HIGHER EDUCATION SECTOR: TRENDS BEAR WATCHING

Credit pressures continue to exist in the higher education sector principally resulting from affordability concerns, increasing tuition discount rates, and demographic trends. On the one hand, the value of higher education persists as evidenced by higher lifetime income levels and lower unemployment rates as one ascends the educational ladder. However, over the last 30 years or so, tuition and fees at both public and private institutions have increased at rates greater than inflation while at the same time student loan debt burdens have increased sharply. In order to try and temper the effect of rising tuition prices, many institutions have been increasing their tuition discount rates, basically institutional financial aid given to students. As the chart below illustrates, the average freshman in 2014 was paying about half of the tuition and fee sticker price! This has put a tremendous amount of stress on many schools in generating net tuition growth, most often the largest driver of revenue.

Average Tuition Discount Rate by Student Category

In the Northeastern, Mid-Western, and even some Western states, the number of high school graduates has been declining and will likely continue on this trajectory for the foreseeable future given population shifts to warmer climates and areas of the county where the cost of living may be lower. The most acute pressure exists for the smaller, private institutions with low enrollment, lower financial resource levels, higher reliance on student charges for operating revenue, and lacking a clear strength or niche. Recent examples of the trouble faced by some of these schools include a missed debt service payment from Emmanuel College of Georgia in November of 2015.

*Preliminary estimate
Source: NACUBO Tuition Discounting Survey, 2003 to 2014


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and the almost-closure of Sweet Briar College of Virginia in March of 2015. Emmanuel College, a small school enrolling about 800 students in Franklin Springs, GA, failed to make a debt service payment in November of 2015. Sweet Briar College, a small, private women's school in Virginia, announced in March that the school would close that August due to financial challenges and enrollment declines. In June, a circuit court judge in Virginia approved a plan to keep the college open for another year, though its status beyond this is very much uncertain.

**Fall Enrollment Percentage Change by College Size**

In spite of these trends/forces, demand still remains strong for many institutions in the sector. Larger private universities are generally less reliant on net tuition revenue and may derive significant portions of their revenues from federal research grants, auxiliary enterprises (housing/dining/athletic facilities) and endowment spending. Financial resource levels relative to debt and operations, key rating factors that determine the credit quality of a university, have largely rebounded since the recession, especially at the highest rated private institutions. Strong demand and cost advantages at public schools, particularly for in-state students, offset concerns over tuition and fee increases, which arise from diminished state appropriations.

In 2016 and beyond we anticipate that smaller private schools located in the Northeast and Midwest will continue to face the toughest headwinds while many larger public and private institutions with strong market positions will be better able to weather the storm. At Standish we favor flagship public universities, along with private universities that possess strong academic programs, clear niche offerings such as in the STEM fields, strong financial resource levels, and diverse revenue streams.