How Fit Is Your School? The Methodology Behind Forbes' 2019 College Financial Health Grades.

The majority of the nation's institutions of higher education are in precarious financial straits, as many tuition-dependent colleges compete to fill freshman classes in order to stay open. Forbes' sixth report on the financial health of private-not-for profit colleges finds that the overall financial well being of colleges has deteriorated and many are in danger of closing or merging. Student demand is tapering, tuition pricing (and discounting) is growing, and unfortunately many administrations and faculties are loath to adapt to this new reality.

This is not a moment; it's a trend. The outlook for the higher-education sector is negative, according to analysts at credit agencies Moody's and Fitch Ratings. And while both public and private schools are feeling the heat, according to Fitch's Emily Wadhwani, "The typical credit characteristics of a public institution are better suited for weathering with resilience declining demand. … In general, [private colleges] are more pressured than their public counterparts."

That pressure is painfully evident in Forbes' College Financial Health Grades. The number of D-graded colleges, those with GPA's less than 1.5, have swelled from 110 when we started grading finances in 2013 to 177 today—a 61% increase. Only 34 schools, including Harvard, Brown and MIT, earn A+'s.

To grade the schools, we used data from the Department of Education's IPEDS database. We averaged the figures from the two most recent "final release" fiscal years, 2016 and 2017. Only private not-for-profit colleges with at least 500 students and sufficient data were examined, and the lowest grade we gave out was a D.

The GPA's and grades measure financial health as determined by nine components:

1. Endowment Assets Per FTE (15%): This is year-end endowment assets divided by the number of 12-month full-time equivalent students. Denison University was the lowest-scoring school to still get full credit, with $337,980 per student; Columbia University got 14.9%, with $334,870. Eleven schools boast over $1,000,000 in endowment per student; only one, Princeton, eclipses $2 million.

2. Primary Reserve Ratio (15%): This "liquidity"-oriented ratio analyzes how well a university's "expendable assets" could quickly cover its annual expenses without straining its normal operations. Expendable assets are defined as total unrestricted net assets, plus temporarily restricted net assets plus debt related to property, plant and equipment, minus property, plant and equipment net of accumulated depreciation, divided by total annual expenses. Schools needed just beneath a ratio of 2.5, or two years and six months, to get full credit. Grinnell College in Iowa—whose endowment fund was once under the stewardship of Warren Buffett—is once again the top score, with a ratio over 14. University of Pennsylvania, despite its A+ grade, slides in just under 1.0.

3. Viability Ratio (10%): Similar to the primary reserve ratio, the viability ratio measures the amount of expendable assets a college has relative to its debt load. Many colleges carry no debt and therefore received full credit. The cutoff for a perfect score is just above 2.5. Dartmouth has a ratio of 4.8. Davis & Elkins College, a tiny school in Appalachia, was in the midst of a $100 million fundraising campaign during the years pulled for the list; by paying down its debt, it had a viability ratio of over 65—and the school now boasts no debt, according to its president, Chris Wood.

4. Core Operating Margin (10%): This measures operating profit, otherwise known as “surplus.” We looked at core revenues for education, as measured by the DOE, minus core expenses. In other words, how well is a college meeting its annual obligations, like instruction expenses and student services, from the tuition, grant, gift, contract and investment revenue it takes in? Of the 933 schools ranked, 384 had negative margins. Standouts like Bates College and Berea College got near perfect scores, with operating margins around 43%.

5. Tuition As A Percentage of Core Revs (15%): Tuition-dependent schools, where tuition revenues account for more than 60% of their core revenues, tend to be at higher risk. Price discounting can have a big effect on these schools’ viability, and enrollment shortfalls can mean budget misses, and potentially layoffs or cost cutting. Any college where tuition dependency is less than 10% of revenues gets a perfect score. Three schools rely on tuition for less than 5% of their revenues: College of the Ozarks, California Institute of Technology and Grinnell College.

6. Return On Assets (10%): This metric divides the change in net assets over the year for an institution by the assets at the beginning of the year. This answers the simple question of whether an institution’s assets are actually growing. Only 204 saw their assets shrink; online degree leader Southern New Hampshire University, which Forbes profiled in March, earned a perfect score with an over 30% ROA.

7. Admission Yield (10%): Is a college students’ first choice, or a last choice? This measure looks at the percentage of admitted students who actually choose to enroll. For this metric, we averaged the last three available years of data. Near the top of the pack is College of the Ozarks (profiled by Forbes in 2018), with an average yield over 89%. Meanwhile, colleges like High Point University and Drexel University have safety-school-type ratios, of less than 20%.

8. Percent Freshman Getting Institutional Grants (7.5%): Turns out, giving out merit scholarships does not necessarily mean a school is well-endowed and generous; it may just be desperate. This figure measures the percentage of students getting discounts, otherwise known as institutional grants, to entice enrollment. Schools where the percent is less than 40%, like Wake Forest University and Tufts University, get full credit. Fordham University and Wofford College got half credit because 90% of their first-year students receive institutional grants.

9. Instruction Expenses Per FTE (7.5%): This measure is an indicator of how much funding the particular institution devotes to the core mission of higher education per full-time-equivalent student. Washington University in St. Louis, Yale and Stanford all spend over $100,000 per student, though spending over $45,000 per student got a perfect score. The College of Idaho, graded an A, spends less than $10,000 on instruction.

Forbes.com

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Nov 27, 2019