

University of Hawaii Board of Regents

University of Hawaii; Public Coll/Univ - Unlimited Student Fees

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Credit Profile		
US\$8.89 mil univ rev bnds (University of Hawaii) ser 2012A dtd 02/22/2012 due 06/30/2019		
<i>Long Term Rating</i>	A+/Stable	New
University of Hawaii Brd of Regents, Hawaii		
University of Hawaii, Hawaii		
University of Hawaii Board of Regents (MBIA of Illinois) ser 2002A		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
University of Hawaii Brd of Regents (University of Hawaii) (MBIA of Illinois) ser 2006A		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'A+' rating to the University of Hawaii Board of Regents' university revenue refunding bonds, series 2012A, issued for the University of Hawaii (UH). Standard & Poor's also affirmed its 'A+' long-term rating and underlying rating (SPUR) on revenue bonds outstanding issued by the board for the university. The ratings reflect our view of the system's strong operations, despite state funding challenges and growing enrollment. Per our government-related entity (GRE) criteria and due in part to the university's unique geography, we view the state and university system as strongly linked. The outlook is stable.

More specifically, the ratings reflect our opinion of the university's:

- Comprehensive nature as the state's (AA/Stable) only public system of higher education;
- Historically strong financial performance, characterized by solid operating margins despite significant cuts in state funding (which accounts for about one-third of the university's operating revenue), and a modest operating surplus in fiscal 2011;
- Stable enrollment;
- Manageable maximum annual debt service burden of about 3%; and
- Measurable fundraising growth, as demonstrated by the completion of a capital campaign in 2009 that yielded 50,000 new donors and raised \$282 million against a goal of \$250 million.

Partially offsetting the preceding credit strengths is our view of the university's:

- Strong reliance on the state for operating and capital funds, in a challenging economic environment, and
- Low financial resource ratios for the rating category at June 30, 2011, with unrestricted net assets (UNA) equal to less than 1% of both adjusted operations and debt. However we note that the ratios improve when adjusting UNA for the university's share of other postemployment benefits (OPEB) liability (for better comparability) to 21% of adjusted operations and 51% of debt.

Proceeds from the 2012A bonds are expected to refund the university's 2001B bonds (about \$8.8 million). Historically, the university system has not often used revenue debt financing. The system had about \$637 million of revenue debt outstanding as of June 30, 2011; all debt is fixed rate. There are three slightly different security structures that we rate the same based on our view of the broad, interconnected mix of pledged revenues available for debt service. About 44% of the university's debt is secured by dedicated revenue streams, which we consider a strength. Debt service is level at about \$45 million through 2033, with maximum annual debt service of \$46.5 million occurring in 2016 (excluding the Build America Bonds, or BABs, interest subsidy), making for what we view as a low debt burden of under 3%. Management has indicated that it may issue up to \$180 million of new debt within the next 18 months.

Network revenues secure the 2001B, 2006A, 2009, 2010B, 2010B-2, and 2012A bonds (about \$355.3 million as of June 30, 2011). Network revenues include receipts from auxiliaries as well as Special and Revolving fund appropriations. Network net revenues were about \$27.2 million in fiscal 2011. The pledge of appropriations is subordinate to the 2002A and 2006A bonds. Funds available from Special and Revolving fund appropriations were \$603.4 million in fiscal 2011.

The \$138.6 million series 2010A-1 (taxable BABs) and 2010A-2 bonds, whose proceeds were used toward the construction of a cancer research building, are also secured by the above network and Special and Revolving fund appropriations and are additionally secured by cigarette tax revenues. The Cancer Research Special Fund receives two cents per cigarette sale to be used solely for 2010A debt service or operations of the cancer center. The fund had a balance of \$31 million in June 2011, and debt service for these bonds was paid solely through this fund in fiscal 2011.

The university also has about \$132.5 million of bonds outstanding that are separately secured by a lien on Special and Revolving funds of the university and network revenues as well as state-allocated and -appropriated money from the Hawaii Tobacco Settlement Special Fund. In fiscal 2011, this fund yielded \$12.8 million for debt service on the 2002A and 2006 bonds.

Outlook

The stable outlook reflects our anticipation that during the two-year outlook period, university enrollment will remain stable or grow, reflecting the university's unique position in the state; the university will effectively manage state appropriation cuts; management will continue to address deferred maintenance needs; and the debt burden will remain manageable.

We could take a positive rating action during the outlook period if financial resources grow relative to the rating category, there is sustained positive adjusted operating financial results on a cash basis (adjusting for OPEB liabilities), enrollment remains stable, and growth continues in research, fundraising, and endowment.

We could take a negative rating action if positive operating trends do not hold, there is a significant increase in debt burden without a commensurate increase in revenues, or financial resources decline relative to the rating category.

Enterprise Profile

Demand

Founded in 1907, the university serves as Hawaii's flagship research institution as well as the state's designated land-grant institution. Today it is the state's only public higher-education system and has about 85% of the higher-education market in Hawaii. UH is a comprehensive institution offering programs in campuses located throughout the state. Degrees range from certificate programs to doctoral-level study. The oldest campus, the university's flagship, was established in Manoa, in Honolulu, on the island of Oahu, in 1907. The university established a four-year residential campus in Hilo in 1970 and then added an upper-division college in West Oahu in 1976. The university system also includes seven community colleges in various locations, which account for slightly more than half of its growing enrollment.

As a whole, the system enrolled 60,330 (headcount) students in fall 2011, about the same as the previous year. Full-time-equivalent enrollment is much lower, at 40,458, reflecting the large percentage of community college students (more than half) in the system. Admissions standards vary by campus: Manoa, Hilo, and West Oahu are all fairly competitive, and the university accepts about 75% of applicants at these three campuses (and about the same for transfer applicants). The community colleges accept nearly 100% of their applicants. In fall 2011 there were 43,598 applications to the system, a small increase from fall 2010; the applications were about evenly split between community colleges and four-year institutions. The articulation agreements between the community colleges and the four-year schools are strong, and students are automatically enrolled in a four-year college when they complete an associate's degree. Management expects continued growth, especially at the community colleges. About 30% of students -- the state's current limit -- at the four-year institutions are from out of state; officials recently raised the limit to 35%. Student quality at the flagship Manoa campus is consistent with national averages, with the average entering class SAT score of 1085 for fall 2011.

Management

The university is governed by a 15-member board of regents who are nominated by a council and appointed by the governor and confirmed by the legislature. Senior management remains stable. The system has current investment and debt policies.

GRE

In accordance with our criteria for government-related entities (GREs), our view of a "moderately high" likelihood of extraordinary government support is based on our assessment of UH's "strong" link with Hawaii given the state's history of regular, ongoing operating support and capital support for academic facilities, as well as the state's ability to appoint the university's governing board and to provide additional funding as needed (subject to legislative approval). In addition, our assessment is based on UH's "important" role in the state's economy compared with that of other state GREs, given its position as the flagship institution of higher education, its provision of health care-related education, its position as a designated land-grant institution, and its role as a general contributor to economic development in the state. The university is a state educational institution created pursuant to the state constitution and statutes.

Financial Profile

Operations

Adjusted operating performance has been historically positive; however, in fiscal 2008 through fiscal 2011, it was negative on an unadjusted basis. In fiscal 2011, there was an audited positive change in net assets of \$139.7 million; however, when primarily adjusted for capital moneys (\$219.9 million), operating results were negative \$77.6 million on a full-accrual basis. But if a further adjustment of OPEB costs, that are paid for by the state, is made, operations are positive. On a cash basis, with depreciation of \$85.6 million in fiscal 2011, they were positive \$8 million, according to our calculation, or positive \$156 million, including the OPEB adjustment. In our view, the university has managed well since fiscal 2009 when the university declared financial exigency.

Revenue diversity

The university receives a substantial amount of state financial support, about 45% of its \$1.5 billion in operating revenues. Research funding has grown to about \$488 million in fiscal 2011 from \$337.7 million in fiscal 2005. Net tuition accounts for a relatively small, but growing portion, at about 16% of operating revenues. Undergraduate tuition and fees at the Manoa campus for 2011-2012 is \$9,100 for in-state students. In 2006, the regents approved a 15% tuition increase each year for six years, starting in fiscal 2007 -- in effect doubling tuition during that period -- although the university also increased financial aid during that time. The board of regents approved another multiyear tuition fee increase on Oct. 26, 2011, with modest tuition increases in the near term. Student charges currently remain affordable, in our opinion. Tuition at the community colleges, which represent half of system enrollment, is much lower than that of the four-year campuses.

State appropriations

After two biennia of state appropriation growth, the system lost about 10% of its operating appropriation in fiscal 2010. The system received \$460.5 million in fiscal 2009 and about \$422.6 million in fiscal 2010. However, the reduction was more nuanced as, in addition to a \$46 million reduction by the legislature in fiscal 2010, the governor restricted another \$52 million. These cuts were offset with \$22 million in American Recovery and Reinvestment Act funds (which management reports has been reinstated in the fiscal 2012 operating appropriation when those federal moneys are no longer available), tuition increases, salary reductions, and a decrease in workforce. A similar cut from the fiscal 2009 base occurred in fiscal 2011, and projected appropriations in fiscal 2012 (\$376.1 million) and fiscal 2013 are flat. Despite operating appropriation cuts, the university received capital appropriations in the 2009-2011 biennium (more than \$350 million in state general obligation bond funding for renovations and other capital improvement projects). Beginning in fiscal 2009, the university's share of overhead costs was transferred out of the university's budget, thus making the appearance of an even larger drop in state appropriations.

Financial resources

Total net assets in fiscal 2011 were \$1.98 billion, an increase of \$139.7 million from the previous year. Of the \$1.98 billion, \$5.5 million was unrestricted and \$798 million was expendable. The UNA number continues to drop while total net assets are rising due to the accounting of OPEB liabilities. The university's share of the state's OPEB liability was \$318.1 million in fiscal 2011. Management stated that these funds are available to the university. Without adjustments, financial resource ratios are very low for a public university in this rating category, in our view, with UNA at June 30, 2011 of \$5.5 million, equal to less than 1% of fiscal 2011 expenses and debt. However when the \$318.1 million is added back to unrestricted net assets, the UNA-related ratios improve to 20.9% of adjusted operating expenses and 50.8% of debt, about average for the rating category.

Endowment and fundraising

The university had about \$253 million in its endowment pool as of Dec. 31, 2011, with the majority of the funds (about \$197 million) held at the separate university foundation. The effective endowment payout policy in fiscal 2010 was 4%, which we view as conservative, and remained so in fiscal 2011. The university and the foundation invest their funds separately. The foundation reported that the investment return for calendar 2011 was negative 1.6%. Foundation funds are invested in a diversified mix of 20% marketable alternative assets; 20% U.S. equities; 16% global equities; 16% real assets; 13% fixed income; and the balance in private equity, venture capital, and cash. The university-held endowment was up by 0.5% for calendar year 2011 and is invested in 47% domestic equities, 40% fixed income, and the balance in international equities and cash.

The university completed a \$250 million centennial capital campaign in June 2009, raising \$282 million, the majority of which has been collected. More than half of the donors to the campaign were first-time donors to the university. The university is currently planning a larger campaign.

Debt

Historically, the university system has not often used revenue debt financing. The system had about \$637 million of revenue debt outstanding as of June 30, 2011. There are three slightly different security structures that we rate the same based on our view of the broad, interconnected mix of pledged revenues available for debt service. Management has indicated that it may issue up to \$180 million of new debt within the next 18 months. Overall, debt is low for the rating category, in our view, with a debt burden of under 3%.

Related Criteria And Research

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- USPF Criteria: Higher Education, June 19, 2007

Ratings Detail (As Of February 6, 2012)		
University of Hawaii Brd of Regents, Hawaii		
University of Hawaii, Hawaii		
University of Hawaii Brd of Regents univ rev bnds ser 2002A (FGIC)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
University of Hawaii Brd of Regents (University of Hawaii) univ rev bnds ser 2006A (Berkshire)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
University of Hawaii Brd of Regents (University of Hawaii) univ rev bnds (University of Hawaii) ser 2006A		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
University of Hawaii Brd of Regents (University of Hawaii) univ rfdg bnds (University of Hawaii) ser 2006A		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Univ of Hawaii Brd of Regents (Univ of Hawaii) univ rev bnds ser 2009A		
<i>Long Term Rating</i>	A+/Stable	Affirmed

Many issues are enhanced by bond insurance.

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