

CREDIT OPINION

10 February 2022

Update

✓ Rate this Research

RATINGS

University of Toronto

Domicile	Ontario, Canada
Long Term Rating	Aa1
Type	LT Issuer Rating
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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University of Toronto (Canada)

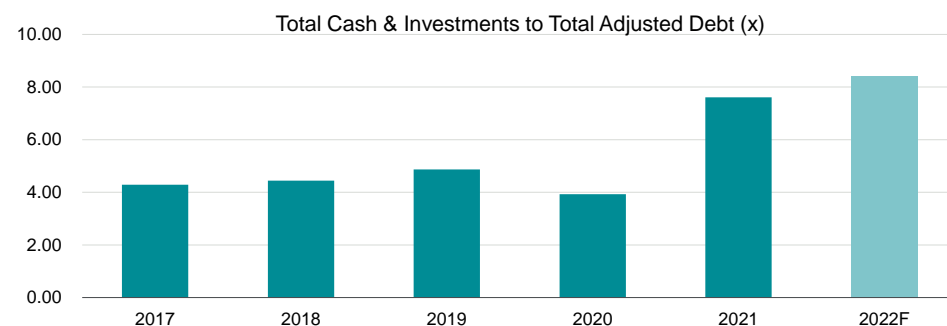
Update to credit analysis

Summary

The credit profile of the [University of Toronto](#) (Aa1 stable) (U of T) reflects its flagship status as Canada's largest and top-ranked post-secondary institution, global brand recognition of its academic and research quality, and balance sheet strength including its endowment funds valued at CAD3.2 billion at April 30, 2021. The credit profile also reflects diversified revenue sources and a lower reliance on provincial funding than most Canadian peers. These strengths provide a buffer against the adverse fiscal impacts of the coronavirus pandemic as well as provincial restrictions on tuition fees. Pressure could also arise if the pandemic results in a shift in student demand and/or perception of the value of higher education.

Exhibit 1

U of T maintains very strong balance sheet strength from low debt and high cash and investment levels



(fiscal years ending April 30)

Sources: University of Toronto, Moody's Investors Service

Credit strengths

- » Exceptional wealth and liquidity and low leverage
- » Very strong governance and management that provide stability
- » Global brand recognition and research strength provides resilience against enrolment pressures

Credit challenges

- » Manageable operating pressures from the coronavirus pandemic and provincial restrictions on tuition
- » Sizeable pension expenses and pension liabilities

Rating outlook

The stable outlook reflects our view that the university will maintain exceptional levels of wealth and liquidity, manageable debt levels, and continued strong fundraising capacity, which provide a significant buffer against enrolment and funding pressures. The stable outlook further reflects our expectation that the university will continue to navigate the pandemic environment with minimal enduring impacts on its credit profile.

Factors that could lead to an upgrade

The rating could be upgraded following a sustained period of strong positive operating performance and increasing enrolment numbers, in conjunction with a material increase in endowment and liquidity levels in line with Aaa-rated global peers.

Factors that could lead to a downgrade

A sustained decline in enrolment demand, including from international students, leading to weaker financial performance and operating deficits, would lead to downward rating pressure. A material decline in liquidity and investment returns, or a material deterioration of the funded status of its pension plan, would also contribute to downward rating pressure.

Key indicators

University of Toronto (fiscal years ending April 30)

Key Indicators	2017	2018	2019	2020	2021	2022F
Operating revenue (CAD millions)[1]	2,905.2	3,068.8	3,184.7	3,300.7	3,412.4	3,524.0
EBIDA margin (%)	18.1	19.9	18.2	18.6	19.4	19.6
Total cash and investments (CAD millions)	4,558.0	4,821.0	5,259.0	5,418.0	6,949.0	7,643.9
Total cash & investments to total adjusted debt (x)	4.29	4.44	4.87	3.93	7.61	8.40
Total cash & investments to operating expenses (x)	1.77	1.80	1.86	1.85	2.32	2.48
Annual debt service coverage (x)	13.2	15.2	14.5	15.3	17.5	18.1

[1] Revenue is net of scholarship expenses.

Sources: University of Toronto, Moody's Investors Service

Detailed credit considerations

Baseline credit assessment

The credit profile of U of T, as expressed by its Aa1 stable rating, reflects a BCA for the university of aa1. The rating also incorporates a moderate likelihood of extraordinary support coming from the [Province of Ontario](#) (Aa3 stable) in the event that the university faced acute liquidity stress.

Exceptional wealth and liquidity and low leverage

The university maintains exceptional levels of wealth and liquidity from continued growth in cash and investments. Adjusted total cash and investments, including endowments, stood at CAD6.95 billion at April 30, 2021, providing 7.6x coverage of total adjusted debt and 2.3x coverage of operating expenses, ratios which compare favourably to global peers. Despite our expectation of continued modest pressure on liquidity to address coronavirus-related fiscal pressures, we expect that the university will be able to replenish its cash and investment levels from strong operating results and solid investment returns.

The university's endowment portfolio is the largest among Canadian universities, totaling CAD3.2 billion at April 30, 2021. Endowment growth was supported in 2020-21 by new donations and favourable investment earnings as investment returns rebounded. The Long-Term Capital Appreciation Pool, which had a fair value of CAD3.8 billion at April 30, 2021 and includes all assets of the endowment fund, has seen significant growth in recent years in large part due to the growth in endowment balances. Nevertheless, the pool's investment returns continue to exhibit significant annual volatility which results in uncertainty in performance.

U of T has also been highly successful in its fundraising activities, including its recent Boundless fundraising campaign, and we expect that it will be able to maintain a competitive advantage in attracting donations relative to peers. The university receives significant

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donations and gifts for research and capital projects, including a recent CAD250 million gift for human health and health care initiatives. These enable the university to capitalize on its brand name and profile and its ability to generate sizeable philanthropic interest and donations despite competition for fundraising dollars both domestically and internationally.

U of T's credit profile also benefits from low levels of leverage. The university issued its latest debenture in 2011 and we do not anticipate new debt issues over the next 2-3 years. U of T's practice in recent years has been to finance capital projects from non-debt sources, including funding its capital plan from a combination of departments' operating reserves, provincial and federal funding, and donations. Debt affordability, as measured by annual debt service coverage, stood at 17.5x at April 30, 2021, a level that exceeds peer ratios.

Very strong governance and management that provide stability

The success of U of T in maintaining a strong balance sheet and balancing its core operational financial results while meeting academic goals, is underpinned by very strong governance and management and the development and execution of multi-year frameworks for academic and financial planning.

U of T's strong governance is also evident in its planning and responses related to the coronavirus pandemic. This included a swift and successful conversion of in-person classes early on during the pandemic to online courses, and scenario analysis of potential operating outcomes. The university also puts strong emphasis on a decentralized style of governance and decision making. Each faculty is responsible for developing its own budget and adhering to self-imposed revenue and expense targets, which allows the faculties to be more entrepreneurial in areas where they see greater demand and by extension generate positive operating results. The university itself still maintains control over collective bargaining, however, which takes a certain amount of expenditure control out of the hands of individual faculties.

The University of Toronto Asset Management Corporation (UTAM), a non-share capital corporation whose members are appointed by the university, manages the investment assets of the university's Long-Term Capital Appreciation Pool (which includes assets of the endowment fund) and the Expendable Funds Investment Pool (including short- to medium-term funds). UTAM has also committed to sustainable initiatives by reducing its carbon footprint by 2030 by 40% relative to 2017 levels.

Global brand recognition and research strength provides resilience against enrolment pressures

U of T is Canada's largest post-secondary institution located in the Province of Ontario across three campuses in downtown Toronto, Mississauga and Scarborough. U of T is Canada's preeminent research university and consistently places as the top ranked Canadian school and one of the top 20-25 global schools in international rankings, underpinning its international brand.

U of T's excellent market profile and global recognition has contributed to the university's ability to attract consistently high historical global demand and increase enrolment and revenue numbers even in the face of provincial funding and enrolment constraints. Along with its affiliations, including several hospitals, the university also continues to be the leader among Canadian universities in securing federal government research funding from the three granting councils and from other federal programs. U of T's research strength is also evident in the number of prestigious research chairs, including 33 new or renewed "Canada Research Chairs" and 3 "Canada 150 Research Chairs" at the university.

The university's outstanding market profile and high student demand resulted in historically robust enrolment growth, with total full-time equivalent (FTE) growth of nearly 30% between 2009-10 (65,402) and 2020-21 (84,807). The rise in enrolment and contribution to revenue growth has been supported by a faster growth in international students than domestic students, and international students now represent around a quarter of total FTE students.

The reliance on international students continues to expose U of T to manageable pressures from the adverse impact of the coronavirus pandemic on international enrolment given continued, although easing, global travel restrictions, and to global trade and political tensions. Much of the historical international growth has come from Asia, and in particular from China. The number of Chinese students more than doubled over the last 5 years and now constitute around 60% of international students. The significant dependence on international tuition revenue exposes it to revenue concentration from a single region or country and to political risk from potential diplomatic tensions, as evidenced by recent tensions between Canada and China and previous tensions between Canada and Saudi Arabia.

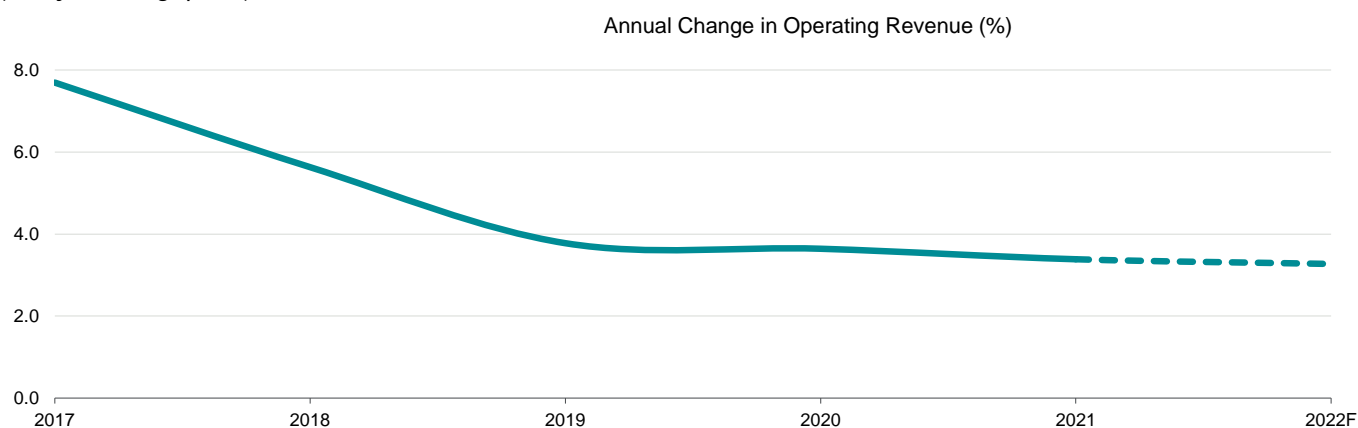
Manageable operating pressures from the coronavirus pandemic and provincial restrictions on tuition

The coronavirus pandemic creates near-term fiscal challenges for the university, in addition to pressures from provincial restrictions on tuition fees. U of T, along with higher education institutions globally, has faced operating revenue declines mainly from its ancillary operations (student housing, parking, dining and sales) and higher pandemic-related costs. A lengthy period of travel restrictions and campus closures created some uncertainty in international student enrolment, although we expect enrolment to remain robust as travel restrictions ease. Future pressure could arise if a permanent shift in the perception of the value of higher education as a result of the pandemic were to result in a sustained decline in demand, although we currently view the probability of this risk materializing to be relatively low.

Operating results have also been challenged by provincially mandated freezes in domestic tuition rates for 2020-21 and 2021-22 following a mandated 10% reduction in 2019-20. The mandated restrictions weaken U of T's ability to generate revenue from tuition or to offset any international revenue pressure from domestic fees. Additionally, although deferred by three years due to the pandemic, the province expects to transition its operating grants to reflect a greater emphasis on performance metrics, which could create volatility in government grants in the future.

Exhibit 3

Cumulative pressures contribute to weaker revenue growth (fiscal years ending April 30)



Source: Moody's Investors Service, University of Toronto

Despite the weakened level of operating funding, U of T has a lower reliance on ongoing provincial funding than most of its rated domestic peers (around 20-25% of operating revenues). This lower reliance provides U of T with greater autonomy and flexibility in managing its finances and academic programs from own-source revenues, cushioning some of the impact of the challenges in funding environment relative to peers. U of T can rely on additional mitigants to offset fiscal and enrolment pressures. Mitigants include increasing international student fees, which are not subject to provincial controls, as well as reducing administrative costs. These mitigants, along with strong summer and fall enrolments, additional pandemic-related government funding and strong investment returns, contributed to a consolidated surplus of CAD726 million in 2020-21, although we expect continued weak ancillary revenues in 2021-22 before an anticipated rebound in 2022-23.

Sizeable pension expenses and pension liabilities

U of T's financial profile remains pressured by sizeable annual pension expenses representing around 4-5% of total expenses. For 2020-21, pension expense totaled CAD143 million, a significant amount that reflects a rise in expenses over the last few years.

U of T has historically recorded large pension deficits given significant unfunded pension liabilities. The university was previously granted entrance into the provincial solvency funding relief program, and received solvency funding relief measures. As of July 1, 2021 the university transitioned to a jointly sponsored defined benefit pension plan, the University Pension Plan Ontario (UPP), with two other universities. As at the July 1, 2021 transition date, the pension plan was in a surplus of CAD792.5 million. Under the UPP, U of T will be required to fund any future deficits for the first 10 years which maintains funding pressure on the university, however subsequently the costs will be gradually shared among participants in the UPP. Further, while we expect continued strong investment

returns in 2021-22 and 2022-23 as asset values and returns improve amid a gradual market rebound, the year-over-year volatility in investment balances and returns creates volatility in pension deficit levels.

Extraordinary support considerations

Moody's assigns a moderate likelihood of extraordinary support coming from the Province of Ontario in the event that the university faced acute liquidity stress.

ESG Considerations

How environmental, social and governance risks inform our credit analysis of U of T

Moody's takes into account the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of U of T, the materiality of ESG to the credit profile is as follows:

Exposure to environmental risks is not material to the U of T's credit profile. The university owns land and owns / operates buildings which may be subject to environmental risks (e.g. asbestos in older buildings or clean-up following construction), but these risks are small and the university proactively manages them through its facilities maintenance.

The university has moderate exposure to social risks. Social considerations principally relate to developments in public policy on education, in particular Ontario's objective of promoting improvements in tuition affordability through mandated provincial tuition fee restrictions. We also consider the coronavirus outbreak as a social risk which adds a high degree of uncertainty on enrolment levels as students may alter their plans on attending universities during a global health pandemic. These pressures are mitigated by an excellent global brand leading to consistently strong enrolment demand and significant liquidity.

Exposure to governance risks is material and governance risk is low. Governance considerations include a robust institutional framework and prudent financial planning which has resulted in multi-year balanced budgets and strong operating results. Each faculty is responsible for developing its own budget and adhering to self-imposed revenue and expense targets. Faculties tend to encourage and explore entrepreneurial ideas for boosting revenue. Oversight is strong from its Governing Council including its boards and committees.

Further details are provided in the "Detailed credit considerations" section above. Our approach to ESG is explained in our cross-sector methodology [General Principles for Assessing Environmental, Social and Governance Risks](#).

Rating methodology and scorecard factors

The assigned baseline credit assessment (BCA) of aa1 is in line with the scorecard indicated outcome of aa1. For details of our rating approach, please refer to the [Higher Education](#) (August 2021) and [Government-Related Issuers](#) (February 2020) methodologies.

University of Toronto		
Scorecard Factors and Sub-factors	Value	Score
Factor 1: Scale (15%)		
Adjusted Operating Revenue (USD Million)	2,607	Aaa
Factor 2: Market Profile (20%)		
Brand and Strategic Positioning	Aaa	Aaa
Operating Environment	Aa	Aa
Factor 3: Operating Performance (10%)		
EBIDA Margin	19%	Aa
Factor 4: Financial Resources and Liquidity (25%)		
Total Cash and Investments (USD Million)	5,656	Aaa
Total Cash and Investments to Operating Expenses	2.3	Aaa
Factor 5: Leverage and coverage (20%)		
Total Cash and Investment to Total Adjusted Debt	7.6	Aaa
Annual Debt Service Coverage	17.5	Aaa
Factor 6: Financial Policy and Strategy (10%)		
Financial Policy and Strategy	Aa	Aa
Scorecard-Indicated Outcome		aa1
Assigned BCA		aa1

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

Ratings

Exhibit 5

Category	Moody's Rating
UNIVERSITY OF TORONTO	
Outlook	Stable
Issuer Rating	Aa1
Senior Unsecured -Dom Curr	Aa1

Source: Moody's Investors Service

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