S&P Global
Ratings

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Queen's University

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Queen's University

Rationale

Issuer Credit Rating
AA+/Stable/--

The ratings on Queen's University reflect the university's stand-alone credit profile (SACP), which S&P Global Ratings assesses at 'aa+' based on the university's extremely strong enterprise and very strong financial profiles. Queen's strong financial resilience and independence allow the ratings to exceed those on Ontario under our government-related entities (GRE) criteria.

We believe the university benefits from an extremely strong enterprise profile, characterized by its excellent market position, as well as solid student demand and enrollment. Queen's full-time equivalent students (FTEs) increased 3.4% to 23,640 in fall 2015, supported by growth in both graduate and undergraduate enrollment. In our opinion, student quality metrics continue to be strong and compare well with those of rated Canadian peers. This is primarily reflected by the university's historically high retention and average entry grade rates of 94.4% and 89.1%, respectively, in fall 2015. First-year selectivity (offers to applications) and six-year graduation rates remained superior to those of peers, at 44.9% and 84%, respectively. In our opinion, the university also benefits from strong management and governance practices, and excellent economic fundamentals given Ontario's very strong economy.

In our opinion, Queen's very strong financial profile is primarily supported by a history of adequate financial performance, excellent levels of available resources, and a moderate debt burden. The university's adjusted operating margin was 1.8% in fiscal 2015, which was in line with the fiscal 2014 median for U.S. public universities in the 'AA' category and somewhat below that of most rated Canadian peer institutions. In our view, the university's debt burden is moderate especially in light of the healthy level of available resources at the end of fiscal 2015, at 170.5% of total pro forma debt. As well, pro forma maximum annual debt service was modest, at 3.2% of 2015 adjusted operating expenditures. With the university issuing no debt in the near term, we expect that debt metrics will remain in line with current levels. We believe that Queen's operating pressures related to the tuition framework, potential for flat or even lower government grants, and increasing salaries and benefits expenditures, as well as its considerable postemployment liabilities and a significant deferred maintenance backlog somewhat offset its financial profile strengths.

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 view of the university's role as one of Canada's most reputable higher education institutions, and its significant research capacity. The province's oversight, program approval rights, and tuition regulation over Queen's suggest a strong link to it. Also supporting this view is that the province provides substantial operating grants, which account for a significant portion (close to 25%) of the university's total revenue.

We rate Queen's 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 Queen'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 Queen's ownership structure, in which the government is neither an owner nor shareholder. Moreover, none of its board of trustees' members is appointed by the province. 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 the province 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.

Established by Royal Charter in 1841, Queen's is a midsize, research-intense university in Kingston that offers a variety of undergraduate and graduate degrees across its six faculties (arts and science, education, engineering, health sciences, law, and business) and two schools (graduate studies and policy studies). The university provides leading-edge research in a variety of areas, including computational science and engineering, globalization studies, mental health, biomedical sciences, and energy systems. Queen's is a member of the U15, a group of leading research-intensive universities in Canada. In fiscal 2015, it received C$145 million in research-related grants and contracts, which have been fairly stable in the past several years.

Liquidity

In our opinion, Queen's liquidity is exceptional. At fiscal year-end 2015, consolidated cash and investments totaled C$1.3 billion, up about 17% from fiscal 2014. Total cash and investments represented 4.7x total pro forma debt. Unrestricted financial resources available for debt service stood at C$476.4 million, which was about 12% higher than the previous year's C$425.6 million. This equaled 59.5% of adjusted operating expenses, and covered 170.5% of pro forma debt. In our opinion, these ratios are strong and compare well with those of the university's peers.

Queen's endowment was C$919 million, up 15% from the previous year. It is the second-largest endowment among Ontario universities, after University of Toronto, and it almost doubled since 2009. The university has a conservative endowment draw, in our view, with a long-term payout target rate of 4% of the endowment's market value. In fiscal 2015, the endowment paid out C$30.5 million, or about 8% higher than the previous year's spending, reflecting a strong increase in total endowment value.

Outlook

The stable outlook reflects our expectation that, in the next two years, Queen's will maintain an exceptional market position and demand, positive adjusted net margins, and abundant financial resources. We expect its available resources to remain in excess of 35% of adjusted operating expenses and cash and investments to be over 3x total debt; and that provincial support to the university will not decline beyond our current estimates. The outlook also reflects our expectation that Queen's relationship with the province will be stable.

We could take a negative rating action if the university's student quality were to deteriorate due to an increase in selectivity ratio to more than 50%; or if financial performance were to deteriorate because of lower government grants or a material decline in enrollment, pushing net operating margins into deficits. A negative rating action on Ontario will also result in a similar rating action on Queen's, given that the university depends on ongoing support from the province, which prevents us from rating it more than three notches above Ontario under our GRE criteria. Moreover, negative government intervention from the province, or a significant reduction in Queen'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 those on Ontario, depending on the severity.

A positive rating action during our two-year outlook horizon is unlikely, given mostly the university's significant operating pressures and reliance on provincial grants, which can be unilaterally altered, with a higher risk of cuts in times of provincial budget stress.

Government-Related Entities Methodology: Moderately High Likelihood Of Extraordinary Provincial Government Support

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 view of the university's role as one of Canada's most reputable higher education institutions, and its significant 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 a significant portion (close to 25%) of the university's total revenue.

We rate Queen's 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 Queen'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 Queen's ownership structure, in which the government is neither an owner nor shareholder. Furthermore, none of its board of trustees members is appointed by the province. 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.

Although we believe that the province's overall support for universities will remain good, Ontario has imposed some savings targets on the universities. Moreover, in March 2013, the province announced changes to the tuition framework, reducing the cap on annual increases to an average of 3% for undergraduate programs and 5% for professional and graduate programs over the next four years (from a maximum annual average of 5% institution-wide). As well, the government is undertaking a formula funding review in fiscal 2015-2016, which focuses on student outcomes and institutional differentiation. The SACP on Queen's incorporates the ongoing support from Ontario, and we believe that the province's budgetary constraints and limiting of tuition increases will not materially affect the SACP within the two-year outlook horizon.

Enterprise Profile

Industry risk

Industry risk addresses the higher education sector's overall cyclicality and competitive risk and growth by applying various stress scenarios and evaluating barriers to entry, levels and trends of profitability, substitution risk, and growth trends observed in the industry. We believe the higher education sector represents a low credit risk compared with other industries and sectors.

Economic fundamentals

Queen's students predominantly come from Ontario (68.1% in fall 2015). This level has slowly decreased in the past five years, while international student intake and the share of students coming from the rest of Canada continued to grow.

In our view, Ontario's real GDP per capita, which in 2014 was US$46,500, anchors our assessment of the university's economic fundamentals. The province's population was about 13.8 million in 2015, with good income indicators and some moderate employment and population growth projected.

Market position and demand

In our opinion, Queen's benefits from strong enrollment demand and exceptional student quality, which support its competitive position. It had 23,640 FTEs in fall 2015, up 3.4% from the previous year and 12.2% since fall 2011. This partially reflected graduate expansion efforts, which the university undertook alongside other Ontario universities following the province's promise to fund more graduate spaces. Queen's graduate students accounted for about 18.2% of total enrollment. Management expects applications for fall 2016 to remain strong.

Queen's is a highly selective university with exceptional student quality. The university's first-year students had a high average entry grade of 89.1% for fall 2015. In fall 2015, its first-year undergraduate offer rate (the ratio of offers to applicants) was the lowest of its peers, at 45%, while its matriculation rate was 41%. The fall 2015, six-year graduation rate was what we view as high, at 84%, as was its first year retention rate of 94%.

Management and governance

Three bodies including the board of trustees, the senate, and the university council, are responsible for governing Queen's. The university secretariat administers all three.

The board is responsible for overseeing financial matters, administering property, appointing vice-principals, and appointing the principal. It functions through a standing committee structure and is formed of 25 members: three ex officio and 22 elected, none of them appointed by the province. The senate exercises general control and supervision over academic affairs. The council serves as both an advisory and ambassadorial body to the university as a whole and is responsible for the chancellor's election.

We expect the senior management team to be stable in the next two years. The university prepares externally audited financial statements, which have been unqualified, and operating and capital budget documents are robust and transparent. It approves annually three-year plans for its operating budget and has a number of transparent financial policies in place, including investment and debt policies.

Queen's has a five year strategic plan that guides its long-term strategies based on its mission. Plan performance is reviewed annually and progress is tracked against specific activity indicators and identified risks are also monitored. The university prepares operating budgets and interim reports comparing its actual results to plans. It has an enterprise risk framework that guides its identification and management of risks. Management breadth and expertise are good, in our opinion.

Financial Profile

Financial management policies

Our analysis of financial policies includes a review of Queen's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure and a comparison of these policies with those of peers. Overall, we view Queen's transparency and disclosure to be good, with policies and procedures in place to adequately mitigate risks. The university conducts its activities according to a three-year operating budget that is aligned with its strategic plan and contains what we view as reasonable assumptions. Queen's prepares externally audited financial statements, which have been unqualified, and it has formal policies in place, including investment and debt policies.

Financial results

In our view, Queen's financial performance remained good in fiscal 2015. Its operating margin was 1.8% of adjusted operating expenses, above the 1.4% recorded in the previous year, primarily due to an increase in tuition revenues as result of higher enrolment levels, and strong investment revenues. At the same time, adjusted operating expenditures grew at a smaller pace (by 0.7% versus 2.4% in 2014) on what we view as effective budgeting and cost controls. Queen's fiscal 2015 margin is in line with the fiscal 2014 median for U.S. public universities in the 'AA' category and somewhat below that of most rated Canadian peer institutions. Like those of its Canadian peers, Queen's salaries and benefits expenditures are a significant strain, typically accounting for about 55% of its total reported expenditures.

The university expects a C$1.8 million operating fund surplus in fiscal 2016, well above the C$11.7 million budgeted operating deficit. This was primarily the result of higher student fees due to above-target enrollment, which together with higher government grants and lower utilities costs, more than offset a weak investment income and increased faculties and schools allocations. Its core operating budget typically accounts for 60%-65% of its total expenditures (its other expenditures relate to ancillary, research, consolidated entities, capital, and trust). The university expects to continue to balance its operating budget for fiscal years 2017-2019, primarily after drawing down on unit carryforward balances. It estimates that the drawdown portion on its central cash reserves will end in fiscal 2017. Although the university does not prepare consolidated forecasts, we expect that, including ancillary operations which tend to generate positive cash flow, the university will maintain consolidated surpluses in the next two years.

Queen's dependence on student-generated revenues grew steadily in the past several years and represented 33% of 2015 adjusted operating revenues. This was in line with that of other Canadian and 'AA' rated U.S. public universities. Similar to Canadian peers, it has somewhat limited flexibility to increase these revenues. Ontario monitors and guides tuition rates and student aid (through the tuition framework), and enrollment expansion (through operating grants). However, universities have the final decision on these matters and on their long-term strategies. The current tuition framework reduces the cap on annual increases to an average of 3% for undergraduate programs and 5% for professional and graduate programs until fiscal 2017 (from a maximum annual average of 5% institutionwide under the previous framework). Universities have some flexibility on how they increase tuition among programs as long as the total increase entitywide is below the cap. The province has also made some changes that have affected the entire university sector, including reduced base operating grants and reduced grants based on enrollment of full-time international students and new requirements to meet efficiency targets.

Financial resources

Unrestricted financial resources available for debt service stood at C$476.4 million, which was about 12% higher than the previous year's total of C$425.6 million. This equaled 59.5% of adjusted operating expenses, and covered 170.5% of pro forma debt. In our opinion, these ratios are strong and compare well with those of Queen's peers. At fiscal year-end 2015, consolidated cash and investments totaled C$1.3 billion, up about 17% from fiscal 2014. Total cash and investments represented 162.8% of adjusted operating expenditures, or about 4.7x total debt. The university has a policy of maintaining minimal cash balances with single counterparties.

Queen's endowment was C$919 million in fiscal 2015, up 15% from the previous year. It is the second-largest endowment among Ontario universities, after University of Toronto, and has almost doubled since 2009. The university has a conservative endowment draw, in our view, with an annual spending rate targeted at about 4% of the endowment's market value. In fiscal 2015, the endowment paid out C$30.5 million, or about 8% higher than the previous year's spending, reflecting a strong increase in total endowment value.

Queen's manages its pooled endowment fund, pooled investment funds, and sinking funds with different mandates. It manages its pooled investment funds with a slightly more conservative mandate and limits them to Canadian equities, global equities, and fixed income. The funds have a short-term horizon. The pooled investment fund's annual returns (net of fees) were 0.2% in as of March 31, 2016, down from 10.0% in fiscal 2015 due to weak market conditions. Queen's manages the pooled endowment fund with a long-term horizon, and it has some illiquid assets. The endowment fund asset allocation, at March 31, 2016, was 56.3% Canadian and international equities, 33.5% fixed income and absolute return, and 9.4% real assets. The endowment fund's annual return was 1.8%, down from 12.0% the fiscal 2015. The university has an investment committee that determines the strategy for the pooled endowment and investment funds, as well as short-term investments and sinking funds.

We believe Queen's has a strong fundraising capacity. In fiscal 2016, the university has finalized its 10-year fundraising campaign, which reached C$548.8 million, exceeding its C$500 million goal. During the campaign, it received a C$50 million donation for its school of business from Stephen J.R. Smith, a Queen's alumnus.

Debt and contingent liabilities

As of fiscal 2015, Queen's pro forma debt outstanding was C$279.4 million, including the university's additional C$60 million drawdown under its bank loan in fiscal years 2015 and 2016. Total debt includes three fixed-rate bullet bonds (one due in 2032 and two in 2040, representing 77% of total debt), an amortizing bank loan to pay for two new residences (maturing in 2030), and a small mortgage. As of March 31, 2016, the university held C$73.5 million in sinking funds to repay its three bullet debentures outstanding. We do not net sinking funds from debt; rather, we include the sinking funds in our measure of internally restricted net assets.

Queen's estimated pro forma maximum annual debt service is about C$25 million, or 3.1% of its adjusted fiscal 2015 expenses. We view this as a moderate debt burden for the current rating especially in light of the healthy level of available resources at the end of fiscal 2015, at 170.5% of total debt. Although Queen's contemplates new capital projects and deals with a significant deferred maintenance backlog of C$253.6 million in fiscal 2015, it does not expect to fund them with additional debt issuance; therefore, we expect that the university's debt metrics will remain in line with current levels in the next two years. To address its deferred maintenance spending, Queen's will allocate C$7.1 million per year from its operating budget until fiscal 2018. In addition, the university's portion of provincial funding for fiscal years 2016 and 2017 grew to C$1.6 million from C$1.1 million. As well, it expects to receive an additional C$1.8 million in fiscal 2017, in light of Ontario's commitment to supplement its facility renewal funding across the system from fiscal years 2016-2020.

Queen's maintains a defined contribution pension plan with a defined-benefit component that provides a minimum level of benefits, which is in a deficit position and requires ongoing deficit payments, putting some pressure on the university's cash flows. As of August 2014, Queen's estimated its going-concern pension deficit to be C$53 million on a market basis and C$175 million on a smoothed basis, and projected a solvency deficit of C$285 million. Based on these valuations, the university's annual going-concern deficit payments rose to C$20.7 million starting with fiscal 2016 (up from C$14.4 million as of its last actuarial valuation in 2011). In fiscal 2015, Queen's qualified for temporary solvency funding relief program, under which it has elected to defer solvency deficit payments for another three years, to Sept. 1, 2018. We expect greater clarity around the amount and timing of the solvency pension deficit payments after the university formalizes its valuation as of August 2017 (it currently estimates them at about C$19 million after fiscal 2019). As part of the valuation process, Queen's will be required to submit a plan for funding its deficits.

The university took several initiatives to manage its pension deficit, including increased employee contributions. Moreover, Queen's budgets an additional 4.5% employer contribution increase to cover the increased going-concern payments effective September 2015 and to create a reserve for pension solvency. Queen's is exploring other options for its pension plan, which could include merging the Queen's pension plan with a new jointly sponsored pension plan (JSPP) for Ontario universities. A move to a JSPP, which would not be subject to solvency payment regimes, could help improve Queen's cash flows. It would not eliminate the university's going-concern obligations.

Queen's has moderate contingent liabilities that relate primarily to other postemployment benefits. Its 2015 other benefit's plan liabilities totaled C$74.7 million. Other contingent liabilities include potential litigation payouts, which the university believes would be immaterial, and a small liability for the decommissioning of a joint subatomic physics laboratory.

Queen's University -- Financial Statistics

	--Fiscal year ended April 30--					Medians for 'AA' U.S. public colleges & universities, 2014**
	2016	**2015**	**2014**	**2013**	**2012**	
Enrollment and demand						
Headcount	24,853	24,027	23,018	22,465	22,226	34,431
Full-time equivalent	23,640	22,869	21,899	21,412	21,062	32,265
First year acceptance rate (%)	44.9	43.5	41.8	41.2	41.7	68.6

Queen's University -- Financial Statistics (cont.)

	--Fiscal year ended April 30--					Medians for 'AA' U.S. public colleges & universities, 2014**
	2016	2015	2014	2013	2012	
First year matriculation rate (%)	40.5	41.4	40.7	42.6	43.8	MNR
Undergraduates as a % of total enrollment (%)	77.7	77.8	77.5	77.3	77.6	77.7
First year retention (%)	94.4	94.9	94.6	94.4	94.0	85.0
Graduation rates (six years) (%)*	84.0	85.3	86.0	84.1	86.6	55.4
Income statement						
Adjusted operating revenue (C$000s)	N.A.	814,859	806,128	782,858	762,227	MNR
Adjusted operating expense (C$000s)	N.A.	800,502	795,193	776,298	761,692	MNR
Net adjusted operating income (C$000s)	N.A.	14,357	10,935	6,560	535	MNR
Net adjusted operating margin (%)	N.A.	1.8	1.4	0.8	0.1	1.8
Provincial grants to revenue (%)§	N.A.	32.5	33.2	32.8	31.1	21.4
Student dependence (%)	N.A.	33.0	30.3	29.8	28.1	32.4
Investment income dependence (%)	N.A.	9.0	8.1	7.9	3.6	2.4
Debt						
Debt outstanding (C$000s)	N.A.	241,354	224,683	221,074	227,266	689,891
Pro-forma debt	N.A.	279,400	224,683	221,074	227,266	
Current debt service burden (%)	N.A.	2.03	2.38	2.39	2.44	3.30
Current MADS burden (%)	N.A.	2.97	3.28	3.31	3.38	3.50
Pro-forms MADS burden (%)	N.A.	3.23	3.28	3.36	3.38	
Financial resource ratios						
Endowment market value (C$000s)	N.A.	918,978	800,238	710,251	616,797	631,508
Cash and investments (C$000s)	N.A.	1,303,432	1,116,892	977,887	880,893	MNR
Adjusted UFR (C$000s)	N.A.	476,364	425,569	375,928	331,177	MNR
Cash and investments to operations (%)	N.A.	162.8	140.5	126.0	115.6	63.5
Cash and investments to debt (%)	N.A.	540.0	497.1	442.3	387.6	163.0
Cash and investments to pro-forma debt (%)	N.A.	466.5	497.1	442.3	387.6	
Adjusted UFR to operations (%)	N.A.	59.5	53.5	48.4	43.5	36.1
Adjusted UFR to debt (%)	N.A.	197.4	189.4	170.0	145.7	102.1
Adjusted UFR to pro-forma debt (%)	N.A.	170.5	189.4	170.0	145.7	
Average age of plant (years)	N.A.	13.0	12.2	10.4	9.7	12.2

Queen's University -- Financial Statistics (cont.)						
	--Fiscal year ended April 30--					Medians for 'AA' U.S. public colleges & universities, 2014**
	2016	**2015**	**2014**	**2013**	**2012**	
OPEB liability to total liabilities (%)	N.A.	7.9	7.8	6.9	7.2	5.4

*Median figure is five-year graduation rate. §Median figure is state appropriations to revenue. **U.S. median figures are in U.S. dollars. N.A.--Not available. MNR--Median not reported. MADS--Maximum annual debt service. UFR--Unrestricted financial resources. Average age of plant = accumulated depreciation/depreciation and amortization expense.

Related Criteria And Research

Related Criteria

- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Methodology: Not-For-Profit Public And Private Colleges And Universities, Jan. 6, 2016
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Ratings Detail (As Of June 6, 2016)	
Queen's University	
Issuer Credit Rating	AA+/Stable/--
Senior Unsecured	AA+
Issuer Credit Ratings History	
14-Dec-2012	AA+/Stable/--
05-Aug-2010	AA+/Negative/--
01-Nov-2002	AA+/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.