

CREDIT OPINION

30 August 2023

Update



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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.

Contacts

Adam Hardi, CFA	+1.416.214.3636
Vice President-Senior Analyst	
adam.hardi@moody's.com	
Jonathan Holmes	+1 647.417.6302
Associate Analyst	
jonathan.holmes@moody's.com	
Michael Yake	+1.416.214.3865
Associate Managing Director	
michael.yake@moody's.com	

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University of Toronto (Canada)

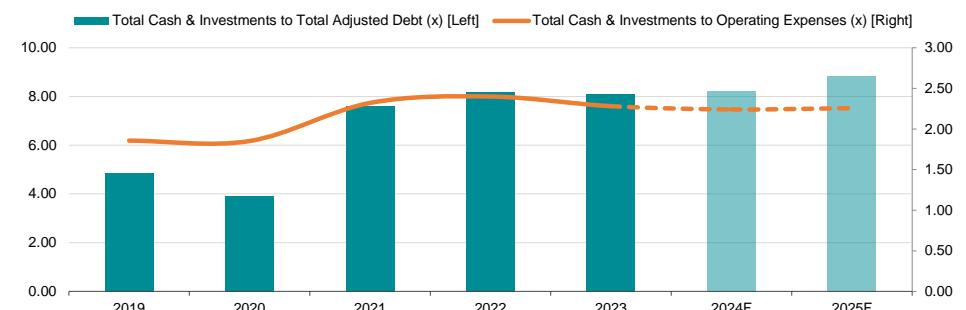
Update to credit analysis

Summary

The credit profile of the [University of Toronto](#) (U of T, Aa1 stable) reflects its global brand recognition and its flagship status as Canada's largest and top-ranked post-secondary institution, which allow the university to attract significant student demand, research funding and donations. Exceptional levels of cash and investments, including endowment funds valued at CAD3.3 billion at April 30, 2023, provide significant coverage of debt and expenses. The credit profile also reflects diversified revenue sources and a lower reliance on provincial funding than most Canadian peers, although ongoing provincial restrictions on tuition fees constrain a key revenue source. Further, inflationary operating and capital cost pressures will keep future expenses elevated relative to historical levels.

Exhibit 1

Cash and investment coverage of debt and expenses will remain very strong, in line with recently improved levels



Credit strengths

- » Exceptional wealth and liquidity and low leverage
- » Very strong governance and management which underpin reputation
- » Global brand recognition and research strength along with consistent enrolment growth

Credit challenges

- » Operating challenges from provincial tuition caps and elevated inflation levels
- » Sizeable pension expenses and pension liabilities

Rating outlook

The stable outlook reflects our view that the university will continue to see strong student demand which will support continued operating surpluses. High levels of cash and investments and the university's strong fundraising capacity will also help mitigate inflationary cost pressures and provincial restrictions on tuition fee increases.

Factors that could lead to an upgrade

The rating could be upgraded following a sustained improvement in operating margins above 20%, along with significant easing of provincial funding restrictions on tuition fees, or a material increase in cash and investment balances.

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 cash and investment balances and investment returns, or a material deterioration of the funded status of its pension plans, would also contribute to downward rating pressure.

Key indicators

Exhibit 2

University of Toronto

Year ending April 30	2020	2021	2022	2023	2024F	2025F
Operating revenue (CAD millions)[1]	3,300.7	3,412.4	3,450.9	3,533.8	3,696.8	3,837.5
EBIDA margin (%)	18.6	19.4	17.2	11.5	12.0	11.5
Total cash and investments (CAD millions)	5,418.0	6,949.0	7,456.0	7,706.0	7,860.1	8,253.1
Total Cash & Investments to Total Adjusted Debt (x)	3.93	7.61	8.18	8.11	8.24	8.84
Total Cash & Investments to Operating Expenses (x)	1.85	2.32	2.40	2.28	2.24	2.26
Annual debt service coverage (x)	15.3	17.5	15.7	10.7	11.7	11.6

[1] Revenue is net of scholarship expenses.

Sources: University of Toronto and 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 positive) 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 CAD7.7 billion at April 30, 2023, providing 8.1x coverage of total adjusted debt and 2.3x coverage of operating expenses, ratios which compare favourably to global peers. Although we project that still elevated inflation and high levels of capital spending will put modest pressures on liquidity, the university will be able to replenish its cash and investment levels from strong operating results and solid investment returns in line with its returns over the last few years.

The university's endowment portfolio is the largest among Canadian universities, totaling CAD3.3 billion at April 30, 2023 despite limited year-over-year growth (2022: CAD3.2 billion). Endowment growth is supported by new donations and investment gains as investment returns rebounded. The Long-Term Capital Appreciation Pool, with a fair value of CAD3.9 billion at April 30, 2023 and includes all assets of the endowment fund, has seen significant growth in recent years. Nevertheless, the pool's investment returns continue to exhibit annual volatility which adds some uncertainty to investment performance.

U of T has also been highly effective in its fundraising activities. The university launched a new fundraising campaign in 2021 ('Defy Gravity') with a goal to reach CAD4 billion in donations over 10 years. To date, the campaign generated over CAD1.6 billion, and we

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expect that it will be able to leverage its brand name and reputation to maintain a competitive advantage in attracting donations relative to peers. The university receives significant donations and gifts for research and capital projects, including a recent CAD25 million gift for its Scarborough Academy of Medicine and Integrated Health. These gifts demonstrate the university's ability to capitalize on its brand name and profile and 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 aided by its strong cash generation. The university last issued debentures in 2011 and we do not anticipate new debt issues over the next three 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. We expect that the university may issue a modest amount of new debt related to its capital infrastructure and energy retrofit programs. Debt affordability, as measured by annual debt service coverage, stood at 10.7x at April 30, 2023, a level that exceeds the peer median.

Very strong governance and management which underpin reputation

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 through the development and execution of multi-year frameworks for academic and financial planning. The board and senior leadership continue to ensure and monitor that sound policies and practices are in place.

The university puts strong emphasis on a decentralized style of governance and decision making. Each faculty is responsible for developing its own budget and for adhering to self-imposed revenue and expense targets. This allows the faculties to be more entrepreneurial in areas where they see greater demand and by extension generate positive operating results. At the same time, the university itself still maintains control over collective bargaining, 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 to achieve net zero carbon emissions associated with the endowment portfolio by no later than 2050.

U of T's strong governance has also been evident in its planning and response to the coronavirus pandemic over the last three years. 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.

Global brand recognition and research strength along with consistent enrolment growth

U of T is Canada's largest post-secondary institution located in the Province of Ontario, with 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 global schools in international rankings, underpinning its international brand.

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 "Canada Research Chairs" and "Canada 150 Research Chairs" at the university.

U of T's excellent market profile and global recognition has contributed to the university's ability to attract consistently high global demand and increase enrolment and revenue numbers even in the face of provincial funding and enrolment constraints. The number of total full-time equivalent (FTE) students has grown consistently each year to 86,297 in 2022-23, up more than 7% over the last five years. 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 30% 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

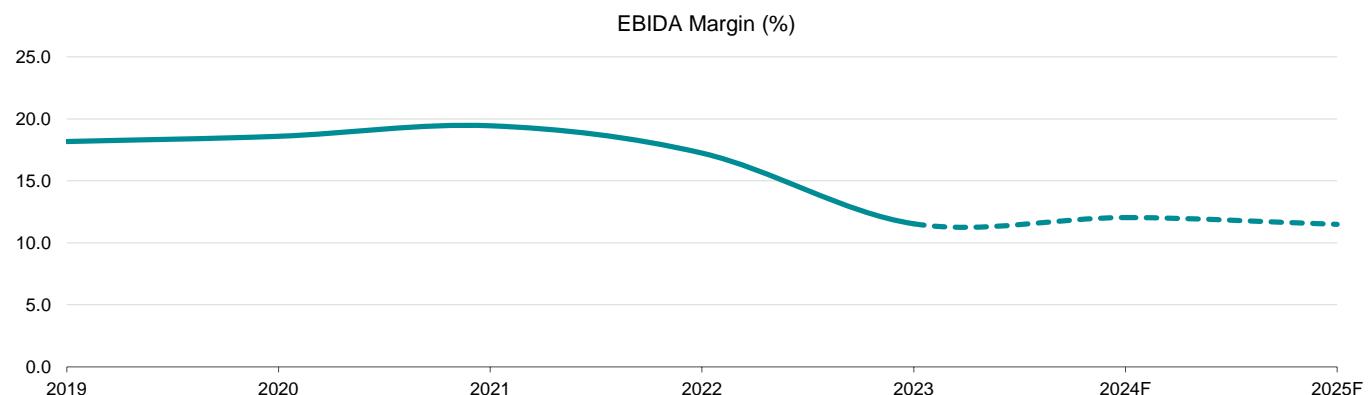
students more than doubled over the last 5 years and constituted around 55% of international students in 2022-23. The significant dependence on international tuition revenue exposes it to revenue concentration from a single region or country and to political risk from potential diplomatic tensions, as evidenced by recent tensions between Canada and China. Nevertheless, the university made an effort in recent years to diversify its international student population, a trend we expect will continue over the next several years. Enrolment from India has been especially robust, constituting over 8% of international students in 2022-23, a level that has more than doubled since 2017-18. The university has also seen strong international student growth from Indonesia, Turkiye, Brazil and Iran.

Operating challenges from provincial tuition caps and elevated inflation levels

Along with other Ontario universities, U of T currently faces an evolving provincial government framework which led to negative operating impact on the university in recent years. Specifically, the province mandated freezes in domestic tuition rates over the last three years, following previously mandating a 10% reduction in 2019-20. The mandated restrictions resulted in weaker tuition revenues for the university and weakened its ability to offset any international revenue pressure from domestic fees. Additionally, the province is transitioning its operating grants in 2023-24 to reflect a greater emphasis on performance metrics, which could create volatility in government grants in the future. These combined pressures have resulted in weaker growth in operating revenues than in previous years despite solid EBIDA margins of 11.5% in 2022-23 with our estimate of similar levels in 2023-24 and 2024-25 (Exhibit 3).

Exhibit 3

Operating challenges will continue to exert pressure on EBIDA margins



Fiscal year ending April 30

Sources: University of Toronto and Moody's Investors Service

Despite these challenges, U of T has a lower reliance on ongoing provincial funding than most of its rated domestic peers (20% of operating revenues for U of T in 2022-23 vs. the domestic peer average of 35%). This lower reliance provides U of T with greater autonomy and flexibility in managing its finances and academic programs from own-source revenues and additional mitigants, cushioning some of the impact of the challenges in funding environment relative to peers.

At the same time, inflationary pressures on operating and capital costs, including general cost escalation from rising salaries and benefits which currently make up approximately 60% of total expenses, present additional revenue and expense challenges. In the current high inflationary environment, U of T – similar to peers - could see pressure as expiring collective agreements are renewed. High levels of borrowing costs and a high cost of living in the Toronto area could unfavourably impact student demand.

Sizeable pension expenses and contingencies

U of T's financial profile remains pressured by sizeable annual pension expenses representing around 4-5% of total expenses. For 2022-23, pension expense totaled CAD141 million (4.1% of total expense).

U of T has historically recorded large pension deficits given significant unfunded pension liabilities. 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 is required to fund any future deficits on the assets and liabilities transferred into the plan for the first 10 years, which could create funding pressure on the university, however subsequently the costs will be gradually shared equally between participating employers and employees in the UPP.

We expect that the recent sharp rise in interest rates in response to high inflation would pressure the funded status of the pension plan. U of T estimates that each 0.25% change in the discount rate creates a CAD250 million change in pension obligations. To mitigate potential future declines in the funded status, U of T maintains a pension risk contingency which stood at CAD95 million in 2022-23 and which will gradually decline to CAD50 million by 2026-27.

Extraordinary support considerations

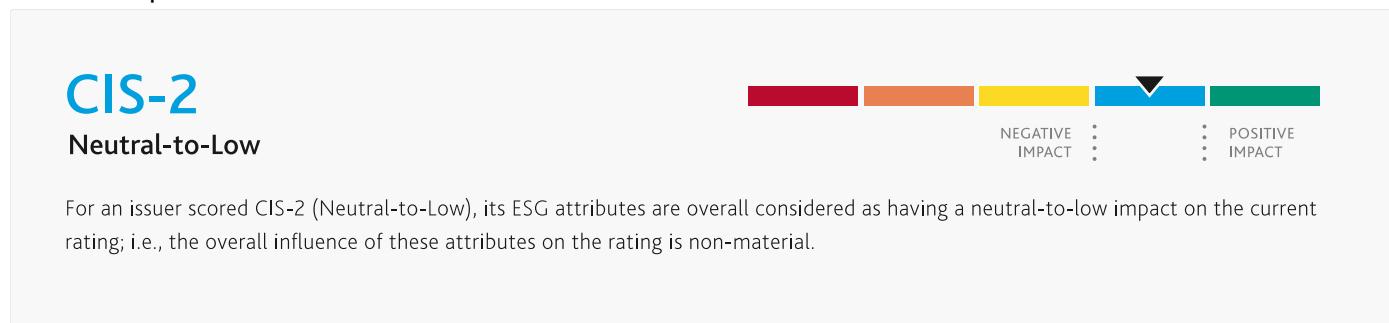
Moody's assigns a moderate likelihood of extraordinary support coming from the Province of Ontario in the event that the university faced acute liquidity stress.

ESG considerations

U of T's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 4

ESG Credit Impact Score



Source: Moody's Investors Service

U of T's neutral-to-low (**CIS-2**) ESG Credit Impact Score reflects its low exposure to environmental risks, moderate pressures from social risks, and sound governance.

Exhibit 5

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

The **E-2** issuer profile score (IPS) reflects the university's low exposure to environmental risks as its infrastructure is built to withstand the typical range of weather patterns. While it owns land and buildings which may be subject to environmental risks (e.g., asbestos in older buildings or clean-up following construction), these risks are modest and the university proactively manages them through its operations and facilities maintenance.

Social

The **S-3** IPS reflects a decline in the university entrance-age population in Ontario, and pressures from tuition revenue declines given provincial funding policies designed to address affordability, both on tuition setting and support to students. U of T has a higher share of international students than most rated universities, which helps offset pressures from domestic tuition fees but exposes it to political and economic risk including immigration trends and changes in policies on immigration eligibility. These pressures are partly mitigated by strong selectivity ratios and solid enrolment demand and a favourable central government immigration policy.

Governance

The **G-2** IPS reflects management's credibility, track record and ability to anticipate and mitigate risks. A robust institutional framework and prudent financial planning also contributes to multi-year balanced budgets and strong operating results. The university puts strong emphasis on a decentralized style of governance and decision making, allowing for funding allocations between the university's departments. The organizational structure is typical of Canadian universities with strong oversight from the Governing Council and committees, although provincial representation on the board exposes the university to potential government intervention.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.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 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.

Exhibit 6

University of Toronto
(fiscal year ending April 30, 2023)

Scorecard Factors and Sub-factors	Value	Score
Factor 1: Scale (15%)		
Adjusted Operating Revenue (USD Million)	2,665	Aaa
Factor 2: Market Profile (20%)		
Brand and Strategic Positioning	Aaa	Aaa
Operating Environment	Aa	Aa
Factor 3: Operating Performance (10%)		
EBIDA Margin	12%	A
Factor 4: Financial Resources and Liquidity (25%)		
Total Cash and Investments (USD Million)	5,675	Aaa
Total Cash and Investments to Operating Expenses	2.3	Aaa
Factor 5: Leverage and coverage (20%)		
Total Cash and Investments to Total Adjusted Debt	8.1	Aaa
Annual Debt Service Coverage	10.7	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 7

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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