S&P Global Ratings

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American University, District Of Columbia; CP; Private Coll/Univ - General Obligation

Primary Credit Analyst:
Nicholas K Fortin, Boston + 1 (312) 914 9629; Nicholas.Fortin@spglobal.com

Secondary Contact:
Jessica H Goldman, Hartford + 1 (212) 438 6484; jessica.goldman@spglobal.com

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American Univ GO		
Long Term Rating	A+/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'A+' issuer credit rating (ICR) and long-term ratings on various series of bonds issued for American University (AU), D.C.
- In addition, S&P Global Ratings affirmed its 'A-1' short-term rating on the university's series 2011 commercial paper (CP) program.
- The outlook, where applicable, is stable.

Security

As of fiscal 2022 year-end, total debt was $745.4 million, largely composed of long-term, fixed rate debt. Total debt outstanding also includes minor finance and operating leases. The series 2015, series 2017, and series 2019 bonds are structured with bullet maturities. The university also maintains a $125 million CP program, which, as of fiscal 2022 year-end, was undrawn. All of the university's debt is a general obligation of AU. Management indicates that there are no plans to issue further debt over the outlook period.

Credit overview

We assess AU's enterprise profile as very strong, characterized by relatively stable demand characteristics and a broad draw for students offset by student success metrics, which are somewhat soft relative to those of similarly rated peers. We assess the financial profile as strong, with a history of robust operating margins and an impressive financial management team offset by an expectation for softer operations over, at least, the next year and all existing bonds that have bullet maturities. We believe these credit factors, combined, lead to an indicative standalone credit profile of 'a+' and a final rating of 'A+.'

The 'A-1' rating reflects our view of AU's self-liquidity program. The university committed several sources of funds, including its working capital and endowment, to support its existing unenhanced CP program ($125 million is authorized with currently nothing outstanding and no planned draws). As of Mar. 31, 2023, AU identified about $413.8 million in (undiscounted) assets available same or next day. We will monitor both the sufficiency and liquidity available on a monthly basis to ensure the university can cover a failed remarketing for the existing CP. In our opinion, there is sufficient liquidity provided through the money held in domestic equities, cash and high-quality, short-term, and fixed-income securities.

The rating reflects our assessment of AU's:

- History of consistent, positive full-accrual operations, although we expect operations will finish closer to breakeven over the next two years;
- Enrollment, which remains flat relative to fall 2017 levels despite some variability due to the pandemic and capacity constraints on campus; and
- Experienced and highly capable management team, which we believe can guide the university through adversity.

Offsetting these strengths, in our view, are AU's:

- A somewhat risky debt profile, which is structured with, exclusively, bullet maturities; and
- Financial resources, which grew steadily over the past five years, but remain modest relative to adjusted operating expenses and total debt.

AU is located on two campuses on 84 acres in northwest Washington, D.C. and is an independent, private, coeducational institution. The university's academic programs are offered through eight major divisions: The College of Arts and Sciences, The School of Public Affairs, Kogod School of Business, Washington College of Law, The School of Communication, The School of Education, The School of International Service, and The School of Professional Studies and Executive Education. Within these divisions, the university offers 80 bachelor's degrees, 99 master's degrees, 11 doctoral degrees, JD, LLM, SJD, and MLS degrees and certificates and associate degrees.

Environmental, social, and governance

We analyzed the university's environmental, social, and governance (ESG) credit factors pertaining to its market position, management and governance, and financial performance. Health and safety risks, which we consider to be a social risk factor, have largely abated and are neutral in our credit rating analysis. All other environmental and governance credit factors are also neutral in our credit rating analysis.

Outlook

The stable outlook reflects our expectation that the university's enrollment will, after some variability in the past several years, stabilize over the outlook period and that student success and demand metrics will, generally, remain at their current, solid levels. The stable outlook further reflects our expectation that, over the outlook period, operations will likely finish closer to breakeven on a full-accrual basis, but that management will continue to find operating efficiencies in order to work back to positive operations.

Downside scenario

We could consider a negative rating action if a trend of enrollment declines materializes and demand characteristics weaken, if AU consistently generates full-accrual operating deficits, or if there is weakening of available resources. During the two-year outlook period, we do not anticipate any additional debt, but expect any issuance would be accompanied with commensurate growth in financial resources.

Upside scenario

A higher rating or positive outlook is unlikely during the outlook period due to the university's debt and available resource ratio levels that remain below average for the rating category. We could consider a positive rating action if the university shows substantial growth in available resources with no significant increase in debt while generating, at least, breakeven full-accrual operations and maintaining or improving current student demand metrics.

Credit Opinion

Enterprise Profile

Market position and demand

AU's demand profile is healthy, in our view, with a broad geographic draw, generally selective admissions, and solid matriculation relative to rating category medians. After rising in 10 of 11 years between fall 2009 and fall 2019, enrollment at AU has fluctuated, with declines in three of the past four years. After a nearly 4% pandemic-driven decline in fall 2020, management loosened selectivity in fall 2021, leading AU to welcome a first-year class of 2,372, its largest on record. This healthy first-year class drove undergraduate full-time equivalent (FTE) enrollment, which typically comprises around 60% of total FTE enrollment, up 9.5% to 8,031. At the same time, the university matriculated, for its second consecutive year, more than 1,800 graduate students, which drove graduate FTE enrollment to 3,766 from 3,428 in fall 2020. Management indicates that while this enrollment growth was great for the university and demonstrated AU's ability to bounce back from the pandemic, the university was overenrolled. Because of this, the university intentionally tightened admissions to near pre-pandemic levels in order to stay within capacity constraints, leading AU to welcome a smaller first-year class of 1,768. This, coupled with fewer new graduate students, drove FTE enrollment down 5.6% to 12,654 in fall 2022. Given the current housing capacity, management indicates that the university is currently at, or very close to, its maximum on-campus enrollment.

Management expects demand will remain steady but stresses its commitment to providing housing for students, which limits the university's ability to materially grow its on-campus population. For fall 2023, management indicates that first-year applications are relatively stable year-over-year, which it believes will yield a class sized similarly to fall 2022. We believe AU is capable of stabilizing enrollment due to seemingly solid demand, but also due to management's identification of and commitment to improving the university's somewhat modest student success metrics; at 86.3% and 79.5%, first-to-second-year retention and graduation, respectively, are low compared with those of peers of similar caliber and rating. Given the university's past strategic plan successes, we expect these metrics will improve over the coming years, which, with steady demand, could keep enrollment stable.

In May 2021, AU publicly launched a $500 million campaign called "Change Can't Wait". The campaign seeks to enhance AU students' experience, increase faculty research and training, and build upon AU's brand in the D.C. area while also connecting with the community. To date, AU has raised $404 million in commitments to date, with management fully expecting to reach its goal by campaign close in fiscal 2024.

Management and governance

Since June 2017, Sylvia Burwell has led the university as its fifteenth president. Before joining AU, Ms. Burwell served as secretary of the U.S. Department of Health and Human Services. Following the retirement of longtime CFO Doug Kudravetz, AU appointed Dr. Bronté Burleigh-Jones as CFO, vice president, and treasurer in 2021. Before AU, Dr. Burleigh-Jones served Dickinson College as vice president of finance for eight years. In addition, Dr. Peter Starr became provost at AU in July 2020 after serving as dean of the university's college of arts and sciences for 11 years. In April 2022, Dr. Linda Aldoory was named as Dr. Starr's replacement as dean. We believe that, overall, the senior team remains stable, and the detailed financial management and tenure of the financial management team provides stability at the current rating. Management sets two-year detailed operating budgets, which reflect contingencies, deferred maintenance, and routine plant renewal (which is less than annual depreciation expense), but do not reflect generally accepted accounting principles.

The board of trustees, which is self-perpetuating, has 31 members, with a limit of 50. Trustees serve for a minimum of a three-year term. Board members are approved by both the General Board of Higher Education and the Ministry of the United Methodist Church.

Financial Profile

Financial performance

Historically, AU has demonstrated consistently positive operating performance, which has lent strength to the overall credit profile. For more than 10 years up until fiscal 2018, the university generated full-accrual operating margins in excess of 6%, but the pandemic has caused some variability in the university's operating success. In fiscal 2021, management enacted a several expense-cutting measures including delayed capital spending, temporarily suspending retirement contributions, a one-week furlough of all faculty and staff, freezing salary increases, implementing a hiring freeze, cutting operating costs, and reducing the salary of certain school administrators. We believe these cost reductions were prudent and helped offset a 10% decline in net tuition revenue and a more than 70% decline in auxiliary revenue. With those reductions and the recognition of federal pandemic-relief funding, AU recorded a modest 1.1% full-accrual operating deficit. In fall 2021, the university welcomed its largest first-year class, saw its second consecutive year of healthy graduate level matriculants, and returned to near-pre-pandemic levels of operation on campus, which, combined, helped adjusted operating revenue up nearly 30% in fiscal 2022. Gross tuition revenue and auxiliary revenue, which combined make up on average 85% of AU's total adjusted operating revenue, rebounded to above pre-pandemic levels. The university also recognized some federal pandemic-relief funds in fiscal 2022. The return to on campus operations, coupled with inflationary and labor market pressures, also drove expenses up 17% compared with fiscal 2021 and 9.5% compared with fiscal 2019, the last fiscal year prior to the pandemic. Overall, the university ended the year with a healthy 8.2% full-accrual operating surplus.

Over the outlook period, we expect operations will finish closer to breakeven. In years past, robust full-accrual operating surpluses were partially driven by steady enrollment growth, rising tuition, and modest year-over-year expense increases. Given the university's current capacity constraints, we expect enrollment will remain relatively flat over the outlook period, which will require management to focus on its tuition and financial aid strategy. We also expect that macroeconomic pressures will slowly lift operating expenses and that the university's continued investment in its employees, students, and campus, while a positive, will come with increased costs. Management indicates that a space-management project is in the works that would optimize the use of university space.

Financial resources

In our view, AU's financial resources are modest for the size and scale of university operations, particularly relative to rating category medians and similarly rated peers. Since fiscal 2017, cash and investments grew 42.6% to nearly $1.4 billion in fiscal 2022 from $951.6 million. This healthy growth was attributed to steady investment returns and consistent full-accrual operating surpluses, but also to the holding of excess bond proceeds in cash; in fiscal 2021, the university recorded about a $115.6 million cash inflow related to its "tap" issuance of the series 2019 bonds. The university recorded similar influxes in cash following the first series 2019 and series 2017 issuances. Importantly, much of the cash currently held by the university is earmarked for various projects across campus. The university's investments alone grew to approximately $1.2 billion in fiscal 2022 from $934.1 million in fiscal 2017. Despite this growth, AU's financial resource metrics remained relatively flat due to the university's growing operations and issuance of debt. Cash and investments relative to adjusted operating expenses were 157.0% in fiscal 2022, down from a high of 190.4% in fiscal 2021. The metric softened in fiscal 2022 largely due to the university's return to full on-campus operations and that impact on operating expenses. Cash and investments to total debt was 182% in fiscal 2022, down slightly year over year. We view this metric in particular as weak relative to rating category medians and that of similarly rated peers. Looking forward, we expect these metrics will remain relatively stable but believe that rising operating expenses could lead to some pressure. Furthermore, we expect the university will, over the coming years, spend down cash to complete capital projects, which we believe could also weaken these metrics.

AU's endowment was valued at $947.8 million as of January 2023. In spring 2020 AU divested its endowment from fossil fuels, as part of the school's overall sustainability goals. Otherwise there have been no material changes to the endowment's asset allocation recently or any expected. According to management, the university can access about 55% of the endowment on a monthly basis. The university's endowment spending policy is 5% of a rolling three-year average although the effective rate is generally below or equal to 3%. Management does not plan any changes to the endowment draw in the near term.

In 2024, AU is expected to break ground on its Student Thriving Complex, a $103.5 million investment in the university campus, which includes renovations to several buildings on campus and the construction of a new athletic facility. The project will be funded with $40 million from AU's "tap" issuance, at least $40 million from fundraising, and approximately $20 million from other sources. Management indicates that there are several other capital projects planned for the medium-term, although details, at this point, are unavailable.

Debt and contingent liabilities

As of fiscal 2022 year-end, total debt was $745.4 million, which includes the series 2015, series 2017, and series 2019 bonds. Total debt outstanding also includes $4.7 million in operating leases and immaterial capital leases. All of the university's long-term debt is fixed rate and secured by a general obligation of the university. The university's long-term debt is structured as bullet maturities, which we view as a credit risk. However, management indicates that, while there are no designated sinking funds established, funds are being set aside each year for the purpose of repaying each series of debt as they come due. We believe the university is also exposed to contingent liquidity risk due to its $125 million CP program, which, as of fiscal 2022 year-end, is undrawn. The program is supported by the university's own self liquidity. We've identified approximately $413.8 million of same- or next-day liquidity, which we believe partially mitigates this risk.

Given the bullet maturities, we smooth debt service in accordance with our criteria over the remaining life of the university's debt and estimate maximum annual debt service of $53.1 million, equivalent to 6.1% of fiscal 2022 adjusted operating expenses. While we view the university's maximum annual debt service as somewhat high, we believe it could come down over time given the lack of additional debt plans.

American University, D.C.--Enterprise And Financial Statistics

	--Fiscal year ended June 30--					--Medians reported for 'A' category rated private colleges and universities--
	2023	2022	2021	2020	2019	2021
Enrollment and demand						
Full-time equivalent enrollment	12,654	13,400	12,538	13,031	13,091	3,350
Undergraduates as a % of total enrollment	55.1	54.7	53.4	53.3	52.0	83.3
First-year acceptance rate (%)	40.6	64.1	38.7	36.1	31.5	70.3
First-year matriculation rate (%)	22.3	18.8	20.8	26.2	29.3	18.0
First-year retention rate (%)	86.3	90.5	84.8	86.8	87.8	85.2
Six-year graduation rate (%)	79.5	78.8	79.1	78.8	79.8	74.9
Income statement						
Adjusted operating revenue ($000s)	N.A.	934,522	725,665	823,257	835,859	MNR
Adjusted operating expense ($000s)	N.A.	863,992	733,874	798,297	789,327	MNR
Net operating margin (%)	N.A.	8.2	-1.1	3.1	5.9	1.6
Change in unrestricted net assets ($000s)	N.A.	-44,020	170,366	8,078	41,116	MNR
Tuition discount (%)	N.A.	30.5	30.4	27.8	27.7	41.1
Student dependence (%)	N.A.	82.2	81.8	85.2	83.7	82.2
Research dependence (%)	N.A.	6.4	6.2	4.5	3.5	3.7
Debt						
Debt outstanding ($000s)	N.A.	745,406	746,046	640,500	640,500	110,132
Current MADS burden (%)	N.A.	6.1	7.1	5.4	5.7	4.2
Average age of plant (years)	N.A.	14.3	14.7	14.5	13.8	15.3
Financial resource ratios						
Endowment market value ($000s)	N.A.	908,905	890,547	722,011	727,117	318,702
Cash and investments ($000s)	N.A.	1,356,754	1,396,979	1,044,116	1,087,207	MNR
Cash and investments to operations (%)	N.A.	157.0	190.4	130.8	137.7	179.3

American University, D.C.--Enterprise And Financial Statistics (cont.)						
	--Fiscal year ended June 30--					--Medians reported for 'A' category rated private colleges and universities--
	2023	2022	2021	2020	2019	2021
Cash and investments to debt (%)	N.A.	182.0	187.3	163.0	169.7	369.5

MADS--Maximum annual debt service. Total adjusted operating revenue = unrestricted revenue less realized and unrealized gains/losses and financial aid. Total adjusted operating expense = unrestricted expense plus financial aid expense. Net operating margin = 100*(net adjusted operating income/adjusted operating expense). Student dependence = 100*(gross tuition revenue + auxiliary revenue) / adjusted operating revenue. Current MADS burden = 100*(MADS expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Average age of plant = accumulated depreciation/depreciation and amortization expense. N.A.--Not available. MNR--Median not reported. Note: Operating leases not included in debt ratios prior to fiscal 2021.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022