

RatingsDirect®

University of Louisville, Kentucky; Public Coll/Univ - Unlimited Student Fees

Primary Credit Analyst:

Gauri Gupta, Chicago 312-233-7010; gauri.gupta@spglobal.com

Secondary Contact:

Jessica A Matsumori, San Francisco (1) 415-371-5083; jessica.matsumori@spglobal.com

Table Of Contents

Rationale

Outlook

Enterprise Profile

Financial Profile

University of Louisville, Kentucky; Public Coll/Univ - Unlimited Student Fees

Credit Profile

US\$56.515 mil gen receipts bnds ser 2016D due 03/01/2036

Long Term Rating AA-/Stable New

US\$29.165 mil taxable gen receipts bnds ser 2016E due 03/01/2028

Long Term Rating AA-/Stable New

US\$28.985 mil gen receipts rfdg bnds ser 2016F due 03/01/2028

Long Term Rating AA-/Stable New

Univ of Louisville cons ed bldg rev bnds ser 2003-O, 2005-P (GRE)

Long Term Rating AA-/Stable Affirmed

Rationale

S&P Global Ratings has assigned its 'AA-' long-term rating to the University of Louisville, Ky.'s (UofL, or the university) series 2016 D and E general receipts bonds and series 2016 F general receipts refunding bonds. At the same time, we also affirmed our 'AA-' long-term rating on the university's outstanding general receipts bonds. The 'AA-' ratings on these bonds are based on a security pledge that, in our opinion, is equivalent to an unlimited student-fee pledge. The outlook on all ratings is stable.

We assessed UofL's enterprise profile as very strong, characterized by historically stable enrollment, and a good demand profile, as well as its strong research presence. Despite these strengths, the university has certain ongoing challenges at the board level that have also resulted in presidential turnover and legal actions that are still pending to be resolved. We assessed UofL's financial profile as very strong, with consistent operating surpluses on a cash basis, although less consistent on a full-accrual basis, and a low pro forma maximum annual debt service (MADS) burden, offset by low available resources to debt for the rating category. Combined, we believe these credit factors lead to an indicative stand-alone credit profile of 'aa-' and a 'AA-' rating on the university's bonds.

UofL's rating is currently rated above that on the state of Kentucky; the university rating is not directly linked, capped, or dependent on the rating on the state. We believe this differential is warranted while acknowledging the university derives a significant amount of financial support from the state through its operating appropriation, and limited capital support. Nevertheless, it is not entirely dependent on state support as about 80% or more of its operating revenue is derived from sources not directly tied to the state (e.g., tuition and fees, health care operations, grants and contracts revenue, and auxiliary operations revenue). In addition, we view UofL's financial resources as healthy and enhanced by robust philanthropic support.

The 'AA-' rating reflects our view of the university's:

- Co-flagship status in Kentucky as an overall comprehensive research university;

- Growing enrollment, with fall 2016 full-time equivalent (FTE) headcount at 18,814;
- Positive operating performance on a cash basis, although inconsistent on a full-accrual basis with break-even fiscal 2016 full-accrual operations; and
- Manageable pro forma MADS burden of 3.16% of fiscal 2016 operating expenses and a conservative, fixed-rate debt service structure that is frontloaded with rapid amortization.

Partially offsetting those credit strengths are:

- A constrained state budget and appropriation environment;
- Challenges with the Kentucky legislature involving the university board of trustees; and
- Only adequate financial resources for the rating as of June 30, 2016, with adjusted unrestricted net assets (UNA) equal to 16.8% of adjusted operating expenses and 72.5% of pro forma debt.

The university plans to use the net proceeds from the series 2016 D and E bonds for the expansion of its Papa John's Cardinal Stadium. The net proceeds of series 2016 F bonds will be used to refund existing series 2008 debt. The general receipts bonds are secured by certain operating and nonoperating revenues of the university, including student registration fees, nongovernmental grants and contracts, recoveries of facilities and administrative costs, sales and services, auxiliary enterprises, state appropriations, gifts, investment income, and other nonoperating revenues. The 'AA-' ratings on these bonds are equivalent to an unlimited student-fee pledge, in our view.

Total pro forma debt for the university is, in our view, manageable at about \$283.5 million, with no variable-rate debt and no swap contracts. As of fiscal 2016, total debt includes general receipts bonds of approximately \$164.8 million and \$39.9 million of metro government revenue bonds (issued by the University of Louisville Athletic Assn. and backed by a guaranty from the University of Louisville Foundation), and some notes, energy lease, and capital lease obligations. Total MADS of approximately \$35.1 million reflects what we consider to be a manageable 3.2% of fiscal 2016 operating expenses. The university is in preliminary stages of discussion to issue additional debt for campus housing and improvement of the IT infrastructure, but the timing and amount of issuance is still unknown at this point.

Founded in 1798 as the Jefferson Seminary, the University of Louisville was established by legislative charter in 1846. Today, it consists of 13 academic schools and colleges, including a medical school and law school. UofL is state-supported and has close historical and legal ties with the Louisville metropolitan area. The university is primarily undergraduate (71%) and in-state (84%) and operates three campuses. The Belknap Campus is three miles from downtown Louisville and houses seven of the university's colleges and schools. The Health Sciences Center is in downtown Louisville's medical complex and houses the university's health-related programs and the University of Louisville Hospital. The Shelby Campus holds the National Crime Prevention Institute and the Division of Distance and Continuing Education. In recent years, the university has also expanded academic offerings at both off-site and international locations. It provides on-campus housing in residence halls and apartments for more than 3,000 students (approximately 20% of total FTE enrollment).

Outlook

The stable outlook reflects S&P Global Ratings' expectation that the university will achieve balanced operating results on a full-accrual basis in the next two years. We also anticipate that the university will continue to grow enrollment

and demand, as well as have continued success in awarded research funding and fundraising. We expect it to maintain or improve its available resource ratios.

Downside scenario

Credit factors that could lead to a negative rating action during the outlook period include weakening operating performance with deficits on a full-accrual basis, further weakening of available resource ratios relative to the rating, or the issuance of debt without a commensurate increase in revenues or resources. We would also view any further issues with the Kentucky legislature regarding the university board resulting in long-term reputational risk as a negative factor.

Upside scenario

It is unlikely that the university's available resources will increase significantly relative to the rating during the next two years to warrant a positive rating action, although we would view this positively.

Enterprise Profile

Industry risk

Industry risk addresses the higher education sector's overall cyclical and 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.

Economic fundamentals

In our view, the university has good geographic diversity, although about 84% of students come from in-state. As such, our assessment of the University of Louisville's economic fundamentals is anchored by the local GDP per capita.

Market position and demand

Total FTE enrollment has remained fairly steady during the past five years. For fall 2016, there was a 1% growth with a FTE of 18,814 students. Total headcount enrollment in fall 2016 was 22,640, up by 1.2% from fall 2015. Management expects the same trend and slight growth going forward for fall 2017.

After a decline in applications for fall 2015, the university saw a 5.7% increase in freshmen applicants to 10,165 in fall 2016 from 9,614 in fall 2015, which is the highest in the past five years. Selectivity remained relatively stable at 72% for fall 2016 compared to 71% for fall 2015; although this is better than the historical selectivity of 79% in the past years. A solid 39% of those accepted chose to enroll, for a freshman class of 2,883. The average ACT score of incoming freshmen has remained high at 25.5 in fall 2016. Management indicates that its focus has been on improving academic quality and retention; it expects enrollment to stabilize or increase modestly. Transfer students represent a sizable portion of each entering class. For fall 2016, there were 959 transfer students compared to 1,531 for fall 2015. Although declining, this represents about 33% of all new undergraduate students.

The total mandatory tuition and fees for an in-state, undergraduate student is \$11,069 (including a 5% tuition increase). Including room and board, total cost per student is about \$20,204. As per management, there is a commitment not to increase tuition for fiscal 2018.

UofL completed a comprehensive capital campaign, "Charting Our Course," in 2014, raising over \$1 billion. This campaign included fundraising for academic scholarships and programs, faculty and research development, investment in athletic facilities, and to support the academic units.

Management and governance

In June 2016, Dr. James R. Ramsey resigned from his position as the university president. Simultaneously, the governor of Kentucky dismissed the old board and appointed a new one. Following these actions, a lawsuit was filed by the attorney general that instituted the university's old board back in practice. Consequently, the university is currently functioning with two distinct board of trustees. As of right now, there is an ongoing appeal on the court decision regarding the board, i.e., to determine the legality of the governor's dismissal of the first board and to determine which board has authority to govern the university. As per management, the board continues to meet regularly and there has been no negative effect on the day-to-day operations of the university. In the interim, Dr. Neville Pinto is the acting president. Previously, Dr. Pinto was the dean of the college of engineering at University of Louisville. The university's board typically consists of 17 members who are appointed by the governor to staggered six-year terms, plus a member of the teaching faculty, a member of the university's permanent staff, and a student member each serving one-year terms.

The university had added a position of vice provost for strategic enrollment management to continue to grow enrollment. Although there is uncertainty associated with the university board of trustees, we believe this has not trickled down to hurt the university operations. Besides the above, there have been no changes to the senior management team, which has remained stable.

As of fiscal 2015, UofL has formed a consolidation agreement with six hospitals to create an integrated, comprehensive statewide health-care network in the state called the Kentucky One Health Partnership. The agreement partnered the University of Louisville, University of Louisville Hospital/James Graham Brown Cancer Center, Jewish Hospital & St. Mary's HealthCare, Catholic Health Initiatives and its Kentucky-based operation Saint Joseph Health System, to extend care throughout the state. Management reports that this new partnership will provide research synergies for the university by extending the research and teaching programs for UofL statewide. Management also reports that there is no university debt issuance involved in this project, and it doesn't anticipate any negative financial implications. Part of the agreement, in fact, includes support for clinical service lines in UofL's medical school of about \$135 million over five years.

Financial Profile

Financial management policies

The university has formal policies for investments and debt. It operates according to a multiyear strategic plan. The university meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there may be some areas of risk, the organization's overall financial policies are not likely to weaken its future ability to pay debt service. Our analysis of financial policies includes a review of the organization's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure and a comparison of these policies to peers.

Financial performance and revenue diversity

In our opinion, the university has good revenue diversity. Historically, financial operations have generated consistent operating surpluses on a full-accrual basis. However, during the past few years, operations have fluctuated on a full-accrual basis, while remaining positive on a cash basis (excluding depreciation of over \$50 million).

The audit for fiscal 2016 year ended June 30, 2016 showed a deficit of \$96.8 million before capital funding and transfers from the UofL Foundation. After adjustments to exclude unrealized and realized loss/gain on investments, and include contributions from the foundation (\$93.5 million, which includes endowment spent on operations directly from the foundation of \$45 million in fiscal 2016), the university had a slight deficit of \$500,000 on a full accrual basis. The contributions from UofL are adjusted for in the operating revenues as they are offsetting the expenses for the foundation paid by the university.

On a cash basis, the operations remain much stronger before depreciation expense of about \$51.3 million in fiscal 2016. We consider this as break-even operations on a full-accrual basis.

Clinical services and practice plan revenues were \$269.3 million in fiscal 2015, or 24% of total operating revenues. These revenues relate to patient care performed in clinics under contractual arrangements with governmental and private insurers, to laboratory services, and to clinical support provided by affiliated hospitals and the university's professional practice plan. Clinical services and practice plans revenue increased by \$16.9 million (or 6.7%) in fiscal 2016, primarily due to increased revenue from the university clinics. Management reports that it expects continued growth from this operation.

Total state operating appropriations were \$142.2 million in fiscal 2016, up slightly from \$140.7 million in fiscal 2015 (but down 4% from fiscal 2014's \$147.3 million). For fiscal 2017, management is expecting a further decline in appropriations due to pension challenges at the state level. Management dealt with state decreases in prior years by monitoring expenses, and we believe the university is better able to deal with state funding cuts due to its diverse revenue streams, with state appropriations accounting for only 12.8% of revenues in fiscal 2016. Clinical services revenues account for 24% of revenues, followed by tuition and auxiliary fees (28%), and grants and contracts (7.5%).

Available resources

In fiscal 2016, available resources were what we consider low for the rating category, with \$186.3 million of adjusted UNA (including the foundation's UNA and UNA of the real estate foundation, debt service reserves, and adjusted for other postemployment benefit [OPEB] liabilities) equal to 16.8% of operating expenses and 72.5% of pro forma university debt.

The university's endowment had a market value of \$740 million as of June 30, 2016. The current asset allocation is 19.4% marketable alternative investments, 45.2% U.S. and international equity (including emerging markets), 10.4% fixed income and cash, 13.9% private investments, and 11.1% real assets. The endowment spending policy is 5.5% of the weighted average market value from the preceding three years, which is, in our opinion, fairly standard.

Debt and contingent liabilities

The college provides a defined-contribution pension plan for its employees; the plan is fully funded by definition. Thus, the implementation of GASB 68/71 in fiscal 2015 had no effect on the university's audited financial results. The annual

OPEB cost is calculated based on the annual required contribution of the employee. At the end of fiscal 2016, the university's net OPEB obligation was \$36.3 million.

University of Louisville, KY Selected Financial Statistics						
	Fiscal year ended June 30					Medians
	2017	2016	2015	2014	2013	Public colleges and universities 'AA' 2015
Enrollment and demand						
Headcount	22,640	22,367	22,599	22,483	22,293	MNR
Full-time equivalent	18,814	18,601	18,779	18,651	18,487	32,632
Freshman acceptance rate (%)	72.7	71.3	71.7	71.5	76.3	71.7
Freshman matriculation rate (%)	39.0	41.2	41.0	43.4	42.0	MNR
Undergraduates as a % of total enrollment (%)	70.8	71.5	71.5	71.4	71.3	77.7
Freshman retention (%)	80.2	79.4	80.6	78.0	77.0	85.5
Graduation rates (five years) (%)	N.A.	46.3	47.3	N.A.	45.8	MNR
Income statement						
Adjusted operating revenue (\$000s)	N.A.	1,111,309	1,039,828	957,258	896,116	MNR
Adjusted operating expense (\$000s)	N.A.	1,111,816	1,059,160	957,036	932,100	MNR
Net adjusted operating income (\$000s)	N.A.	(507)	(19,332)	222	(35,984)	MNR
Net adjusted operating margin (%)	N.A.	(0.05)	(1.83)	0.02	(3.86)	2.10
Estimated operating gain/loss before depreciation (\$000s)	N.A.	50,788	34,007	56,555	21,434	MNR
Change in unrestricted net assets (UNA; \$000s)	N.A.	(19,265)	7,887	(5,306)	(57,853)	MNR
State operating appropriations (\$000s)	N.A.	142,213	140,744	147,256	144,066	MNR
State appropriations to revenue (%)	N.A.	12.8	13.5	15.4	16.1	21.0
Student dependence (%)	N.A.	28.0	29.4	30.8	31.0	42.4
Healthcare operations dependence (%)	N.A.	24.2	24.3	23.8	21.6	MNR
Research dependence (%)	N.A.	7.1	7.3	8.3	9.4	MNR
Endowment and investment income dependence (%)	N.A.	0.2	0.1	0.1	0.1	0.8
Debt						
Outstanding debt (\$000s)	N.A.	238,335	251,892	266,512	291,474	646,050
Proposed debt (\$000s)	N.A.	81,385	N.A.	N.A.	N.A.	MNR
Total pro forma debt (\$000s)	N.A.	283,560	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	35,163	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	2.95	3.12	3.92	3.88	MNR
Current MADS burden (%)	N.A.	3.59	3.77	4.17	N.A.	3.70
Pro forma MADS burden (%)	N.A.	3.16	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value (\$000s)	N.A.	738,982	844,288	876,825	741,774	642,929
Related foundation market value (\$000s)	N.A.	730,227	836,615	883,190	815,181	612,539
Cash and investments (\$000s)	N.A.	180,707	197,692	159,336	218,875	MNR

University of Louisville, KY Selected Financial Statistics (cont.)

	Fiscal year ended June 30					Medians
	2017	2016	2015	2014	2013	Public colleges and universities 'AA' 2015
UNA (\$000s)	N.A.	(6,939)	12,326	4,439	9,745	MNR
Adjusted UNA (\$000s)	N.A.	186,352	147,967	184,190	196,989	MNR
Cash and investments to operations (%)	N.A.	16.3	18.7	16.6	23.5	51.7
Cash and investments to debt (%)	N.A.	75.8	78.5	59.8	75.1	162.6
Cash and investments to pro forma debt (%)	N.A.	63.7	N.A.	N.A.	N.A.	MNR
Adjusted UNA to operations (%)	N.A.	16.8	14.0	19.2	21.1	30.3
Adjusted UNA plus debt service reserve to debt (%)	N.A.	86.3	65.3	75.1	76.2	86.7
Adjusted UNA plus debt service reserve to pro forma debt (%)	N.A.	72.5	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	16.0	14.6	13.0	12.0	12.4
OPEB liability to total liabilities (%)	N.A.	7.9	7.3	6.1	5.3	MNR

N.A.--Not available. MNR--Median not reported. MADS--maximum annual debt service. UNA--Unrestricted net assets.

Ratings Detail (As Of December 2, 2016)

University of Louisville gen rcpts bnds		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
University of Louisville gen rcpts rfdg bnds		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
University of Louisville PCU_USF		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
University of Louisville cons ed bldg rev bnds ser N (AMBAC) (GRE)		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
University of Louisville gen rcpts ser 2007A (MBIA) (MBIA of Illinois) (GRE)		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Copyright © 2017 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.