

Research

University Of North Carolina At Wilmington Corp. Housing I LLC University Of North Carolina At Wilmington; Auxiliary - Stand Alone

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Credit Profile

2008

Unenhanced Rating A-(SPUR)/Stable Affirmed

University of North Carolina at Wilmington Corporation Housing II LLC, North Carolina

University of North Carolina at Wilmington, North Carolina

University of North Carolina at Wilmington Corporation Housing II LLC COPs 2006

Unenhanced Rating A-(SPUR)/Stable Affirmed

University of North Carolina at Wilmington Corp Hsg I LLC, North Carolina

University of North Carolina at Wilmington, North Carolina

University of North Carolina at Wilmington Corp Hsg I LLC (University of North Carolina at Wilmington) certs of part 2005

Unenhanced Rating A-(SPUR)/Stable Affirmed

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services has affirmed its 'A-' long-term rating and underlying rating (SPUR) on the University of North Carolina At Wilmington Corp. Housing I LLC and University of North Carolina At Wilmington Corp. Housing II LLC's certificates of participation (COPs)--series 2005, 2006, and 2008 issues, respectively, issued for the University Of North Carolina At Wilmington (UNCW).

The rating on the COPS bonds is lower than, and differentiated from, an unlimited student fee pledge, reflecting our view of the narrow stream of pledged revenues including net revenues generated by facilities financed by the COPs, as well as the additional housing and auxiliary system revenues available to support the lease payments. The rating reflects a history of healthy combined debt service coverage and a five-year average occupancy rate close to 100% for all university housing (including the facilities associated with the COPS pledge), with expectations for continued good coverage and occupancy. The rating also reflects the university's strong managerial and financial commitment to its student housing projects. While Standard & Poor's does not maintain a public issuer credit rating on UNCW, we have reviewed the underlying demand characteristics and financial profile of the university as part of this analysis.

The ratings also reflect our view of UNCW's:

- Moderately weak legal provisions applicable for all series that include a 1.1x rate covenant, but with good actual coverage, as calculated by management, at 1.42x in fiscal 2013 and at 1.55x in 2014;

- Firm security pledge backing all bond series, which includes a pledge of revenue generated by the housing facilities and a subordinate pledge of net dining revenue (after payment of the university's housing and dining system debt and general revenue debt) and parking system net revenue (after payment of the university's general revenue debt);
- Very strong demand for the university's housing, with occupancy rates averaging close to 100% occupancy for the past five fiscal years;
- Favorable demand trends with increases in headcount enrollment, freshman applications, and improving student quality; and
- Substantial, albeit recently diminished, operating support, from North Carolina.

In our opinion, partially offsetting credit factors include:

- Financial resources for the university that remain below the rating category medians with unrestricted net assets of \$101 million as of June 30, 2014, accounting for 35% of adjusted operating expenses and 43% of outstanding debt, but resources are growing;
- Above-average total debt burden; and
- A relatively small endowment compared with peer institutions.

The UNCW Corp. is a North Carolina nonprofit and IRS-recognized tax-exempt corporation created to enhance the university's educational mission, including without limitation, assisting with the acquisition of capital assets for the university. The projects funded by the various rated series of bonds are the only capital assets of the company, which appear on its balance sheet as net investment in direct financing leases current and noncurrent (the investment in the assets appear on the university's financial statements; its student life housing staff manages the facilities). UNCW Corp. leases the housing facilities funded by the series 2005, 2006, and 2008 COPs to the university and the university manages the facilities.

The series 2008 COPs (\$59 million outstanding as of June 30, 2014) were issued largely to finance the construction and equipping of a suite-style student housing facility (phase III) consisting of approximately 662 beds, in four residential buildings, with a related 1,000-space, four-level parking facility and recreational and retail facilities. The series 2008 COPs are on parity with the series 2006 (\$37 million par outstanding) series 2005 (\$27 million) COPs. The series 2006 COPs largely financed the construction and acquisition of a 603-bed apartment-style student housing facility (phase II) and its related parking and recreational facilities. The series 2005 COPs largely financed the construction and acquisition of a 518-bed apartment-style student housing facility (phase I) and its related parking and recreational facilities. All of these projects were completed on time and within budget and, with the completion and full occupancy of all of the projects, the university increased the percentage of students living on campus to approximately 40% from 23%.

A debt service reserve fund exists for all series and must equal the least of the maximum annual debt service, 125% of the average annual debt service requirements in each fiscal year, or 10% of the proceeds of the certificates. There are no definite plans for additional debt for student housing over the next two years.

For the fiscal year ended June 30, 2014, coverage as calculated by management for the dormitory system and dining system following the payment of required reserves was good at 1.55x, and 1.42x in fiscal 2013. The bond documents also require 1.0x coverage for phases I and II individually including the funding of reserves. The phases are in compliance with these covenants and coverage improved through fiscal 2014, but it is lighter on a project basis. We

understand that management expects coverage for the system and the projects to remain above required levels, however, DSC will likely not remain at current levels as debt service rises over time. We would view a trend of improving DSC coverage favorably.

Outlook

The stable outlook reflects our expectation that, over the next two years, demand for the housing system will remain strong and DSC will be adequate, well above required levels. We also expect that the university's financial performance will remain stable despite a challenging state funding environment, demand for the university's programs will remain strong, and the university's financial resources will remain adequate for the rating category.

We would consider a positive rating action if the university continues to realize strong student and housing demands and posts a trend of solid and improving DSC for the combined housing and dining system such that coverage is above 1.6x.

A trend of weakened occupancy and DSC that is close to covenanted levels could lead to a negative rating action, but we consider this unlikely during the outlook period. Also, significant reductions in state support, weakened university operating performance, or significant additional university debt that is not commensurate with the growth of financial resources or revenues could also pressure the rating, but we consider this unlikely during the outlook period.

Enterprise Profile

University of North Carolina at Wilmington

The University of North Carolina at Wilmington was established in 1947 as a two-year college in Wilmington, when the citizens of New Hanover County approved a tax levy. The institution was granted four-year status in 1963 and became the sixth university in the University of North Carolina (UNC) system in 1969. In 1985, the UNC Board of Governors granted comprehensive Level I status to the university. Currently, the university offers 54 undergraduate and 26 graduate degree programs, as well as two doctorates in marine biology and education leadership and administration. An interim chancellor was named in July 2014 following the departure of the prior chancellor. We understand that a search for a permanent replacement is underway and that a new chancellor will be named in 2015. An internal leader in the business office was named vice chancellor for business affairs in 2014 following the movement of the prior vice chancellor to another UNC system university. We believe that this transition has proceeded smoothly and we expect that the search and selection of a new university chancellor will occur within the next year. We believe that the university has a strong managerial and financial commitment to its student housing and auxiliary projects; this supports good occupancy levels and good coverage for the projects.

Demand and enrollment

Enrollment has grown steadily for over five years and the vast majority of the students are undergraduates. Total student headcount at the university was 14,570 students in fall 2014, an increase of 4.5% over the prior year and 13% since fall 2009. Full-time equivalent enrollment was 13,616, which is 17% higher than the fall 2009. About 90% of students enrolled in fall 2014 were undergraduates, which is similar to the past.

Student demand continues to be strong with a high number of out-of-state students seeking admission to UNCW. Freshman applications totaling 11,523 in fall 2014 were down a slight 2.7% from the prior year, but 3% higher than fall 2012 and 24% greater than fall 2009. The university's acceptance rate weakened to 58.6% for fall 2014 from 52% the prior year, while the matriculation rate improved to 32.0%, from 31.5% the year prior. We consider these rates solid for the rating category. Typically about 18% of Wilmington undergraduate enrollees are from out of state, which management intends to maintain with close attention to tuition pricing and out of state recruitment. The university would like to grow undergraduates at a steady rate (about 55 students annually), and longer term growth would require some capacity expansion over the medium term by standardized test scores is above average and improving, with SAT scores of 1,191 for the fall 2014 semester. Retention rates are strong at 86.4% for fall 2014 and the six-year graduation rate is solid at 70.8%. These rates compare favorably with the category medians and to other institutions in the UNC system.

Graduate enrollment has increased at strong rates for the past three years to 1,618 students enrolled in fall 2014. We understand that the addition of new programs will likely grow enrollments in the near term.

Housing system

UNCW offers a total bed capacity of 4,143 student beds (2,360 beds in 10 residences that were built between 1970 and 2003, 518 beds in phase I, 603 beds in phase II, and 662 beds in phase III). The university opened phase I, Seahawk Village, consisting of six apartment buildings in fall 2006. Phase II, Seahawk Landing, which consists of seven apartment buildings, opened in fall 2007. Both of these facilities are located on the university's campus and are geared toward upperclassmen. The university opened the phase III project in the fall of 2009, and it consisted of four residential buildings with suite-style accommodations. Occupancy at three phases has averaged 98% to 101% in the fall and between 94% and 98% occupancy in the spring since the openings. We consider occupancy solid, especially because the university does not have a residency requirement. Demand for all university housing is very strong as characterized by an average occupancy rate for the fall term approaching or slightly exceeding 100% for the past five fiscal years. We understand that the private market continues to service excess housing demand with new projects scheduled to come online in the near term and the university has no current plans for additional residence halls. The university may consider the addition of another residence hall if demand remains robust with growing enrollments.

Financial Profile

State appropriations

The university has historically received strong funding for operations and capital from North Carolina, but, as with many states, budget stress has resulted in cuts to higher education. State appropriations accounted for a strong 34.2% of the university's operating revenues in fiscal 2014, which we consider a credit strength. While state appropriations increased 1% in fiscal 2014 to \$97.6 million, management expects a slight decrease in state support for fiscal 2015. Over the past several years, lower levels of state operating support have been partially offset by increased tuition revenue and enrollment growth funding from the state. All UNC system institutions had to submit a fiscal 2016 budget with a 2% reduction in state support; the actual level of future support is unknown. Public universities in North Carolina also benefit from capital support from the state. Historically, the state had been generous with capital appropriations to the university for its academic buildings, thus keeping debt levels low. However, as with operating

appropriations, the state has reduced capital support over several years. UNCW did not receive any state capital support appropriations from 2009 to 2013, and received \$3.1 million in fiscal 2014 for repair and renovations.

Operations

UNCW's financial operations have historically been good, but the reduction in state appropriations has put pressure on the budget and adjusted operating performance is balanced with small margins recently. In addition to reductions in state appropriations, the university has had limited tuition increases and reduction in federal funding. The university's two main revenue sources are tuition and other student-generated revenues at 49% and state operating appropriations at 34% of total operating revenues in fiscal 2014. We exclude investment income/loss and include state appropriations, noncapital grants, endowment payouts, noncapital gifts, and interest expense in our assessment of adjusted operating performance. UNCW has generated positive operating results on this adjusted basis for the past three fiscal years including a \$1 million surplus in fiscal 2014, a \$2 million surplus in fiscal 2013, and a \$3 million surplus in fiscal 2012. Fiscal 2014 net tuition revenues grew at a slower pace (3.6%) compared with the trailing three year average of 9%, and adjusted revenue grew a total of 1.5%. Expenses grew a modest 2% in fiscal 2014 following a 5.6% increase in fiscal 2013 and a 1% reduction in fiscal 2012. Positive operations can be credited to increasing tuition revenue and expense controls. Total net assets increased annually during the past five years to \$445 million in fiscal 2014, a 29% increase over fiscal 2009.

Endowment and financial resources

The university's endowment was approximately \$85.3 million as of June 30, 2014, following an annual return of 14.6%. The university holds the bulk of the endowment funds, with just \$4 million held by the Foundation of the University of North Carolina Wilmington. Financial resources are improving and remain adequate for the rating category, in our opinion. As of June 30, 2014, unrestricted net assets totaled \$101 million, equal to 35% of adjusted operating expenses and 43% of outstanding debt.

Debt

On June 30, 2014, outstanding debt was about \$234 million, with a current debt service burden of 6.3% of fiscal 2014 operation expenses, which we consider above-average. The university's debt profile largely consists of certificates of participation (\$124 million), which are related to the housing projects funded by the series 2005, 2006, and 2008 COPs and revenue bonds (\$102 million). The university's general revenue debt is secured by an available funds pledge, which includes much broader revenue sources. Available funds totaled about \$175 million in fiscal 2014, up from \$122 million in fiscal 2010. Available funds provided 8.25x coverage of maximum annual debt service in fiscal 2014. We understand that management intends to seek about \$11.5 million of self-liquidating debt for a guaranteed energy savings program in early 2015. We believe that the university can absorb this modest increase in debt at the current rating. The university has no additional confirmed debt plans, but projects may be considered under the new chancellor next year.

Table 1

| University Of North Carolina At Wilmington Housing Statistics | | | | |
|---|---------------------------------|-------|-------|-------|
| | -- Fiscal year-ended June 30 -- | | | |
| | 2015 | 2014 | 2013 | 2012 |
| Occupany | | | | |
| Main Campus housing beds | 2,360 | 2,360 | 2,360 | 2,360 |

Table 1

| University Of North Carolina At Wilmington Housing Statistics (cont.) | | | | |
|--|------|------|------|------|
| Main campus occupancy in the Fall semester (%) | 103 | 100 | 101 | 105 |
| Seahawk Village beds | 518 | 518 | 518 | 518 |
| Project housing occupancy in the Fall semester (%) | 99 | 96 | 99 | 98 |
| Seahawk Landing beds | 603 | 603 | 603 | 603 |
| Project housing occupancy in the Fall semester (%) | 98 | 96 | 99 | 99 |
| Seahawk Crossing beds | 662 | 662 | 662 | 662 |
| Project housing occupancy in the Fall semester (%) | 98 | 99 | 99 | 99 |
| Coverage Levels | | | | |
| Phase I coverage (x)* | N.A. | 1.28 | 1.10 | 1.06 |
| Phase II coverage (x)* | N.A. | 1.27 | 1.12 | 1.02 |
| Total Project and Dormitory System + Dining System Coverage (x)¶ | N.A. | 1.55 | 1.42 | 1.41 |

*Coverage for phase I and II must equal or exceed 1x (coverage here includes payments to reserves). ¶Coverage for the Dormitory System and the Dining System must exceed 1.1x. N.A. -- Not available.

Table 2

| | --Fiscal year ended June 30-- | | | | | Medians for 'A' rated public colleges and universities |
|--|--------------------------------------|-------------|-------------|-------------|-------------|---|
| | 2015 | 2014 | 2013 | 2012 | 2011 | 2013 |
| Enrollment and demand | | | | | | |
| Headcount | 14,570 | 13,937 | 13,733 | 13,145 | 13,071 | 12,911 |
| Full-time equivalent | 13,616 | 13,110 | 12,880 | 12,331 | 12,221 | 10,622 |
| Freshman acceptance rate (%) | 58.6 | 52.0 | 54.2 | 52.9 | 56.5 | 70.9 |
| Freshman matriculation rate (%) | 32.0 | 31.5 | 33.9 | 36.2 | 36.1 | 37.4 |
| Undergraduates as a % of total enrollment (%) | 88.9 | 89.2 | 89.9 | 90.6 | 89.8 | 86.1 |
| Freshman retention (%) | 86.4 | 86.4 | 86.0 | N.A. | 87.0 | 72.4 |
| Graduation rates (five years) (%) | N.A. | N.A. | N.A. | N.A. | N.A. | 43.1 |
| Income statement | | | | | | |
| Adjusted operating revenue (\$000s) | N.A. | 285,520 | 281,239 | 266,973 | 259,466 | MNR |
| Adjusted operating expense (\$000s) | N.A. | 284,510 | 278,804 | 263,941 | 266,262 | MNR |
| Net adjusted operating income (\$000s) | N.A. | 1,010 | 2,435 | 3,032 | (6,796) | MNR |
| Estimated operating gain/loss before depreciation (\$000s) | N.A. | 17,205 | 17,021 | 17,152 | 7,015 | MNR |
| Change in unrestricted net assets (UNA; \$000s) | N.A. | 17,635 | 23,123 | 7,273 | (563) | MNR |
| State operating appropriations (\$000s) | N.A. | 97,602 | 96,879 | 91,313 | 89,350 | MNR |
| State appropriations to revenue (%) | N.A. | 34.2 | 34.4 | 34.2 | 34.4 | 26.5 |
| Student dependence (%) | N.A. | 49.0 | 47.6 | 46.3 | 44.7 | MNR |
| Debt | | | | | | |
| Outstanding debt (\$000s) | N.A. | 233,695 | 240,304 | 250,015 | 252,156 | 123,000 |
| Total pro forma debt (\$000s) | N.A. | 233,695 | N.A. | N.A. | N.A. | MNR |

Table 2

| University Of North Carolina At Wilmington, Financial And Enrollment Statistics (cont.) | | | | | | |
|---|------|---------|---------|---------|---------|--------|
| Current debt service burden (%) | N.A. | 6.06 | 5.73 | 6.28 | 5.57 | 4.10 |
| Current MADS burden (%) | N.A. | 7.47 | 7.62 | 8.05 | 7.98 | MNR |
| Financial resource ratios | | | | | | |
| Endowment market value (\$000s) | N.A. | 85,285 | 73,765 | 65,928 | 62,826 | 33,348 |
| Related foundation market value (\$000s) | N.A. | N.A. | N.A. | N.A. | N.A. | 68,500 |
| Cash and investments (\$000s) | N.A. | 209,874 | 184,849 | 188,610 | 198,389 | MNR |
| UNA (\$000s) | N.A. | 100,722 | 83,087 | 59,964 | 52,691 | MNR |
| Adjusted UNA (\$000s) | N.A. | 100,722 | 83,087 | 59,964 | 52,691 | MNR |
| Cash and investments to operations (%) | N.A. | 73.8 | 66.3 | 71.5 | 74.5 | 47.0 |
| Cash and investments to debt (%) | N.A. | 89.8 | 76.9 | 75.4 | 78.7 | 93.3 |
| Cash and investments to pro forma debt (%) | N.A. | 89.8 | N.A. | N.A. | N.A. | MNR |
| Adjusted UNA to operations (%) | N.A. | 35.4 | 29.8 | 22.7 | 19.8 | MNR |
| Adjusted UNA plus debt service reserve to debt (%) | N.A. | 43.2 | 35.1 | 24.3 | 21.0 | 53.3 |
| Adjusted UNA plus debt service reserve to pro forma debt (%) | N.A. | 43.2 | N.A. | N.A. | N.A. | MNR |
| Average age of plant (years) | N.A. | 10.7 | 11.0 | 10.6 | 10.0 | 12.7 |
| OPEB liability to total liabilities (%) | N.A. | N.A. | N.A. | N.A. | 0.0 | 4.8 |

N.A.--not available. MNR --median not reported.

Related Criteria And Research

Related Criteria

USPF Criteria: Higher Education, June 19, 2007

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