S&P Global Ratings

RatingsDirect®

McMaster University

May 16, 2024

This report does not constitute a rating action.

Primary contact

Elisa Lopez cortes
Toronto
1-416-507-2574
elisa.lopez.cortes
@spglobal.com

Secondary contacts

Adam J Gillespie
Toronto
1-416-507-2565
adam.gillespie
@spglobal.com

Sabrina J Rivers
New York
1-212-438-1437
sabrina.rivers
@spglobal.com

Research assistant

Adam Paunic
Toronto
1-6474803543
adam.paunic
@spglobal.com

Credit Highlights

Overview

Enterprise profile	Financial profile
--McMaster University's market position and excellent student quality metrics underpin the university's very strong enterprise risk profile.	--We expect McMaster will face operating pressures for the next two years, but that high domestic demand and steady grants will support robust financial performance.
--Strong management is navigating enrollment stagnation due to modest weakening in international student demand.	--In our view, McMaster's debt burden remains moderate while maximum annual debt service continues to decrease.
--The economic and demographic fundamentals of the Province of Ontario remain very strong and help sustain domestic demand.	--We expect very strong financial resources will continue to boost the university's financial risk profile.

S&P Global Ratings' long-term issuer credit rating on McMaster University is 'AA'. This reflects our combined assessment of McMaster's very strong enterprise risk and financial risk profiles, supported by the university's superior reputation as a research-intensive, medical doctoral university and member of the U15, a group of leading universities in Canada. We expect that overall enrollment will be steady, as domestic enrollment is projected to increase slightly, while we expect a decline in international undergrad enrollment due to weaker global demand coupled with the federal government's announced cap on the number of overseas students. McMaster's very strong financial resources compared with debt underpin the university's credit quality.

The rating also reflects our opinion of a moderately high likelihood that the Ontario government would provide extraordinary support in the event of financial distress.

Outlook

The stable outlook reflects our view that McMaster will maintain an excellent market position, which will support very strong operating margins, and will continue to hold high levels of financial resources compared with debt. The outlook also reflects our expectation that the university's relationship with the Province of Ontario will be stable and that our assessment of the likelihood of extraordinary support will remain moderately high.

Downside scenario

We could lower the rating in the next two years if management fails to maintain balanced operating margins, diminishing levels of cash and investments, and issues additional debt to complete its capital plan. All else being equal, a negative rating action on Ontario of up to one notch is unlikely to result in a similar rating action on McMaster. However, government intervention that negatively affects the university or a significant reduction in the university's resilience to an Ontario default scenario could cause us to lower the rating.

Upside scenario

We could raise the rating if the university improves its selectivity ratio to below 50% while increasing its enrollment growth rates, or if we project cash and investments will stabilize above 6x debt outstanding.

Rationale

McMaster’s very strong enterprise risk profile is supported by the university's academic reputation.

Our rating on McMaster is supported by our assessment of the higher education sector as a low-risk industry. The sector has low competitive risk compared with other sectors because it is anti-cyclical in nature. The university benefits from excellent economic fundamentals, as measured by the province's GDP per capita, estimated at almost US$55,400 in 2024.

McMaster's robust market position and steady enrollment trends underpin the university's enterprise risk profile, even amid uncertain conditions marked by lower international demand. Despite these challenges, McMaster’s resilient demand persisted, with full-time equivalents (FTEs) totaling 35,472 in fall 2023, up slightly by 0.4% from the previous year. We believe FTEs will remain largely flat in the next year but increase in the following two years. Meanwhile, the university's enrollment growth plan still focuses on attracting a more diverse base of international students; in our opinion, McMaster will keep its current international share at 17% of total enrollment in the next couple of years.

In fall 2024, the Canadian government will implement a national cap on international study visa applications. This cap will result in a reduction of approved permits, accounting for students applying for extensions, marking a decrease from 2023 numbers. The cap will not apply to current permit holders, primary and secondary school students, and master's or doctoral students. Provinces have received allocations from the cap based on their respective populations.

We expect that Ontario will see a significant reduction in new international students due to its already disproportionately high number of overseas students. However, we do not expect a substantial reduction in admitted international students at the university, we could see reduced demand in response to the changing policies.

Market quality metrics remain strong, comparing well with those of similarly rated Canadian universities, as evidenced by McMaster's high retention rate of 92% on a three-year, weighted-average basis and almost 94% of faculty holding advanced degrees in 2023. Lastly, the selectivity rate was upheld at 52% on average in the past three years; we expect it to remain above 50% in the next two years.

In our view, McMaster's management expertise, governance practices, and financial management policies are very strong and in line with those of other high investment-grade Canadian universities. Although the university president recently announced he will step down in 2025, the university's academic and operational priorities remain guided by McMaster's strategic plan and strategic mandate agreement with the province, and we do not foresee any change in these priorities. The university provides a detailed three-year operating budget and capital plan. Management reviews plan performance annually, tracks progress against specific activity indicators, and monitors risks identified through its enterprise risk management framework. The university has formal policies for endowments, investments, and debt; it also meets standard annual disclosure requirements. Overall, we view McMaster's transparency and disclosure as very good, with policies and procedures to adequately mitigate external risks, including climate and cyber risks.

Despite operating challenges, McMaster will maintain a strong financial risk profile.

McMaster will face hurdles such as higher operating costs and constrained revenue flexibility partly due to stagnant growth in the share of international undergraduates, which will stress its financial performance. We expect cost-saving efforts and strategic revenue management will help to mitigate inflationary pressures. We anticipate operating margins will fall but remain very strong at 13% on a five-year average, supported by stable tuition revenues, grants, and research grants.

Similar to that of other Canadian universities, McMaster's limited flexibility to raise student-generated revenues somewhat offsets its strong financial performance. This is primarily because Ontario monitors and guides domestic tuition rates and student aid (through the tuition framework) and domestic enrollment expansion (through operating grants).

In our view, McMaster has a moderate debt burden compared with that of most similarly rated universities. Debt outstanding mainly consists of four fixed-rate bullet bonds totaling C$390 million due between 2052 and 2071, and an amortizing bank loan of C$11.6 million. We estimate maximum annual debt service at 2.5% of the university's adjusted operating expenses in fiscal 2024. At fiscal year-end 2023, the university held C$58 million in sinking funds to repay its bullet debentures. It also has a long-term obligation of C$19.5 million for the eventual decommissioning of its nuclear reactor. We don't expect McMaster to increase its debt in the next one-to-two years.

In our view, the university has very robust financial resources supported by cash and exceptional investment performance. We estimate that in fiscal 2024, total cash and investments were C$2.3 billion or 5.5x total debt, and we expect the ratio will be stable in the next two years.

We believe McMaster has some exposure to contingent liabilities through its two public-private partnerships (PPPs). However, in our opinion, they are unlikely to lead to additional direct financial obligations for the university. The graduate student residence started partial occupancy in 2023, despite some infrastructure hold-ups caused by technical water-related issues. These delays did not result in any major financial impacts. The second PPP is an undergraduate student residence that is expected to open in fall 2026. Although these projects are structured such that there is no recourse to the university, they still provide or will provide important services to students in support of the university's mission. Therefore, we believe that if the projects were to experience significant stress, McMaster might be compelled to carry out more direct oversight or support, which has not been necessary to date. Still, based on its public disclosures, we do not believe the university has any additional contingent liabilities that could materially affect our view of its credit profile. We will continue to monitor these PPPs, as the university is planning to launch more projects using the same model.

The funded status of McMaster's pension plan resulted in a surplus of C$13.9 million compared with a deficit of C$6.8 million in 2022 (on an accrual basis). Despite market volatility, management believes initiatives to manage the pension, including higher employee and employer contributions, will allow it to cover any special solvency pension deficit payments that might be required in the longer term.

Moderately high likelihood of extraordinary provincial government support

We believe that the university has an important role in the province, specifically because postsecondary education is one of Ontario's priorities in both expenditure and mandate after health care and school boards; therefore, in accordance with our criteria for government-related entities (GREs), our view is that McMaster has a moderately high likelihood of extraordinary government support. Our view also reflects the province's oversight, program approval rights, and tuition regulation over McMaster, which suggests a strong link to it. Also supporting our assessment of the link are the large operating grants received from the province, accounting for about 20% of McMaster's total revenue.

We rate McMaster two notches above Ontario. The maximum differential is three notches, 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 measurable likelihood that McMaster'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 McMaster's ownership structure, in which the government is neither an owner nor shareholder. We consider the risk of extraordinary negative government intervention low, given the university's operational independence and important public policy role.

The Ontario government implemented the 10% reduction and freeze on domestic tuition fees in the 2019-2020 academic year, and it is in place, at a minimum, until fiscal 2027. In February 2024, the provincial government unveiled a C$1.3 billion funding package to support the higher education sector in Ontario. This funding includes a C$900 million stabilization fund to be distributed over three years, contingent on institution-specific audits and efficiency measures. Consequently, we expect a modest increase in ongoing operating funding from the province in the medium term. We continue to believe there is a moderately high likelihood that the province would support McMaster in a distress scenario.

Environmental, Social, And Governance

We analyzed McMaster’s risks related to environmental, social, and governance factors and determined them to be neutral in our overall credit analysis. Health and safety social risks are factors to consider and could stress demand and finances; we will keep monitoring the changes in socioeconomic and demographic profiles due to policies on international students.

Key Statistics

McMaster University -- Selected Indicators

	--Fiscal year-end April 30--					
(Mil. C$)	2020	2021	2022	2023	2024f	U.S. public universities 2022 'AA' medians
Enterprise profile						

McMaster University -- Selected Indicators

(Mil. C$)	--Fiscal year-end April 30-- 2020	2021	2022	2023	2024f	U.S. public universities 2022 'AA' medians
Full-time equivalent enrollment (FTE; no.)	32,147	34,791	35,161	35,315	35,472	41,783
Annual FTE change	4	8	1	0	0	0
Undergraduate selectivity rate (%)	52	59	52	52	53	73
Undergraduates as a % of total FTE enrollment	86	87	87	87	86	80
Retention rate (%)	91	94	92	92	92	92
Graduation rates (six years) (%)	81	82	82	82	84	71
Financial profile						
Adjusted operating revenue	1,173	1,220	1,368	1,500	1,421	MNR
Adjusted operating expense	1,080	1,068	1,154	1,248	1,300	MNR
Net adjusted operating margin (%)*	9	14	19	20	9	3
Student dependence (%)	34	37	35	33	36	37
Government operating grant dependence (%)	24	23	21	19	20	17
Endowment and investment income dependence (%)†	3	10	10	14	6	1
Cash and investments	1,515	1,919	2,033	2,195	2,323	2,838
Cash & investments to adjusted operating expenses (%)	140	180	176	176	179	115
Outstanding debt	273	272	421	421	420	1,143
Cash & investments to debt (%)	554	706	483	521	553	278
Maximum annual debt service/total operating expense (%)	2	2	3	3	2	MNR

*As % of adjusted operating expense. †Includes the adjustments for fair value. f--Forecast. MNR--Median not reported.

Rating Component Scores

McMaster University -- Rating score snapshot

Industry risk	2
Economic fundamentals	1
Market position	2
Management & governance	2
Enterprise risk profile	2
Financial performance	2
Financial resources	1
Debt and contingent liabilities	2
Financial risk profile	2
Stand-alone credit profile	aa
Issuer credit rating	AA

Related Criteria

- Criteria | Governments | General: Global Not-For-Profit Education Providers, April 24, 2023
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Outlook For Global Not-For-Profit Higher Education: Credit Quality Divergence Continues, Dec. 7, 2023
- U.S. Not-For-Profit Public College And University Fiscal 2022 Medians And Ratios: Road To Recovery Is Paved With Federal Funding; Hazards Remain, July 25, 2023

Ratings Detail (as of May 16, 2024)*

McMaster University	
Issuer Credit Rating	AA/Stable/--
Senior Unsecured	AA
Issuer Credit Ratings History	
20-May-2016	AA/Stable/--
08-Dec-2010	AA-/Stable/--
09-Sep-2002	AA/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings 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.