New Issue: MOODY'S ASSIGNS A3 RATING TO UNIVERSITY OF SAN FRANCISCO'S $80 MILLION OF SERIES 2011 REVENUE BONDS; OUTLOOK REMAINS POSITIVE

UNIVERSITY WILL HAVE $167 MILLION OF PRO-FORMA DEBT, INCLUDING CURRENT OFFERING

California Educational Facilities Authority
Higher Education
CA

Moody's Rating

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Moody's Outlook Positive

Opinion

NEW YORK, Jan 10, 2011 -- Moody's Investors Service has assigned an A3 rating to the University of San Francisco's ("USF" or the "University") Series 2011 revenue bonds issued through the California Educational Facilities Authority ("CEFA"). The sale was originally scheduled for November 1, 2010 and is now expected to sell on January 24, 2011. At the same time, Moody's has affirmed the A3 rating on the University's outstanding Series 2005A and 2006 bonds, which are expected to be refinanced by the current offering. Following the refinancing, the University will have $166.4 million of outstanding debt, $84.2 million of which is variable rate debt enhanced by letters of credit.

The University's Series 2000 and 2003 bonds are presently supported by letters of credit (LOCs) from Allied Irish Bank ("AIB") (rated Baa3/P-3), and the Series 2005 bonds are supported by a Bank of America (rated Aa3/P-1) LOC. USF expects to substitute all three letter of credits with ones from JP Morgan Chase Bank N.A. (rated Aa1/P-1) expected to occur on or before February 7, 2011. For complete details of the letter of credit substitution, please see our forthcoming report.

RATINGS RATIONALE: The rating is based on the University's solid market position supported by healthy net tuition per student growth, the University's prudent fiscal management which has resulted in positive operating performance, solid balance sheet cushion and healthy liquidity profile supporting a debt profile with variable rate exposure.

LEGAL SECURITY: Gross unrestricted revenue pledge of the University of San Francisco and a negative pledge on the main campus.

PURPOSE: The current offering will refund the University's outstanding Series 2005A and 2006 auction rate series and to fund certain capital improvement projects on campus.

DERIVATIVES: The University has been an active user of interest-rate swap agreements related to its variable rate debt, with five LIBOR-based agreements now in place with Bank of America (rated Aa3/P-1) as the counterparty. The University plans to terminate portions of the swap agreements associated with the Series 2005A and 2006 auction rate series, and to apply the non-terminated portion to the currently unhedged Series 2000 and 2003 variable rate demand bonds. As December 31, 2010, the total mark-to-market value for all of the swaps was approximately negative $15.3 million for the University. Under these swap agreements, there is no collateral posting or rating trigger for the University. Should the University amend the documents to adversely affect the counterparty's rights or obligations under the agreement, there are certain covenants the University must maintain including, a net assets ratio test (unrestricted net assets minus plant to total indebtedness) of 60% and accreditation by the Western Association of Schools and Colleges and accreditation of the University's law school by the ABA. Should the university fail to meet these covenants once the documents have been amended, the agreements will terminate.

STRENGTHS:

* Sizable and growing comprehensive urban Jesuit institution, located in the city of San Francisco, offering broad array of undergraduate, graduate and professional programs; total full-time equivalent enrollment of over 9,000 students in fall 2010;
* Despite the recent difficult economic environment, healthy operating performance based on conservative management, with a robust average three-year operating margin of 6.9% and good average annual debt service of 3.4 times; Moody's expects management's ability to control expense growth and budget conservatively will result in comparable operating performance going forward;
* Solid financial reserves with fiscal 2010 expendable resources of $164.8 million cushioning debt by 0.87 times and 0.62 times annual operations;
* Healthy liquidity with unrestricted monthly liquidity of $108.6 million providing over 129 monthly days cash on hand and 1.76 times coverage of variable rate debt with a tender feature;
* Current offering to refund the University's outstanding auction rate series, significantly changing the University's debt portfolio from 98%
variable rate debt to 49%.

CHALLENGES:

* Highly competitive environment for students, with the University competing with lower-priced public universities, as well as other private colleges and universities in the area; the University remains dependent on student charges (84% of revenues) necessitating careful enrollment management;

* Although resources have grown, the University’s expendable resource base of $119.5 million in fiscal 2009 is smaller than the Moody’s FY 2009 A-rated private college and university median for large institutions of $131.8 million; favorably, expendable resources have increased 38% to $164.8 million, in line with its peers;

* Variable rate exposure adds risk to the credit profile, as $84 million or 49% of its debt is in the variable rate mode, supported by three separate Letters of Credits (LOCs), currently two with AB, one with Bank of America. The University expects to replace all three with LOCs from JP Morgan Chase, N.A. Given the University’s operating flexibility and good liquidity, we believe the risks are adequately associated with the University’s debt profile at the current rating level.

MARKET/COMPETITIVE POSITION: GROWING ENROLLMENT IN HIGHLY COMPETITIVE MARKET; DIVERSE PROGRAM OFFERINGS AND URBAN SETTING CONTRIBUTES TO MARKET STRENGTH

Moody’s anticipates that the University of San Francisco will continue to maintain solid student demand given the University’s unique market position as an urban comprehensive Jesuit institution, located in the city of San Francisco. Founded in 1855, the University offers a broad array of undergraduate, graduate and professional programs, including a law school and a growing nursing school. The University has a sizeable enrollment base of 9,203 full time equivalents in fall 2010, over a 15% increase in the past five years. As of January 2011, management notes total freshman applications have increased by 33% compared to the same time last year. Notably, approximately 38% of the FTE are at the graduate or professional level, providing a diverse student base and support for good net tuition per student due to less tuition discounting needed. Management continues to budget conservatively for modestly increasing enrollment levels at the undergraduate program, while focusing enrollment strategies on off-campus growth and graduate programs where the University has additional facilities capacity.

In fall 2010, the University's accepted 68% of freshman applicants, compared to the Moody's median for A-rated large institutions of 60%. At the same time, 19% of accepted students chose to enroll, compared to the 25% Moody's median, highlighting the strong competition in California for higher education from lower-priced public institutions and numerous other comprehensive private universities in the west and northwest.

OPERATING PERFORMANCE: CONSISTENT OPERATING SURPLUSES PROVIDE HEALTHY DEBT SERVICE COVERAGE; GRADUATE PROGRAMS AND LAW SCHOOL PROVIDE DIVERSITY IN TUITION REVENUES

The University's prudent budgeting and financial management practices have contributed to solid operating performance. Despite the recent economic downturn, from 2008 to 2010, the University's annual operating margin averaged a healthy 6.9%, resulting in approximately 3.4 times average debt service coverage. In FY2010, the University provided a significant increase in financial aid, reflected in the total tuition discount rose by over 2 percentage points to 25.7%, however operation margin remained healthy at 8% as management offset the increase in financial aid with cost cutting and cost containment strategies. The University maintains an endowment spending policy 4.5% of a three-year moving average.

The University remains dependent on student charges to fund operations, with tuition and auxiliary revenues compromising 86% of operating revenues in fiscal 2010 (on Moody’s adjusted basis). However, the variety of academic programs does provide diversity in the source of revenues derived from students, with approximately 33% coming from the law school and the graduate programs. The University’s diverse program offerings and significant graduate enrollment, combined with improved demand, has resulted in healthy growth in net tuition per student, reaching $22,342 in fiscal 2009 (a 5% increase from the prior year), above the Moody’s A-rated median for large private institutions ($20,420). In FY2010, net tuition increase by 0.5% to 22,459, despite the large increase in tuition discounting as noted above. USF’s dependency on student charges as the primary source of operating revenues stresses the importance of continued successful recruitment and retention of students as well as the University's ability to continue to grow net tuition per student in a challenging economic environment.

BALANCE SHEET POSITION: FINANCIAL RESOURCE BASE GROWTH PROVIDES ADEQUATE CUSHION FOR DEBT AND OPERATIONS; CURRENT FIXED RATE OFFERING WILL REFUND OUTSTANDING AUCTION RATE

We expect USF's continued reinvestment of operating surpluses and fundraising efforts to contribute to long-term strengthening of the balance sheet. Positive investment returns and conservative fiscal practices have produced a 38% increase in FY2010 from FY 2009, which had decreased 30% due to investment losses. The FY 2010 expendable resources of $164.8 million provide a solid coverage of 0.97 times pro-forma debt and 0.68 times annual operations.

With the end of the University’s $175 million capital campaign in May 2007, and the recent weak economic environment, USF’s gift revenues have averaged $13.4 million (FY2008-2010) compared to $26 million in FY2006. The University currently is fundraising for its Center for Science analogues and, raising $35 million to date against the $50 million project. The campaign is expected to run to December 31, 2011. We expect continued efforts to build gift capacity to increase the University's financial resource base over time.

The University's investment return was a favorable 12.1% for FY 2010 following a negative 18.4% return in FY2009. As of September 30th, the calendar year return to date was 5.2%. The endowment was allocated as follows: 22% traditional domestic equities, 16% traditional international equities, 16% fixed income, 10% hedge funds, 23% private equity, 9% in commodities and 2% in cash. As of the end of FY2010, USF had approximately $28.9 million of unfunded private equity commitments. The University retains Monticello Associates as an investment advisor.

After the current offering, the University will have approximately 49% of its debt portfolio ($84 million) in a variable rate mode with a tender feature. The University currently has three series of letter of credit (LOC) enhanced bonds, two with Allied Irish Bank (rated Ba2/P-3) and one with Bank of America, N.A., (rated Aa3/P-1), and expects to replace all three letter of credits with letters of credit from JP Morgan Chase, N.A. (“JP Morgan”) by February 7, 2011. The current letter of credit agreements contain certain covenants which, if breached, could result in acceleration of the bonds or the University having to post all of its unrestricted revenues into a bondholder trustee held collateral fund, pursuant to the 1996 loan agreement between the University and CEFA. Specifically, the Bank of America agreement currently contains the following financial covenants - maintaining an asset coverage ratio (unrestricted net assets less investment in plant/direct debt) greater than 50%; debt
Unrestricted Monthly Liquidity: $108.6 million
Average Debt Service Coverage: 3.44 times
Average Operating Margin: 6.9%
Expendable Resources to Operations: 0.68 times
Expendable Resources to Pro-Forma Direct Debt: 0.97 times
Expendable Financial Resources: $164.8 million
Total Financial Resources: $276.9 million
Total Pro-Forma Direct Debt: $167 million
Freshmen Matriculation: 19%
Freshmen Selectivity: 68%
Total FTE Enrollment: 9,203 FTE

KEY INDICATORS (FY 2010 financials (FYE 5/31/10), Fall 2010 enrollment)

commensurate growth in financial resources; increase in variable rate debt in amount and percentage of total debt, particularly without
Deterioration in operating performance and cash flow resulting in thinning debt service coverage levels; dramatic deterioration of unrestricted
Outlook
The positive outlook is based on our expectation of the University sustaining its solid market position supporting healthy net tuition per student
deteriorate, the pace of change in the rating could be more rapid due to the potential acceleration of these liabilities and the potential for
What could change the rating-DOWN
Continuation of robust operating margins and further growth of financial resources to provide a strong cushion for debt and operations, including
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Continuation of significant success in future fundraising; continued strengthening of student market position.

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Monthly Days Cash on Hand (unrestricted funds available within 1 month divided by operating expenses excluding depreciation, divided by 365 days): 175.8 days

% of Revenues from Tuition and Auxiliaries: 84%

CONTACTS
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RATED DEBT
CEFA Series 1996 (fixed rate): insured by National Public Guarantee Corp.

CEFA Series 2005A (auction rate) & Series 2006 (auction rate): A3; insured by National Public Guarantee Corp. (expected to be refunded with current offering)

CEFA Series 2000 and 2003 (variable rate): enhanced Baa3/VMIG3 based on letter of credit provided by Allied Irish Bank (expires May 28, 2011); expected to be replaced by letter of credit provided by JP Morgan Chase (rated Aa1/P-1), on or before February 7, 2011

CEFA Series 2005 (variable rate): enhanced Aa3/VMIG1 based on letter of credit provided by Bank of America (expires August 18, 2011) expected to be replaced by letter of credit provided by JP Morgan Chase (rated Aa1/P-1), on or before February 7, 2011

METHODOLOGY
The principal methodology used in this rating was Moody's Rating Approach for Private Colleges and Universities published September 2002.

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