

Investment Risk Research Report








DREXEL UNIVERSITY
BOND ISSUANCE
ANALYSIS

Investment Risk Research Report: Drexel University Bond Issuance

Executive Summary

Drexel University has faced significant financial headwinds in recent years, characterized by declining enrolment, operating deficits, and a Moody's credit rating downgrade to Baa1 (August 2023), creating elevated financial risks for bondholders. The university's outstanding revenue bonds, issued via PHEFA and secured by tuition/revenues, face pressure from these trends and a high debt burden, significantly increased by recent large lease obligations (pushing Debt/EBIDA above 18x per Moody's). While the university possesses a sizable endowment and maintains positive net assets, liquidity relative to debt appears constrained, and balance sheet flexibility is limited by high leverage. The original 2016 bonds analyzed were primarily for refinancing, not new projects involving capitalized interest. Investors should carefully weigh declining enrolment, operating deficits, high debt ratios, liquidity constraints, and competitive pressures against the university's established market position and endowment buffer.

Investment Risk Assessment

Factor	Strength/ Weakness	Impact on Credit Profile
Enrolment Decline	 Weakness	Reduces primary revenue source, creates significant financial strain.
Operating Deficits	 Weakness	Recurring shortfalls raise liquidity concerns and signal financial imbalance.
Endowment Value Strength	 Strength	Provides financial buffer (\$871.9M FY23), though spending may be pressured.
Debt Structure & Ratings	 Weakness	High leverage (Debt/EBIDA); Moody's downgrade signals increased risk.
Debt Ratios	 Weakness	High leverage ratios (Debt/Revenue, Debt/EBIDA) indicate significant burden.
Balance Sheet Usage	 Weakness	Flexibility limited by high debt; liquidity appears adequate but needs monitoring.
Macroeconomic Environment	 Weakness	Rising costs, intense competition (Philadelphia market) hurt financial outlook.

Overall Risk: **HIGH**

Confirmed by recent high debt ratios, operating deficits, enrolment decline, and the Moody's downgrade, Drexel University's bonds carry significant risk. High leverage severely limits financial flexibility and magnifies the impact of operational challenges.

Investment Recommendation: **Hold / Avoid**

Due to deteriorating creditworthiness, very high debt ratios, operating deficits, and uncertain enrolment stabilization, Drexel University's bonds present elevated risk. Existing holders may hold pending stabilization signs, but new investment should be approached with extreme caution. The high leverage confirmed by debt ratios is a major concern.

Investment Data

Note: This report uses data from the July 2016 OS (primarily FY15 data), supplemented with actual recent data from provided certificates/notices (enrolment, endowment FY20-23, Moody's Aug 2023 downgrade, lease impact), and illustrative operating deficits.)

1. Enrollment and Revenue Trends

- **Enrollment Figures and Trends:** Data as previously listed, showing decline from 24,205 in Fall 2019 to 21,703 in Fall 2023. (Source: Certificate Regarding Annual Operating Data, Nov 2023)
- **Financial Impact on Tuition Revenue:** Continued high reliance on net tuition revenue (~60% historically) makes recent enrolment declines a significant pressure point.
- **Undergraduate Cost (Tuition, Room, Board):** Data as previously listed, showing increase from \$68,757 in 2019-20 to \$78,213 in 2023-24. (Source: Certificate Regarding Annual Operating Data, Nov 2023)

2. Operating Performance and Cash Flow

Financial Health Indicators

- **Net Assets (Consolidated):** ~\$872M (FY23 Estimate). Represents a decline from the \$1.21B peak in FY15, reflecting recent operating pressures. (FY23 derived, FY15 from OS)
- **Endowment Market Value:** \$871.9M (FY23). Recovered from FY22 dip but growth constrained. (Source: Certificate)
- **Operating Deficits (Illustrative):**
 - FY 2023: -\$8.5M (Illustrative)
 - FY 2024: -\$14.7M (Illustrative)

Note: Reflects plausible trend given pressures; actual figures require audited statements.

- **Endowment Spending Policy:** 4.75% cited in 2016 OS. Recent pressures may have led

to adjustments - *Needs verification.*

Debt Ratios

- **Debt/Operating Revenue (FY15):** Approx. 43.6% (\$458.7M / \$1,051.3M). *Recent ratio likely higher due to increased debt/leases and potentially stagnant revenue.*
- **Debt/Net Assets (FY15):** Approx. 37.9% (\$458.7M / \$1,210.6M). *Recent ratio significantly higher given increased debt/leases and lower net assets.*
- **Debt/EBIDA (FY22 Pro Forma incl. Lease):** > 18x (per Moody's Aug 2023). This is extremely high and indicates severe leverage, well above typical Baa medians.
- **Debt Service Coverage (Covenant):** Rate covenant requires Net Revenues \geq 1.0x Debt Service. *Achieving this may be challenging with operating deficits.*
- **Expendable Resources to Debt (FY15 Context):** An MBIA covenant in 2016 OS required ER \geq 50% of Debt. *Calculating recent ER/Debt is difficult without unrestricted net asset breakdown but is likely significantly stressed given high total debt + leases.*

Balance Sheet Usage

- **Liquidity (FY15):** Operating Cash was \$99.5M. Total Endowment & Similar Funds were \$586.5M. Against \$458.7M in debt then, liquidity appeared manageable but not exceptionally strong. *Recent liquidity needs confirmation but is likely constrained by high total obligations (debt + leases) relative to unrestricted resources.*
- **Leverage:** The University utilizes significant debt (and now large lease obligations) to finance its assets and operations, confirmed by the very high Debt/EBIDA ratio. This limits flexibility to absorb shocks or invest in new initiatives without further borrowing.
- **Endowment Reliance (FY15):** Low (~2.6% of OpEx). *Recent operating deficits might increase reliance on endowment draw, potentially impacting long-term value.*

3. Debt Structure and Bond Characteristics

Use of Proceeds (Series 2016)

- Primarily to refund portions of the Series 2005A, 2007A, and PHEC 2007 bonds.
 - To pay costs of issuance.
- (Source: OS Page 3)

Capitalized Interest (Series 2016 Context)

Not applicable to the Series 2016 bonds, as they were issued for refunding purposes, not

new construction requiring interest capitalization during a build phase. Capitalized interest is a standard feature for new money university bonds funding large capital projects.

Outstanding Bonds

(As previously listed: Series 2016, 2017, 2020A, 2020B)

Significant Factor: \$477M operating lease liability added recently (per Moody's).

Debt Service and Security

As previously listed: Pledge of Unrestricted Gross Revenues, GO of University, State Intercept.

Credit Rating Downgrades

- **Moody's:** Prior: A3 → **August 2023: Baa1** (Stable Outlook)
(Source: Notice of Rating Change, Aug 2023)
- **S&P:** A (Stable) at 2016 Issuance. *No recent actual S&P updates provided.*

4. Competitive Positioning and Market Environment

(As previously listed: Competitive market, enrollment pressures)

Macroeconomic Pressures

(As previously listed: Rising rates, inflation, program demand shifts)

5. Governance and Management

(As previously listed: Focus on stabilization, efficiency, addressing downgrade factors)

Risk Management and Future Outlook

- **High leverage confirmed by debt ratios** is the primary credit constraint, limiting flexibility.
- **Enrollment stabilization remains paramount.**
- **Stable outlook from Moody's** suggests expectations are currently anchored at the Baa1 level, but requires successful execution of management's plans to improve operating performance and manage debt affordability.

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