside scenario

We could raise the rating if the university improves expendable resources to debt and operations and continues its strong surpluses, while strengthening its enterprise profile relative to the 'AAA' rating category.

Downside scenario

Although unlikely, we could lower the rating if VU experiences difficulty in maintaining positive surpluses, or if the university issues significant debt that weakens financial resources to levels inconsistent with the current rating level.

Enterprise Profile

Industry risk

Industry risk addresses the higher education sector's overall cyclicality as well as 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. Our assessment of Vanderbilt's industry risk incorporates the separation of health-care operations and assumes the university will generate a significantly lower percentage of revenues from health-care operations.

Economic fundamentals

In our view, Vanderbilt has geographic diversity because most students come from around the nation and outside the U.S. Only 16% of all students and 9% of undergraduates are from Tennessee. Therefore, the U.S. GDP per capita anchors our assessment of the university's economic fundamentals.

Market position and demand

Founded in 1873, Vanderbilt is a private, coeducational, nonsectarian university in Nashville. The institution's 10 schools and colleges are on a well-maintained 330-acre campus. It has 41 residence halls, 54 academic buildings, and a 40,000-seat football stadium. The university's 10 schools and colleges include: College of Arts and Science (the largest), Blair School of Music, Divinity School, School of Engineering, Graduate School, School of Law, School of Medicine, School of Nursing, and Owen Graduate School of Management, as well as the Peabody College of Education and Human Development. The institution's leading competitors include Duke University, Yale University, Harvard University, and Princeton University.

VUMC operates as a not-for-profit academic medical center financially and is legally distinct from the university. It runs the hospitals and clinics, clinical departments, and the physician practice plan. VU is responsible for the school of medicine's and school of nursing's faculty appointments and promotions and Ph.D programs in biomedical sciences, as well as research in the basic science departments and related centers. Vanderbilt conveyed its clinical assets and operations to VUMC. The two entities have an academic affiliation agreement through which VU receives an indexed payment to support its research. In addition, the university receives payments through a trademark license agreement for the use of the Vanderbilt name.

Demand

In fall 2018, total enrollment was 12,824, of which 54% were undergraduates. Vanderbilt has no plans to increase its undergraduate enrollment. While freshman applications declined slightly in two of the past five years, applications peaked in two years (fall 2016 and 2018) within the same period. Management reports a 9% increase in applications to 34,313 in fall 2018 as a result of the university's reputation for its financial assistance. VU offers need-blind admissions and meets 100% of demonstrated student need. Beginning in fall 2009, the university eliminated need-based loans from the undergraduate financial-aid packages and, depending on each student's circumstances, it replaced those loans with grants and scholarships.

Vanderbilt is quite selective, having accepted only 10% of its applicants for fall 2018. The matriculation rate has gradually improved from 41% in fall 2013 to 49% in fall 2018, which we consider strong due to the competition for high-quality students. In our opinion, the geographic draw is diverse, with only 9% of undergraduates from Tennessee. We consider student quality strong, with an average ACT score of 34. We also view student retention as strong, with 97% of freshmen returning for their sophomore year. We believe the university continues to have a strong demand profile given its high selectivity. We expect overall enrollment will be stable.

Fundraising

In 1999, VU began a $1 billion capital campaign, which it increased to $1.25 billion and then to $1.75 billion by June 30, 2011. It closed the campaign at fiscal year-end 2011, having raised gifts and pledges of $1.94 billion. The total includes more than $400 million of stock, which the Ingram family and the Ingram Charitable Fund donated to the university in the past decade. Given that the strategic plan was recently finalized, Vanderbilt is in the initial stages of planning a new capital campaign and preparing to launch its next fundraising campaign that will focus on need-based financial aid for all students, furthering the residential college halls' system, and other discovery and learning initiatives. In the six years since the most recent campaign ended, VU has raised $732 million of private gifts and pledges for operating, plant, and endowment. The university continues to work to enhance its philanthropic support, raising $253 million in fiscal 2018. Alumni participation has also increased, rising to 28% in fiscal 2018, and the university is looking to improve this participation rate over the next several years.

Management and governance

The senior leadership team is stable with significant institutional experience. The chancellor has spent 30 years at the university, including 11 in his current role. There are 56 members of the board of trust, consisting of 24 regular trustees and 32 trustee emeriti, who do not vote. The board governs Vanderbilt and operates under a standard committee structure. Management recently completed a university-wide strategic plan. The strategic initiatives center on four priority areas: launching new trans-institutional programs that strengthen research and graduate and undergraduate programs; defining the residential, research-based undergraduate liberal arts education; leading technology development; and becoming leaders in health-care innovation.

Financial Profile

Financial management policies

Vanderbilt has formal policies for its endowment as well as its debt and liquidity. It monitors liquidity closely relative to its endowment, capital, and debt needs. As with other institutions with large endowments, VU's management places importance on oversight and operations of its endowment. The financial policies assessment reflects our opinion that, although there might 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 VU's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure, as well as a comparison of these policies with those of similar providers. Overall, we view the financial policies as appropriate for the institution.

Financial performance

The full effect of the separation of VU from VUMC came in fiscal 2017, the first full fiscal year of the separation. We consider the university's revenue streams diverse. The largest components of Vanderbilt's operating revenues are tuition and student fees (42.2%), grants and contracts (11.3%, excluding facilities and administrative cost recovery), and endowment (15.1%). Before the separation, health-care revenues accounted for almost 70% of total operating revenues.

In fiscal years 2017 and 2018, VU reported operating surpluses of $70 million and $93.7 million, respectively. We expect full-accrual operations to remain positive. In fiscal 2018, operating revenue increased $23 million, or 2%. Tuition and fees had a healthy increase due to changes in student enrollment, credit hours, and tuition increases. However, revenues from grants declined, largely due to federal funding constraints. However, the modest growth in revenues was offset by solid expense controls with supplies and services decreasing substantially. This helped VU maintain its robust margins.

Trademark license securitization

As part of the separation from VUMC in April 2016 and in consideration for leveraging the Vanderbilt University brand, VUMC committed to a trademark licensing agreement with VU in perpetuity. In July 2018, VU securitized the upcoming 30-year term of one of the university's trademark revenue streams and the remaining $89.6 million balance of a promissory note receivable. The securitization occurred on a true-sale basis to a group of external investors. As a result of the transaction, VU received $1.43 billion in net cash. VU entered into this transaction to further diversify its revenue stream away from health care and to help build its endowment. The university will invest the net proceeds in the endowment during fiscal 2019. From an operation perspective, we expect that VU will see increased distributions from its endowment and lower revenues from VUMC. The impact of the transaction will help diversify the revenue base but will not change our expectations of continued solid operating margins. On the balance sheet, the endowment will increase but VU will also record a liability associated with the deferred revenue that will amortize over the life of the agreement.

Financial resources

Until the separation from VUMC and defeasance of debt, we had considered VU's financial resources low for the rating category relative to operations. However, given the separation and the significant reduction in debt offset by the transfer of 51% in net property plant and equipment, VU's balance sheet improved significantly. Expendable resources increased by 9% in fiscal years 2017 and 2018. For fiscal 2018, expendable resources were $4.2 billion, representing 288% of operations, and were 631% of pro forma debt including the $300 million direct-placement debt issued after the fiscal year-end.

For fiscal 2018, the endowment had a market return of 12.6%. As of June 30, 2018, its value was $4.6 billion. The endowment's asset allocation is 25.6% in equities, 24.8% in private investments, 20.3% in hedged strategies, 6.8% in real assets, 11% in fixed-income securities, 2.8% in commodities, and 6% in cash. As of Oct. 31, 2018, the university had approximately $1.8 billion in funds available daily, which well exceeded any potential capital calls. Beginning with fiscal 2016, the endowment's spending policy is 5.0% of the average market value for the previous three calendar years. With the increase in endowment, we do not expect any changes to VU's asset-allocation strategy but we would expect Vanderbilt to be affected by the new endowment tax beginning in fiscal 2020. The tax would reduce the endowment value, thereby affecting future earnings and what could be distributed for university programs and student support. However, we do not expect this to have a significant financial impact on the ratings.

Debt and contingent liabilities

Due to the separation, VU reduced its debt, which improved its financial resource ratios. As of June 30, 2018, the institution had $359 million of debt, which included $244 million fixed-rate and $115 million taxable CP. It has authorization for up to $200 million of combined tax-exempt and taxable CP but has no plans to draw on its CP over the near term. In May 2018, VU locked into a note purchase agreement payable over 30 years. VU drew on the full

$300 million note in November 2018 (fiscal 2019) and used a portion of the proceeds to repay all taxable commercial paper outstanding. The remaining proceeds will fund $160 million of the next phases of its residential colleges construction, as well as $25 million for strategic real estate acquisitions. We have reviewed the terms of the note purchase agreement and while there are terms that could lead to acceleration of the debt outstanding, given the strength of VU's balance sheet we do not view this as presenting a significant risk.

Most of VU's debt is fixed-rate and as of June 30, 2018, it had $112 million in fixed payer swaps outstanding after novating and terminating swaps over the past several years. At the end of fiscal 2015, the university had $482.9 million in fixed payer interest rate exchange agreements and posted $84.4 million in collateral. Following the separation, it had $216 million in fixed payer swaps. In fiscal 2016, $150 million of fixed-payer swaps were novated to VUMC, and $115 million in fixed payer swaps were terminated. In 2017 and 2018, VU terminated $50 million of fixed payer swaps. In August 2016, the university terminated all of its $500 million basis swap portfolio. As of June 30, 2018, the mark-to-market value of the $112 million notional fixed payer swaps was negative $28 million. There was no collateral posting required. Given VU's substantial liquid resources, we view the debt portfolio's liquidity requirements as manageable.

Vanderbilt University Enterprise And Financial Statistics

	--Fiscal year ended June 30--					--Medians for 'AA' rated Private Colleges & Universities--
	2019	2018	2017	2016	2015	2017
Enrollment and demand						
Headcount	12,824	12,592	12,587	12,567	12,686	MNR
Full-time equivalent	12,184	12,052	12,085	12,060	12,143	6,335
Freshman acceptance rate (%)	9.6	10.9	10.7	11.7	13.1	25.3
Freshman matriculation rate (%)	48.6	47.1	45.9	43.7	41.5	MNR
Undergraduates as a % of total enrollment (%)	53.5	54.7	54.6	54.8	54.0	71.0
Freshman retention (%)	97.0	97.0	97.0	97.0	97.0	94.5
Graduation rates (six years) (%)	94.0	92.0	92.0	92.0	93.0	MNR
Income statement						
Adjusted operating revenue ($000s)	N.A.	1,536,689	1,505,588	1,411,996	1,352,339	MNR
Adjusted operating expense ($000s)	N.A.	1,442,953	1,435,596	1,345,116	1,330,353	MNR
Net operating income ($000s)	N.A.	93,736	69,992	66,880	21,986	MNR
Net operating margin (%)	N.A.	6.50	4.88	4.97	1.65	2.02
Change in unrestricted net assets ($000s)	N.A.	241,320	171,675	(380,610)	98,826	MNR
Tuition discount (%)	N.A.	44.5	45.1	43.5	44.3	38.0
Tuition dependence (%)	N.A.	35.0	34.1	35.1	36.2	MNR
Student dependence (%)	N.A.	42.2	44.9	44.5	44.7	58.9
Health care operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	N.A.	11.3	11.9	12.7	13.1	MNR
Endowment and investment income dependence (%)	N.A.	15.1	14.9	14.2	13.1	MNR

Vanderbilt University Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					--Medians for 'AA' rated Private Colleges & Universities--
	2019	2018	2017	2016	2015	2017
Debt						
Outstanding debt ($000s)	N.A.	359,072	366,480	299,980	1,222,339	356,370
Proposed debt ($000s)	N.A.	300,000	N.A.	N.A.	N.A.	MNR
Total pro forma debt ($000s)	N.A.	659,072	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	33,658	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	1.53	1.64	8.32	7.94	MNR
Current MADS burden (%)	N.A.	1.20	1.20	1.51	9.64	4.00
Pro forma MADS burden (%)	N.A.	2.33	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value ($000s)	N.A.	4,608,461	4,136,465	3,795,586	4,093,388	1,461,237
Cash and investments ($000s)	N.A.	5,652,333	5,369,472	4,926,631	5,222,522	MNR
Unrestricted net assets ($000s)	N.A.	3,311,041	3,069,721	2,898,046	3,278,656	MNR
Expendable resources ($000s)	N.A.	4,160,753	3,782,002	3,478,176	5,080,670	MNR
Cash and investments to operations (%)	N.A.	391.7	374.0	366.3	392.6	351.2
Cash and investments to debt (%)	N.A.	1,574.2	1,465.1	1,642.3	427.3	480.4
Cash and investments to pro forma debt (%)	N.A.	857.6	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	N.A.	288.3	263.4	258.6	381.9	226.0
Expendable resources to debt (%)	N.A.	1,158.8	1,032.0	1,159.5	415.7	317.0
Expendable resources to pro forma debt (%)	N.A.	631.3	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	12.7	12.5	12.4	12.0	13.7

Ratings Detail (As Of December 13, 2018)

The Hlth & Ed Facs Brd of the Metro Govt of Nashville & Davidson Cnty, Tennessee

Vanderbilt Univ, Tennessee

Nashville & Davidson Cnty Metro Govt Hlth & Ed Fac Brd (Vanderbilt Univ)

Long Term Rating	AA+/Stable	Affirmed

Vanderbilt Univ CP

Short Term Rating	A-1+	Affirmed