NEW YORK, April 06, 2015 -- Moody's Investors Service assigns a Aa3 rating to the University of South Florida's ("USF") proposed $31 million of Series 2015 Capital Improvement Refunding Revenue Bonds (Marshall Center Project). We also assign an A1 to $23 million of Series 2015A Certificates of Participation (COPs) and to the $88 million of Series 2012A COPs. Concurrently, we affirm the Aa2 issuer level rating and the ratings on the outstanding bonds. The bonds are issued through the USF Financing Corporation, a direct support organization of the university. The outlook is stable.

SUMMARY RATING RATIONALE

The Aa2 issuer rating reflects USF's healthy growth of net tuition revenue from a large and stable enrollment and moderate leverage at this comprehensive urban research university. Offsetting factors include political limits on tuition pricing and increased competition for students.

We also have ratings of Aa3 and A1 assigned to specific legal pledges, described in the LEGAL SECURITY section of this report. The rating differentials reflect more limited pledged revenue and associated debt service coverage.

OUTLOOK

The stable outlook reflects expected continued positive operating performance and modest financial resource
growth, with no material increases in debt. The outlook also incorporates the expectation that pledged net revenues will continue to provide sufficient debt service coverage on the various bonds.

WHAT COULD MAKE THE RATING GO UP
- Significant strengthening of USF’s brand and diversification of geographic draw
- Substantial increase of flexible reserves

WHAT COULD MAKE THE RATING GO DOWN
- Sustained deterioration of operating performance, particularly if leading to reduced liquidity
- A material decline in the pledged revenues or insufficient debt service coverage

STRENGTHS
- A return to highly positive operating performance resulting from prudent budgeting and careful planning
- Well positioned to continue growing enrollment driven by favorable demographics of the state and its standing as a large comprehensive research university in Tampa
- Solid unrestricted liquidity available within one month provides 192 days cash on hand
- Manageable financial leverage relative to a sizeable operating base

CHALLENGES
- Some volatility with state appropriations and recent limits on tuition increases adds complexity to budgeting and planning
- Ongoing capital needs to attract students, faculty, and research in light of reduced state capital support
- Indirect exposure to patient care through a faculty practice plan is not reflected in our financial ratios but the healthcare component is an important aspect of USF’s strategy

RECENT DEVELOPMENTS

Based on the structure of proposed transactions, the A1 ratings on the Housing System COPs incorporates the planned removal of the revenues associated with the Andros Complex and Marshall Center Project. At this time, the impact will not materially impact coverage in FY 2016 (FY 2014 gross coverage of 2.6 times and net coverage of 1.4 times) as associated expenses will also be removed and assuming a 3% housing rate increase. Gross revenue associated with these projects was roughly $8 million in 2014 resulting in a $42 million pledge. Further reductions of the revenue pledge could negatively impact the ratings of the COPs.

The release of the Andros Complex (1,050 beds or 18% of the total housing stock), built in the 1960s, poises the university to potentially engage in a public private partnership (P3) with a private developer to finance construction of 2,150 beds over a phased period, netting a 1,100 increase in beds. Occupancy of current housing stock is consistently at or above capacity. USF has not yet received approval from the Florida Board of Governors (BOG), which would be required before moving forward with the P3.

Please refer to the Legal Security section for the Series 2015 Marshall Student Center revenue bonds pledge.

In February, 2015, the BOG unanimously approved the relocation plan for the USF Morsani College of Medicine and Heart Institute to downtown Tampa, recommending it to the legislature and the governor. The planned site location will be on land gifted to the university. The closer proximity to the USF Center for Advanced Medical Learning & Simulation (CAMLs), Tampa General Hospital (TGH), and the USF clinic facility at TGH supports USF’s healthcare and research strategy. The proposed opening is in the fall of 2018. The project cost is estimated at $153 million, with the majority funded by the state and some private gifts.

DETAILED RATING RATIONALE

MARKET POSITION: LARGE COMPREHENSIVE UNIVERSITY BENEFITING FROM CLOSE PROXIMITY TO A GROWING METROPOLIS
USF’s location in the Tampa-St. Petersburg-Clearwater metropolitan area, with strong demographic trends and relatively diverse economy combined with growing student demand from outside of the state, position it for continued stable enrollment. For fall 2014, the university enrolled 39,165 full-time equivalent students, essentially level from the prior fall as it focuses on limiting undergraduate enrollment and modestly growing enrollment through its strong graduate and professional programs. Given USF’s consistent enrollment, we expect demand for its housing and parking facilities to remain strong.

USF’s medical school and affiliation with Tampa General Hospital (A3 positive) benefits the university in growing its research enterprise and and bolsters demand for health related programs. The medical school is up for its eight-year reaccreditation from Liaison Committee on Medical Education (LCME) with the results expected by summer 2015. The physician’s assistant program is up for its initial accreditation, and will support modest enrollment growth. TGH serves as the long-standing academic medical center for USF’s School of Medicine.

The university has impressively grown its research profile, with grants and contracts revenue up 10% from FY 2010 to $351 million in FY 2014. Favorably, USF has diversified funding sources, with private partnerships comprising a large 46% of total award dollars, followed by the federal and state governments at 35% and 19%, respectively in FY 2014. This diversity has aided the university in growing this revenue source during a challenging federal funding environment in which many moderated-sized research universities are experiencing declines in grants and contract revenue. The two largest federal sponsors are the National Institutes of Health and the Department of Health and Human Services, comprising 63% and 10%, respectively, of federal research funding in FY 2014.

OPERATING PERFORMANCE, BALANCE SHEET, AND CAPITAL PLANS: PRUDENT FISCAL MANAGEMENT DRIVES SOLID OPERATING RESULTS AND CONTINUED CAPITAL INVESTMENT EVEN THROUGH VOLATILE STATE FUNDING PERIODS

USF’s strong fiscal oversight and evidence of managing expenses during periods of challenged revenue growth support our expectation that the university will continue to generate positive operations. For FY 2014, USF drove its operating margin back up to nearly 6%, after generating operating deficits due to large state funding cuts in fiscal years 2012 and 2013. The state restored the funding cuts in FY 2014, increased funding for higher education for FY 2015 and the governor has proposed another increase for FY 2016.

USF performed better than initially anticipated in FY 2014 due to strong performance in the state's new performance based funding formula and expense controls. Based on the first 6-months of FY 2015, we expect an operating surplus. In coming years, margins could narrow given the state’s freezing of undergraduate tuition and focus on affordability which could expand tuition-setting limits to graduate programs. However, we expect USF to continue benefiting from the performance based funding model.

USF’s financial resources provide a good cushion relative to a manageable debt burden, with pro-forma debt to revenue of 0.4 times for FY 2014. Through a combination of gift revenue and operating surpluses, financial resources should grow. Expendable financial resources are up after declining for two years due to reduced state support. Fiscal 2014 expendable financial resources of $522.4 million cushion debt 1.1 times and operations 0.5 times in FY 2014. The university is in the midst of a $1 billion comprehensive campaign, having raised $830 million.

At this time, there are no new money debt plans, though the university is investigating use of a developer to finance the costs of updating nearly 20% of its existing housing stock. Other capital projects will be financed through the receipt of state capital support and gifts, including the college of medicine, which has already received most of the appropriation regardless of whether it will remain on USF’s main campus in north Tampa, or be relocated downtown.

Liquidity

USF has good liquidity that is expected to remain favorable due to active fiscal oversight. Unrestricted monthly liquidity of $512 million at the close of FY 2014 provided 195 monthly days cash on hand.

DEBT AND OTHER LIABILITIES: MANAGEABLE FINANCIAL LEVERAGE AND MEASURED REDUCTION IN DEBT STRUCTURE RISKS

USF’s debt burden should remain manageable in the near future as the university has a modest amount of debt outstanding given historically strong support from the state and funding to construct the college of medicine has been appropriated by the state or gift funded. As previously indicated, USF has identified large-scale housing needs to replace obsolete housing stock. Moody’s will evaluate the impact of the financing structure on the
university’s credit profile when plans become more certain.

Debt Structure

All of the university’s debt is fixed rate, but it is exposed to variable rate debt through debt held at its direct support organizations. Pro-forma variable rate debt will constitute approximately 35% of USF’s pro-forma debt portfolio after the remarketing of the Series 2012A bonds to fixed rate.

Debt-Related Derivatives

USF is party to eight floating-to-fixed interest rate swap agreements, with a current notional amount of $235 million on debt of the Financing Corporation and Research Foundation. USF has the optional right to terminate all swaps and there are no termination rating triggers. Two swaps at the Financing Corporation have collateral posting thresholds of $10 million. As of April 2, 2015, there is approximately $10 million of collateral posted. The total fair value on the entire swap portfolio is a liability of $24.5 million as of December 31, 2014.

With the proposed remarketing of the Series 2012A bonds to fixed rate, USF will terminate the swap associated with those bonds, reducing its swap position to $160 million.

Pensions and OPEB

The university’s pension and OPEB costs are moderate, comprising approximately 3% of operating expenses. However, pension funding levels are not predictable as the state sets pension contributions and those statutory contributions have more than doubled for the university over the past three years. Like most other public entities, OPEB is paid on a pay-go basis and, as a result, the net OPEB obligation grew to $75 million as of June 30, 2014.

Most university employees participate in the Florida Retirement System (FRS), which is comprised of two multi-employer, defined benefit cost-sharing plans. The State of Florida establishes contribution rates for participating employers and employees. Contribution rates covering both pension and OPEB for FY 2014 ranged from 6.95% of gross salary for the "regular" class to 19.06% of gross salary for the "special risk" class. Combined USF and employee contributions to the FRS were $15.4 million in FY 2014 and pay-go Investment Plan contributions were $4.6 million.

The State University System also provides a defined-contribution plan for eligible university instructors and administrators. In FY 2014, the university contributed 7.3% of the participant’s salaries less administrative costs for a net contribution of $18.3 million.

MANAGEMENT AND GOVERNANCE: HIGHLY DELIBERATE PLANNING AND STRONG FISCAL PRACTICES

USF's conservative budgeting and short and long-term planning are credit positives that will contribute to ongoing positive operations and strategic programmatic reinvestment. The university is focused on improving efficiencies and carefully exploring the risks and opportunities of various funding vehicles so that it can fund strategic priorities for further revenue growth and diversification.

KEY STATISTICS (FY 2014 financial data, fall 2014 enrollment data)

- Full-Time Equivalent Enrollment: 39,165 students
- Total Financial Resources: $1.05 billion
- Pro-forma Total Direct Debt: $433 million
- Total Operating Revenue: $1.11 billion
- Reliance on Student Charges (% of Moody's-adjusted Operating Revenue): 36%
- Reliance on State Appropriations (% of Moody's-adjusted Operating Revenue): 29%
- Monthly Days Cash on Hand: 192 days
- Operating Cash Flow Margin: 12%
- State of Florida Rating: Aa1 stable
OBLIGOR PROFILE

USF, one of the largest public universities in the nation, is a comprehensive research university enrolling 48,578 headcount enrollment in fall 2014 across its Tampa, St. Petersburg and Sarasota campuses. The university generates $1.11 billion primarily through student charges, state appropriations, and grants and contracts revenue.

LEGAL SECURITY

The Series 2015 revenue bonds for the Marshall Student Center is secured solely by the project revenues, secured by a lien on the student center revenues prior to payment of operating expenses. Additional bonds may be issued with 1.20 times pro-forma maximum annual debt service coverage from net revenues.

The revenue bonds for the parking system debt is payable solely from the net revenues of the parking system of the Tampa campus, including funds derived from a mandatory transportation access fee paid by all students, faculty and staff. All parking system bonds are on parity. An additional bonds test requires 1.2 times pro-forma maximum annual debt service coverage. Debt service coverage is estimated at 1.7 times in FY 2015.

The A1 rating on the certificates of participation is based on the lease-back structure of the debt between the USF Financing Corporation and the university secured solely by a narrow revenue pledge. The COPs are secured solely by Pledged Revenues, which are comprised of the System Revenues and amounts on deposit in the Pledged Accounts, including investment earnings and net proceeds. The COPs are not a general obligation of USF or of the USF Financing Corporation. System Revenues include all gross income and revenues received by the Financing Corporation under various Lease Schedules from the ownership and/or operation of the System Facilities. After the proposed issuance, System Facilities will include the Housing Facilities on the Tampa Campus and the Housing and Parking Facilities on the St. Petersburg Campus. Debt service coverage is estimated at 1.4 times in FY 2015.

The Financing Corporation may issue additional certificates on parity with the COPs provided that the university’s CFO certifies that the System Revenues are projected to be at least 110% of maximum Basic Rent Payments. In addition, the Financing Corporation reserves the right to add and remove facilities and properties from the System Facilities provided that the COPs retain a credit rating of at least equal to the rating in effect prior to the change.

There is no debt service reserve account specifically for the COPs. However, if the undesignated fund balance of the Housing System should fall below the maximum Basic Rent Payment on the outstanding certificates, then the Reserve Requirement for the COPs will equal the maximum Basic Rent Payment in the current Fiscal Year.

USE OF PROCEEDS

The Series 2015 Capital Improvement Refunding Revenue Bonds (Marshall Center Project) is being issued to refund the outstanding Series 2005C Certificates of Participation and pay issuance costs.

The Series 2015A Certificates of Participation is being issued to do a current refunding of the Series 2005A Certificates of Participation and pay issuance costs.

The Series 2012A Certificates of Participation are being remarketed to a fixed rate mode.

RATING METHODOLOGY

The principal methodology used in this rating was U.S. Not-for-Profit Private and Public Higher Education published in August 2011. The additional methodology used in rating the lease backed debt was The Fundamentals of Credit Analysis for Lease-Backed Municipal Obligations published in December 2011. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

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