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CREDIT OPINION
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University of San Diego, CA

Update to credit analysis

Summary

University of San Diego's (USD; A1 stable) credit quality reflects its very good brand as a Catholic university with a comprehensive undergraduate, graduate and professional degree programs with an attractive campus in San Diego. The university's experienced financial management team with disciplined long-term planning will continue to support good operating performance as the university finishes a large-scale capital plan. Total cash and investments have decreased in recent fiscal years as USD self-funded a substantial portion of capital projects, but remain strong at $874 million at the end of fiscal 2023. The university's leverage profile remains moderate with some debt structure complexity. Additional considerations include a high reliance on student charges as a source of revenue and a highly competitive market for students that may temper net tuition revenue growth.

Credit strengths

» Attractive location and up-to-date campus and diverse undergraduate and graduate program offerings supports very good student demand

» Sizable wealth of $874 million in total cash and investments provides very good coverage of debt and operating expenses at a respective 3.4x and 2.2x

» Experienced financial management team with a demonstrated track record of managing expenses and producing favorable operating results, reflected in three-year average EBIDA margin of 13.9%

Credit challenges

» Higher 75% reliance on student charges as a source of revenue in a highly competitive market for students

» Ambitious ongoing capital plan has limited wealth growth over recent fiscal years

» Relatively low fundraising relative to peers, with three-year average gift revenue of $30.5 million

» Moderately elevated leverage profile with exposure to variable rate debt and counterparty risk throughout direct placement and swap agreement require careful debt and liquidity management

Rating outlook

The stable outlook reflects our expectation that USD will maintain stable operating performance that results in annual surpluses and debt service coverage above 2x. It also incorporates expectations that the university will maintain sizeable financial reserves that provide strong coverage of debt and expenses.

Factors that could lead to an upgrade

- Substantial growth of total cash and investments that provides greater coverage of debt and expenses
- Strengthening of brand and strategic positioning evidenced by growing net tuition revenue per student
- Improvement in annual giving that support financial aid commitments and planned capital projects

Factors that could lead to a downgrade

- Sustained weakening of operating performance reflected in declining EBIDA margins and annual debt service coverage over the next two fiscal years
- Material reduction in total wealth and liquidity that reduces coverage of outstanding debt and expenses
- Deterioration of brand and strategic revenue evidenced by declining enrollment and net tuition revenue

Key indicators

Exhibit 1
UNIVERSITY OF SAN DIEGO, CA

	2019	2020	2021	2022	2023	Median: A Rated Private Universities
Total FTE Enrollment	8,300	7,908	8,080	7,924	8,173	5,320
Operating Revenue ($000)	393,068	375,493	340,674	382,482	403,453	239,809
Annual Change in Operating Revenue (%)	5.5	-4.5	-9.3	12.3	5.5	10.7
Total Cash & Investments ($000)	834,965	830,701	1,007,570	891,700	874,452	529,788
Total Adjusted Debt ($000)	150,817	193,711	189,769	261,441	258,039	194,248
Total Cash & Investments to Total Adjusted Debt (x)	5.5	4.3	5.3	3.4	3.4	2.9
Total Cash & Investments to Operating Expenses (x)	2.4	2.4	3.3	2.5	2.2	2.4
Monthly Days Cash on Hand (x)	454	471	625	460	392	417
EBIDA Margin (%)	19.4	14.6	18.0	14.4	9.2	16.2
Total Debt to EBIDA (x)	2.0	3.5	3.1	4.7	7.0	4.9
Annual Debt Service Coverage (x)	7.4	5.7	6.6	5.8	3.5	3.3

Source: Moody's Investors Service

Profile

University of San Diego is a mid-sized private Catholic comprehensive university located in San Diego, California. The university enrolled 8,173 full-time equivalent (FTE) students in fall 2023 and generated $403 million in operating revenue in fiscal 2023.

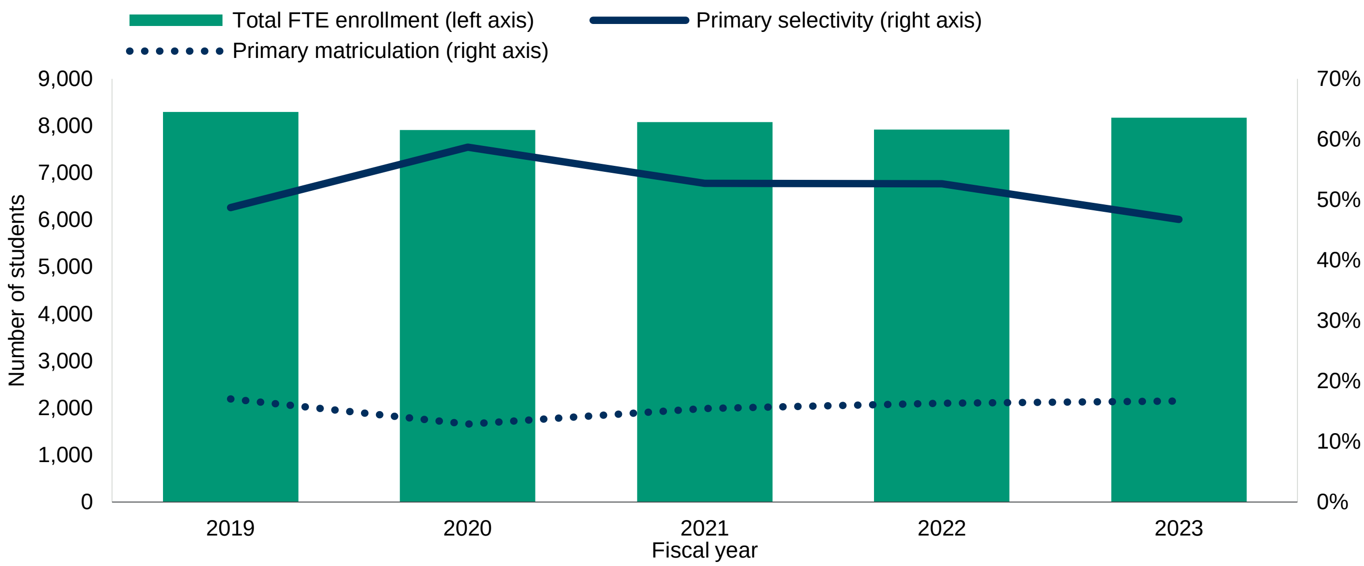
Detailed credit considerations

Market profile

USD's student demand will continued to be supported by its strong brand as a comprehensive Catholic university and location in San Diego. Leadership is implementing strategies to stabilize the tuition discount rate at the current level of about 40%, with plans to grow net tuition revenue through a combination of growing enrollment and modest tuition increases of the next two to three academic years. Enrollment growth is expected to come from a combination of gradually increasing undergraduate class sizes and from greater demand for USD's graduate programs, in law, business and nursing. Net tuition growth will be tempered, however, by a highly competitive market for students as an institutional focus on affordability and meeting the financial aid needs of its student body. Fundraising has grown steadily in over the past three fiscal years, but remains lower than peers, with three-year average gifts per student of $3,744 below the A median of $4,734.

Exhibit 2

USD's good student demand are reflected in its selectivity and stable matriculation metrics

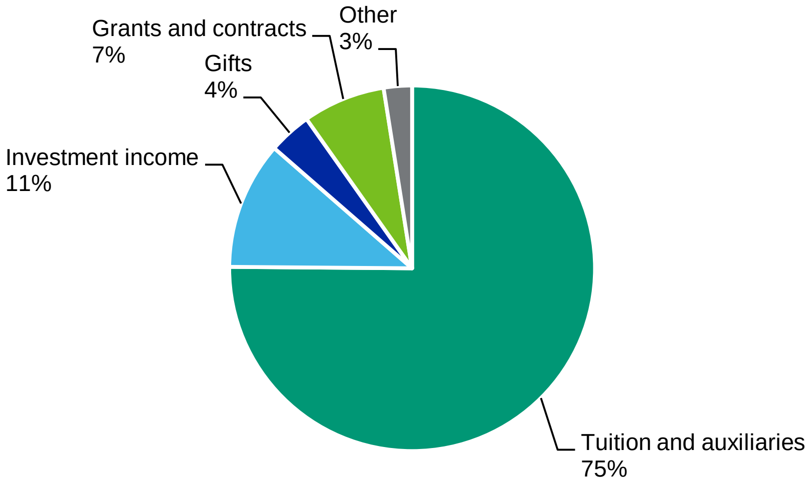


Source: Moody's Investors Service

Operating performance

Disciplined financial management will continue to generate surplus operations and good annual debt service coverage. The university's EBIDA margin narrowed somewhat in fiscal year 2023 to 9.2% because of the impacts of inflation and continued capital investment. Operating performance will improve in fiscal 2024, with an EBIDA margin likely in the low double-digits because of growth in net tuition revenue and expense containment measures put in place by the university's experienced financial management team.

Exhibit 3
USD remains highly reliant on student charges for operating revenue
Fiscal 2023 revenue by source



Source: Moody's Investors Service

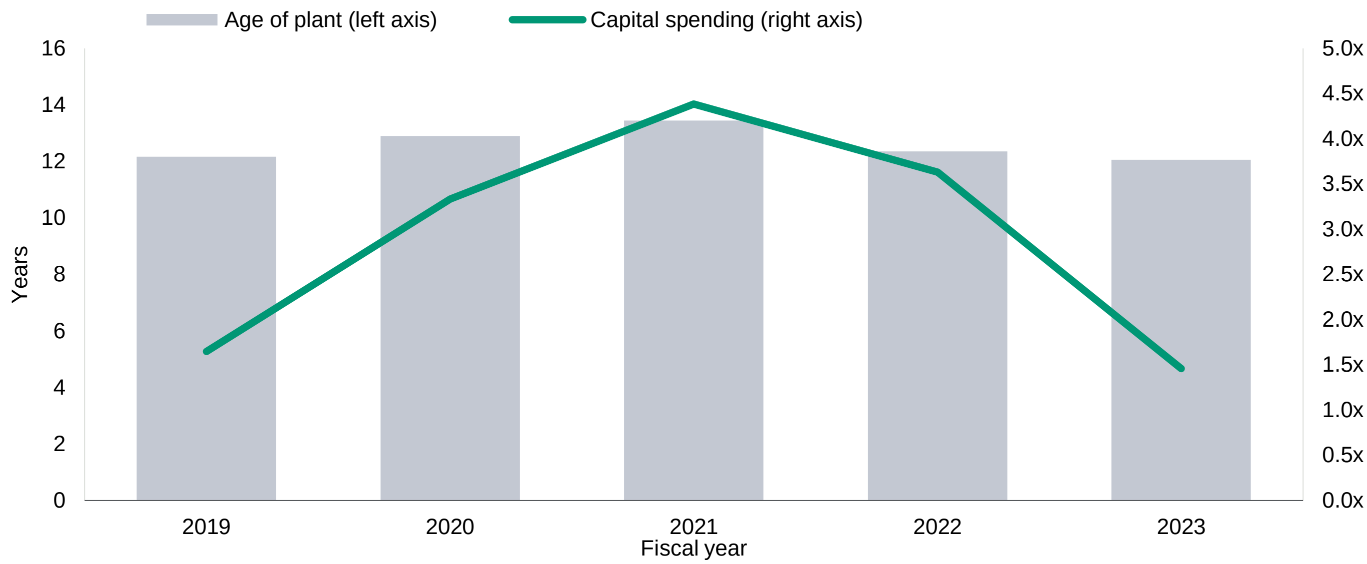
Wealth and liquidity

USD's wealth will remain sizable on an absolute basis, but prospects for growth over the next two to three fiscal years are uncertain given continued investments in campus facilities. Total cash and investments have declined by approximately 13% since fiscal 2021 as the university spends reserves and retained surpluses on its $200 million Renaissance capital plan that concluded in early fiscal 2024. The university's solid financial resources of nearly $875 million do, however, continue to provide good coverage of operating expenses, with fiscal 2023 coverage of 2.2x in line with similarly rated peers.

Prospects for a return to financial reserve growth over the coming fiscal years will depend on leadership's decision to continue to use reserves and fundraising on further capital plans or return to focus on growing the university's quasi-endowment, as it had done before fiscal 2021 when it embarked on the Renaissance Plan. The university maintains a solid liquidity profile with monthly liquidity of $402 million providing for 392 monthly days cash on hand in fiscal 2023. This is down from 625 monthly days in fiscal 2021 and slightly below the median for A rated private institutions. Overall, USD's sizable wealth remains a key credit quality strength, but long-term deterioration of financial reserves and liquidity could lead to negative credit pressure.

Leverage

Exhibit 4
USD's substantial capital spending on the Renaissance Plan has preserved a low age of plant



Source: Moody's Investors Service

The university's leverage will remain manageable as it has no immediate additional borrowing plans and total cash and investments provide a strong 3.4x coverage of total adjusted debt. USD does not plan to issue new debt over the next 3-5 years and is examining whether to pursue additional campus investments that may be funded from fundraising, operating surpluses and existing reserves. The university is also in the planning stages of potential public private partnerships for multiple development projects including additional student housing, which will be incorporated into our credit analysis once the structure, terms, and timing have been established. The university has moderate exposure to debt structure risks through its various financial covenants, counterparty risks, and exposure to variable rate demand debt. It remains in compliance with all covenants and has sufficient treasury management expertise to manage the associated risks.

ESG considerations

University of San Diego, CA's ESG credit impact score is CIS-2

Exhibit 5
ESG credit impact score

ESG considerations do not have a material impact on the current rating.

Source: Moody's Investors Service

University of San Diego's ESG credit impact score is (**CIS-2**) reflecting exposure to social risks along with environmental and governance considerations. Ample financial reserves and good liquidity position provide a buffer to ESG risks.

Exhibit 6
ESG issuer profile scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-3	S-3	G-2

Source: Moody's Investors Service

Environmental

USD's exposure to environmental risks is (**E-3**) largely reflecting physical climate risks while other categories of environmental risks such as carbon transition, natural capital and waste and pollution are low. Physical climate risks include elevated drought risk and some wildfire risk. San Diego County where the university is located has a low water supply, but regional governments' significant investments in water infrastructure including implementing water purification technology to produce potable water largely mitigates the impact to the university. The wildfire risk is mitigated by the county's improvements in disaster preparedness and significant investments in wildfire prevention and response. The university put in place a Climate Action Plan in 2016 and has reduced its energy consumption by 35% and reduced water consumption by 18% between 2010 and 2021. It has announced the goal of becoming carbon neutral by 2035.

Social

USD's exposure to social risks is (**S-3**) reflecting demographic and competitive challenges. Like most of the higher education sector, the university has a mission that is aligned with positive social impact through education and service. The university's ability to achieve rising enrollment and generally increasing net tuition per student help buffer the risks related to heightened competition and demographic challenges. However, demographic pressures will continue to drive increasing financial aid funding needs. Customer relations with key stakeholders are informed by student outcomes that include sound graduation rates and career outcomes. Human capital considerations include the impact of the university's relatively high percentage of tenured faculty on its expense structure offset by flexibility provided by a large portion of part time faculty.

Governance

USD's exposure to governance risks is (**G-2**). Management credibility is evidenced by an ability to execute strategies through integrated strategic, financial, and capital planning. Leadership deploys regular benchmarking and self-assessment, supporting management credibility. Like most higher education institutions, risks related to the board structure reflect the relatively large size of the board including alumni and donors. While most of the up to 45 trustee board positions are self-perpetuating, two trustees as selected by the California Provincial of the Religious of the Sacred Heart, and two trustees are selected by the incumbent Bishop or Administrator of the Roman Catholic Diocese of San Diego. The policies and procedures of the board, along with a smaller executive committee that facilitates the determination of key strategies, provides good oversight and support effective decision-making.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The principal methodology used in this rating was Higher Education Methodology published in August 2021. The Higher Education Methodology includes a scorecard that summarizes the factors that are generally most important to higher education credit profiles. Because the scorecard is a summary and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not match an assigned rating. We assess brand and strategic positioning, financial policy and strategy, and operating environment on a qualitative basis.

Exhibit 7

University of San Diego, CA

Scorecard Factors and Sub-factors		Value	Score
Factor 1:	**Scale (15%)**		
	Adjusted Operating Revenue (USD Million)	403	A
Factor 2:	**Market Profile (20%)**		
	Brand and Strategic Positioning	A	A
	Operating Environment	A	A
Factor 3:	**Operating Performance (10%)**		
	EBIDA Margin	9%	Baa
Factor 4:	**Financial Resources and Liquidity (25%)**		
	Total Cash and Investments (USD Million)	874	Aa
	Total Cash and Investments to Operating Expenses	2.2	A
Factor 5:	**Leverage and coverage (20%)**		
	Total Cash and Investments to Total Adjusted Debt	3.4	Aa
	Annual Debt Service Coverage	3.5	A
Factor 6:	**Financial Policy and Strategy (10%)**		
	Financial Policy and Strategy	Aa	Aa
	Scorecard-Indicated Outcome		A1
	Assigned Rating		A1

Data is based on most recent fiscal year available. Debt may include pro forma data for new debt issued or proposed to be issued after the close of the fiscal year.

For non-US issuers, nominal figures are in US dollars consistent with the Higher Education Methodology.

Source: Moody's Investors Service

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