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Ratings

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Middlebury College, Vermont; Private Coll/Univ - General Obligation

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Long Term Rating	AA/Stable	Affirmed
Vermont Ed & Hlth Bldg Fin Agy (Middlebury College)		
Long Term Rating	AA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'AA' long-term rating on Vermont Educational And Health Buildings Financing Agency's outstanding bonds, issued for Middlebury College (Middlebury).
- The outlook is stable.

Security

As of June 30, 2023, Middlebury had approximately $322.7 million in debt outstanding. Upon including a debt issuance in August 2023, the college's debt increased to $366.8 million (described as pro forma debt in our analysis). This includes $213.3 million in public debt outstanding, $105.3 million in directly placed debt, $45.9 million in a finance lease, and $2.3 million in operating leases. All outstanding debt is fixed rate and a general obligation of Middlebury. Pro forma maximum annual debt service (MADS; smoothed for a bullet payment in fiscal 2047) was manageable, in our view, at $19.6 million, equal to 4.9% of fiscal 2023 operating expenses. We understand that the college may issue a small amount of additional debt in the near term. We will evaluate the full effect of this on the college's credit profile when details become available.

Credit overview

We assessed Middlebury's enterprise risk profile as extremely strong, with excellent demand and student quality at the undergraduate level, a broad geographic recruitment reach, multiple campuses, diverse programs, and fundraising success. We assessed Middlebury's financial risk profile as strong, with a sizable endowment and an average debt burden consistent with the rating category. These strengths are somewhat offset by the trend of operating deficits on a full-accrual basis, although we understand that the management team continues to focus on improving operating results in the near term. We believe that these credit factors, combined, lead to an anchor of 'aa-'. In our opinion, the 'AA' rating on the college's bonds better reflects Middlebury's stronger market position relative to lower rated peers.

The 'AA' rating reflects our assessment of Middlebury's:

- Sizable endowment, with a balance of $1.47 billion as of June 30, 2023;
- Solid reputation with excellent student demand and quality;

- Fundraising success, with contributions running strong for its ongoing comprehensive campaign; and
- Programmatic diversity, with a liberal arts college in Vermont, niche foreign language programs in the U.S. and abroad, and graduate programs in Monterey, Calif.

In our opinion, offsetting credit factors include the college's:

- Trend of full-accrual operating deficits, with recent deficits driven by pressures at its graduate institute;
- Slight deterioration in financial resource ratios relative to debt in recent years and the potential for modest additional debt; and
- Acceleration risk associated with its direct placement debt portfolio, although we view the risk as manageable compared to the college's liquidity levels.

Middlebury College, founded in 1800, is in Middlebury, Vt. It enrolled 2,785 undergraduate students on a full-time equivalent (FTE) basis in fall 2023 and is primarily a residential undergraduate liberal arts college. The campus consists of approximately 350 acres and more than 160 buildings. The Middlebury Institute of International Studies (MIIS) at Monterey, Calif., enrolls about 449 graduate FTE students, and Middlebury's summer programs, including the foreign language programs and the Bread Loaf School of English, enroll about 1,500 students annually, while the Middlebury C.V. Starr Schools abroad enroll about 650 students annually. In addition to its traditional undergraduate academic year program, the institution operates several popular summer-session programs at its main campus in Middlebury, Vt.; the Bread Loaf Campus in Ripton, Vt.; and other sites both domestically and abroad. Middlebury's niches are the foreign language programs, environmental studies, and a liberal arts curriculum.

Environment, social, and governance

We analyzed Middlebury's environmental, social, and governance credit factors related to its market position and financial performance. We view all environmental, social, and governance credit factors as neutral in our credit rating analysis.

Outlook

The stable outlook reflects our expectation that Middlebury will sustain its solid demand position, preserve its operating performance, and maintain the strength of its balance sheet. While the college may note some enrollment declines at the undergraduate level in the near term, we understand this is a strategic decision and not a reflection of its fundamental demand.

Downside scenario

We could consider a negative rating action if operating performance weakens and results in larger operating deficits, if financial resources decline, or if the college issues additional debt without commensurate growth in resource levels.

Upside scenario

We could consider a positive rating action if Middlebury reports full-accrual surpluses on a consistent basis and its financial resource ratios improve to a level comparable to higher-rated peer institutions while maintaining its demand position.

Credit Opinion

Enterprise Risk Profile – Extremely Strong

Market position and demand

Middlebury has an excellent demand profile, with a broad geographic draw (only 4% of the students came from Vermont in fall 2023), highly selective admissions, robust matriculation, and overall stable enrollment, especially at the undergraduate level. Enrollment at the college noted some fluctuation during the height of the pandemic, with a larger class enrolling in fall 2021 due to a lot of deferrals from fall 2020 (which had a higher acceptance rate as a precautionary measure at the start of the pandemic), pent-up demand, and Vermont's successful controls during the pandemic. Middlebury reported enrollment declines in fall 2022 and fall 2023 as management works to bring down the number of undergraduates to right-size the enrollment. We understand that the college expects to bring the undergraduate enrollment closer to the 2,600 student-level in the next couple of years, compared to 2,785 undergraduate students enrolled in fall 2023. The declines in the last two years have also been exacerbated by enrollment pressures at MIIS, with FTE enrollment down to 449 students in fall 2023 from 640 students in fall 2021. We understand that management has detailed plans to reverse these declines and improve the financial performance at MIIS during the next three years.

Middlebury competes with other top-tier liberal arts schools in the U.S.; its primary competitors are Amherst College, Bowdoin College, Carleton College, Pomona College, and Williams College, according to management. Given the national competition for the same high-quality students Middlebury strives to enroll, we consider the 45% matriculation rate for fall 2023 robust. Student retention matches that of the leading schools in the U.S., with a freshman-to-sophomore retention rate of 95%, which we consider strong. The college has a need-blind admissions policy and enrolls about 50% of its freshman class through the early-decision process.

Management and governance

After nearly a decade, Middlebury's president is expected to leave the organization at the end of 2024 with an ongoing national search for the next president. We understand that the college expects to have an internal interim president in place for six months and to appoint a permanent replacement by July 2025. At this time, we expect a smooth leadership transition and view the management team's depth and expertise as solid.

Middlebury rolled out its new comprehensive strategic plan in January 2018. During the past few years, Middlebury also followed an operating plan aimed at enhancing revenues and holding expenses to achieve GAAP operating surpluses. While management showed progress toward this goal and initially expected to achieve breakeven operations by fiscal 2021, the timeline was delayed due to the additional expenses and revenue shortfall associated with the pandemic. Management expects that the college is likely a few years away from achieving this goal.

Financial Risk Profile – Strong

Financial performance

Middlebury has reported a trend of posting operating deficits for over a decade. Although this trend continued in the past year, we understand that the deficit was limited to the college's graduate operations, with the remaining component of its operations improving to at least breakeven levels. Operations generated an $8.2 million deficit (negative 2.1% margin) in fiscal 2023, a $4.6 million deficit (negative 1.2% margin) in fiscal 2022, and a $12.0 million deficit (negative 3.6% margin) in fiscal 2021. These results were supported by $0.8 million in federal relief funds associated with the pandemic in fiscal 2023 and $4.1 million in fiscal 2022. We understand that the management team expects a slight improvement in financial performance in fiscal 2024 followed by further improvements during the next 3-4 years to breakeven levels driven by the team's plan to improve the demand and financial performance at MIIS. We continue to view the college's operating performance as weaker than most peer institutions and would view the move closer to breakeven levels as a positive.

As Middlebury maintains a need-blind admissions policy, its discount rate varies based on student need. The fiscal 2023 tuition discount rate was 42.1%, comparable to the 41.4% in fiscal 2022. The rate is overstated compared to certain peer institutions, though, as it includes the total scholarships provided by the college against just the net tuition revenue (according to management), and not the full comprehensive fee revenue. We consider Middlebury's tuition discount rate as manageable despite its need-blind admission policy. For fall 2023, comprehensive fees totaled $83,880, a 4.5% increase from the prior year. Middlebury's revenue diversity is typical for an undergraduate liberal arts college of its caliber; student revenue generated 68.4% of fiscal 2023 total revenue while investment and endowment income accounted for 16.4% of revenue.

Financial resources

Following a steep increase in fiscal 2021 due to exceptional market performance, financial resources have weakened slightly in the last two fiscal years. Cash and investments totaled $1.49 billion as of fiscal 2023, or 375% of operations and 407% of pro forma debt. Middlebury uses an outside investment manager (Investure LLC) to serve as the external investment office. As of June 30, 2024, the $1.55 billion endowment comprised 25.4% in public equity, 19.2% in venture funds, 18.7% in private equity, 15.2% in hedge funds, 8.2% in real assets, and the remaining assets comprised credit, fixed income, non-marketable assets and cash. Unfunded commitments to private partnerships were approximately $389 million, which we consider relatively high but still manageable at 25% of total investments as on June 30, 2024.

Middlebury has a strong history of fundraising and an active alumni base; we consider these credit strengths. The college has an ongoing $600 million comprehensive campaign that is expected to end in 2028, having raised about $465 million. The alumni participation rate continues to be strong, in our view, at about 33% in 2023.

Debt and contingent liabilities

Middlebury currently has three outstanding series of directly placed debt (series 2016, series 2021 and series 2022), totaling an approximate balance of $105.3 million. We have reviewed the associated loan agreements and believe there are cross-default provisions associated with the debt. However, we view the likelihood of triggering default to be remote. In addition, given approximately $205 million in the college's investments were liquid daily as of June 30, 2024, we believe there is sufficient coverage to address this contingent liability.

Middlebury College, Vermont--enterprise and financial statistics

	--Fiscal year ended June 30--					Medians for 'AA' category rated private colleges & universities
	2024	2023	2022	2021	2020	2023
Enrollment and demand						
Full-time-equivalent enrollment	3,234	3,338	3,443	3,195	3,220	7,994
Undergraduates as a % of total enrollment	86.1	82.6	82.6	80.2	79.6	70.5
First-year acceptance rate (%)	10.4	12.7	13.5	22.0	15.4	14.4
First-year matriculation rate (%)	44.6	38.9	42.5	29.8	40.4	38.4
First-year retention rate (%)	95.0	95.0	95.0	95.0	94.0	95.0
Six-year graduation rate (%)	93.0	94.0	91.0	93.0	93.0	91.1
Income statement						
Adjusted operating revenue ($000s)	N.A.	389,724	373,569	321,157	339,941	MNR
Adjusted operating expense ($000s)	N.A.	397,925	378,120	333,118	351,587	MNR
Net operating margin (%)	N.A.	(2.1)	(1.2)	(3.6)	(3.3)	2.4
Change in unrestricted net assets ($000s)	N.A.	(10,293)	(16,251)	45,088	(26,413)	MNR
Tuition discount (%)	N.A.	42.1	41.4	40.9	38.2	39.3
Student dependence (%)	N.A.	68.4	69.3	66.8	68.2	60.8
Debt						
Outstanding debt ($000s)	N.A.	322,748	310,137	265,505	246,385	612,704
Proposed debt ($000s)	N.A.	44,060	N.A.	N.A.	N.A.	MNR
Total pro forma debt ($000s)	N.A.	366,808	N.A.	N.A.	N.A.	MNR
Current debt service burden (%)	N.A.	5.8	5.2	4.5	4.4	MNR
Current MADS burden (%)	N.A.	4.4	4.9	4.5	4.2	4.9
Pro forma MADS burden (%)	N.A.	4.9	N.A.	N.A.	N.A.	MNR
Average age of plant (years)	N.A.	23.8	23.1	22.7	23.6	14.7
Financial resource ratios						
Endowment market value ($000s)	N.A.	1,468,868	1,467,208	1,511,001	1,133,644	2,219,768
Cash and investments ($000s)	N.A.	1,492,252	1,510,252	1,555,453	1,151,370	2,821,640
Cash and investments to operations (%)	N.A.	375.0	399.4	466.9	327.5	373.7
Cash and investments to debt (%)	N.A.	462.4	487.0	585.8	467.3	472.3
Cash and investments to pro forma debt (%)	N.A.	406.8	N.A.	N.A.	N.A.	MNR

Total adjusted operating revenue = unrestricted revenue less realized and unrealized gains/losses and financial aid. Total adjusted operating expense = unrestricted expense plus financial aid expense. Net operating margin = 100*(net adjusted operating income/adjusted operating expense). Student dependence = 100*(gross tuition revenue + auxiliary revenue) / adjusted operating revenue. Current MADS burden = 100*(maximum annual debt service expense/adjusted operating expenses). Cash and investments = cash + short-term and long-term investments. Average age of plant = accumulated depreciation/depreciation and amortization expense. N.A.--Not available. MNR--Median not reported. MADS--Maximum annual debt service.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022