



## RATING ACTION COMMENTARY

# Fitch Affirms Rhode Island School of Design Revs at 'A+'; Outlook Revised to Stable

Thu 30 Sep, 2021 - 1:49 PM ET

Fitch Ratings - New York - 30 Sep 2021: Fitch Ratings has affirmed Rhode Island School of Design's (RISD) Issuer Default Rating (IDR) at 'A+' and its 'A+' rating on approximately \$116.7 million of outstanding revenue refunding bonds issued by Rhode Island Health and Educational Building Corporation (RIHEBC) issued on behalf of RISD.

The Rating Outlook has been revised to Stable from Negative.

## SECURITY

The higher education facilities revenue and revenue refunding bonds are an unsecured general obligation of the school, payable from legally available revenues of RISD.

## ANALYTICAL CONCLUSION

The 'A+' IDR and bond rating reflect RISD's strong demand profile, with selective admissions, and generally very steady FTE enrollment trends over time. The rating also reflects good cash flow with sufficient cost management flexibility and capacity to curtail expenses as needed. RISD has scaled back capital spending, after a period of heavy capital investing, and has no new borrowing plans. RISD recently completed a private placement fixed-rate restructuring in fiscal 2022 eliminating all of its outstanding variable rate debt and swap obligations. The rating reflects the less risky debt structure and improved RISD's overall financial profile, with resilient leverage metrics (Available Funds [AF] to adjusted debt) supported by strong investment returns.

The revision to Stable Outlook reflects the significant rebound in enrollment in fall 2021, after softening in fall 2020 due to the coronavirus, and the expectation that enrollment will stabilize to at least current levels over the forward-looking period. Given RISD's very strong demand profile and pricing flexibility, such improvement is expected to improve operating performance in fiscal 2022 to at least historical levels. The Outlook revision also reflects a reduction in operating risk, with reversion back to fully on-campus activities, the positive impact on student fee revenues, and reduced likelihood of reliance on supplemental endowment draws and/or bank lines of credit to provide operational support. Fitch expects AF to adjusted debt will remain acceptable for the current rating through a moderate, plausible stress scenario, which includes a market downturn.

## KEY RATING DRIVERS

### Revenue Defensibility: 'aa'

#### Strong Market Position Supports Competitive Demand

Strong demand for RISD's programmatic offerings, driven by the school's leading market position in art and design education, support historically stable enrollment trends and revenues, as well as the 'aa' revenue defensibility assessment. RISD's demand indicators are very competitive with a very low acceptance rate and high yield and retention, and as such the enrollment base is expected to be less sensitive to price increases. RISD realized record enrollment in fall 2021 and enrolled its largest incoming freshmen class with very strong demand metrics supported by record applications and acceptance rates. The 'aa' assessment is

constrained by RISD's heavy reliance on student generated revenues and endowment distributions to generate sufficient economic debt service coverage.

### **Operating Risk: 'bbb'**

Adequate Cash Flow; Slowing but Continuing Capital Needs

Operating cost flexibility is historically adequate with cash flow margins averaging about 15% over the past five years. The dip in fiscal 2021 (5.1% unaudited) reflects risks of a narrow revenue base amid operating variability which supports the 'bbb' operating risk assessment. If Fitch adjusted for investment management fees, this ratio is slightly higher at 6.5%. Fitch expects improved cash flow in fiscal 2022, given a rebound in headcount enrollment. The assessment also reflects moderately high capital spending which RISD paused in fiscal 2021 and 2022, but is likely to be elevated further out given the high average age of plant. Major capital plans are several years away according to management and funded with internal funds and some, but not significant, gifts.

### **Financial Profile: 'a'**

Strong Financial Profile: Downside Risk

RISD's leverage and overall financial profile is consistent with the 'a' assessment, but effectively constrained by its weaker operating risk profile and narrow revenue base. Available funds (AF) to adjusted debt spiked to 198% in fiscal 2021 (unaudited) due to investment market gains, from of 153% the prior year, reflecting a stronger financial position at the 'a' financial profile assessment level. Heading into fiscal 2022, Fitch expects RISD's leverage position could improve with operating improvement and no plans for additional debt. RISD's operating performance remains resilient through a plausible market and operating stress scenario at the current assessment level.

### **Asymmetric Additional Risk Considerations**

No asymmetric risk factors affected the rating.

### **RATING SENSITIVITIES**

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Sustained improvement in demand and annual FTE enrollment from organic growth or through program expansion contributing to growth in net tuition revenue or total revenue;

--RISD's ability to generate and sustain strong cash flow margins above 15%, without support of one-time or non-recurring revenues, which would support growth in available funds;

--Strong capital management and improved leverage ratios maintained above 160%, irrespective of market fluctuations.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Material change in demand profile or reduction in enrollment that contributes to declines in net tuition or total revenue;

--Failure to sustain sufficient cash flow margins at or above 10% needed to generate sufficient economic debt service coverage;

--Inability to manage the five-year capital plan and preserve leverage ratios above 90%.

### **BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more

information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

## CREDIT PROFILE

Founded in 1877, RISD is a private four-year institution that offers 21-degree programs, including fine arts, film/animation/video, design, architecture and art education, to about 2,576 students in fall 2021, encompassing both undergraduate and graduate degrees. The most heavily enrolled degree programs are illustration, industrial design, architecture and graphic design.

RISD's 1.9 million square-foot campus is located in Providence, Rhode Island with specialized facilities supporting studio-based learning. RISD's location adjacent to Brown University is favorable in supporting its Brown-RISD dual degree offerings, which has about a 3% acceptance rate. RISD's regional accreditation by the New England Commission on Higher Education (formerly the New England Association of Schools and Colleges) was renewed in 2016 for a 10-year term.

RISD's President and some members of the executive team recently retired or have become vacant. RISD's CFO has become the interim President until a new President is announced, which is likely in November. Other key positions are in the process of being filled. The college operates under a rolling five-year strategic plan, which was recently completed in fiscal 2021 and runs through 2027. The new plan focuses on improving financial sustainability and looking at revenue opportunities.

RISD benefitted from one-time general operating support related to the CARES Act funds, about \$1.5 million of which was reported in fiscal 2020 and \$1.25 million in fiscal 2021, respectively, which helped ease, but did not fully counter coronavirus impacts. In fiscal 2022, RISD is expected to book another \$1.8 million due to the third round of stimulus funding under the Higher Education Emergency Relief Fund (HEERF III) authorized by the American Rescue Plan (ARP).

RISD elected to have students fully return to campus in Fall 2021 which includes a hybrid model for select classes. The school has resumed operating its residential facilities at full occupancy which consists of 1,447 beds. Fitch's rating sensitivities address potential rating implications under a stress scenario. This scenario assumes a slower economic recovery and prolonged or recurring pandemic-induced disruptions lasting into fiscal 2022, including further tuition, auxiliary and other related revenue pressures on the university's operations.

## ASYMMETRIC ADDITIONAL RISK CONSIDERATIONS

No asymmetric risk factors affected the rating.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

## REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

## ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg)

## RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Rhode Island School of Design (RI)	LT IDR	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Negative

ENTITY/DEBT	RATING			PRIOR
● Rhode Island School of Design (RI) /General Revenues/1 LT	LT	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Negative

[VIEW ADDITIONAL RATING DETAILS](#)

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## APPLICABLE CRITERIA

[U.S. Public Finance College and University Rating Criteria \(pub. 07 Oct 2020\) \(including rating assumption sensitivity\)](#)
[Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 01 Sep 2021\) \(including rating assumption sensitivity\)](#)

## APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Portfolio Analysis Model (PAM), v1.3.2 (1)

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Rhode Island Health &amp; Educational Building Corp. (RI)

EU Endorsed, UK Endorsed

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