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MATERIAL POLICY HEADWINDS FOR PRIVATE HIGHER ED ARE LIKELY MANAGEABLE INVESTMENT RISKS

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Key Takeaways

- Federal policy actions present new risks for many private higher education (higher ed) institutions.
- The federal government appears poised to reduce research funding, change accreditation standards, impose new taxes, and limit the generosity of student aid as it relates to private higher education providers.
- However, the impact on bond portfolios may prove modest as the sector is a relatively small part of the Bloomberg (BBG) Municipal Bond Index¹ (the Index) and new policies mostly impact the market's most resilient issuers.
- In addition, the scope and impact of regulation may change over time.
- And, we believe that issuers may find creative solutions in tandem with state or local government partners.

1. The Bloomberg Municipal Bond Index is an unmanaged index considered representative of the broad market for investment-grade municipal bonds. Bonds in the index have remaining maturities of at least one year. You cannot invest directly in an index.



Regulatory policy in the second Trump administration may exacerbate secular risks for private higher ed bond issuers. The administration has threatened some universities' tax-exempt status. It has frozen federal grant aid for others. Accreditation standards and rules around foreign student enrollment are likely to change. Endowment taxes may rise substantially.

Altogether, the policy environment is likely to further constrain flexibility for issuers. Fortunately, the impact on portfolios is likely to be modest. Private higher education debt represents a small portion of major indices, and the high quality, brand-name issuers most exposed to federal scrutiny are likely to prove more resilient than lower-investment grade (IG) or non-rated peers.

Over the longer term, some of today's policy choices may be adapted to, overcome, abandoned, or reformed. In some cases, state and local governments may opt to support private higher education entities that are essential to regional growth.

HIGHER EDUCATION FACES SECULAR CREDIT RISKS.

As Breckinridge highlighted in its 2024 and 2025 Municipal Market Outlooks, the private higher ed sector faces a variety of secular credit risks, including:

Weak demographics. The number of U.S. high school graduates is expected to peak in 2025 and decline steadily through 2041.² Thirty-eight (38) states will bear the entire decrease, including more significant declines in the Midwest and Northeast. A sharper fall-off in college enrollment seems likely. Already, one-fifth of schools reported enrollment declines of 20 percent or more in the fiscal year 2016 through 2023 (FY16 – 23) period (See Figure 1).

FIGURE 1: PRIVATE UNIVERSITY ENROLLMENT HAS DECLINED IN RECENT YEARS



Source: Merritt Research Services and Breckinridge Capital Advisors, Inc., as of November 2024.

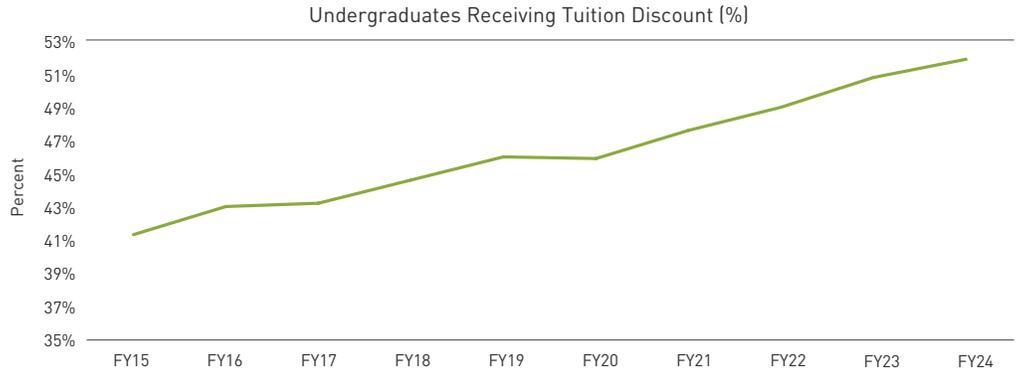
Competition and revenue pressure. As the pool of eligible students shrinks, private colleges and universities are likely to experience further pressure on margins. From FY15 to FY24, the average tuition discount rose from 41 percent to 52 percent across the sector (See Figure 2). The average endowment draw rose from 3.6 percent to 6.6 percent of revenue.³

2. "Knocking at the College Door: Projections of High School Graduates," Western Interstate Commission for Higher Education (WICHE), December 2024. Available at: <https://www.wiche.edu/resources/knocking-at-the-college-door-11th-edition/>.

3. Breckinridge analysis of 666 private universities in a Merritt Research Services database, reporting from FY 15 to FY 24.



FIGURE 2: TUITION DISCOUNTING HAS INCREASED AS SCHOOLS COMPETE FOR STUDENTS

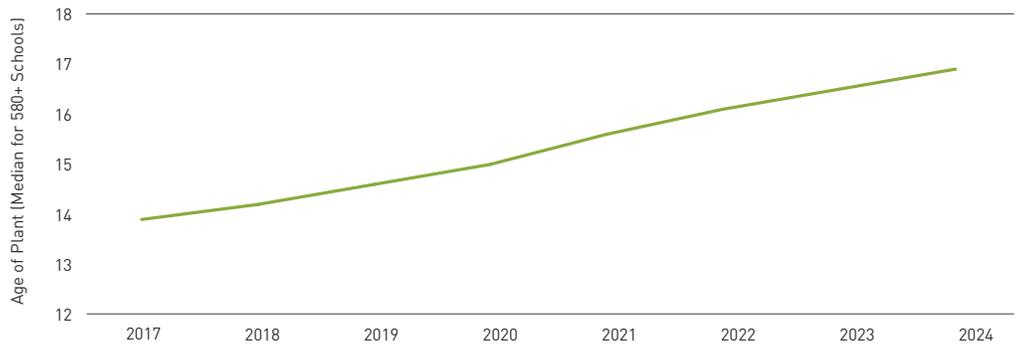


Source: National Association of College & University Business Officers and Breckinridge Capital Advisors, Inc., as of May 2025.

Value proposition. Schools are also competing more directly against lower cost options. This includes reputable online offerings like those from Southern New Hampshire University.⁴ It also includes community colleges, more of which are offering four-year baccalaureate degrees.⁵ Expensive private colleges are competing more often with public universities offering a lower price point.⁶

Deferred maintenance. Operating stress has caused more universities to shortchange capital spending. Age-of-plant (a measure of infrastructure upkeep) has increased from under 14 years to nearly 17 years since 2017 (See Figure 3).

FIGURE 3: DEFERRED MAINTENANCE IS A GROWING CHALLENGE AT MANY PRIVATE UNIVERSITIES



Source: Merritt Research Services and Breckinridge Capital Advisors, Inc., as of May 2025.

4. Penprase, "The Mega-Universities Disrupting Higher Education," Forbes, December 2, 2024. Available at: <https://www.forbes.com/sites/bryanpenprase/2024/12/02/the-mega-universities-disrupting-higher-education/>.

5. Hudson, "Community College Expand Four-Year Degree Options as Illinois Joins National Trend," Diverse Issues in Higher Education, April 1, 2025, available at: <https://www.diverseeducation.com/institutions/community-colleges/article/15741004/community-colleges-expand-four-year-degree-options-as-illinois-joins-national-trend>.

6. "Shifting consumer preferences leave many colleges in the middle struggling for revenue," Moody's Investors Service, January 23, 2025.



FEDERAL POLICY CHOICES LIKELY TO ADD TO CREDIT PRESSURES

The second Trump administration and Congress seek to change the private higher education sector in ways that further limit issuers' financial flexibility. Since taking office in January, policymakers have:

Considered revoking the tax-exempt status of certain universities. Most prominently, the administration has sought to rescind Harvard University's 501(c)(3) status. We anticipate this effort will fail, but should it succeed, it would increase the cost of borrowing for Harvard and set a precedent for other schools across the country.

Frozen federal grant payments and threatened to withhold future grants. Grant aid was rescinded from the University of Maine over its transgender-athlete policies.⁷ The Department of Education froze \$510 million to Brown University over its handling of on-campus antisemitism.⁸ Cornell University had \$1 billion frozen and Northwestern University \$790 million, among others.⁹ Swiftly rescinding grant funds this way is of questionable legality.¹⁰ But in the medium-term, a more austere federal funding environment is likely for some portion of research universities.¹¹ Reductions in grants for the National Institutes of Health, Centers for Disease Control, and other health-related spending may be a particular negative for higher education systems with academic hospital affiliates. The federal reimbursement rate for indirect costs also has been reduced for a mix of grants.¹²

Sought accreditation reforms. Pell Grants and Direct Loans may be applied to the cost of attendance solely at accredited colleges and universities.¹³ An April 23, 2025, executive order hints at reforming the accreditation process to make it harder for universities with an active diversity, equity, and inclusion (DEI) program or culture to earn accreditation.¹⁴ Unaccredited universities would find it much harder to attract students.

Proposed an increase in the private college endowment tax. The House Ways and Means Committee's reconciliation bill increases the endowment income tax from 1.4 percent to as high as 21 percent for endowments exceeding \$2 million per U.S. student.¹⁵ The change would raise \$6.7 billion over 10 years for the federal government and apply to a limited number of schools (See Figure 4), but it would reduce the ability of each to subsidize tuition and other costs of attendance.¹⁶

FIGURE 4: ONLY EIGHT UNIVERSITIES ARE LIKELY TO PAY THE TOP ENDOWMENT TAX RATE

NUMBER OF SCHOOLS	AVERAGE ENDOWMENT (\$BILLIONS)	LIKELY RATE
8	\$24.5	21%
9	\$5.4	14%
16	\$5.2	7%
24	\$3.7	1.4%

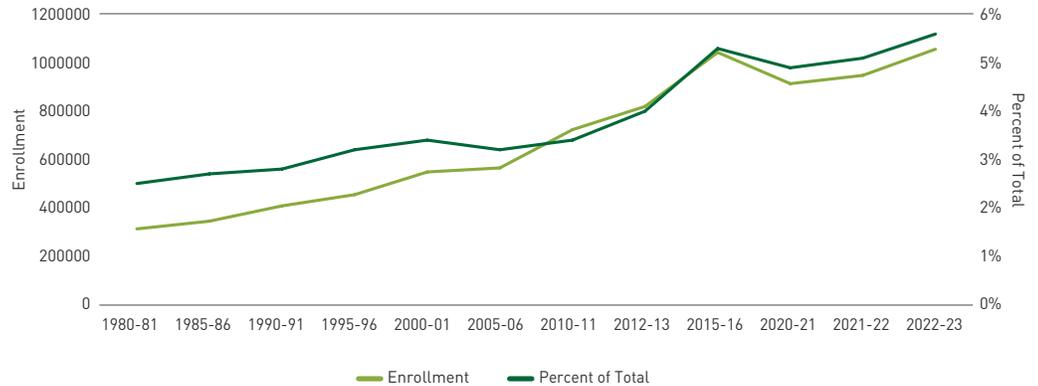
Merritt Research Services and Breckinridge Capital Advisors, Inc., as of May 2025.

7. "USDA suspends Maine university funding after Trump row over transgender athletes," Reuters, March 12, 2025. Available at: <https://www.nbcnews.com/nbc-out/out-politics-and-policy/usda-suspends-maine-university-funding-trump-row-transgender-athletes-rcna196011>.
8. Greenberg, "Brown Becomes Latest Institution to Have Federal Grants Frozen," Inside Higher Ed, April 4, 2025. Available at: <https://www.insidehighered.com/news/quick-takes/2025/04/04/trump-administration-block-browns-federal-grants>.
9. Knott, "Trump Freezes Federal Funding at Northwestern and Cornell," Inside Higher Ed, April 8, 2025. Available at: <https://www.insidehighered.com/news/quick-takes/2025/04/08/northwestern-cornell-face-federal-funding-freeze>.
10. For example, the administration's approach may violate the First Amendment (see: Nat'l Rifle Ass'n v. Vullo, 602 US 175, 189 (2024) and procedural requirements associated with ending a college's federal grant aid (42 USC 2000d-1).
11. Schmidt, Blinder, "Harvard Leaders See Only Bad Outcomes Ahead as They Battle Trump," New York Times, May 8, 2025. Available at: <https://www.nytimes.com/2025/05/08/us/harvard-trump-court-case-negotiation.html>.
12. For example, National Science Foundation grant indirect cost reimbursement has declined to 15%: <https://www.nsf.gov/funding/proposal-budget/indirect-costs>.
13. Hegji, "An Overview of Accreditation of Higher Education in the United States," Congressional Research Service, April 12, 2024.
14. Executive Order, "Reforming Accreditation to Strengthen Higher Education," April 23, 2025. Available at: <https://www.whitehouse.gov/presidential-actions/2025/04/reforming-accreditation-to-strengthen-higher-education/>.
15. Description of the Tax Provisions of the Chairman's Amendment in the Nature of a Substitute to the Budget Reconciliation Legislative Recommendations Related to Tax, Joint Committee on Taxation, p. 325 (May 13, 2025). Available at: <https://waysandmeans.house.gov/wp-content/uploads/2025/05/JCT-Description-of-AINS-to-WM-Committee-Report-Green-Sheet.pdf>.
16. Estimated Revenue Effects of Provisions to Provide for Reconciliation of the Fiscal Year 2025 Budget, Fiscal Years 2025- 2034, p. 5, Joint Committee on Taxation, May 13, 2025. The eight schools impacted by the top endowment tax rate are: Princeton, Harvard, Yale, M.I.T., Stanford, Juliard, Amherst College, and (perhaps) the Princeton Theological Seminary. The last name on this list might be exempted given its religious affiliation.



Disincentivized foreign enrollment. Schools with many foreign students may be subject to the endowment tax in unexpected ways. The tax is imposed on a per-U.S.-student basis; foreign students are excluded from the denominator. This increases the per-student level reported by many colleges and pushes some smaller endowments into the taxable category. It could reduce the incentive to enroll foreign students who often pay full tuition. Nationwide, colleges have increasingly relied on this income. Nearly 6 percent of post-secondary students are now from abroad (See Figure 5).

FIGURE 5: THERE ARE OVER ONE MILLION FOREIGN UNIVERSITY STUDENTS IN THE U.S. REPRESENTING MORE THAN 5% OF TOTAL ENROLLMENT



Recent immigration enforcement actions also may deter foreign students from studying in the U.S. In late May, the administration sought to bar Harvard from enrolling foreign students.¹⁷ Through late April 2025, the administration had moved to cancel over 1,500 student visas in the U.S., often with little notice.¹⁸

Tightened student loan lending rules. On May 5, the Department of Education restarted involuntary collections on defaulted student loans.¹⁹ The decision comes almost two years after pandemic-era loan forbearance was ended.²⁰ The House reconciliation bill may impose liability on universities when students default on their loans.²¹ The end of loose financing policies may further slow enrollment.

The overall federal policy environment caused Moody's Investors Service to place a "negative outlook" on the higher ed sector in March 2025.²²

THE RISKS ARE NONETHELESS MANAGEABLE

Despite credit headwinds, private university holdings are unlikely to meaningfully alter many high-grade muni investors' portfolios. The sector has underperformed year-to-date with the Bloomberg Education Index down 1.2 percent, compared to the broad Bloomberg Municipal Bond Index down only 0.75 percent.²³ However, private university debt comprises only a small portion of the broad market (See Figure 6).

17. Hackman, "Trump Administration Blocks Harvard from Enrolling Foreign Students," The Wall Street Journal, May 22, 2025.

18. Montague and Aleaziz, "U.S. Restores Legal Status for Many International Students, but Warns of Removals to Come," The New York Times, April 25, 2025.

19. "U.S. Department of Education to Begin Federal Student Loan Collections, Other Actions to Help Borrowers Back into Repayment," Press Release, April 21, 2025. Available at: <https://www.ed.gov/about/news/press-release/us-department-of-education-begin-federal-student-loan-collections-other-actions-help-borrowers-get-back-repayment>.

20. See Federal Student Loan Portfolio data, available at: <https://studentaid.gov/data-center/student/portfolio>.

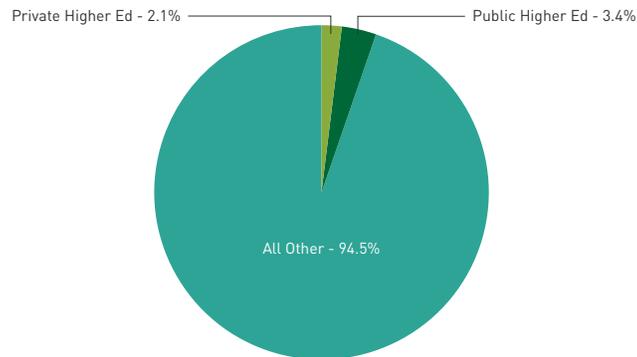
21. Blake, "House GOP Wants to Put Colleges on the Hook for Unpaid Loans. How Would it Work?" Inside Higher Ed, May 19, 2025. <https://www.insidehighered.com/news/government/politics-elections/2025/05/19/whats-house-republicans-risk-sharing-plan>

22. "US: Outlook revised to negative as federal policy actions raise risk across the sector," Moody's Investors' Service, March 18, 2025.

23. InvestorTools Perform data, YTD through May 16, 2025.



FIGURE 6: PRIVATE UNIVERSITY DEBT COMPRISES A SMALL PORTION OF THE BBG MUNICIPAL BOND INDEX (% OF INDEX)



Source: Bloomberg Municipal Bond Index and Breckinridge Capital Advisors, Inc., as of May 2025.

Additionally, current federal policy is focused on the highest quality schools. Only 17 schools will likely be subject to an endowment income tax of 14 percent or more (See Figure 4). Investigations into on-campus antisemitism are concentrated among well-resourced colleges.²⁴ Cuts to research and development (R&D) funding are expected to impact a small number of issuers.²⁵

Affected universities are likely to meet current challenges by adapting to regulations or overcome them. Elite colleges can tap broad alumni donor bases and issue taxable bonds to shore up liquidity.²⁶ Schools are likely to alter endowment-spending and investing policies to stay below income-cap levels and/or avoid reporting enough income to incur taxes, each year. Other issuers are likely to expand their brands by offering new degrees to more domestic students. Numerous schools have already imposed hiring freezes and are right-sizing expenditures.²⁷

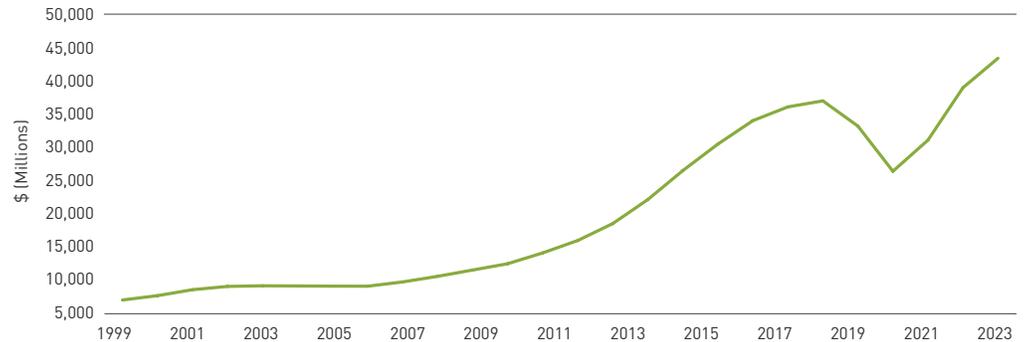
Restrictions on foreign-student enrollment can likely be managed, in the near-term, as well, at least at top-flight universities. For perspective, we estimate that foreign student tuition comprises 7 to 8 percent of Harvard's annual revenue. If needed, the school could increase its admission rate modestly and backfill enrollment declines with a well-qualified domestic talent pool.

Some federal policies are likely to be abandoned or reformed. Courts are likely to reinstate at least a portion of currently frozen grant aid.²⁸ The endowment tax, which exempts sectarian universities, may flout the Constitution's Establishment clause and require adjustments or elimination.²⁹ There is bipartisan support for attracting highly skilled workers and foreign students (the "best and brightest").³⁰ And limiting foreign student enrollment is likely to swell the trade deficit, not shrink it, given that net exports of education services have risen rapidly in recent decades (See Figure 7).

24. Kelchen and Novicoff, "Are Gaza Protests Happening Mostly at Elite Colleges?," Washington Monthly, May 24, 2024. See also, the list of colleges that have received letters from the Department of Education's Office for Civil Rights, available at: <https://www.ed.gov/about/news/press-release/us-department-of-education-office-civil-rights-sends-letters-60-universities-under-investigation-antisemitic-discrimination-and-harassment>.
25. "Federal policies create heightened risk environment for colleges and universities," Moody's Investors Service, April 28, 2025.
26. Albright, "MIT Joins Deluge of Colleges Selling Bonds Amid Funding Threats," Bloomberg, May 5, 2024. Available at: <https://www.bloomberg.com/news/articles/2025-05-05/mit-joins-deluge-of-colleges-selling-bonds-amid-funding-threats>.
27. Associated Press, "Some Universities Are Freezing Hiring and Laying off Staff as Trump Cuts Federal Funding," U.S. News and World Report, March 13, 2025. <https://www.usnews.com/news/us/articles/2025-03-13/some-universities-are-freezing-hiring-as-trump-threatens-federal-funding>
28. Yu and Yu, "Experts Say Harvard Has a Strong Case in legal Battle Against Trump," Harvard Crimson, April 23, 2025.
29. Saulnier, "A higher Power in Hiegher Education: An Exploration of Endowment Taxes, the Establishment Clause, and College Affordability," Boston College Law Review, Vol. 65, Issue 7, 2024. The Establishment Clause of the First Amendment to the U.S. Constitution prohibits the government from establishing a state religion or favoring one religion over another.
30. "The incoming administration should spearhead an immigration legislative agenda focused on creating a merit-based immigration system that rewards high-skill aliens... and the existing employment visa program should be replaced with a system award visas to the "best and brightest." "Mandate for Leadership" (project 2025 document), Heritage Foundation, p. 145 [2023]. See also Yuri Mamchur, "President Trump, Please Staple [Conditional] Green Cards to Graduate Degrees," National Review, February 19, 2025. <https://www.nationalreview.com/2025/02/president-trump-please-staple-conditional-green-cards-to-graduate-degrees/>



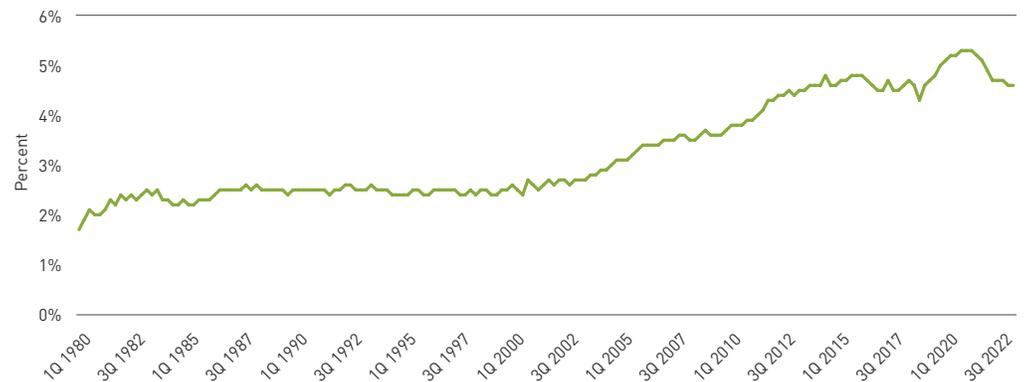
FIGURE 7: NET EXPORTS OF EDUCATION-RELATED SERVICES HAVE GROWN SUBSTANTIALLY IN RECENT YEARS



Source: Bloomberg Municipal Bond Index and Breckinridge Capital Advisors, Inc., as of May 2025.

In some instances, state and local governments are likely to provide private universities with financial support. For example, the education and healthcare sectors comprise large portions of gross product in Baltimore (21 percent), Philadelphia (20 percent), and New Haven (19 percent) counties. Each is home to major research universities and several affiliated academic medical centers.³¹ Replacing lost research funding for these centers may prove a good investment. Historically, only a small portion of state and local capital spending has flowed to R&D, but an uptick is possible if today's more austere federal policy bias proves long-lasting (See Figure 8).

FIGURE 8: R&D SPENDING HAS RISEN BUT REMAINS A SMALL PORTION OF OVERALL STATE AND LOCAL CAPITAL EXPENDITURES



Source: Bureau of Economic Analysis and Breckinridge Capital Advisors, Inc., May 2025.

In the unlikely scenario that Congress or the federal government strips tax-exempt status from economically essential private universities, states might facilitate their conversion to public entities. This kind of creative solution would likely be undertaken only as a last resort. But public universities are subject to no income taxes, may be able to avoid any proposed endowment or foundation tax, and would retain access to the tax-exempt bond market under current law. New Jersey made Rutgers University a public instrumentality in 1956.³² Virginia converted the College of William & Mary to a public university in 1906.³³

31. Breckinridge calculation based on Bureau of Economic Analysis data, 2023.

32. N.J.S.A. 18A:65-1 (Public Law 1956, chapter 61).

33. William & Mary Library, Special Collections Research Center, The Charter, The Transfer, and The Acts of 1888 and 1906. Available on-line: <https://libraries.wm.edu/exhibits/charter-transfer-and-acts-1888-and-1906>.



CONCLUSION

Recent federal policy action in the private university space portends a more austere medium term financial picture for some name brand municipal issuers. The federal government appears poised to reduce research funding, change accreditation standards, impose new taxes, and limit the generosity of student aid as it relates to private higher education providers.

Nonetheless, Breckinridge anticipates that most of these actions will only modestly impact high-grade municipal bond investors' portfolios. Private university bonds likely comprise a small portion of most investors' portfolios, based on their small representation in the Index (See Figure 6). As currently proposed, new policies will often impact issuers often considered to be the market's most resilient. Workarounds, reforms, and lawsuits are likely. In some cases, state and local governments may step up to support issuers.

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