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CREDIT OPINION
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University of Washington, WA

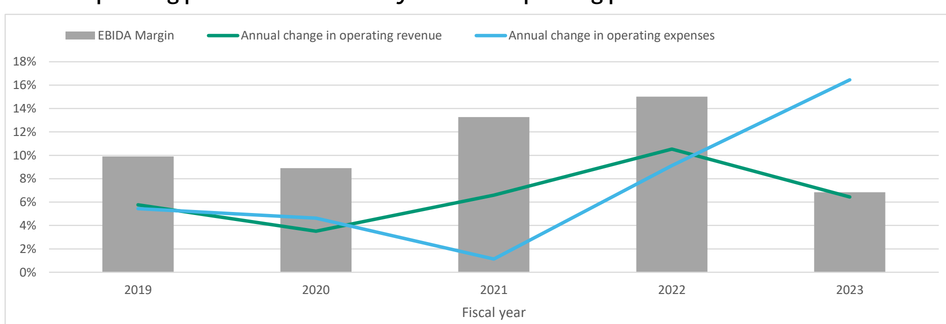
Update following revision to negative outlook

Summary

The University of Washington's exceptional credit quality (Aaa negative) incorporates the synergies and strengths of its large-scale research, healthcare, and educational operations that support its excellent brand and strategic positioning. As the state's flagship university with a comprehensive array of programs, the university benefits from strong student demand. A prominent research profile enhanced by its sizable academic medical center bolster UW's market position. Overall wealth levels are considerable and growing, supported by strong fundraising, but lag Aaa-rated peers when measured against the university's growing scale. UW's governance and management are strong, including integrated planning and very active oversight. The university's primary credit challenge continues to be its exposure to the volatility and thin margins of its healthcare enterprise. In addition, spending pressures at the university are leading to weaker overall operating performance. Relatively high leverage, including a large pension liability, is another offsetting credit consideration.

On January 26, 2024, the outlook was revised to negative from stable.

Exhibit 1
Thinner operating performance driven by increased spending pressure



Source: Moody's Investors Service

Credit strengths

» Sizable scale with a national research profile, strong student demand and major clinical care operations contribute to significant credit strength

» Very strong overall wealth, with $8.5 billion of total cash and investments, enhances financial flexibility

- Consistently robust fundraising, with three year average gifts of $375 million through fiscal 2023, provides funds for academic and capital investment, bolstering excellent strategic position
- Integrated planning and strong fiscal oversight enhance prospects for strengthened operations

Credit challenges

- Exposure to the weakening performance of the healthcare enterprise along with the university's own expense pressures has resulted in a thin operating performance
- Wealth compared to size of operations and monthly liquidity is lower than peers
- Large unfunded pension liability adds to leverage
- Limited tuition pricing flexibility due to state caps on resident undergraduate tuition increases

Rating outlook

The negative outlook incorporates the thinning operating performance and challenges to returning to more robust margins given expense pressures and ongoing weak margins of UW Medicine. In addition, the outlook incorporates the relatively narrow liquidity and wealth compared to the size of its operations.

Factors that could lead to an upgrade

- Not applicable

Factors that could lead to a downgrade

- Further deterioration in healthcare entities' operating performance
- EBIDA margins sustained below 10% given already thinner than peers balance sheet reserves relative to operations and debt
- Material debt plans beyond those outlined or reduction in wealth/liquidity relative to debt and expenses
- For the short term rating, reduction in same day liquidity, increased calls on liquidity, or weakening of debt and treasury management

Key indicators

Exhibit 2
University of Washington, WA

	2019	2020	2021	2022	2023	Median: Aaa Rated Public Universities
Total FTE Enrollment	59,660	60,829	60,359	60,422	60,494	60,644
Operating Revenue ($000)	6,195,024	6,412,529	6,835,587	7,555,487	8,041,838	6,049,826
Annual Change in Operating Revenue (%)	5.8	3.5	6.6	10.5	6.4	10.2
Total Cash & Investments ($000)	6,122,921	6,723,076	8,275,094	8,349,287	8,535,846	11,626,270
Total Adjusted Debt ($000)	6,806,401	7,146,355	7,855,991	8,593,178	8,037,873	5,506,673
Total Cash & Investments to Total Adjusted Debt (x)	0.9	0.9	1.1	1.0	1.1	2.8
Total Cash & Investments to Operating Expenses (x)	1.0	1.1	1.3	1.2	1.1	2.2
Monthly Days Cash on Hand (x)	159	173	214	197	171	230
EBIDA Margin (%)	9.9	8.9	13.3	15.1	6.8	14.2
Total Debt to EBIDA (x)	3.9	4.2	2.6	2.9	6.1	3.2
Annual Debt Service Coverage (x)	3.6	3.0	5.1	5.7	2.5	5.6

Source: Moody's Investors Service

Profile

Founded in 1861, the University of Washington is the State of Washington's flagship university with fall 2023 full time equivalent students (FTEs) of 60,494 on its campuses in Seattle, Tacoma and Bothell. UW's operations are sizable with $8.0 billion of operating revenue in fiscal 2023. UW is also one of the nation's largest research universities with $1.9 billion of research awards for fiscal 2023.

UW operates UW Medicine, whose service area is broad as the only academic medical center and Level 1 trauma care provider for Washington, Wyoming, Alaska, Montana and Idaho (WWAMI). The university's consolidated operations incorporate the UW Medicine's Select Units operations comprising primarily the 810-bed University of Washington Medical Center (UWMC) and other smaller entities. The UWMC includes a second campus consisting of Northwest Hospital (NWH). (NWH joined UW Medicine 2010 and became consolidated under one license with UWMC in January 2020). UW Medicine's Harborview Medical Center, owned by King County and managed by the university, is not included in university results and Valley Medical Center, a public hospital district, with whom UW Medicine participates in a strategic alliance agreement, is reported as a component unit outside the consolidated results. In fiscal 2022 the Fred Hutchinson Cancer Center (FHCC) (A2/stable) entered into a new comprehensive clinical affiliation with UWMC which now governs all of the adult cancer related clinical activities of both organizations. As a result, the FHCC is now reported as a component unit outside consolidated results.

Detailed credit considerations

Market profile

The University of Washington will maintain its excellent brand and strategic positioning anchored by its large, national research enterprises and strong student demand as the state's flagship university. With the scale, diversity, and reputation of its research program including most prominently its medical complex, UW will continue to succeed in an increasingly competitive research environment. Awards that reached $1.9 billion in fiscal 2023 are projected to rise more slowly over the next several years given expectations that federal funds will not rise significantly. The university has well-developed contingency plans to address any federal funding reduction.

Student demand remains favorable, based on UW's academic reputation and diversified programs, with graduate and professional students representing about one-third of total university enrollment. Enrollment in FTEs--around 60,000--and tuition revenue growth has remained moderate and will continue to be driven by non-resident graduates and STEM programs. International students are around 11% of undergraduates and 24% of graduates and professionals. In fall 2023, enrollment grew by 1.2% at the main Seattle campus and Bothell grew by 1% while Tacoma declined by 0.5% following greater declines in the latter two campuses in the prior year. The state retains tuition setting authority for resident undergraduate tuition, which rose by 3.0% in fall 2023.

Operating performance

UW’s operating performance will continue to experience some volatility due to challenging healthcare operations as well as expense pressures at the university. Moody's projects that fiscal 2024 results will be constrained, following a weaker EBIDA result of 6.8% in fiscal 2023, as revenues and expenses are expected by the university to rise at around the same rate. A significantly thinner fiscal 2023 result, well below the stronger EBIDA of 15% fiscal 2022, was due to expense increases of 16.5% which well outpaced revenue growth of 6.4%. Higher expense growth was driven by rising compensation costs related to salary increases and new hiring. The thinner result also incorporated the weak operating performance of health care entities.

State appropriations remain relatively low at approximately 7% of operating revenues. They are projected to rise by a healthy 9.6% to $583 million in fiscal 2024, or 4.4% excluding one-time grants for healthcare entities and some provisions for salary increases. The current biennial capital budget is also supportive through capital appropriations.

The sizeable academic medical center will remain a drag on the university’s performance over the next several years reflecting challenges related to elevated labor costs and length of stay. Patient revenues are substantial, contributing $2.6 billion or 32% to the university's fiscal 2023 consolidated revenue (rising to around 39% if Valley Medical Center is included). The fiscal 2024 operating cash flow margin of UW Medicine Select Units will remain weak, following a thin 2.3% result in 2024.

Financial resources and liquidity

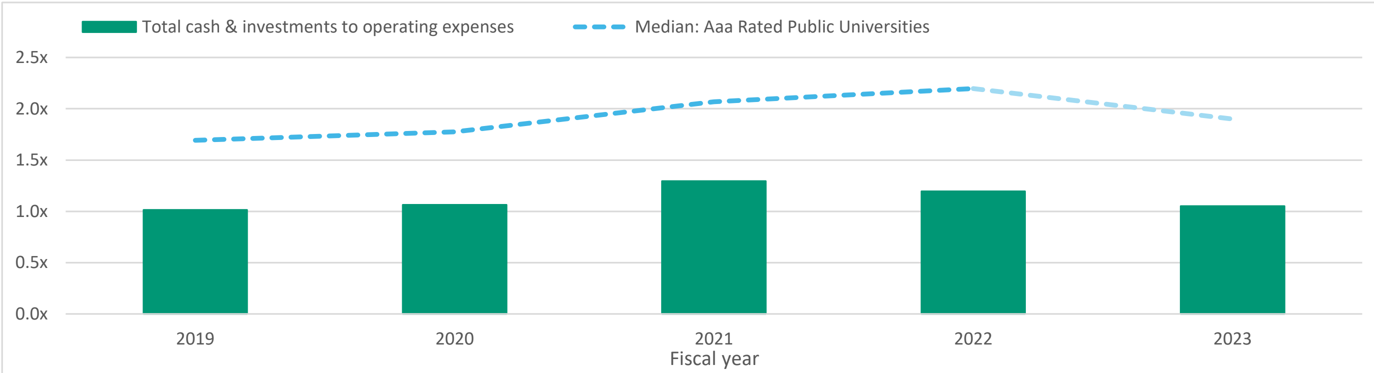
The University of Washington’s growing total wealth provides excellent financial flexibility. Total cash and investments are projected to increase moderately in fiscal 2024 from $8.5 billion in fiscal 2023. UW's exceptional fundraising success along with lowered endowment draws of 4.5% since fiscal 2022 will support growth in reserves. In fiscal 2023 three year average gifts were $375 million. UW's monthly liquidity is modestly lower than the 227 days of Aaa-rated peers (estimated for fiscal 2023), with 171 days in fiscal 2023, but still sufficient relative to business risks.

At June 30, 2023, UW’s Consolidated Endowment Fund (CEF), the university's long term portfolio amounting to $4.9 billion, had a 6.0% gain. The portfolio allocations are consistent with other large endowment portfolios. The university also has $2.9 billion in its Invested Funds (IF) for its operating fund investments, which had a gain of 2.5%. University of Washington Investment Management Company (UWINCO) including a CIO oversee the CEF and IF.

UW’s Commercial Paper program is authorized at $250 million and is rated P-1 based on the university’s self-liquidity. At September 30, 2023 UW reported $1.8 billion of discounted daily liquidity, including one Aaa-mf rated money market fund and US treasuries and agencies. The internal daily liquidity (excluding the largest money market fund) provides an extremely strong nearly 18x coverage of the maximum $100 million of commercial paper that can mature in one business week. The university's external liquidity consists of one line of credit agreement of $100 million with US Bank National Association through September 30, 2024.

Exhibit 3

Overall wealth is strong but lower than Aaa median when compared to the size of operations



The 2023 median is estimated using data collected through January 2024
Source: Moody's Investors Service

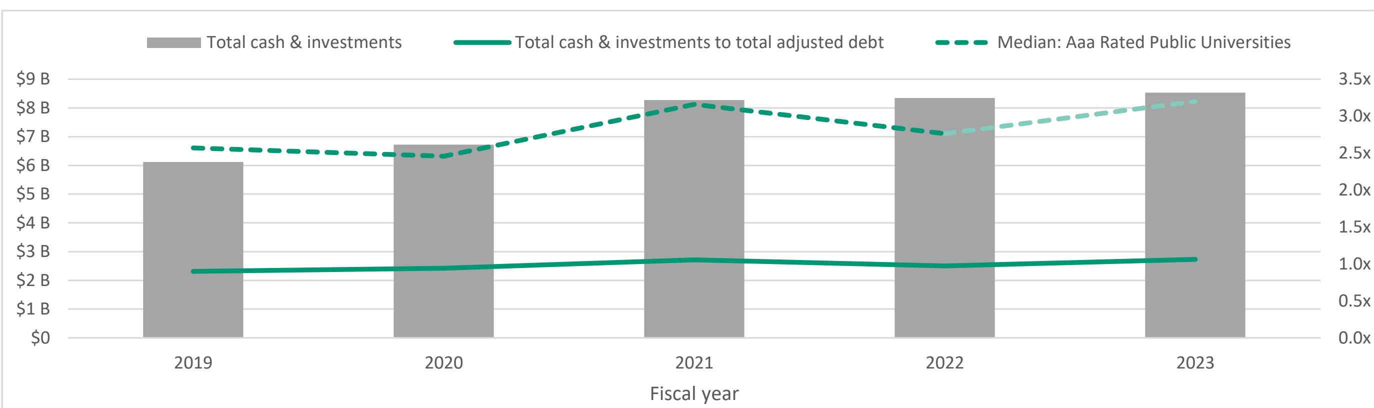
Leverage and coverage

UW's leverage will remain stable over the next several years reflecting a prudent strategy of borrowing roughly in line with amortization. From 2024 to 2028, moderate borrowing is projected at just over $600 million or averaging around $125 million annually, compared to around $110 million in annual maturities. In fiscal 2024, the university plans to issue $92 million new money borrowing and will issue long-term bonds to refund $143 million in commercial paper.

Large pension unfunded liabilities of $4.4 billion (Moody's adjusted net pension liability (ANPL) at June 30, 2023; average over last three years), brings total adjusted debt to just over $8 billion. Total cash and investment to total adjusted debt is just under is 1.1x and well below the Aaa-rated estimated median of 3.2x. Also debt affordability is worse than peers with debt to EBIDA 6.1x above the estimated median of peers at 3.6x.

Exhibit 4

Elevated leverage is partially offset by strong debt management with minimal new borrowing



The 2023 median is estimated using data collected through January 2024
Source: Moody's Investors Service

ESG considerations

University of Washington, WA's ESG credit impact score is CIS-2

Exhibit 5
ESG credit impact score

CIS-2

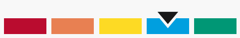
ESG considerations do not have a material impact on the current rating.

Source: Moody's Investors Service

University of Washington's ESG credit impact score is **CIS-2** reflecting the limited impact of ESG factors on the credit rating. The score incorporates the university's excellent brand along with strengths in management credibility that are balanced by human capital, board and organizational structure risks. Substantial wealth and state support partially offset the university ESG risk exposures.

Exhibit 6
ESG issuer profile scores

ENVIRONMENTAL
E-2



SOCIAL
S-2

GOVERNANCE
G-2

Source: Moody's Investors Service

Environmental

Environmental risks are **E-2** across all categories. Seattle, the university's primary location, has some exposure to extreme rainfall. The university adopted its Sustainability Action Plan in 2020 which builds on its Climate Action Plan that was initiated in 2009. The plan sets out specific targets to be achieved over five years addressing energy, transportation, food, waste, academic research, purchasing among others.

Social

University of Washington's social risks are **S-2** with some exposure to human capital risks. Good customer relations with key stakeholders are anchored by the university's flagship status with a sizeable, nationally renowned research enterprises and strong demand for its educational and clinical services. The university's large academic medical center and partnerships with entities within the Seattle research hub enhance its reputation. The university will continue to face competition for students partially mitigated by its flagship status and out of state attendance. The human capital challenges include substantial pension liabilities, unionization and the competitive landscape for nursing and clinical staff.

Governance

The University of Washington's governance risk is **G-2** reflecting the positive impact of management credibility balanced by Board and organizational structure risks. A demonstrated record of highly effective stewardship of a large, operationally complex academic, healthcare and research enterprise reflects management credibility. A highly integrated financial and capital planning framework demonstrates good financial management. The importance of the university's role in the state's economy reinforces state's relationship although funding is comparatively low. The appointment of the university's 11-member Board of Regents by the governor introduces risk related to potential political considerations influencing policies. The organizational challenges reflect the complex network of healthcare entities with various levels of relationship to the university.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The principal methodology used in this rating was the Higher Education Methodology published in August 2021. The Higher Education Methodology includes a scorecard that summarizes the factors that are generally most important to higher education credit profiles. Because the scorecard is a summary and may not include every consideration in the credit analysis for a specific issuer, a scorecard indicated outcome may or may not match an assigned rating. We assess brand and strategic positioning, financial policy and strategy, and operating environment on a qualitative basis.

The two-notch distinction between the assigned rating and the scorecard-indicated outcome acknowledges the university's strong overall wealth and financial flexibility that includes substantial levers to improve operating performance.

Exhibit 7

University of Washington, WA

Scorecard Factors and Sub-factors		Value	Score
Factor 1:	**Scale (15%)**		
	Adjusted Operating Revenue (USD Million)	8,042	Aaa
Factor 2:	**Market Profile (20%)**		
	Brand and Strategic Positioning	Aa	Aa
	Operating Environment	Aa	Aa
Factor 3:	**Operating Performance (10%)**		
	EBIDA Margin	7%	Baa
Factor 4:	**Financial Resources and Liquidity (25%)**		
	Total Cash and Investments (USD Million)	8,536	Aaa
	Total Cash and Investments to Operating Expenses	1.1	Aa
Factor 5:	**Leverage and coverage (20%)**		
	Total Cash and Investments to Total Adjusted Debt	1.1	Aa
	Annual Debt Service Coverage	2.5	Aa
Factor 6:	**Financial Policy and Strategy (10%)**		
	Financial Policy and Strategy	Aa	Aa
	Scorecard-Indicated Outcome		Aa2
	Assigned Rating		Aaa

Data is based on most recent fiscal year available. Debt may include pro forma data for new debt issued or proposed to be issued after the close of the fiscal year.

For non-US issuers, nominal figures are in US dollars consistent with the Higher Education Methodology.

Source: Moody's Investors Service

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