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Research Update:

University of Toronto Upgraded To 'AA+' From 'AA' Following Application Of Revised Criteria

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Overview

- We are raising our long-term issuer credit and senior unsecured debt ratings on the University of Toronto (UofT) to 'AA+' from 'AA' based on the application of our "Methodology: Not-For-Profit Public And Private Colleges And Universities" methodology, published Jan. 6, 2016.
- The ratings reflect our assessment of the university's stand-alone credit profile, which we have revised to 'aa+' from 'aa' based on the university's extremely strong enterprise profile and very strong financial profile.
- We are removing our Under Criteria Observation designation from the ratings.
- The stable outlook reflects our expectation that within our two-year outlook horizon, UofT will maintain an exceptional market position and student demand profile, its operating budgets will remain balanced, and its available resources will remain superior.

Rating Action

On March 8, 2016, Standard & Poor's Ratings Services raised its long-term issuer credit and senior unsecured debt ratings on the University of Toronto (UofT), in Ontario, to 'AA+' from 'AA'. The outlook is stable. At the same time, Standard & Poor's removed the ratings from Under Criteria Observation, where they had been placed Jan. 6.

The upgrade reflects our revised assessment of the university's stand-alone credit profile (SACP), which we have raised to 'aa+' from 'aa' based on the university's extremely strong enterprise profile and very strong financial profile, as determined under our "Methodology: Not-For-Profit Public And Private Colleges And Universities" criteria, published Jan. 6, 2016, on RatingsDirect.

Rationale

The ratings reflect the university's SACP which Standard & Poor's assesses at 'aa+'. The ratings also reflect our view that UofT's strong financial resilience and independence allow the ratings to exceed those on Ontario under our government-related entities (GRE) criteria.

Founded in 1827, UofT is Canada's largest university based on enrollment and has three campuses (St. George, Scarborough, and Mississauga) that together

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accounted for 87,639 students in fall 2015. 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 a strong international reputation for its research.

The SACP on UofT reflects our combined assessment of the university's extremely strong enterprise profile with a remarkable enrollment and demand profile and strong management and governance practices; and its very strong financial profile, with a history of solid financial performance, excellent levels of available resources, and a low debt burden. In our opinion, substantial postemployment liabilities, and the fiscal challenges facing the provincial government, which could affect operating grants, offset some of these strengths.

UofT's enterprise profile primarily benefits from excellent economic fundamentals given Ontario's very strong economy, and a healthy market position and demand. Its enrollment has steadily increased by an average of 3% per year in the past five years, reaching 77,130 full-time equivalents (FTEs) in fall 2015. Graduate students represent about 19% of total enrollment, a level comparable with other national research-intensive universities. We believe UofT's student quality is sound, as reflected by its historically stable retention and average entry grade rates of 91.7% and 85%, respectively, in fall 2015. First year selectivity (offers to applications) and six-year graduation rates remained strong and increased slightly over the past five years, to 75.1% and 73.7%, respectively.

UofT's adjusted operating margin was 8.3% in fiscal 2015, up from 3.7% a year earlier, primarily due to an increase in tuition revenues as result of higher enrolment, and strong investment revenues. At this level, it was above the fiscal 2014 median for U.S. public universities in the 'AA' category and superior to that of most rated Canadian peer institutions. We expect UofT's financial profile will remain very strong in the next two years by the university maintaining abundant financial resources (with available resources in excess of 35% of adjusted operating expenses) and positive adjusted net margins, despite the operating pressures it faces--primarily the tuition framework, potential for flat or even lower government grants, and increasing salaries and benefits expenditures. In our view, the university's debt burden is low for the current rating especially in light of the healthy level of available resources at the end of fiscal 2015, at 165.6% of total debt. With the university issuing no debt in the next two years, we expect that debt metrics will remain in line with current levels and well within the university's internally approved debt limits.

In accordance with our criteria for GREs, 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. Also supporting this view is that the province provides substantial operating grants, which account for about 25.6% of the university's total revenue, and it appoints 16 of 50 Governing Council members.

We rate UofT three notches above Ontario, the maximum differential allowed in accordance with our methodology for rating GREs that we believe depend on ongoing government support. The difference reflects our view of the university's substantial financial assets. We believe there is a measureable likelihood that UofT's financial resources would meet ongoing operational and debt service requirements should the government default and temporarily suspend payments to the university. In addition, the difference reflects UofT's ownership structure, in which the government is neither an owner nor shareholder. We consider the risk of extraordinary negative government intervention to be low, given the university's operational independence, important public policy role, and the government's hands-off approach to the sector. Although the Ontario government faces fiscal challenges and projects it will not return to fiscal balance until fiscal 2017-2018, we do not expect provincial operating grants for postsecondary education to diminish significantly, given this sector's vital public policy role.

Liquidity

UofT's liquidity is exceptional, in our opinion. Consolidated cash and investments totaled C$3.8 billion, up 13% from fiscal 2014. They represented 147.5% of 2015 adjusted operating expenditures, or 5.26x total debt. Unrestricted financial resources (internally restricted net assets and internally restricted endowments) stood at C$1.2 billion, up from C$1.1 billion in fiscal 2014. This equaled about 165.6% of debt and 46.4% of adjusted operating expenses. We believe these ratios will remain more than sufficient to finance all debt service requirements and provide a sufficient buffer to withstand any likely medium-term stress scenario. UfT has the largest endowment among Canadian universities, with a fair value of C$2.1 billion as of the end of April 2015. The endowment has significantly increased in the past 10 years, by about 32% since 2006.

Outlook

The stable outlook reflects Standard & Poor's expectations that, within our two-year outlook horizon, UofT will maintain an exceptional market position and student demand profile, its operating budgets will remain balanced, and its available resources will remain superior. At the same time, Standard & Poor's expects that the university's debt burden will decline modestly or be stable. The outlook also reflects Standard & Poor's expectation that UofT's relationship with the province will be stable.

Downside scenario

We could lower the ratings if adjusted net margins weakened to near balance or sustained deficits as a result of significant reduction in government grants or substantial pressure from rising pension deficits; available resources eroded to less than 35% of adjusted expenditures or less than 100% of debt outstanding; or the demand profile weakened such that a declining trend in applications and FTEs emerged. A negative rating action on Ontario will also result in a similar rating action on UofT, given that the university depends on ongoing support from Ontario, thereby preventing us from rating it more than three notches above the province under our GRE criteria. Moreover, negative government intervention from the province, or a significant reduction in UofT's resilience to an Ontario default scenario as our GRE criteria specify could cause us to lower the ratings, potentially to on par with or below that on Ontario, depending on the severity.

Upside scenario

We consider the possibility of a positive rating action during our two-year outlook horizon unlikely, given our three-notch cap above the rating on the supporting government.

Related Criteria And Research

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Methodology: Not-For-Profit Public And Private Colleges And Universities, Jan. 6, 2016

Ratings List

Upgraded

	To	From
University of Toronto		
Issuer Credit Rating	AA+/Stable/--	AA/Stable/--
Senior Unsecured	AA+	AA

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.