

University of Western Ontario

February 15, 2022

This report does not constitute a rating action.

Credit Highlights

Overview

Enterprise profile

The University of Western Ontario continues to benefit from excellent student quality metrics and a solid market position.

-- Its core catchment area in the Province of Ontario has excellent economic fundamentals and supportive demographics.

-- However, as Western attracts most of its students from Ontario, it has a more limited geographic draw relative to Canadian peers.

-- Despite the impacts of lockdowns and remote learning, student demand and quality have remained high.

Financial profile

Despite operational disruptions, the COVID-19 pandemic has not had a material impact on Western's financial performance.

-- We expect that, driven by strong projected enrollment, the university will continue generating positive operating margins.

-- Very strong operating margins in the past several years fueled by enrollment growth have helped maintain a moderate debt burden.

-- Western's credit profile is bolstered by strong liquidity.

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S&P Global Ratings' long-term issuer credit rating on the University of Western Ontario is 'AA'. The rating reflects Western's 'aa' stand-alone credit profile, which is based on our combined assessment of the university's very strong enterprise and financial profiles. The rating also reflects our opinion of a moderately high likelihood that the Ontario government would provide extraordinary support in the event of financial distress. The pandemic severely disrupted on-campus activities in the past two years; however, Western has continued to generate very strong financial results, with excellent investment returns and healthy student demand helping to offset losses in ancillary operations and flat government funding and domestic tuition revenue.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that, in the next two years, Western will be able to manage its budgetary pressures to generate strong operating margins greater than 5% of adjusted operating expenses on average, its levels of available

resources will remain high, and it will maintain a healthy enrollment and demand profile. The outlook also reflects our expectation that the university's relationship with the province will be stable.

Downside scenario

We could lower the ratings in the next two years if a material disruption to the university's operations impairs enrollment levels and revenue, resulting in significantly weaker financial performance and available resources. Furthermore, evidence of negative government intervention, a strengthening of our assessment of the link between the university and province, or a significant reduction in our assessment of Western's resilience to an Ontario default scenario could also cause us to lower the ratings on the university, potentially to on par with or below those on the province, depending on the severity.

Upside scenario

An improvement in Western's already healthy enterprise profile could lead to a positive rating action. Specifically, a selectivity ratio consistently below 50% or increased geographic diversification of the student body, with out-of-province students accounting for more than 30% of total full-time equivalents (FTEs), could lead to a positive rating action in the next two years.

Rationale

Founded in 1878 and located in the city of London, Ont., the University of Western Ontario is a research-intensive, doctoral university with 12 faculties and schools, including schools of medicine and dentistry, law, engineering, and business. The local population is approximately 422,000. As of fall 2021, the university had 36,828 FTE students on its main campus, a 4.4% increase from the previous year. It also has affiliations with three research institutes, three university colleges, and two teaching hospitals.

Western's very strong enterprise profile is characterized by a healthy demand profile and market position, as well as good management and governance practices. In fall 2021, the first-year selectivity rate (offers-to-applications) of 64% was higher than typical; however, this is in-line with peer Canadian universities, which all increased domestic offers in anticipation of a drop in international student enrolments. Consequently, Western's total headcount in fall 2021 rose 4.8%, with substantial growth in graduate student numbers helping to offset a modest decline in international enrollment. A high proportion of students (77%) are from Ontario, and we therefore view Western's student draw as having limited geographic diversity relative to that of some peers. The university is working toward increasing its international student body and expanding its source countries, which could support revenue diversity. Western has consistently demonstrated strong retention rates greater than 90% and six-year graduation rates averaging almost 84% in the past four years. Also supporting our assessment is our view of the higher education sector's low industry risk, with counter-cyclicality and low competitive risk and growth. In addition, the university benefits from excellent economic fundamentals, as measured by the province's GDP per capita, which we estimate to be about US\$50,000 in 2021; good income indicators; and moderate employment and population growth projections.

In our view, the university's senior administration has sufficient depth and expertise, and has demonstrated consistent operational effectiveness, as evidenced by a track record of healthy operating margins that we believe lends stability to the credit profile. Overall, we consider Western's transparency and disclosure good, with policies, procedures, and risk management capacity to adequately identify, monitor, and mitigate risks. The university typically conducts its activities according to a four-year operating and capital plan that contains what we view as appropriate assumptions. It prepares externally audited financial statements, which have been unqualified, and has formal policies for endowments, investments, debt, and reserves.

We assess Western's financial profile as very strong, supported by very strong operating margins of almost 14% on a three-year weighted-average basis. Western's fiscal 2021 ended with a very high net operating margin of 15.7% (S&P Global Ratings adjusted), reflecting operating expenditure constraint and high investment income following very strong market returns. However, this was tempered by lower sales and service revenue due to limited on-campus activities. The university anticipates ending fiscal 2022 in a balanced position, with slightly higher revenues largely caused by increased tuition revenue. This will be mitigated by higher-than-expected pandemic-related expenditures and lower-than-anticipated ancillary operations revenues (housing, parking, food services, etc.), which continue to generate weaker results.

Similar to that of Canadian peers, the university's limited flexibility to increase its student-generated revenue somewhat offsets its strong financial performance. This is primarily because Ontario monitors and guides domestic tuition rates and student aid (through the tuition framework), and enrollment expansion (through operating grants, which are not expected to increase in real terms).

Western has what we view as very healthy liquidity. At fiscal year-end 2021, our measure of its available resources (internally restricted net assets plus internally restricted endowments) increased to C\$1.23 billion from C\$968 million the year before. This was sufficient to cover more than 95% of adjusted expenses on a three-year weighted-average basis. At fiscal year-end 2021, total cash and investments increased slightly to C\$2.7 billion from C\$2.3 billion in 2020, equal to almost 7.9x debt outstanding and more than 2x our measure of available resources, indicating very robust liquidity. This high level of cash bolsters our assessment of the financial resources potentially available to the university under a stress scenario. Given that we expect the broader material impacts of the omicron variant to be temporary, Western's liquidity will remain more than sufficient to fund all debt service requirements and provide a significant buffer against medium-term stress.

Western has the eighth-largest endowment among Canadian universities, with a market value of C\$990 million at fiscal year-end 2021. While endowment growth is historically stable year-over-year, high investment returns during the fiscal year of C\$175 million were key in bolstering this growth. Approximately C\$32 million of endowed investment returns were allocated for spending in fiscal 2021, in line with the university's spending policy of 4% of the five-year average market value of the endowment.

In our view, the university has a moderate debt burden. At fiscal year-end 2021, total gross debt outstanding was C\$344.6 million and consisted of: two 40-year fixed-rate bullet debentures totaling C\$288.7 million (maturing in 2047 and 2057); C\$9.4 million related to Western's research park; and C\$46 million in amortizing banker's acceptances (from a C\$100 million nonrevolving facility maturing in fiscal 2027). In our view, Western's debt structure is aggressive, because more than 50% of total debt is non-amortizing; however, the university has established sinking funds to help repay the bullet debentures (C\$39 million at the end of fiscal 2021), partially mitigating the associated risks. Our estimate of maximum annual debt service (which includes an estimated principal component for non-amortizing debt) equals 3.7% of adjusted fiscal 2021 expenses. In our view, the university's debt burden is manageable, given Western's good operating performance and the healthy level of available resources equal to 3x debt based on a three-year weighted average. The university does not expect to take on additional external debt in the next several years and we believe that debt service coverage will remain more than adequate throughout our outlook horizon.

Among rated Canadian universities, Western is the only one to sponsor a wholly defined-contribution pension plan for current employees, shifting the plan's investment risks away from itself. This contrasts with some institutions that face the potential requirement to make special solvency payments on their pension plan deficits. The university has a legacy defined-benefit plan that was in a very modest surplus position of C\$280,000 at fiscal year-end 2021. We do not consider the liabilities associated with this plan significant. Most of Western's postemployment liabilities relate to unfunded non-pension benefits, such as medical and dental. At fiscal year-end 2021, these liabilities amounted to C\$565.3 million, up 0.6% from the previous year. The university took steps to contain the costs of these liabilities in previous labor negotiations.

Based on public disclosures, we do not believe that Western has any additional contingent liabilities that could materially affect our view of its credit profile.

Moderately high likelihood of extraordinary provincial government support

In accordance with our criteria for government-related entities, our view of Western's moderately high likelihood of extraordinary government support reflects our assessment of the university's important role in the province, given that postsecondary education is one of Ontario's priorities in both expenditure and mandate (after health care and school boards), despite recent changes to university funding. Moreover, our assessment of Western's important role recognizes the absence of viable private alternatives. It also reflects the university's size, strong reputation, and research capabilities, which would make it hard to replace. The province's oversight, program-approval rights, and tuition regulation over Western suggest a strong link to the government. Also supporting this

view is that the province provides substantial operating grants, which account for about 21% of the university's total revenue, and it appoints four of 28 board members.

We rate Western two notches above Ontario. The differential reflects our view that there is a measurable likelihood that the university's substantial financial resources would meet ongoing operational and debt service requirements should the government default and temporarily suspend payments to Western. In addition, the differential reflects our belief that the university operates independently of the Ontario government as an autonomous legal entity with ownership of its assets. The board is responsible for the management, administration, and control of Western's property and other assets and all business affairs. We consider the risk of extraordinary negative government intervention to be low, given the university's operational independence, important public policy role, and the government's hands-off approach to the sector.

In January 2019, the government of Ontario imposed a 10% reduction to domestic tuition for the 2019-2020 academic year and a freeze in 2020-2021 and 2021-2022. Furthermore, the province did not provide additional grant revenue to offset the tuition cut and has yet to release an updated tuition framework beyond fiscal 2022. Neither the federal nor provincial government has announced any material financial support to the post-secondary sector. Although we are not expecting any material increase in ongoing operating or capital funding from the province in the medium term, we continue to believe that there is a moderately high likelihood that the province would provide support to Western in a distress scenario.

Key Statistics

University of Western Ontario -- Selected Indicators

	--Fiscal year ended April 30--					Medians for 'AA' U.S. public colleges & universities*
(Mil. C\$)	2022	2021	2020	2019	2018	2020
Enterprise profile						
Full-time equivalent enrollment (no.)	36,828	35,259	33,737	33,353	33,059	38,513
Selectivity rate (%)	63.5	66.3	53.4	54.9	51.5	68.9
Undergraduates as a % of total enrollment	79.8	80.6	79.9	80.5	80.5	78.7
Retention rate (%)	N.A.	N.A.	94.5	93.6	93.4	86.7
Graduation rates (%)	N.A.	85.0	82.9	83.4	83.2	MNR
Financial profile						
Adjusted operating revenue	N.A.	1,280.4	1,290.2	1,305.6	1,259.4	MNR
Adjusted operating expense	N.A.	1,106.5	1,160.7	1,146.4	1,100.3	MNR
Net adjusted operating margin (%)†	N.A.	15.7	11.2	13.9	14.5	0.8
Student dependence (%)	N.A.	35.6	35.1	35.3	34.6	40.0
Government operating grant dependence (%)	N.A.	21.0	20.6	20.4	20.9	19.3
Investment income dependence (%)	N.A.	18.0	3.1	7.1	6.3	1.3
Outstanding debt	N.A.	344.6	352.6	360.8	376.6	1,021.7

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Maximum annual debt service/total operating expense (%)	N.A.	3.7	3.5	3.7	3.9	3.3
Available resources to adjusted operating expenses (%)	N.A.	111.2	83.4	79.1	71.1	36.2
Available resources to total debt (%)	N.A.	357.1	274.7	251.5	207.8	104.9

*U.S. median figures are in U.S. dollars. †As % of adjusted operating expense. N.A.--Not available. MNR--Median not reported.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Published Oct. 10, 2021
- General Criteria: Methodology: Not-For-Profit Public And Private Colleges And Universities, Published Jan. 6, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, Published March 25, 2015
- General Criteria: Principles Of Credit Ratings, Published Feb. 16, 2011

Related Research

- Outlook For Global Not-For-Profit Higher Education: Out Of The Woods But Not Yet In The Clear, Published Jan. 20, 2022
- Australia, Canada, Mexico, And U.K. Universities Medians Report: Credit Metrics Remain Largely Stable Through Persistent Headwinds, Published June 30, 2021
- U.S. Not-For-Profit Public College And University Fiscal 2020 Median Ratios, Published June 23, 2021
- 'Back To School' Will Take On New Meaning This Fall, Published May 27, 2021

Ratings Detail (as of February 15, 2022)*

University of Western Ontario

Issuer Credit Rating	AA/Stable/--
Senior Unsecured	AA

Issuer Credit Ratings History

26-Feb-2013	AA/Stable/--
14-Dec-2010	AA/Negative/--
04-May-2007	AA/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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