MOODY'S
INVESTORS SERVICE

CREDIT OPINION
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Update

Contact

Eva Bogaty 415-274-1765
VP-Senior Analyst
eva.bogaty@moodys.com

Pranav Sharma 212-553-7164
AVP-Analyst
pranav.sharma@moodys.com

Diane F. Viacava 212-553-4734
VP-Sr Credit Officer
diane.viacava@moodys.com

University of San Francisco, CA

Update - Moody's affirms University of San Francisco, CA's A2; outlook stable

Summary Rating Rationale

Moody's Investors Service has affirmed University of San Francisco, CA's A2 rating. The rating reflects the university's relatively larger scale, with over 10,000 students, growing revenue and reserves. USF has good strategic positioning as an urban Jesuit comprehensive university in San Francisco with a large graduate student population, and healthy philanthropic support and accumulated reserves.

These factors are counterbalanced by thinning operations due to slower net tuition revenue growth, and weak and variable matriculation of incoming students making budgeting difficult. Unrestricted giving, operating reserves, and growth in liquidity and total cash and investments will help the university absorb below-budget freshmen enrollment of fall 2015. The university's debt structure poses some remarketing and acceleration risk which is mitigated by good headroom under the covenants, and more than sufficient liquidity to repay the debt.

Credit Strengths

» Urban location, Jesuit niche and substantial graduate and professional enrollment bolster market profile and add stability and top-line revenue growth

» Substantial accumulated reserves, and growing liquidity with 217 days cash through careful budgeting and gifts

» Responsive fiscal management leading to three-year average operating margin of 6.4%, and at least break-even in fiscal (FY) 2016 despite lower than anticipated enrollment

» Growing philanthropic support for capital plan and strategic initiatives, with $26 million of gift revenue

Credit Challenges

» Highly competitive student market evidenced by low 13% matriculation of incoming students and 2% contraction in net tuition per student

» Concentrated revenue with almost 90% derived from student charges

» Recent turnover of key academic and admissions personnel requires careful transition as USF seeks to stabilize freshman matriculation

» Weakening operations as expense growth has outpaced revenue growth

» Debt structure adds counterparty and rollover risk with 45% variable rate debt with financial covenants, and swaps

Rating Outlook

The stable outlook incorporates expectations of at least FY 2016 break-even operations with stronger cash flow in FY 2017 from stabilized enrollment and financial aid and expense controls.

Factors that Could Lead to an Upgrade

» Substantial growth in cash and investments, particularly unrestricted reserves

» Improved student demand, including resumption of growth of net tuition per student, stabilization of freshmen enrollment and improved matriculation

Factors that Could Lead to a Downgrade

» Further weakening of operations in FY 2017

» Failure to make fall 2016 budget for incoming class

Key Indicators

Exhibit 1

UNIVERSITY OF SAN FRANCISCO, CA					
	2011	2012	2013	2014	2015
Total FTE Enrollment	9,472	9,669	9,773	10,297	10,828
Operating Revenue ($000)	294,889	310,361	333,628	346,245	355,869
Annual Change in Operating Revenue (%)	12.6	5.2	7.5	3.8	2.8
Total Cash & Investments ($000)	347,660	326,122	355,874	409,453	451,977
Total Debt ($000)	162,595	186,200	180,825	175,440	169,685
Spendable Cash & Investments to Total Debt (x)	1.5	1.2	1.3	1.6	1.9
Spendable Cash & Investments to Operating Expenses (x)	1.0	0.8	0.8	0.9	0.9
Monthly Days Cash on Hand (x)	238	200	190	203	217
Operating Cash Flow Margin (%)	20.8	17.9	16.9	14.8	12.1
Total Debt to Cash Flow (x)	2.6	3.4	3.2	3.4	4.0

Source: Moody's Investors Service

Recent Developments

Recent developments are incorporated in the Detailed Rating Rationale.

Detailed Rating Rationale

Market Profile: Urban Location and Substantial Graduate Programming Add Stability

USF's diverse programming, Jesuit niche and urban location in economically vibrant San Francisco are a competitive advantage. Strategic positioning is very good with its location, strong reinvestment in campus facilities and solid demand for graduate and professional programs offsetting tough competition for undergraduates. Enrollment will remain stable in the near term at over 10,000 FTE students, with growth in graduate and professional programs balancing flat to declining undergraduate enrollment.

Fall 2015 was a particularly weak admissions year with matriculation of under 13% and the freshmen and transfer classes missing the budget by several hundred students. Weak enrollment was due to an aggressive change in admissions strategies attempting to improve selectivity and reduce tuition discounting at the same time. University staff acted quickly to evaluate and address the issues and has rolled out a new, moderated and higher touch admissions and financial aid strategy for fall 2016. This new strategy, which was developed with the help of several consultants, should stabilize freshmen and undergraduate enrollment.

USF's future ability to grow net tuition revenue is modestly stronger than many A2 peers, as higher-paying graduate and professional students represent almost 40% of enrollment. The university will likely resume growth of net tuition per student in the 3-4% range in FY 2017. Growth of net tuition per student slowed in recent years, with rising tuition discounting and low tuition increases, and after a 2.2% contraction in FY 2015 is expected to be flat again in FY 2016.

Operating Performance: Conservative Budgeting and Strong Oversight Balance Tuition Dependence

The university's careful fiscal stewardship and conservative budgeting are key credit considerations in the A2 affirmation and stable outlook. Operations have weakened in recent years, but remain solidly positive with 12% operating cash flow and good debt service coverage of over 3 times. Although net tuition revenue is expected to be approximately $5.5 million below budget in FY 2016, the university is forecasting a very thin surplus due to budgeted reserves and expense controls. FY 2016 operations will be further bolstered by an $8 million unrestricted gift, to likely produce improved cash flow. The university plans to return to surplus operations (without gifts) in FY 2017, as it institutes several expense cuts.

Weak revenue diversity with almost 90% derived from student charges is mitigated by the university's program diversity and large pool of graduate and professional students. Overall net tuition revenue will continue to grow at 4% or more, even with the gap in FY 2016.

Wealth and Liquidity: Gifts and Surpluses Support Capital Needs and Resource Growth

USF's resources will continue to provide sound cushion to debt and operations for the A2 rating. Total cash and investments cover debt at 2.7 times, just below the median of 3 times for private A-rated universities. Gift revenue, surpluses and investment returns contribute to continued growth of resources, allowing the university to support healthy capital investment and grow reserves.

The university is in the midst of a $300 million comprehensive campaign for which it has raised $70 million in cash and pledges. The campaign is expected to be completed in 2022. Gifts will support the endowment and scholarships, facilities ($75 million) and program support.

In order to meet high demand for student housing, USF is embarking upon a public-private partnership with a developer to complete a 600 bed housing facility. The university will ground lease the land to the developer, who would design and build the dormitory to USF's specifications. USF will lease the facility for a 20-year period, after which it will be donated to the university. The facility will be ready for students in summer 2019, at which point USF expects to report it as a capital lease. Given the housing need and its importance to the undergraduate recruiting process, the strategic benefits of this facility are credit positive.

Management reports minimal additional debt plans, with most capital needs to be met through fundraising.

LIQUIDITY

USF's liquidity is growing and sufficient relative to operations, with 217 monthly days cash, but remains slightly weaker than peers. Monthly liquidity of $191 million provides a healthy 2.5 times coverage of demand debt.

Leverage: Modest Leverage with Excellent Debt Affordability

The university's large annual principal amortizations and revenue growth and solid cash flow have allowed it to maintain a modest operating leverage position relative to peers. Debt affordability is high for the A2 rating at under 4 times debt to cash flow. This indicates a strong ability to absorb the modest debt and operating lease plans currently on the horizon.

DEBT STRUCTURE

The university's 44% variable rate demand bonds (VRDBs), with letter of credits and interest rate swaps pose manageable acceleration and counterparty risk given good liquidity. The majority of USF's debt is regularly amortizing with some larger bullet maturities in 2021 and 2023, for which the university has strong planning.

The 2012 Term Loan with JPMorgan Chase (JPMC) amortizes in small annual amounts and has a final payment due of $17 million as of 5/31/23. The university's Series 2000, 2003 and 2005B are VRDBs backed by letters of credit (LOC) from JPMC which are up for renewal in February 2017.

All of the university's debt contain certain covenants which, if breached, could result in acceleration of the bonds and loan, or the university having to post all of its gross unrestricted revenues into a bondholder trustee-held collateral fund. The JPMC agreements contain financial covenants to maintain a liquidity ratio greater than 60%, reported twice a year, and debt service coverage of at least 1.2 times. USF exceeds these with ample 290% and 2.5 times coverage at May 31, 2015. Under the Series 2011 bonds, the university must generate revenue such that maximum annual debt service is less than 10% of USF gross unrestricted revenues (8.5% as of 5/31/15, and projected at 7.5% for FY 2016 and beyond) and enroll more than 4,400 FTE.

DERIVATIVES:

DEBT-RELATED DERIVATIVES

USF has four swaps with Bank of America to hedge its variable rate debt. The swaps have limited credit risk given the university's good liquidity, and lack of collateral posting requirements. The university is, however, required to meet certain covenants (unrestricted net assets to debt of 60% and WASC accreditation for the law school) should it choose to amend the swaps. Should the university fail to meet these covenants once the documents have been amended, the agreements will terminate.

PENSIONS AND OPEB

The university's exposure to pension and other post-employment health benefits is extremely limited. Participation in a defined contribution pension plan and a long-closed deferred compensation plan offers the university legal flexibility to change contributions. Currently pension related expenses are approximately $15,000, a manageable 4% of total operations.

Governance and Management: Sound Fiscal Stewardship and Improved Oversight with Key Personnel Transition

The university's sound fiscal stewardship underpins the A2 rating. Conservative budgeting, multi-year forecasting, regular budgetary oversight and nimbleness at addressing shortfalls add stability and flexility to act strategically.

Senior leadership and the board acted quickly to resolve issues from the recent admissions shortfall, and have strengthened oversight and management of admissions. Two key leadership positions are currently being filled, with a new provost joining in February 2016 and an open search for a new Director of Admissions. The successful integration of these personnel will be pivotal in the university's ability to resume stability in undergraduate admissions.

Legal Security

Bonds are secured by a gross unrestricted revenue pledge of the University of San Francisco and a negative pledge on the main campus

Use of Proceeds

Not applicable

Obligor Profile

The University of San Francisco is a large, urban Jesuit university with over 10,000 full-time equivalent students and $356 million of operating revenue. The university is located in the city of San Francisco.

Methodology

The principal methodology used in this rating was Global Higher Education published in November 2015. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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Contact

Eva Bogaty 415-274-1765
VP-Senior Analyst
eva.bogaty@moodys.com

Diane F. Viacava 212-553-4734
VP-Sr Credit Officer
diane.viacava@moodys.com

Pranav Sharma 212-553-7164
AVP-Analyst
pranav.sharma@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

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