Washington Economic Development Finance Authority, Washington University Of Washington; CP; Lease; Public Coll/Univ - Unlimited Student Fees

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Rationale

Standard & Poor’s Ratings Services assigned its 'AA+' long-term rating and stable outlook to University of Washington’s (UW) series 2009B general revenue bonds. At the same time, Standard & Poor's affirmed its 'AA+' long-term and underlying rating (SPUR) on the university's outstanding general revenue debt, issued by the university and the Washington Economic Development Finance Authority. Finally, Standard & Poor's affirmed its 'A-1+' short-term rating on UW’s outstanding commercial paper (CP) notes.

In our opinion, the general revenue bond rating is based on the university's:

- Position as one of the top research universities in the U.S., with $1 billion in sponsored research funding in fiscal 2008;
- Diverse revenue base, including a medical center (not rated by S&P), and financial support from Washington State (general obligation rating of ‘AA+/Stable’) of about 12% (or $388 million) of adjusted total revenues in fiscal 2008, although operating appropriations have been cut for the upcoming biennium;
- Average debt burden of 4.7%, with two bullet maturities in 2037 and 2040 and manageable upcoming debt plans;
- Good financial resources, with 2008 unrestricted net assets (UNA) equal to 30% of expenses, 87% of pro forma debt supported by impressive fund raising efforts, and a still healthy endowment with an estimated market value of $1.8 billion as of Sept. 30, 2009; and
- Stable and increasing enrollment.

Offsetting the foregoing strengths, in our opinion, are recent declines in state financial support; expected slim, but break-even budgetary operating results for the current fiscal 2009; and investment losses in line with current market trends.
Series 2009B bond proceeds will be used to fund a variety of capital projects, including plans at the University of Washington Medical Center, construction of the new business school, and expansion of the housing and dining system. Management expects to issue the bonds as fixed-rate, taxable Build America Bonds with a bullet maturity in 2036. The debt burden during bullet maturity years is 4.7% of operating expenses, while maximum annual debt service (MADS) during non-bullet years is 2.5%. Post-issuance, there will be about $1.374 billion worth of debt and authorized CP ($250 million); $32 million of which will be outstanding after this issuance. The ‘A-1+’ short-term rating on the CP reflects a pledge of self-liquidity of the university and an additional standby note purchase agreement, which we consider to be a strong line of credit. Liquidity to cover any failed remarketing is covered first and specifically through the pledge of a standby note purchase agreement; self-liquidity of the university would be utilized only on a secondary basis. Excluding authorized but unissued CP, UW’s total outstanding debt as of June 30, 2009, was approximately $1.025 billion. The university does not have any variable-rate debt outstanding. The university expects to issue approximately $250 million of additional debt within the next two fiscal years for various projects.

Bond payments will be made from UW general revenues, which comprise all non-appropriated revenue, excluding appropriations, grant direct costs, restricted gifts, and some fees. As of June 30, 2009, the university also added auxiliary revenues to the general revenue pledge. The auxiliary system includes the University Medical Center, parking system, intercollegiate athletics system, and housing and dining system. Outstanding auxiliary debt (approximately $72 million) has a prior claim on these auxiliary revenues. General revenue totaled more than $806 million in fiscal 2008, including student tuition and fees ($365.9 million), grant indirect cost recovery ($197 million), sales and services revenue ($111 million), and investment income ($76 million). Estimated fiscal 2009 general revenues, with or without the inclusion of auxiliary system revenues, was not available at the time of this report.

**Outlook**

The stable outlook reflects our assumption that additional debt issuances will be met with a commensurate growth in financial resources or revenue. Furthermore, the stable outlook reflects our anticipation of continued enrollment management, successful fundraising, and financial strength ratios consistent with the rating category. We expect the university to sustain positive operating performance through a potentially challenging state funding environment and maintain stable operating performance at the medical center.

**Demand**

Headcount enrollment increased 3% in fall 2009 to 46,115. Full-time equivalent enrollment also rose 2.5% to 43,996. Enrollment is effectively capped at the main campus, though there is room for expansion at the two smaller branch campuses. Approximately 80% of students attending UW are from the state of Washington. First-year applications increased 6.8% to a university high of 21,268 for fall 2009. The acceptance rate improved to 58.0%, while the matriculation rate declined slightly but was a still good 43.5%. The incoming freshmen class was slightly smaller this year, due to state funding decreases. Student quality is good, with average SAT scores for fall 2009 at 1210.
Finances
The fiscal 2009 audit was not available as of this report. University revenue sources (adjusted) remain diversified, and in 2008 included 32% from grants and contracts, 13% from net tuition, 12% from state operating appropriations, and nearly 29% from patient care revenues. The university's large research base received $1.05 billion in fiscal 2008. More than a quarter of the university's operating revenues come from patient services. The medical center is self-supporting.

After several years of 7% annual increases, state operating appropriations were cut for the 2009-2011 biennium; net of anticipated federal stimulus money, management expects appropriations to be down $214.2 million for the biennium. The legislature has approved a tuition increase of up to 14% beginning in fall 2009 in order to help offset this decline. Undergraduate resident tuition for fall 2009 was raised 14% from the previous year, and is a still competitive $7,692. Even with the tuition increase, the university is taking several steps to reduce its expenses to achieve a break-even budget for fiscal 2010 and forward.

UW's income before other revenues for the fiscal year ending June 30, 2008, showed a $30 million deficit, including $200 million of depreciation expenses. Because investments are held at the university level instead of with a separate foundation, investment gains and losses can significantly impact UW's operating results for the year. Consequently, it is our opinion that the operating performance in fiscal 2007 ($426 million surplus) was somewhat overstated, while performance in fiscal 2008 ($30 million deficit) is somewhat understated, with investment income of $77 million in fiscal 2008 compared with $503 million in fiscal 2007 contributing to that result. University management reports that on a budgetary basis, 2008 operating results were balanced, and that fiscal 2009 budgetary results were likewise. Total university net assets were $5.1 billion in 2008, of which $1 billion was unrestricted; UNA increased nearly 6% in fiscal 2008. UNA is a slightly low 30% of adjusted operating expenses ($3.3 billion in fiscal 2008) and a good 87% of pro forma debt ($1.16 billion), including $32 million of outstanding CP (or 73% with the full authorized CP).

UW’s endowment was about $1.8 billion as of Sept. 30, 2009. The endowment declined approximately 29% since the end of fiscal 2008, in line with current market trends, but has since seen some positive returns. The portfolio is diversified, and is invested in 14% domestic equities, 21% international equities, 16% fixed income, 21% marketable alternatives, 12% real assets, and 16% other investments.

University Of Washington Medical Center
University of Washington Medical Center is a significant operating component of the overall university, representing 29.5% of fiscal 2008 operating revenues, and supporting approximately $102.48 million of debt (not rated by S&P). UW Medicine is comprised of the flagship facility hospital, University of Washington School of Medicine (450 beds), Harborview Medical Center (413 beds), University of Washington Physicians, University of Washington Physician’s Network (7 primary care clinics), and Air Lift Northwest. UW Medicine also has a one-third ownership interest in the Seattle Cancer Care Alliance and a one-half ownership interest in the Children's University Medical Group, and has affiliations with Fred Hutchison Cancer Institute and Children's Hospital. UW Medicine is a leading healthcare provider throughout the state of Washington. UW Medical Center and Harborview account for 6% of the discharges and 12% of the net hospital revenue in the state
UW Medicine, through the College of Medicine faculty practice plans (UW Physicians and Children's University Medical Group), has more than 1,900 active faculty physicians and other health care providers practicing across a broad range of specialties. Key services include cardiology, trauma, oncology, transplantation, and a broad array of adult and pediatric medical and surgical specialty and sub-specialty services.

Admissions increased slightly in fiscal 2009 to 19,322 from 18,993 in fiscal 2008 with a total of 133,468 patient days in 2009. Management expects to derive further volume growth with the implementation and maturation of Northwest Hospital & Medical Center's affiliation with UW Medicine and continued recruitment of additional faculty across a range of specialties. The Health Resources Northwest Affiliated Group had $106.6 million of debt outstanding in fiscal 2008, but it is separately secured and is not expected to become an obligation of the University.

Government Related Entity (GRE)
In accordance with our criteria for government-related entities (GREs), we based our view of a "moderate" likelihood of extraordinary government support on our assessment of UW's "strong" link with the state of Washington given the state's history of annual operating appropriations and occasional extraordinary capital support for higher-education institutions in the state. We also based our assessment on UW's "limited" role in the state's economy compared with that of other state GREs, given the university's place within the state's higher education system and its contributions to the state's economic development.

Related Research

Ratings Detail (As Of November 10, 2009)

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Many issues are enhanced by bond insurance.
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