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Arizona College's Mega-Borrowing Breaks Bond-Market Ground.

- **Grand Canyon University sells $1.2 billion of junk-rated bonds**
- **It's first college corporate junk-bond deal: Bloomberg data**

A private university in Arizona broke new ground in the fixed-income universe this month with a $1.2 billion debt sale, in the first junk borrowing to hit the corporate-bond market from the higher-education sector.

The sale by Grand Canyon University, a mostly online college in Phoenix that was founded in 1949, stands out among the pristine school credits that typically bring large corporate deals. Those issuers are often top-rated Ivy League names, with endowments in the billions of dollars. Grand Canyon University is rated Ba1 by Moody's Investors Service, one step below investment grade, and according to Bloomberg data, its bond issue is unprecedented.

The sale, which closed Thursday, comes as returns on junk-rated corporate and municipal debt are outpacing the broader U.S. bond market by a wide margin in 2021 as yields remain historically low. Although the debt went through the corporate market and is taxable, it also drew the attention of muni buyers. They were following it for its novelty and extra yield, and also because of their familiarity with higher-ed borrowers, which often sell tax-exempt securities.

Grand Canyon University is one of the nation's largest Christian universities, with over 113,400 students enrolled as of the end of September, according to bond documents. While many are online, the school has grown its Phoenix campus as well. There are over 23,600 in-person students, almost 10 times the number in 2008. Net revenue in fiscal 2021 totaled $1.3 billion.

"The uniqueness of the bond structure is reflected in the uniqueness of the university," Brian Mueller, president of the school, said in an interview.

The school was founded as a nonprofit, but after its finances struggled, a group of investors formed a company and turned it into a for-profit university in 2004, bond documents say. According to the documents, in 2018, it transitioned back to a non-profit, and sold senior secured debt that year to finance the $876.6 million purchase of those assets.

The U.S. Department of Education doesn't recognize the school as a nonprofit. But that doesn't impact the school's ability to attract students, bond documents say. According to Moody's, it's recognized as a nonprofit by the Internal Revenue Service, the Higher Learning Commission — the university's regional accreditor — and the state of Arizona.

The proceeds of this month's sale will be used in part to refinance that 2018 note. Mueller said the move has generated savings, but declined to specify an amount.

Evident Lure

For buyers seeking extra yield and comfortable with the risk, the lure of the deal is evident. A portion that matures in 2028 sold with a 5.125% yield, compared with about 3.5% on a Bloomberg index of similarly rated debt. Seven-year Treasuries yield about 1.45%.

Moody's gives the bonds a stable outlook and says the university benefits from its "clear market niche" of online education. But it also says the school's high debt level compared to its cash and investments weighs on the rating, and added that the competition for online students will intensify over the next decade.

The admission rate for what the school calls traditional students — who take class on campus — was about 80% in fall 2020, when applications climbed to 48,918, from 34,096 in 2016, bond documents show.

Junette West, the vice president of business and finance, said the school conducted about 25 investor calls for the transaction.

"There was quite a bit of interest," she said.

Higher-ed issuers have sold about $4 billion of corporate debt this year, including offerings from the top-rated Massachusetts Institute of Technology as well as Howard University, which is one step above junk. That's a bit above the $3.6 billion average since 2010, data compiled by Bloomberg show.

Last year, with long-term borrowing costs near record lows and the pandemic straining finances, such issuance set a record $11.7 billion.

'Pathbreakers'

That boom, which included sales from well-known issuers, increased corporate investors' comfort with higher-education credits, which benefited Grand Canyon University this month, said John Augustine, who leads higher-ed finance for Barclays Plc, the deal's sole underwriter.

"Those were the pathbreakers for Grand Canyon University," he said in an interview. "People saw the success of those billion-dollar-plus plus higher-ed transactions, both in terms of pandemic needs and refunding needs. That did play to their advantage."

The offering drew interest from investors such as insurers and bond funds, Augustine said in a release from the school.

The university intends to grow in-person enrollment to 40,000 and online enrollment by an average of 5% to 6% per year, bond documents say.

Mueller said the school doesn't have plans to sell debt again to fund that growth. It plans to invest $500 million to expand its campus, financed from cash, he said. He said he expects its credit rating to rise to investment grade in the next year or two.

"In the past, small and elite has won the day," he said. "And in the future, it's going to be larger and very flexible."

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By Amanda Albright

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— With assistance by Jack Pitcher, Gowri Gurumurthy, and Dan Wilchins