Spurring Standards for State Subsidies

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Agenda

- Current State Funding Environment
- Performance Funding
- Potential Credit Impacts
Since the current recession, almost all public universities have experienced reductions in state funding

• Though some increases in fiscal 2013 and 2014, not likely to return to pre-recession increases.
  • Have not kept up with the rate of enrollment and/or inflation

• Increased appropriations = Increased oversight from state legislators.
  • Legislators want “more bang for the buck”
By the numbers

Overall Increase of 5.7%
FY 13-14

Largest Increase by State
FY 13-14

New Hampshire: 27.3%
North Dakota: 19.2%
Florida: 17.6%

Largest Decrease by State
FY 13-14

Wyoming: -8.1%
Louisiana: -5.6%
West Virginia: -4.7%

Better than 5 year change from FY 09-14
- 1.2% decline when including state funding only
- 4.1% decline when including ARRA funding

Source- State Higher Education Officers and Illinois State University
Performance Funding
## Performance Based Funding vs. Performance Budgeting

<table>
<thead>
<tr>
<th>Performance Budgeting</th>
<th>Performance Based</th>
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<tr>
<td>• General linkage to what state appropriations “buy”</td>
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<td>• Indirect, discretionary and uncertain</td>
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<tr>
<td>• Most institutions followed performance budgeting in the past</td>
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<tr>
<td>• Tied directly to what state appropriations “buy”</td>
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<td>• Formulaic and direct</td>
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<td>• Today moving more toward performance based funding</td>
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Performance funding by state

Red = at two and four year institutions
Blue = at four year institutions only
Yellow = in transition
Challenges

Performance Based Funding

Who decides the rewards?

Focus on institutional improvement or institutional competition?

Do we have money to invest in improvements?

How do we provide timely data?

What indicators to use? Are these ideal given my institution’s mission?
Challenges Continued

- What happens to the chronic "losers?"
- If the state wants to only fund certain programs---impact of high vs. low demand programs?
- How will demographics impact measures?
- What happens when institutions only accept the best of the best?
- Will performance funding be sustainable through economic cycles?
What Challenges/Opportunities Do You See?
Potential Credit Impacts
Higher Education Criteria Summary

Enterprise Profile
- Enrollment
- Market Position and Demand
- For Publics– State Appropriations
- Competitive position/ Peer group comparisons

Financial Profile
- Operating Performance
- Financial Resources
- Endowment
- Fundraising
- Debt and debt profile

Rating
Credit Factor Impacts

In general, we aren’t likely to see major rating shifts solely as a result of performance funding.

Why?

State Appropriations continue to decrease as a source of revenue.

Highly rated issuers with greater financial resources and revenue diversity have minimized the disruption to operations.

Institutions with fewer financial resources and a greater reliance on state funding have experienced increased fiscal pressure.
State Appropriations (% of total revenue)

Source Standard & Poor's 2014
However, performance based funding could impact some enterprise and financial profile factors:

“Skimming off the cream”— could result in better selectivity and matriculation measures.
- May result in a decrease in enrollment in the short term.

Improved retention rates could improve operations.
- “Cheaper to retain a student than recruit”.

Higher investment in programming and infrastructure that could affect already stressed budgets.
- Continue the “weak getting weaker and strong getting stronger” argument.
Conclusion

Performance Funding is still in its infancy and a dramatic departure from the past:

• S&P will continue to monitor broader economic changes, state budgets, performance-funding trends, and overall enrollment patterns -- to evaluate how these continue to play into affordability and credit

• Credit impact is muted currently because performance funding is not a large part of total revenues but direction of this initiative and any shifts in institutional characteristics will warrant close review.
Thank You

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