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New Issue

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Missouri State University, MO

New Issue - Moody's Assigns A1 to Missouri State University's Series 2016A Auxiliary Revenue Bonds; Outlook Stable

Summary Rating Rationale

Moody's Investors Service has assigned an A1 rating to Missouri State University's (MSU) proposed $13 million Auxiliary Enterprise System Revenue Bonds, Series 2016A. The proposed bonds have an expected final maturity in 2039. Concurrently, we also affirm the Aa3 ratings on outstanding Educational Facilities Revenue Bonds, the Aa3 issuer rating, and the A1 ratings on outstanding Auxiliary Enterprise System Revenue Bonds. The outlook is stable.

The Aa3 ratings reflect MSU's important role as the second largest provider of public higher education in the state of Missouri (Aaa stable) with steady student demand, solid unrestricted liquidity, manageable debt levels, and sound financial management. Offsetting challenges include a state-imposed cap on in-state undergraduate tuition increases, past volatility in state funding, and potential for additional pension contribution rate increases. The A1 rating for the Auxiliary Enterprise System bonds reflects the narrower pledge and limited revenue stream supporting debt service.

Credit Strengths

» Strong regional brand as Missouri's second largest public university with steady demand, serving 17,560 full-time equivalent students in fall 2015

» Very good unrestricted liquidity, with 205 days cash on hand, providing solid financial flexibility

» Strong financial management, evidenced by solid FY 2015 cash flow of 13.7%, contributing to consistently healthy operations

» Well-managed capital planning, providing manageable financial leverage and a predictable fixed-rate debt structure

Credit Challenges

» Weak Missouri high school demographic trends, potentially suppressing enrollment growth

» State-imposed cap on annual tuition increases for undergraduate resident students, limiting net tuition revenue growth

» History of volatility with state appropriations, including mid-year reductions, adding complexity to budgeting and planning

» Exposure to potential increases to defined-pension contribution rates, beyond the increase in FY 2018, adding an additional expense burden

Rating Outlook

The stable outlook reflects expectations that MSU will continue to benefit from healthy student demand and stable state funding, contributing to maintenance of favorable operations. It also incorporates expectations of no material increase in financial leverage near-term.

Factors that Could Lead to an Upgrade

» Significant growth in total wealth relative to debt and operations, while making ongoing investment to plant and programs

» Meaningful improvement in revenue diversity

Factors that Could Lead to a Downgrade

» Material enrollment declines or deterioration of pledged revenues and debt service coverage

» Continued slower pace of growth of cash and investments relative to Aa3 peers, resulting in weakening of balance sheet ratios

» Material increase in debt without compensating increase in reserves

Key Indicators

Exhibit 1

MISSOURI STATE UNIVERSITY

	2011	2012	2013	2014	2015	Sensitivity 2015 + $13M
Total FTE Enrollment	16,297	16,435	16,799	17,129	17,560	17,560
Operating Revenue ($000)	277,557	276,120	280,376	290,414	299,388	299,388
Annual Change in Operating Revenue (%)	1.2	-0.5	1.5	3.6	3.1	3.1
Total Cash & Investments ($000)	223,723	228,201	225,746	243,702	251,281	251,281
Total Debt ($000)	121,311	115,793	110,211	142,489	157,855	179,439
Spendable Cash & Investments to Total Debt (x)	1.5	1.6	1.7	1.4	1.3	1.1
Spendable Cash & Investments to Operating Expenses (x)	0.7	0.7	0.7	0.7	0.7	0.7
Monthly Days Cash on Hand (x)	224	223	203	205	205	205
Operating Cash Flow Margin (%)	17.7	15.1	15.2	14.2	13.7	13.7
Total Debt to Cash Flow (x)	2.5	2.8	2.6	3.5	3.9	4.4
Annual Debt Service Coverage (x)	5.2	3.8	3.6	3.4	2.9	2.9

Source: Moody's Investors Service

Recent Developments

Recent state legislation will result in a $1.9 million withholding of the $5 million capital appropriations that university was set to receive towards its Glass Hall project. While this will not have a material impact on the university's financial position, it underscores the continued risk of potential additional state funding reductions.

Detailed Rating Considerations

Market Profile: Healthy Student Demand as Missouri's Second Largest Public University

As the second largest public university in Missouri with a strong regional brand, MSU is poised to maintain very good strategic positioning. Over the last five years, enrollment has steadily increased with full-time equivalent (FTE) students up 8% to 17,560 students in fall 2015. Furthermore, the yield on incoming freshman has consistently remained in the 42%-44% range, further underscoring the healthy student demand. This enrollment success is reflective of the university's good programmatic diversity, favorable pricing structure, and strategic capital investments. These factors will help support additional enrollment growth, even as the pipeline of Missouri high school graduates softens. Based on preliminary fall 2016 data, overall enrollment growth is consistent with recent year trends, and the university continues to draw good demand from undergraduate, graduate, distance learning, and transfer students.

Pricing flexibility will continue to be constrained by state imposed caps on in-state undergraduate tuition increases. Annual increases are limited to the consumer price index (CPI), which is set at 0.7% for FY 2017. Favorably, despite this, net tuition per student continues to increase, up an average of 3% annually over the last three years to $7,397 in FY 2015. Furthermore, along with growing undergraduate in-state enrollment, the university has also had success increasing the numbers of graduate and out-of-state students, who are not subject to these tuition pricing restrictions. From fall 2011-15, total FTE graduate enrollment has increased 8%, and out-of-state enrollment grew 4 percentage points to 13% in fall 2015. Continuing to grow the graduate student body and draw more out of state students, while maintaining a strong foothold in the core Missouri market, is critical to growing student charges. This is essential given the increasing dependence on student charges, accounting for 55% of FY 2015 operating revenue compared to 50% in FY 2011.

Operating Performance: Prudent Financial Management Provides Continuously Solid Operating Margins and Debt Service Coverage

Close budgetary oversight and steady student demand will support continued operating surpluses and strong debt service coverage of around 3 times (coverage of all debt service from Moody's calculated cash flow). Based on preliminary 2016 results, projected cash flow in the 15%-17% range represents a continuation of favorable operating performance. After recent years of state funding volatility, appropriations are expected to increase 6% in FY 2017, fueled in part by the university's consistently strong performance on the performance based funding model. While exposure to emerging expense and funding uncertainty adds some unpredictability, management has a demonstrated history of containing expense growth and generating surplus operations. This, along with expected growth in tuition revenue and state funding, the universities two largest revenue sources, will contribute to ongoing operating stability.

Wealth and Liquidity: Growing Reserves and Strong Liquidity Provide Good Cushion to Debt and Operations

MSU's solid and growing financial reserves afford good financial flexibility, allowing it to comfortably absorb the $13 million of new debt. However, strategic investments have limited growth of financial reserves over the last five years, with total cash and investments of the university and affiliated foundation increasing 28%, which lags peers. Favorably, FY 2015 spendable cash and investments of $203 million provide a healthy cushion to pro-forma debt and operations of 1.1 and 0.7 times, respectively.

Potential near-term capital projects include new student housing project, expected to cost in the $30-$40 million range, and renovations to an existing residence hall. With a steady pay down of debt and manageable financial leverage, the university has moderate additional debt capacity at the current rating level. Recent and additional capital projects, including the recent renovation and expansion of the College of Business, provide important upgrades that are essential to preserving market appeal and competing to attract additional out-of-state students.

LIQUIDITY

Liquidity will continue to be a credit strength, providing a solid cushion relative to operations. The reported $148 million in unrestricted monthly liquidity at FYE 2015 provides 205 monthly days cash on hand, which is substantially stronger than the FY 2015 Aa3-rated public university median of 143 days. With an all fixed-rate debt structure, healthy operations, and no exposure to unfunded commitments, potential unexpected calls on liquidity are limited.

Leverage: Manageable Financial Leverage and Sound Capital Planning

MSU's well-managed capital strategies will help maintain a manageable debt burden relative to financial reserves and operations. Pro-forma debt to operating revenue of 0.6 times is sound, albeit modestly elevated relative to recent years. Favorably, consistently healthy operations contribute to maintenance of very good debt affordability, evidenced by 4.4 times pro-forma debt to cash flow in FY 2015.

Debt service on the proposed Series 2016A bonds will be supported by a $29 per semester student fee commencing in fall 2017, which was voted upon by students. This fee is projected to generate $1 million annually, which covers the entire debt service on the new health and wellness center.

DEBT STRUCTURE

The all fixed-rate debt structure with relatively level annual debt service payments provides for budgeting predictability and future debt capacity. Pro-forma annual debt service peaks at $15 million in FY 2018 before falling incrementally through the 2041 final maturity. The debt burden is manageable relative to operations with pro-forma maximum annual debt service (MADS) representing just 5% of FY 2015 operating expenses.

DEBT-RELATED DERIVATIVES

There are no debt-related derivatives.

PENSIONS AND OPEB

Exposure to post-employment benefit obligations present moderate credit risk, with MSU's total adjusted debt of $552 million, including pension liability, much higher than total debt. University employees participate in either a state-administered, cost sharing, defined benefit plan, Missouri State Employees' Retirement System (MOSERS), or College and University Retirement Plan (CURP), a defined contribution plan. In recent years, MSU's share of its contributions to its state-run pension systems have been fixed at 16.97% of covered payroll. However, university contributions are expected to rise about 2.48 percentage points in FY 2018, which amounts to approximately $2.6 million in added pension expenses. While exposure to additional increases beyond FY 2018 remains a long-term credit risk, pension costs remain manageable relative to operations, representing a modest 4.4% of total FY 2015 expenses.

Post-retirement health benefits are provided through a defined benefit plan administered by the university, which has the authority to set and amend benefit provisions. OPEB contributions are stable limiting the growth of the liability, which was $3.6 million in FY 2015.

Governance and Management: Integrated Capital, Programmatic, and Financial Planning

MSU is led by a strong management team that regularly engages in self-assessment, benchmarking, and monitoring of the university's competitive position. Solid leadership and oversight contributes to the university's very good strategic positioning. A commitment to strategically invest in programmatic and capital initiatives helps enhance the overall brand. Furthermore, financial planning is conservative, with budgets incorporating reasonable assumptions that allow for comfortable absorption of any unexpected funding or expense uncertainty. The university regularly allows students to vote on capital projects, which both contributes to healthy relations with the student body and provides for a fee to offset the added debt service burden.

Legal Security

The Educational Facilities Revenue Bonds are unsecured general obligations of the university, with respect to which the full faith and credit of the University, excluding state appropriated funds and funds pledged to payment of Auxiliary Enterprise System Revenue Bonds, is pledged to make payments. The Educational Facilities Revenue Bonds have a sum sufficient rate covenant and a negative mortgage pledge.

The Series 2016A Bonds are on parity with the other Auxiliary Enterprise System Revenue Bonds and are secured by a more limited pledge of the University’s net income and revenues from its Auxiliary Enterprise System, after payment of costs of operation and maintenance. The Auxiliary Enterprise System consists of 11 residence halls (4,020 beds), bookstore, health and wellness center, parking facilities, athletic and recreation facilities, and certain auxiliary operations of the West Plains Campus. The university has benefited from a support agreement in which a donor's trust pays an amount equal to 47.54% of annual debt service payments on the Series 2015A bonds, amounting to approximately $1.8 million annually. However, a recent bankruptcy protection filing has jeopardized the future of this annual subsidy, although the trust has made its most recent payment. While this adds some uncertainty, the consistently healthy performance of the auxiliary system mitigates its impact. At FYE 2016, the 2015A bonds had $47 million outstanding.

The Auxiliary Enterprise System bonds are rated one notch lower than the Educational Facilities Revenue Bonds, reflecting the narrower and potentially more volatile revenue pledge. At FYE 2016, projected Auxiliary Enterprise System pledged revenue totaled $20 million, providing 1.7 times annual debt service coverage and good headroom above the 1.1 times coverage rate covenant. This coverage is expected to remain solid given the university's healthy student demand and consistent enrollment growth. Even if the annual $1.8 million annual subsidy from the donor's trust were to be eliminated during FY 2016, coverage would have remained a solid 1.6 times.

Use of Proceeds

Proceeds of the proposed Series 2016A bonds will be used to finance the construction of a new 36,000 square foot health and wellness center, demolish an existing health center, and provide for other capital improvements to the auxiliary system.

Obligor Profile

Founded in 1905, MSU is the second largest public university in the state, with FY 2015 operating revenue of $290 million and 17,560 full-time equivalent students in fall 2015. The university's enrollment reflects its comprehensive four-year campus in Springfield and an open admissions two-year program in West Plains. Business and health sciences are among the most popular areas of study. In FY 2015, MSU had operating revenues of $290 million.

Methodology

The principal methodology used in this rating was Global Higher Education published in November 2015. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 2

Missouri State University

Issue	Rating
Auxiliary Enterprise System Revenue Bonds, Series 2016A	A1
Rating Type	Underlying LT
Sale Amount	$12,785,000
Expected Sale Date	10/18/2016
Rating Description	Revenue: Public University Limited Pledge

Source: Moody's Investors Service

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