STANDARD & POOR'S RATINGS SERVICES
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University of Toronto

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University of Toronto

Major Rating Factors

Issuer Credit Rating
AA/Stable/--

Strengths:

- Solid financial results in fiscal 2013
- Strong enrollment and student demand characteristics
- Strong liquidity levels

Weaknesses:

- Substantial-but-stable postemployment liabilities
- Significant-but-manageable debt

Rationale

The ratings on the University of Toronto (UofT) reflect Standard & Poor's Ratings Services' view of the university's strong and rebounding financial results in fiscal 2013, very strong reputation and student demand characteristics, and strong liquidity position and unrestricted net financial resources. A substantial-but-stable burden of postemployment benefits and significant debt offsets some of these strengths, in our opinion. Using our "USPF Criteria: Higher Education" and "Principles Of Credit Ratings," we have assessed UofT's SACP at 'aa'.

In accordance with our criteria for government-related entities, our view of the university's "moderately high" likelihood of extraordinary government support reflects our assessment of its "important" role in the province, given that postsecondary education is one of Ontario's priorities in both expenditure and mandate (after health care and school boards), and that there are no viable private alternatives. It also reflects our assessment of UofT's role as Canada's largest university in enrollment and research capacity. The province's oversight, program approval rights, and tuition regulation over the university suggest a "strong" link to it. We rate UofT 'AA' in line with the 'aa' SACP, which is higher than the rating on the province, because the independence of the university's governing bodies, its considerable financial resources, and a track record of non-interference from the province convince us that there is a measurable likelihood that it would not default on its obligations under a short-lived provincial default scenario in which all government funding was temporarily disrupted.

Financial results rebounded strongly in fiscal 2013 (year ended April 30) as UofT recorded a consolidated surplus of 6.8% of total consolidated revenues. The fiscal 2013 surplus was better than the long-term average and a substantial improvement from the fiscal 2012 deficit. Long-term consolidated surpluses have averaged about 3% of annual revenues, by our estimates. Adjusted for amortization of deferred capital contributions and capital assets, the university recorded a modified cash surplus of 5.9%, which was also better than the previous year. Although UofT has budgeted for balanced operating results for fiscal years 2014 and 2015, we believe it might modestly outperform its forecasts.

The university exhibited what we view as strong enrollment, demand, and student quality characteristics in fiscal 2013 as favorable trends continued. Full-time equivalent students (FTEs) increased 3.3% to 70,311 in fiscal 2013, up from the previous increase of 2.2% in fiscal 2012 and above the five-year average of about 3%. We expect FTEs to rise again for fiscal 2014, by close to 3%. We believe that the province's commitment to fund more than 40,000 new university spaces and the expected stable growth in university-age population in the Greater Toronto Area in the next five years should help UofT achieve its growth targets. Student quality metrics continued to be strong as well, in our opinion. The acceptance rate (offers-to-applicants) and the matriculation rate were virtually unchanged at 51% and 34%, respectively, in fiscal 2013, both in line with the five-year averages. The average entry grade was 85% for the arts and science cohort entering in the fall of 2013 and 92% for engineering students. The graduation rate improved to 71% from 69% a year earlier. Overall, the university's student quality metrics compare well with those of similarly rated Canadian peers.

We believe UofT's substantial postemployment liabilities constrain its ratings somewhat. At the end of April 2013, its defined benefit pension deficits were C$955 million on a going-concern basis and C$1.3 billion on a solvency basis. Both deficits were down from a year earlier. The biggest improvement was with the solvency deficit, which fell almost 25% in fiscal 2013, compared with a 14% decline in the going concern deficit. The improvement came on higher investment returns and a special payment of C$66 million the university made in fiscal 2013. Under the current pension contribution strategy, UofT estimates its annual special pension payments budget, which includes estimated pension special payments and other related costs, will be C$87 million for fiscal 2014, rising to C$92 million for fiscal 2015 and C$97 million for fiscal 2016. As well, the university also had a C$735 million nonpension postemployment deficit in fiscal 2013. Because there is no legislative requirement to maintain assets against these liabilities (unlike pensions), the university funds these on a pay-as-you-go basis, similar to other universities.

Although declining, UofT's debt burden remains significant. Total debt stood at C$726 million at fiscal year-end 2013, virtually unchanged from the previous year-end. The debt represented 31% of adjusted revenues, which was also unchanged from the previous fiscal year, and C$10,326 per FTE, which was down thanks to higher FTE numbers. The fiscal 2013 debt service coverage ratio (DSCR), which was effectively interest-only, was 3.4x, a solid improvement from the fiscal 2012 DSCR. Interest expense was up slightly, at 1.7% of adjusted revenues. We consider the university's debt burden to be manageable and broadly in line with those of peers. With no debt issuance expected in the next two years, UofT's debt metrics should improve with rising operating revenues and enrollment. We expect that debt should fall below 27% of operating revenues and C$9,500 per FTE by fiscal year-end 2016.

Liquidity

The university has the largest endowments among Canadian universities, with a fair value of close to C$1.7 billion as of the end of April 2013. It has a conservative endowment draw, in our view, with an annual spending rate of 3.0%-5.0% of the opening market value of the endowments. In fiscal 2013, the endowments paid out about C$70 million, which represented about 4% of total endowments. Consolidated cash and investments totaled C$3.15 billion, up 9.5% million from fiscal 2012. Total cash and investments represented 132% of consolidated expenditures, or more than 4x total debt. Unrestricted financial resources (internally restricted net assets and internally restricted endowments) stood at slightly more than C$1.0 billion, up from the fiscal 2012's restated total of C$836 billion. This equaled about 138% of debt and 42% of consolidated annual expenses.

Outlook

The stable outlook reflects Standard & Poor's expectations that, within our two-year outlook horizon, UofT will maintain its strong student demand profile, its operating budgets will remain balanced, and its debt burden will decline modestly or remain stable at a minimum. We could revise the outlook to negative or lower the ratings if operating deficits were to emerge as result of a significant reduction in government grants or substantial pressure from rising pension deficits; or the debt burden were to increase considerably. Conversely, significantly reduced unfunded postemployment liabilities, a significant decline in debt, or a material rise in unrestricted financial resources could result in an upward revision to the outlook or the ratings.

Government-Related Entities Methodology: Moderately High Likelihood Of Extraordinary Provincial Government Support

In accordance with our criteria for government-related entities, our view of UofT's moderately high likelihood of extraordinary government support reflects our assessment of its important role in the province, given that postsecondary education is one of Ontario's priorities in both expenditure and mandate (after health care and school boards), and that there are no viable private alternatives. It also reflects our assessment of the university's role as Canada's largest university in enrollment and research capacity. The province's oversight, program approval rights, and tuition regulation over UofT suggests a strong link to it. Also supporting the link is the university receiving 27% of total revenues from provincial operating grants, and the province's appointment of some board members. Although Ontario is facing significant fiscal challenges and projects large provincial deficits in the medium term, we believe that postsecondary education will remain a top priority for the province and that overall support for the university sector will remain stable.

Following our "USPF Criteria: Higher Education" and "Principles Of Credit Ratings" criteria, we have assessed UofT's SACP at 'aa'. We rate the university 'AA' in line with the 'aa' SACP, which is higher than the rating on the province, because the independence of its governing bodies, its considerable financial resources, and a track record of non-interference from the province convince us that there is a measurable likelihood that it would not default on its obligations under a short-lived provincial default scenario in which all government funding was temporarily disrupted.

Background

Founded in 1827, UofT is Canada's largest university based on enrollment and has three campuses (St. George, Scarborough, and Mississauga). More than 82,000 students attended the three campuses in 2013. The university offers a variety of undergraduate, graduate, postgraduate, and professional degrees across its 18 faculties and schools. It also has affiliations with seven colleges, 65 centers and institutes, and nine Toronto hospitals. UofT employs more faculty and staff and offers a greater range of courses than any other Canadian university. It is also Canada's most important research institution and has gained an international reputation for its research.

Management

A 50-member board governs the university. The province appoints 16 of the 50 governors. The board appoints the president, senior administrators, and other senior staff. The board's decisions include approval of strategic plans, academic programs, budgets, capital expansion, fundraising, research, and employment policies.

In March 2013, UofT elected a new president for a five-year term. The new president has been with the university for the past three decades. There has been no significant turnover among the senior management team in recent years and we expect the team to be quite stable in the next two years. The university approves a five-year operating budget annually and has a number of financial policies in place, including investment policies and a new debt policy.

Favorable Enrollment And Demand Trends Continued In 2013

Positive trends in enrollment, demand, and student quality continued in 2013, in our opinion. Full-time equivalent students (FTEs) increased 3.3% to 70,311 in fiscal 2013, up from the 2.2% increase in fiscal 2012 and above the five-year average of 3.0%. We expect FTEs to grow again for fiscal 2014 by close to 3%. The forecast growth is the result of strong graduate enrollment growth (7.1%) and more modest undergraduate growth of 3.1%. UofT projects that its graduate students, which historically represented about 20% of the total student population, will increase to 22.3% by fall 2017. It expects most of the increase to be at its largest campus (St. George) and will be primarily domestic. The university expects to increase undergraduate enrollment at its Scarborough and Mississauga campuses, with 43% of this coming from international students. International enrollment, which has been rising steadily, was 15.7% (of total FTEs) in fiscal 2014 and should reach 17% by fiscal 2016. We believe that the province's commitment to fund more than 40,000 new university spaces and the expected stable growth in university-age population in the Greater Toronto Area (close to 60% of UofT's enrollment intake comes from the area) in the next five years should help the university achieve its growth targets.

Student quality metrics continued to be strong in fiscal 2013, in our opinion. The acceptance rate (offers-to-applicants) was virtually unchanged at 51% in fiscal 2013, in line with the five-year average. The matriculation rate was also virtually unchanged at 34% and in line with the long-term average. The average entry grade for the Faculty of Arts & Science was 85% for the cohort entering in the fall of 2013 and 92% for engineering students. The fiscal 2013 retention rate of first-year students was 91%, little changed from the previous year. The graduation rate improved to 71% from 69% a year earlier. Overall, UofT's student quality metrics compare well with those of similarly rated Canadian peers, except for its matriculation rate, which was lower than those of almost all peers.

Financial results rebound strongly in fiscal 2013

The university's financial results rebounded strongly in fiscal 2013 as it recorded a consolidated surplus of 6.8% of total consolidated revenues. The surplus was better than the long-term average and a substantial improvement on the fiscal 2012 deficit of 1.4% of total consolidated revenues. Before that deficit, the most recent one occurred in fiscal 2008 as a result of investment losses stemming from the financial crisis. Absent those extraordinary deficits, UofT's surpluses have averaged about 3% of annual revenues, by our estimates. On a modified cash basis (adjusted for amortization of deferred capital contributions and capital assets), the university recorded a surplus of 5.9%, which was also better than the previous year.

Total expenses declined substantially (12.5%) in fiscal 2013 from the restated fiscal 2012 levels. The decline was due entirely to significantly lower future benefit expenses. Salary expense rose 3.8% in fiscal 2012, reflecting negotiated increases and more faculty and staff. Salary and benefit costs are UofT's biggest expense; they represented about 47% of total expenses in fiscal 2013 and continue to be its biggest source of budgetary pressure, as is the case with all other rated Canadian universities. As for all other expense areas, some expense items rose modestly while other recorded small declines, so that the increase in all non-employee-related costs in fiscal 2013 was held to 2.5%.

Revenues increased 6.5% in fiscal 2013 on higher student fees, investment income, donations, and other income. The increase in student fees, the largest single revenue increase, was due in most part to higher enrollment; the increase in investment income was the result of better investment returns. Total government grants fell 2.4% in fiscal 2013, due almost entirely to reduced research and restricted purpose grants; operating grants were virtually unchanged despite increased enrollment. Government grants are UofT's biggest revenue source, representing about 43% of total revenues in fiscal 2013, followed by student fees, at 37%. Ontario operating grants represented 27% of the university's total revenues. We do not expect revenues to increase strongly in the next two years. The government has capped tuition increases at 3% (for domestic undergraduate students) annually and its own deficits will constrain its ability to provide increased support for Ontario universities. However, UofT's strategy of increasing international enrollment could provide some uplift to revenues, given that tuition rates for international students are unregulated. On the other hand, we think it is unlikely that provincial operating grants will decline significantly in the next two years, given postsecondary education's vital public policy role.

The university made a lump sum pension contribution of C$150 million to its registered plans in June 2011 to relieve pressure on the operating budget, and will make another before July 1, 2014. In addition, under its current pension contribution strategy, UofT will increase its annual pension special payments budget, which includes estimated pension special payments and other related costs, by C$70 million over five years. Annual special payments will rise to C$97 million (fiscal 2016) from C$27 million (fiscal 2011). Furthermore, the university plans to increase those payments by another C$15 million per year (phased in over three) beginning in fiscal 2017, if the actuarial valuation happening later this year shows a larger-than-expected going-concern pension deficit. Although the increased annual special payments represent additional budgetary pressure, we believe that UofT's preparations will ensure that the increased costs will be manageable over the next two years.

According to the university's fiscal 2015 budget, operating results will be balanced for fiscal years 2015-2019. The budget assumes that domestic undergraduate tuition fee growth will be capped at 3% over the five-year budget period and growth in government operating grants will be minor. Nevertheless, operating revenues are forecast to rise at an annual rate of about 6%. With the forecast balanced budgetary results, expenditures should rise at the same rate as revenues in the five-year period, with academic expenses accounting for the majority of budgeted operating expense growth.

Solvency Relief Moderates Current Pension Contributions

UofT has several defined benefits plans that provide pension and other postemployment benefits to its employees. At April 30, 2013, its defined benefit pension deficits were C$955 million on a going-concern basis and C$1.3 billion on a solvency basis. Both were down from a year earlier. The biggest improvement was with the solvency deficit, which fell almost 25% in fiscal 2013, compared with a 14% decline in the going-concern deficit. The improvement came on higher investment returns and a special payment of C$67 million in fiscal 2013.

The pension plan deficit on an accounting basis was C$1.1 billion, down about 10% from C$1.25 billion at fiscal year-end 2012. Under the new accounting rules effective April 30, 2013, pension liabilities will be valued using funding assumptions used for the going-concern valuation, reducing the difference between the accounting and going-concern deficits. The changes had the effect of reducing the fiscal 2012 accounting basis deficit to C$1.25 billion from close to C$2.0 billion under the old rules. The university made employer contributions at June 30, 2013, of C$161.4 million, including C$94.8 million of current service funding and C$67 million of special payment funding.

UofT had a C$735 million nonpension postemployment deficit (accounting basis) in fiscal 2013. Nonpension postemployment benefits include medical and dental coverage and long-term disability. Because there is no legislative requirement to maintain assets against these liabilities (unlike pensions), the university funds these on a pay-as-you-go basis, similar to other universities.

In 2012, UofT received the approval for stage 1 of the province's solvency relief, which substantially reduced its annual special pension-related payments to C$67 million for fiscal 2013 (from C$200 million in absence of the solvency relief). The special pension payments budget will increase to C$87 million in fiscal 2014, reaching C$97 million by fiscal 2016.

The university will apply for stage 2 of the province's solvency relief (which extends the amortization period of the solvency pension deficit to 10 years from five) after receiving the results of its next required actuarial valuation as of July 1, 2014. It estimates it will achieve 100% of the savings targets required by the province, which meets the conditions required for acceptance to stage 2 relief. The 10-year amortization solvency payment period associated with stage 2 relief would begin July 1, 2015. With the extended repayment period, the pension contribution strategy (based on the July 1, 2011 actuarial reports) indicates annual special pension payments to be C$110 million from fiscal years 2016-2024, decreasing to C$76 million thereafter. Of the C$110 million special pension payment, UofT plans to fund C$76 million in cash (as part of the C$97 million set aside from the operating budget) and C$34 million through noncash letters of credit.

Capital Plan

In fiscal 2013, capital expenditures totaled almost C$205 million. Of the total, the majority (86%) was for buildings and equipment and furnishings, with the remainder going to library books. Spending on buildings totaled C$100 million, including the reconstruction of the North building, construction of the Kaneff building, and renovation of the Davis laboratory on the Mississauga campus, the construction of the Pan-Am Games Aquatics and Athletics Centre on the Scarborough campus, and the construction of the Goldring Centre and expansion of the Rotman building on the St.

George campus.

For fiscal 2014, UofT forecasts that it will spend C$237 million. Again, the bulk of spending will go to buildings and equipment and furnishings. Library books and land acquisition will make up the balance. The university is budgeting for an even bigger capital program for fiscal 2015. Total capital spending is estimated to be C$245 million and it will be for the same key priorities of buildings, equipment, and books.

We do not expect UofT to issue debt for any of the above capital work. Debt has been a secondary source of capital spending historically. The university has largely paid for projects with government capital grants, donations, and other sources of internal financing. It plans to fund the majority of new capital projects in fiscals 2014 and 2015 through internal budgets, and the remainder with provincial funding.

UofT's deferred maintenance liability, including asbestos containment and removal, was C$594 million in fiscal 2013. Its fiscal 2014 budget includes C$13.0 million annually, rising to C$17.5 million in a few years, to address deferred maintenance at the St. George campus (estimated at C$435 million), with additional funds set aside for the Mississauga and Scarborough campuses. The university also charges departments for the space they use, encouraging more effective use of available space and helping contain costs.

Significant-But-Manageable Debt Burden

UofT's total gross debt outstanding stood at C$726 million at the end of fiscal 2013, which was virtually unchanged from the previous year-end. The debt represented 31% of adjusted revenues, which was also unchanged from the previous fiscal year, and C$10,326 per FTE, which was down thanks to higher FTE numbers. These levels are broadly in line with those of key peers such as University of Western Ontario, and Queen's University but higher than those of University of British Columbia.

The fiscal 2013 DSCR, which was effectively interest-only, was 7.0x, a solid improvement on the fiscal 2012 DSCR, owing to fiscal 2013's substantially stronger financial results. Interest expense was up slightly at 1.7% of adjusted revenues.

With no debt issuance expected in the next two years, UofT's debt metrics should improve with rising operating revenues and enrollment. We expect that debt should fall below 27% of operating revenues and C$9,500 per FTE by the fiscal year-end 2016.

Most of the university's debt consists of bullet debentures, which it uses to mainly finance capital projects. To repay its debt, UofT sets aside principal payments from academic divisions into a self-imposed sinking fund (the long-term borrowing pool). At fiscal year-end 2013, these assets totaled C$130 million, which the university invests together with the endowment fund.

In November 2012, UofT approved a new debt strategy that sets what we view as prudent debt limits. This increases the university's total debt limit to C$1.4 billion for fiscal 2014, of which C$1.05 billion is set as external debt. UofT's debt outstanding, external or internal, is well below the two limits. We do not expect the university to issue any external debt in the next two years.

Financial Resources

UofT has the largest endowments among Canadian universities, with a fair value of close to C$1.7 billion as of the end of April 2013. It has a conservative endowment draw, in our view, with an annual spending rate of 3.0%-5.0% of the opening market value of the endowments. In fiscal 2013, the endowments paid out about C$70 million, which represented about 4% of total endowments.

At fiscal year-end 2013, consolidated cash and investments totaled C$3.15 billion, up 9.50% million from fiscal 2012. Total cash and investments represented 132% of consolidated expenditures, or more than 4x total debt, in line. Unrestricted financial resources (internally restricted net assets and internally restricted endowments) stood at slightly more than C$1.0 billion, which was up from the previous year's restated total of C$836 billion (C$258 million before the restatement). This equaled about 138% of debt and 42% of consolidated annual expenses.

Also at fiscal year-end 2013, 51.3% of the portfolio was in fixed-income securities, 45.4% in Canadian and international equities, and 3.3% in cash. The endowment fund's annual return (net of investment fees and expenses) was 11.4%, which was a dramatic improvement on the previous year's return of 1.0% and the 5.8% target return.

Fundraising

At fiscal year-end 2013, total endowments stood at C$1.66 billion. In November 2011, UofT launched its Boundless campaign, with a fundraising goal of C$2.0 billion. By year-end 2013, the university and its affiliated federated universities had received C$1.3 billion in donations. The majority of the funds will likely have external restrictions, which tends to be the case for about 85% of total endowment. However, we believe that even these provide strength, by producing spendable endowment income. Furthermore, endowments restricted for scholarships or faculty chairs enhance a university's profile, attracting quality students and faculty.

University of Toronto -- Peer Comparison*

	--University of Toronto--		**--University of British Columbia--**		**--Queen's University--**		**--University of Western Ontario--**	
	2013	**2012 (restated)**	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**
Rating at Dec. 31	AA/Stable/--	AA/Negative/--	AA+/Stable/--	AA+/Stable/--	AA+/Stable/--	AA+/Stable/--	AA/Stable/--	AA/Stable/--
Enrollment and demand								
Headcount	80,899	79,085	57,550	56,198	24,042	24,343	38,454	38,038
Full-time equivalent (FTE)	70,311	68,088	50,254	48,563	21,904	21,713	31,018	30,679
Acceptance rate (offers to applications; %)	51.2	52.1	45.8	47.4	41.1	40.5	51.0	54.2
Matriculation rate (registrants to offers; %)	33.6	32.5	53.0	53.3	42.6	45.1	21.9	22.1

University of Toronto -- Peer Comparison* (cont.)

Undergraduate FTEs as % of total FTEs	79.9	79.8	82.5	82.7	82.3	82.6	81.3	81.3
Income statement (C$000s)								
Adjusted operating revenues	2,523,400	2,395,300	2,111,772	2,038,375	782,858	762,227	1,049,744	1,030,914
Adjusted operating expenses	2,399,400	2,412,200	2,050,781	1,981,303	776,298	761,692	987,065	955,810
Adjusted operating balance (% of adjusted operating expenses)	5.2	(0.7)	3.0	2.9	0.8	0.1	6.4	7.9
Adjusted operating balance before depreciation and amortization	199,600	56,100	176,073	162,915	37,070	32,740	100,953	111,814
Tuition and student fee dependence (% of adjusted operating revenue)	37.4	35.4	20.8	20.2	29.8	28.1	29.4	27.9
Debt								
Debt outstanding (C$000s)	726,000	727,700	414,688	415,471	221,074	227,266	316,185	216,319
Current debt service burden (% of adjusted operating expenses)	1.7	1.5	2.6	1.3	2.4	2.5	2.4	1.5
Current adjusted debt service coverage (x)	5.8	2.5	3.8	7.5	2.6	2.4	4.9	8.7
Financial resource ratios								
Endowment market value (C$000s)	1,663,700	1,518,100	1,166,994	1,074,824	710,251	616,797	431,853	371,732
Endowment per FTE ($)	23,662	22,296	23,222	22,133	32,426	28,407	13,923	12,117
Cash and investments (C$000s)	2,403,600	2,095,600	806,546	718,165	871,781	802,251	781,469	694,573
Cash and investments to adj. operating expenses (%)	131.4	119.4	41.4	43.6	126.0	115.6	108.8	93.1
Cash and investments to debt (%)	434.3	395.8	204.6	207.9	442.3	387.6	339.7	411.3

University of Toronto -- Peer Comparison* (cont.)								
Adjusted unrestricted financial resources (UFR; C$000s)	1,002,700	836,000	398,779	326,881	371,580	331,177	391,981	292,715
Adjusted UFR to adjusted operating expenses (%)§	41.8	34.7	19.4	16.5	47.9	43.5	39.7	30.6
Adjusted UFR to debt (%)§	138.1	114.9	96.2	78.7	168.1	145.7	124.0	135.3
Unfunded liabilities to total liabilities (%)	42.9	43.8	0.3	0.4	17.0	20.7	24.4	25.7

*All adjustments and ratios follow "USPF Criteria: Higher Education" calculation method. §Adjusted UFR equals adjusted internally restricted net assets plus internally restricted endowments.

Related Criteria And Research

Related Criteria

- Principles Of Credit Ratings, Feb. 16, 2011
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- USPF Criteria: Higher Education, June 19, 2007

Ratings Detail (As Of April 17, 2014)	
University of Toronto	
Issuer Credit Rating	AA/Stable/--
Senior Unsecured	AA
Issuer Credit Ratings History	
22-Mar-2013	AA/Stable/--
17-Mar-2011	AA/Negative/--
26-Sep-2003	AA/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.