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CREDIT OPINION
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Grand Canyon University, AZ

Update following revision of outlook to negative

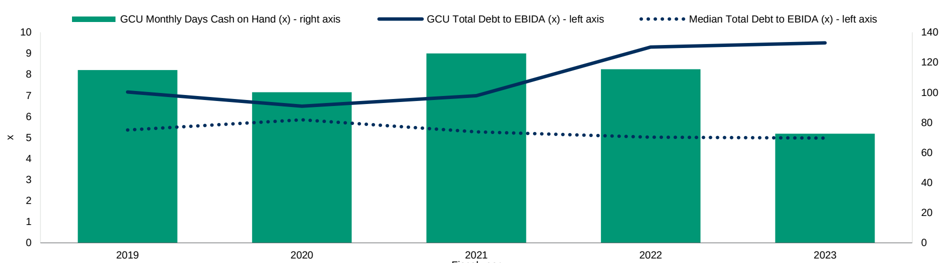
Summary

Grand Canyon University's (Ba1 negative) credit quality acknowledges its substantial and broad academic program diversity. Effective enrollment management in online and on campus segments will provide the university with the ability to invest in new programs and facilities while generating adequate debt service coverage. Regulatory risk weighs on credit quality, including active litigation with the US Department of Education and other agencies. High financial leverage also weighs on credit quality, with total cash and investments to debt well below sector medians combined with the need to re-market shorter duration debt in a higher interest rate environment. While the relationship between GCU and Grand Canyon Education (GCE), including elements codified in the Master Services Agreement (MSA), has demonstrated itself as high functioning, the longer term nature of the MSA and various exit payment provisions constrains the credit quality of the university. The MSA provisions include a 60% revenue share for almost all of GCU's revenue in exchange for various services GCE provides. Unrestricted liquidity declined in fiscal 2023, as the university continued to invest in dormitory facilities and drew on bank loans while providing the banks with cash and investment collateral.

On January 8, 2024 Moody's revised Grand Canyon University's outlook to negative from stable.

Exhibit 1

Unrestricted liquidity decreased and debt affordability weakened as GCU used cash and debt to continue capital investment in fiscal 2023



Median Total debt to EBIDA for private universities includes estimate for fiscal 2023
Source: Moody's Investors Service

Credit strengths

- Substantial scale with 2023 operating revenue of $1.4 billion aided by market responsiveness and sustained record of enrollment growth
- Operating discipline with EBIDA margin of 10.2% in fiscal 2023
- Low average of age plant at 4.2 years with recent capital investment

Credit challenges

- High financial leverage with 2023 total debt to EBIDA at 9.5x combined with increasing interest expense and near term bullet maturities
- Durable Master Services Agreement with Grand Canyon Education consumes 60% of student revenue in exchange for services
- Ongoing regulatory tension and litigation with the US Department of Education and other agencies
- Complexity of organizational structure, including governance and leadership overlap with for-profit service provider GCE

Rating outlook

The negative outlook incorporates some uncertainty regarding the pace of recovery in unrestricted liquidity as well as the regulatory environment. The higher interest rate environment also informs the outlook, with EBIDA net of debt service coverage key to the ability to fund strategic investments. The outlook remains sensitive to maintaining healthy headroom over the 55 Days Cash on Hand and Debt Service Coverage Ratio financial covenants.

Factors that could lead to an upgrade

- Marked gains in unrestricted liquidity and total cash and investments with total cash and investments to operating expenses moving to above 0.5x
- Ongoing enrollment and revenue growth
- Favorable resolution of litigation with the US Department of Education and other agencies

Factors that could lead to a downgrade

- Further heightened regulatory scrutiny or unfavorable resolution of litigation
- Decline in operating performance including reduction in debt service coverage to below 1.3x
- Decline in enrollment or operating revenue
- Reduction in unrestricted liquidity especially if combined with weaker debt service coverage
- Substantial increase in total debt or further collateralization of cash and investments

Key indicators

Exhibit 2
GRAND CANYON UNIVERSITY, AZ

	2019	2020	2021	2022	2023
Total FTE Enrollment	44,084	47,493	48,951	49,435	52,490
Operating Revenue ($000)	1,130,823	1,222,511	1,288,816	1,333,270	1,373,786
Annual Change in Operating Revenue (%)	N/A	8.1	5.4	3.4	3.0
Total Cash & Investments ($000)	325,655	307,603	407,438	395,730	385,953
Total Adjusted Debt ($000)	1,070,543	1,046,075	1,160,764	1,278,319	1,326,413
Total Cash & Investments to Total Adjusted Debt (x)	0.3	0.3	0.4	0.3	0.3
Total Cash & Investments to Operating Expenses (x)	0.3	0.3	0.3	0.3	0.3
Monthly Days Cash on Hand (x)	115	100	126	115	73
EBIDA Margin (%)	13.2	13.2	12.9	10.3	10.2
Total Debt to EBIDA (x)	7.2	6.5	7.0	9.3	9.5
Annual Debt Service Coverage (x)	2.8	2.7	2.9	2.5	1.3

Source: Moody's Investors Service

Profile

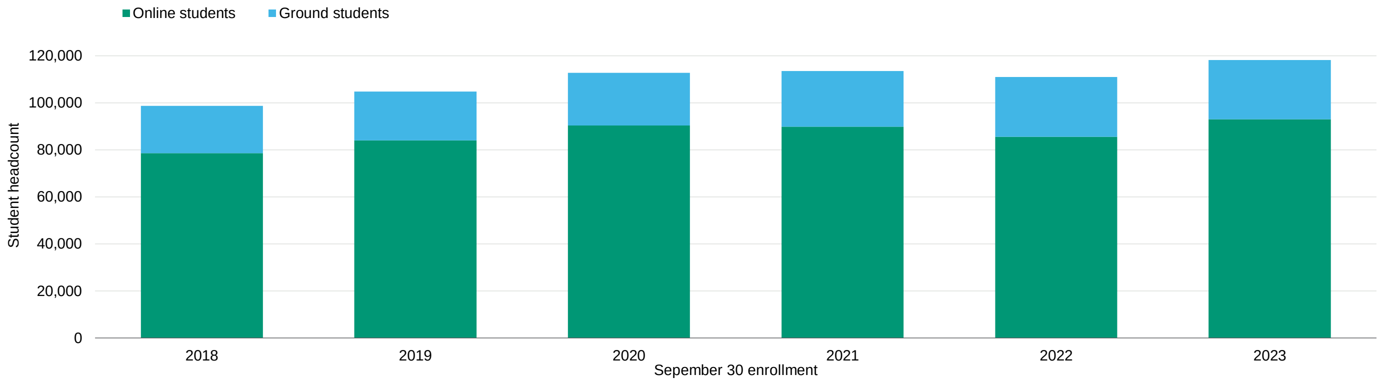
Grand Canyon University is a large, Christian university based in Phoenix, Arizona. Founded in 1949, the university has had nonprofit status for the majority of its years, but was reorganized as a for-profit university between 2004 and 2018. As of Fall 2023 the university enrolled roughly 107,000 headcount students across on campus, online and hybrid modes. Operating revenue was $1.4 billion in fiscal 2023 with over 97% reliance on tuition and auxiliary revenue. The university has made substantial investments in student life including intercollegiate athletics. The university is a Division I member of the Western Athletic Conference.

Detailed credit considerations

Market profile

Grand Canyon University has achieved remarkable growth over the last decade benefitting from effective market analytics, efficient recruitment, and scalable instructional delivery. Profitability in many programs has allowed the university invest in new academic programs as it now includes 330 graduate and undergraduate degrees programs, emphases and certificates. Leadership aims to grow on campus/ground enrollment to 40,000 headcount students. The university's pricing strategy for ground students aims to support access and a relative pricing advantage to many private higher education providers. Tuition has remained flat for thirteen years at $16,500 per academic year. Room and board rates increased to an average of $9,910 for the 2023-2024 academic year.

Exhibit 3
An 8.7% increase in online students in fall 2023 over the prior year, will aid results as ground student enrollment flattens



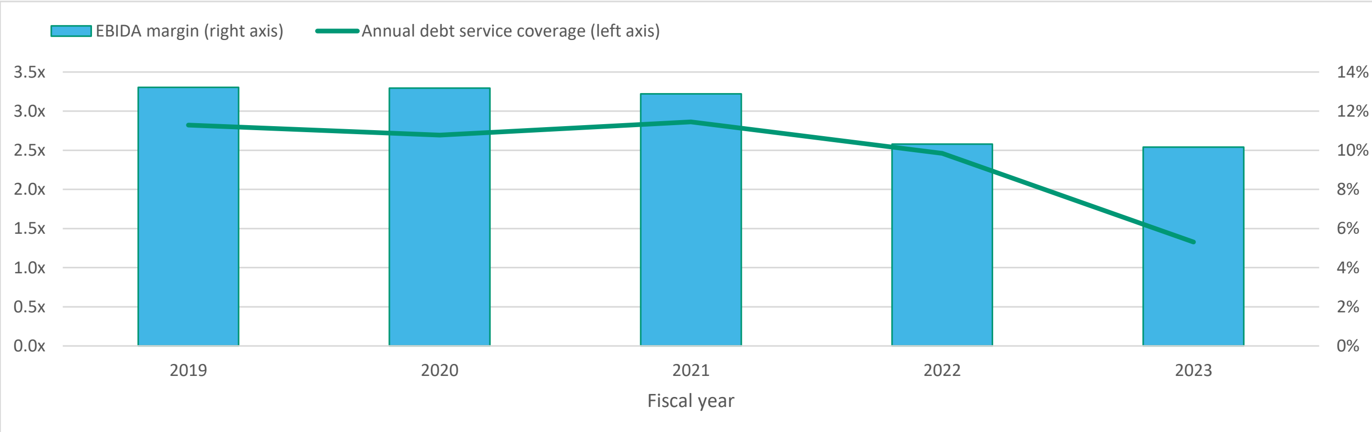
Source: Grand Canyon University disclosure data

As a formerly private, for-profit university with ongoing ties to its prior owner, GCU will continue to attract regulatory scrutiny. This scrutiny will likely be an abiding credit risk and informs our view of the operating environment. The university is highly reliant on federal awards and reported federal award expenditures of $1.2 billion in fiscal 2023. University leadership believes it is being unjustly targeted by officials associated with the US Department of Education, Federal Trade Commission and Department of Veterans Affairs and is defending its interests. The university is incurring staff costs as well as outside auditing and legal fees in its defense. While recognized as a private, nonprofit corporation by the Internal Revenue Service, the Higher Learning Commission (the university's regional accreditor), and the State of Arizona, the US Department of Education treats the university as for-profit based on its "Review of the Change in Ownership and Conversion to Nonprofit Status of Grand Canyon University" dated November 6, 2019. The university is challenging the determination. In October 2023 the Department of Education Office of Federal Student Aid announced a $38 million fine against the university related to how it communicated the cost of its doctoral programs including continuation credits. The university is appealing the decision through the appropriate channels.

Operating performance

Grand Canyon University should continue to generate sound operating performance even as increasing interest expense will underscore the importance of EBIDA remaining above $150 million to service debt, invest in facilities and fund strategic efforts. The 60% revenue share for the broad services provided by GCE limits the university's net revenue and is applied to all student charges including incremental student housing revenue for dorms built after the conversion. The reliance on student charges is over 95% with limited other sources of revenue. The Master Services Agreement runs for 15 years, with optional 5 year renewals. Coordination between GCU and GCE should allow for positive operating performance and potential for scalable growth. While operating budget discipline and financial controls are very good, the fair financial policy score is weighed down by management's growth ambitions. The pace of investment in facilities even as it slows in fiscal 2024 will continue to weigh on operating results and limit the ability to grow financial reserves as expenses continue to grow.

Exhibit 4
GCU's EBIDA margin and annual debt service coverage softened in fiscal 2023

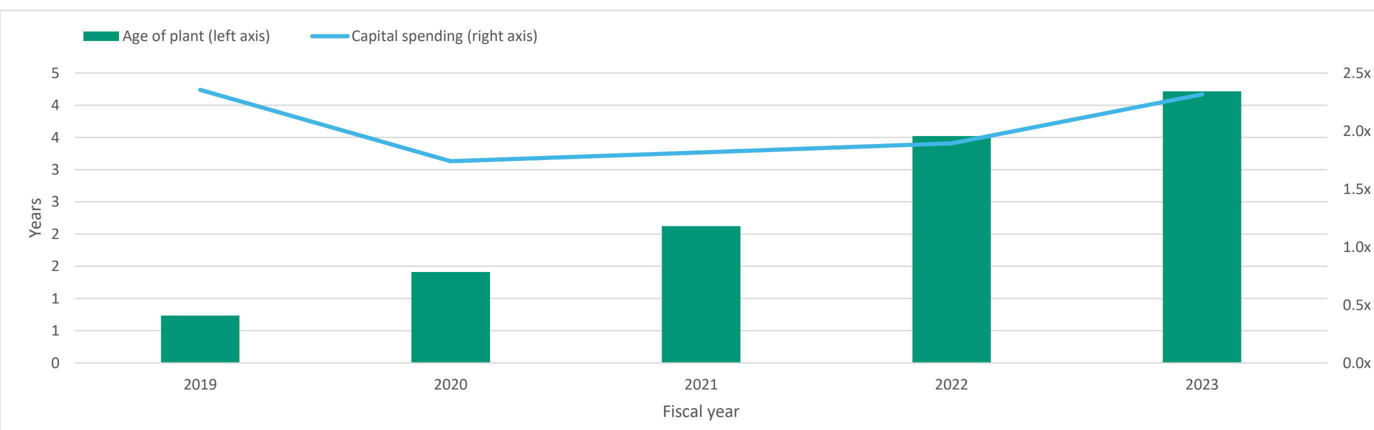


Source: Moody's Investors Service

Wealth and liquidity

Given its limited operating history and donor support, GCU's wealth is primarily operating reserves. With increasing construction costs and the ongoing investment in dormitory and other facilities, the university spent $132 million in purchases of capital in fiscal 2023. It drew $80 million on two lines of credit for the capital funding. When combined with other impacts, total cash and investments declined by around $10 million in fiscal 2023. Because the university agreed to post collateral against the lines of credit, the amount of its unrestricted liquidity declined by $139 million. This translates to monthly days cash on hand declining to 81 days from 115 days for the prior year. With estimated capital purchases in fiscal 2024 of around $80 million and online student revenue growth, there are prospects for some improvement in unrestricted liquidity in fiscal 2024. Total cash and investments to operating expenses will remain relatively weak and given the university's business model and limited history of donor support, this condition will likely remain a credit weakness relative to more established competitors.

Exhibit 5
While the university's capital plan has consumed a material portion of cash flow from operations, it benefits from a favorable average age of plant

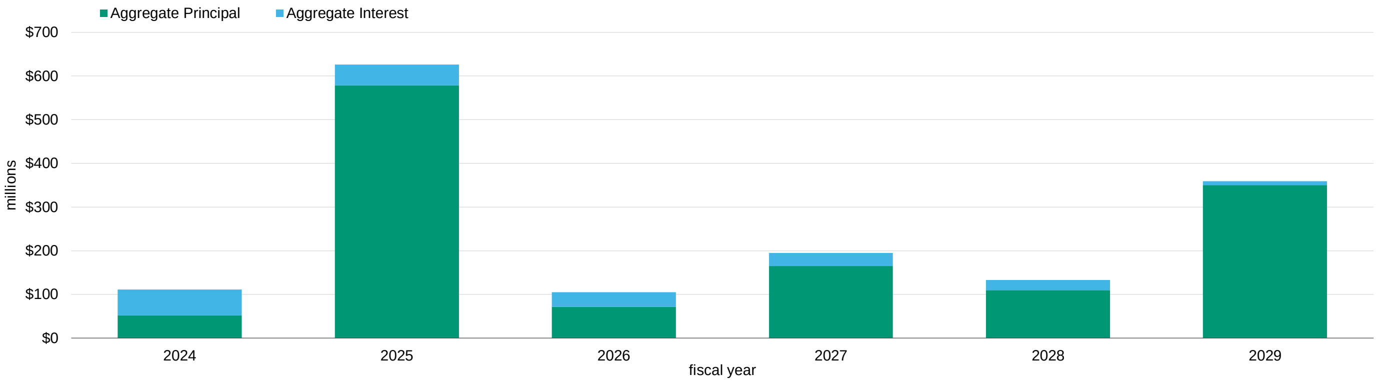


Source: Moody's Investors Service

Leverage

Substantial financial leverage combined with an increasing cost of capital since 2021 will continue to constrain GCU's financial flexibility. Total debt was around $1.3 billion at the end of fiscal 2023, or 97% of operating revenue. At fiscal year 2023, the university's total cash and investments to total adjusted debt was 0.3x. The Seres 2021B bonds have a relatively brief tenor with final maturity in fiscal 2029 and limited principal retirement. This structure introduces market access and interest rate risks in advance of the scheduled maturity in 2029.

Exhibit 6
GCU plans to refinance a portion of its near term bullet maturities in calendar year 2024



Source: Grand Canyon University

ESG considerations

Grand Canyon University, AZ's ESG credit impact score is CIS-4

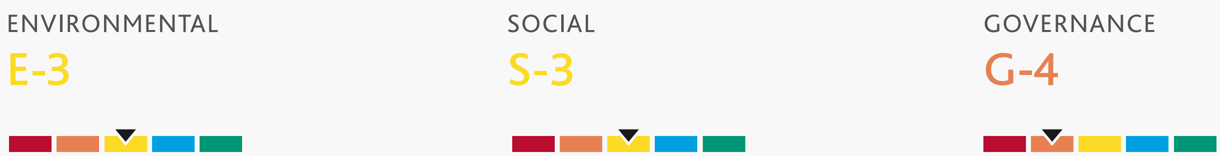
Exhibit 7
ESG credit impact score

ESG considerations have a discernible impact on the current rating, which is lower than it would have been if ESG risks did not exist. The negative impact of ESG considerations on the rating is higher than for an issuer scored CIS-3.

Source: Moody's Investors Service

Grand Canyon University's ESG Credit Impact Score is **CIS-4**. While the relationship between GCU and Grand Canyon Education (GCE) including elements codified in the Master Services Agreement (MSA) has demonstrated itself as high functioning, the longer term nature of the MSA and various exit payment provisions constrains credit quality. The university's record of effective recruitment and enrollment management combined with financial discipline partially mitigate a portion of the ESG risks, the university remains exposed to shifts in federal regulatory oversight and requirements.

Exhibit 8
ESG issuer profile scores



Source: Moody's Investors Service

Environmental

Grand Canyon's exposure to environmental risks (**E-3**) incorporates physical climate risks. The primary drivers of potential heat stress and water stress for the primary Phoenix campus inform the score. A geographically distributed online customer base partially mitigates that exposure. GCU also benefits from both the state and local government's long history of successfully managing its water resources and consumption. Management's commitments to sustainability also partially offset the exposures and include energy efficient design elements in its recent capital expansion and rooftop rainwater collection for irrigation.

Social

Grand Canyon's **S-3** is primarily driven by its exposure to customer relations, demographic, and human capital risks. While the university will benefit from Arizona's growth, other key markets face increasing competition and declines in the number of high school graduates along with shifts in consumer preferences. Customer relations are aided by very strong demand for the university's various nursing degree programs with favorable outcomes including high median earnings for graduates. Increasing competitiveness for online degree programs does add to social risks. With regard to human capital risks, the university benefits from workforce flexibility with a very high proportion of part time faculty which offers some risk protection relative to the expense constraints of its revenue share agreement. As a formerly private, for-profit university with ongoing ties to its prior owner, GCU will continue to attract regulatory scrutiny.

Governance

Grand Canyon's **G-4** incorporates organizational structure elements adding to credit risks. The university is fairly young in its current incarnation with a track record of successful implementation of enrollment management strategies and scalable growth supporting management credibility. Structural considerations include that GCU's president is also the CEO and board chair of GCE. While the interests are aligned and codified, potential conflicts of interests exist between a publicly traded for profit service provider and a non-profit university. The university aims to mitigate the related risks through the mechanism of Master Services Agreement Committee with four senior management leaders from GCE and four senior management leaders from GCU. The GCU board also has an MSA sub-committee to manage elements of the relationship. The organizational structure and the effectiveness of managing potential conflicts of interest will continue to inform our credit opinion.

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 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.

Exhibit 9

Grand Canyon University, AZ

Scorecard Factors and Sub-factors		Value	Score
Factor 1:	**Scale (15%)**		
	Adjusted Operating Revenue (USD Million)	1,374	Aa
Factor 2:	**Market Profile (20%)**		
	Brand and Strategic Positioning	Ba	Ba
	Operating Environment	Ba	Ba
Factor 3:	**Operating Performance (10%)**		
	EBIDA Margin	10%	A
Factor 4:	**Financial Resources and Liquidity (25%)**		
	Total Cash and Investments (USD Million)	386	A
	Total Cash and Investments to Operating Expenses	0.3	B
Factor 5:	**Leverage and coverage (20%)**		
	Total Cash and Investments to Total Adjusted Debt	0.3	B
	Annual Debt Service Coverage	1.3	Baa
Factor 6:	**Financial Policy and Strategy (10%)**		
	Financial Policy and Strategy	Ba	Ba
	Scorecard-Indicated Outcome		Baa3
	Assigned Rating		Ba1

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.

Fiscal 2023 values

Source: Moody's Investors Service

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