S&P Global
Ratings

RatingsDirect®

Oregon Facilities Authority Reed College; Private Coll/Univ - General Obligation

Primary Credit Analyst:
Ying Huang, San Francisco (1) 415-371-5008; ying.huang@spglobal.com

Secondary Contact:
Kevin Barry, New York (1) 212-438-7337; kevin.barry@spglobal.com

Table Of Contents

Oregon Facilities Authority
Reed College; Private Coll/Univ - General Obligation

Credit Profile		
Oregon Facs Auth, Oregon		
Reed Coll, Oregon		
Oregon Facs Auth (Reed Coll) PCU_GO		
Long Term Rating	AA-/Stable	Affirmed
Oregon Facs Auth (Reed Coll) PCU_GO		
Long Term Rating	AA-/A-1/Stable	Affirmed

Rating Action

S&P Global Ratings affirmed its 'AA-' long-term rating on the Oregon Facilities Authority's series 2017A revenue bonds, issued for Reed College. At the same time, we affirmed the 'AA-' long-term component and the 'A-1' short-term component of the rating on Reed's series 2008 bonds. The short-term rating on the series 2008 bonds reflects a standby bond purchase agreement provided by Wells Fargo Bank N.A. expiring in January 2023. The outlook on all long-term ratings is stable.

Based on unaudited financial statements prepared by management as of June 30, 2020, Reed College's outstanding debt was about $99 million. Approximately 34% of the debt consists of the series 2008A variable-rate debt, a portion of which is synthetically fixed with an interest rate swap, and the remaining 66% consists of the series 2017A fixed-rate debt. All of the outstanding bonds are secured by a general obligation of the college. While the college's total debt load is relatively low compared with that of similarly rated peers, we view the maximum annual debt service (MADS) burden of 6.1% as above average for the rating category. Management does not expect to issue any additional debt within the outlook period.

Due to the outbreak of the COVID-19 pandemic, Reed transitioned classes online in March 2020 and issued refunds to students for room and board, resulting in a total net impact on auxiliary revenue of about $2.8 million. Auxiliary revenues make up 9.3% of total operating revenues, which we view as manageable. Some expense savings partially offset the unplanned expenses, and therefore the college was able to post an operating margin in fiscal 2020 that was similar to those of the last couple of years. For fall 2020, the college reports 1,416 students on a full-time-equivalent (FTE) basis as of Aug. 23, which was one week before classes start. Management expects a modest drop over the course of the semester, currently estimated at 5% of the budgeted enrollment of 1,400 FTEs. Reed is teaching classes in a hybrid mode, with a mix of online and in-person instruction. Reed has reduced the occupancy of residence halls by providing a single-bed room for every student on campus to limit the density. The school has also established several tents to be used as outdoor classrooms. Students, faculty, and staff are regularly being tested for COVID-19. For fiscal 2021, management anticipates incremental costs related to Reed's COVID-19 response. Overall, the college plans to fund an operating deficit in fiscal 2021 with a combination of cost containment measures and existing balance sheet reserves. International enrollment makes up about 11% of total enrollment; hence, we believe there could be potential impact on the overall demand from international enrollment. While we recognize that these are unprecedented times, we acknowledge that Reed has taken prudent measures to address the situation. We believe Reed has ample liquidity to cover any short-term disruptions, with about $89 million in investments liquid weekly, and about $149 million liquid monthly as of June 30, 2020. In addition, as part of the federal government's CARES Act stimulus funding, the college was allocated $842,657, half of which has been distributed for direct aid to students, and the remainder to be used at the college's discretion during fiscal 2021 to reimburse eligible costs. We believe the college has adequately adopted contingency measures to help combat the spread of COVID-19, and we will continue to monitor the evolving situation.

All of the fiscal 2020 financial ratios in this report are based on unaudited draft financial statements prepared by management, and management doesn't anticipate significant changes in the final report.

Credit overview

We assessed Reed's enterprise profile as very strong, characterized by above-average student quality and a sound management team, offset by the relatively weak and still deteriorating selectivity and matriculation rates. We assessed Reed's financial profile as very strong, with consistently healthy operating margins despite a modest deficit anticipated by management in fiscal 2021, robust expendable resource ratios for the rating, moderate dependence on student and endowment revenues, and an above-average MADS burden. We believe these credit factors, combined, lead to an indicative stand-alone credit profile of 'aa-' and a final rating of 'AA-'.

The long-term component of the ratings reflects our view of Reed College's:

- Consistently positive operating margins, with fiscal 2020 producing a healthy 6.2% operating margin despite the COVID-19 impacts;
- Robust balance sheet for the rating category, with fiscal 2020 expendable resources equal to 3.1x of annual operating expenses and 4.1x of debt; and
- Skilled management team that has continued to attract and retain quality students.

In our view, the preceding credit strengths are in part offset by:

- Increased competition among other top liberal arts colleges for the college's high-quality students, as demonstrated by a decreasing matriculation rate over the past few years;
- Above-average MADS burden of 6.1%; and
- Average endowment draw of 5.05% in fiscal 2020, though we note that the college has decreased the draw from 5.3% in fiscal 2014, and is budgeting to decrease the draw to 5.0% in fiscal 2021.

The stable outlook reflects our expectation that, despite pressures from COVID-19, during the next two years, the college will continue to compete with other top liberal arts colleges for students and will not see sustained material operating deficits, while maintaining generally stable student enrollment and demand and robust available resources.

Founded in 1908, Reed College is a liberal arts institution that attracts high-quality undergraduate students from across the U.S. The median freshman ACT score was 31 in fall 2020, which is significantly above average. Reed College shares student cross-applications and admissions with institutions such as Brown University, R.I.; University of California, Berkeley; University of Chicago; and Pomona College, Calif.

Environment, social, and governance (ESG) factors

We believe Reed faces elevated social risk due to the uncertainty surrounding the pandemic's duration and its total impact on the 2020-2021 academic year. We view the risks posed by COVID-19 to public health and safety as a social risk under our ESG factors. Despite elevated social risk, we consider the college's environment and governance risks in line with our view of the sector as a whole.

Stable Outlook

Downside scenario

We could take a negative rating action if enrollment, matriculation, or available resources decline significantly; if the college reports materially and consistently weaker operating performance beyond our expectations for fiscal 2021; or if the college issues significant debt such that it begins to pressure the MADS burden or available resource ratios. Although we think the college has taken proactive steps to address COVID-19, and understand the virus to be a global risk, we could consider a negative rating action should unforeseen pressures related to the pandemic materially affect demand, finances, or the trajectory of the college.

Upside scenario

Although not expected during the outlook period, we could consider a higher rating over time if the college sees significant and consistent improvement to selectivity and matriculation rates while maintaining a healthy operating margin. We would also view significant growth in available resources favorably.

Credit Opinion

Enterprise Profile

Economic fundamentals

In our view, the college has exceptional geographic diversity, with only 6% of fall 2019 students coming from Oregon. As a result, our assessment of Reed's economic fundamentals is anchored by the U.S. GDP per capita.

Market position and demand

Historically, the college's enrollment has been relatively stable. The broad five-year trend indicates that enrollment has historically fluctuated around the 1,400 student level, with a low of 1,360 FTE students in fall 2014 and a high of 1,472 in fall 2018. FTE fell slightly to 1,440 in fall 2019 (a 2% decrease from 2018), and declined modestly again in fall 2020 based on preliminary enrollment data. Management is currently estimating that FTE will fall 5% below budgeted enrollment of 1,400 this year due to the pandemic. In the long term, management continues to be committed to maintaining a student-faculty ratio of 10 to 1, and anticipates that FTE will hover around the 1,400 mark.

Reed College continues to compete for high-quality students both nationally and regionally, and its student base is increasingly geographically diverse, with 94% of its students coming from out of state in fall 2019. The college received 5,815 applications in fall 2019, representing a 2.4% decrease from the prior year. Reed has undertaken several other initiatives related to recruitment including an early-action application, and collaborative recruitment travel with other liberal arts colleges that it considers peers, such as Pomona College, Colorado College, and Swarthmore. As a result of the pandemic, Reed's application process will be test blind for the next two years.

The college's selectivity rate has weakened over the past few years to at 40% in fall 2019, up from 35% in fall 2018 and 31% in fall 2016. The freshman retention rate for fall 2019 was good at 91%, although down slightly from a high 94% in fall 2013 and below the rating category median. As with many schools, we expect retention to be weaker this fall.

The matriculation rate at Reed College has been gradually declining during recent years, with fall 2019 matriculation of 17.2%. Management attributes this trend to a shift in the quality of students it attracts and the competing institutions to which they apply. Management stated one of its goals was to continue making Reed's facilities and offerings more attractive to students. Like retention, we expect the matriculation rate will be weaker in fall 2020, based on preliminary data.

Tuition is $60,310 for the 2020-2021 school year, and has increased by an average of 3.97% per year over the past five academic years. These tuition increases have not materially affected enrollment. The overall tuition discount rate increased slightly to 35.9% in fiscal 2019 from 35.3% in fiscal 2018, but was down from 38.9% in fiscal 2017. We view the college's ability to maintain a relatively stable enrollment trend while moderating its tuition discount rate favorably.

Management and governance

Audrey Bilger was appointed as Reed's new president in July 2019, after serving as the vice president for academic affairs and dean of the college and professor of English at Pomona College. A new chief investment officer also joined the college in August 2019. In addition, the college hired a new vice president of student life in July 2020. The rest of the management and board leadership has been relatively stable. The college is governed by a self-perpetuating board of trustees that consists of at least 30 members. We will continue to monitor the performance of the college and the stability of senior management team as the new president settles in.

Reed incorporates identified strategic priorities into annual departmental plans, budget models, and fundraising initiatives. We expect the college to update long-term plans and fundraising goals when its new president has assessed the school's strategic direction following the COVID-19 pandemic. In our view, the college has good management practices. We would view improvement in the selectivity and matriculation rates as a result of the college's strategic initiatives favorably.

Financial Profile

Financial management policies

Reed College has formal policies for endowment, investments, and debt. Reed also has a formal endowment liquidity policy and meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there may be some areas of risk, Reed's overall financial policies are not likely to negatively affect its future ability to pay debt service. Our analysis of financial policies includes a review of the college's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure and a comparison of these policies with those of comparable institutions.

Financial performance

Reed College continues to decrease its reliance on endowment spending in recent years in an effort to preserve its endowment. We note that the college has lowered its endowment spending rate by 25 basis points in the past five fiscal years, with a budgeted 5.0% draw for fiscal 2021. We view this change favorably especially as the college continues to post healthy operating margins in fiscals 2019 and 2020. We consider the fiscal 2020 rate to be average. The draw is on a rolling 13-quarter average of fair value of the endowment.

Net tuition revenue has increased in every year since fiscal 2015. Net tuition revenue rose by 7.2% during fiscal 2019 to $51.7 million, from $48.3 million in the previous fiscal year, and further grew by 2.3% to $52.9 million in fiscal 2020. Over the past five years, Reed has produced consistently positive margins. The college saw a healthy surplus of $8.8 million (or a 6.9% margin) in fiscal 2019 and a similar surplus of $8.2 million (or a 6.2% margin) in fiscal 2020, though down from a surplus of $12.3 million (or a 10.0% margin) in fiscal 2018. Due to the incremental costs and lost revenue associated with the pandemic, management expects deficit operations on a full-accrual basis in fiscal 2021. While the ongoing financial impacts of COVID-19 are difficult to project, we believe Reed has historically budgeted conservatively and we will monitor its operating performance as things evolve.

Available resources

At June 30, 2019, Reed College's available resources (as measured by expendable resources) decreased by 5% from the previous year to $416.1 million. This decrease followed two fiscal years of growth exceeding 10%. As of June 30, 2020, the available resources declined further by 2.9% to $404.1 million in fiscal 2020, which was partially driven by investment volatility and increased other postemployment benefit liabilities due to assumption changes. Reed's available resources represent a good 3.1x operating expenses and 4.1x of outstanding debt in fiscal 2020. In our opinion, Reed College's available resource measures continue to be strong for the rating, though these ratios could become pressured over time if expendable resources decline or if Reed decides to issue additional debt.

Reed College's endowment was relatively stable in fiscal 2019, growing 0.4% to $580 million as of June 30, 2019. However, due to the recent market volatility, the endowment market value declined modestly to $569 million as of fiscal year-end 2020. As of June 30, 2020, the endowment's allocation included 39% in equities, 22% in absolute return investments, 23% in private equity, 11% in real assets, and 5% in cash and fixed income. According to management's liquidity schedule, about 24% of total nonprivate investments were liquid weekly, 41% were available within one month, and 49% were available within three months.

In addition to a separate defined contribution pension plan and a defined contribution retiree health plan for employees hired after July 1, 2006, the college maintains a defined benefit retiree medical insurance plan for certain employees hired before July 1, 2006, with a total $34.1 million benefit obligation as of fiscal year-end 2020. We also note that the college has a good history of fundraising, with a fiscal 2020 alumni participation rate of 24%, and last finished a comprehensive capital campaign in 2012, raising $200 million in gifts and pledges. The college is in the midst of a short-term initiative to raise $50 million by Dec. 31, 2020, and has raised 93% of this goal. The college expects to launch its next capital campaign when the new president has established strategic goals, likely after the college has recovered from the operational impacts of COVID-19.

Debt and contingent liabilities

As of June 30, 2019, the college's debt totaled $99 million. Additionally, the college has one interest rate swap with an outstanding notional amount of $8.9 million and a mark-to-market value of negative $877,956 as of June 30, 2020. The college's debt service structure has debt service payments totaling $4.9 million in fiscal 2020 and steadily escalates to an estimated MADS of $8 million in 2041, a structure that in our view limits the college's flexibility to issue additional debt. The debt burden when using MADS is 6.1%, which we consider above average, leaving little flexibility for additional debt. Reed College does not have any direct placement debt and does not have plans for any type of additional debt at this time.

Reed College, Oregon--Enterprise And Financial Statistics

	--Fiscal year ended June 30--					Medians for 'AA' rated private colleges & universities
	2020 (unaudited draft)	2019	2018	2017	2016	2018
Enrollment and demand						
Headcount	1,471	1,503	1,470	1,427	1,476	MNR
Full-time equivalent	1,440	1,472	1,432	1,397	1,416	6,429
Freshman acceptance rate (%)	39.5	35.0	35.6	31.3	35.0	22.2
Freshman matriculation rate (%)	17.2	17.4	20.5	19.9	22.3	MNR
Undergraduates as a % of total enrollment (%)	99.0	98.7	98.4	98.8	98.4	67.8
Freshman retention (%)	91.0	88.0	88.0	87.0	88.0	95.0
Graduation rates (six years) (%)	76.0	81.0	80.0	78.0	82.0	MNR
Income statement						
Adjusted operating revenue ($000s)	140,209	136,718	135,454	129,081	134,899	MNR
Adjusted operating expense ($000s)	132,001	127,896	123,148	123,161	120,368	MNR
Net operating income ($000s)	8,208	8,822	12,306	5,920	14,531	MNR
Net operating margin (%)	6.22	6.90	9.99	4.81	12.07	2.30
Change in unrestricted net assets ($000s)	(6,444)	(911)	20,295	29,362	(55,431)	MNR
Tuition discount (%)	35.7	35.9	35.3	38.9	38.6	37.9
Tuition dependence (%)	58.7	59.1	55.1	54.5	50.4	MNR
Student dependence (%)	68.1	70.1	66.1	65.6	61.0	58.3
Health care operations dependence (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Research dependence (%)	1.3	1.1	0.9	1.0	1.6	MNR
Endowment and investment income dependence (%)	20.6	21.1	20.5	21.4	19.3	MNR
Debt						
Outstanding debt ($000s)	98,995	100,530	101,995	77,790	79,240	386,585

Reed College, Oregon--Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--					Medians for 'AA' rated private colleges & universities
	2020 (unaudited draft)	**2019**	**2018**	**2017**	**2016**	**2018**
Proposed debt ($000s)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Total pro forma debt ($000s)	98,995	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma MADS	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	3.74	3.89	2.86	2.96	2.83	MNR
Current MADS burden (%)	6.06	6.26	6.50	5.68	5.82	4.10
Pro forma MADS burden (%)	N.A.	N.A.	N.A.	N.A.	N.A.	MNR
Financial resource ratios						
Endowment market value ($000s)	569,284	579,820	577,790	539,668	484,078	1,603,114
Cash and investments ($000s)	650,113	651,237	639,593	604,124	552,557	MNR
Unrestricted net assets ($000s)	360,031	366,475	367,386	347,091	317,729	MNR
Expendable resources ($000s)	404,149	416,062	438,632	390,625	352,767	MNR
Cash and investments to operations (%)	492.5	509.2	519.4	490.5	459.1	333.1
Cash and investments to debt (%)	656.7	647.8	627.1	776.6	697.3	505.9
Cash and investments to pro forma debt (%)	656.7	647.8	N.A.	N.A.	N.A.	MNR
Expendable resources to operations (%)	306.2	325.3	356.2	317.2	293.1	228.6
Expendable resources to debt (%)	408.3	413.9	430.1	502.2	445.2	320.2
Expendable resources to pro forma debt (%)	408.3	413.9	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	17.8	18.8	17.4	17.1	16.9	13.9

N.A.--Not available. MNR--Median not reported. 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 debt service burden = 100*(current debt service expense/adjusted operating expenses). Current MADS burden = 100*(maximum annual debt service expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Expendable resources = unrestricted net assets + temp. restricted net assets - (net PPE- outstanding debt). Average age of plant = accumulated depreciation/depreciation and amortization expense.

Related Research

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020