

CREDIT OPINION

18 April 2016

New Issue

Rate this Research >>

Analyst Contacts

Mary Kay Cooney 212-553-7815
 AVP-Analyst
 marykay.cooney@moodyys.com

Karen Kedem 212-553-3614
 VP-Sr Credit Officer/
 Manager
 karen.kedem@moodyys.com

Joshua M Levine 212-553-4826
 Associate Analyst
 joshua.levine@moodyys.com

Northern Kentucky University

New Issue - Moody's Assigns A1 Underlying and Aa3 Enhanced to Northern Kentucky Univ's \$45M 2016 Ser A&B; Outlook Stable

Summary Rating Rationale

Moody's Investors Service has assigned an A1 underlying and Aa3 enhanced rating to Northern Kentucky University's (NKU) proposed \$44.6 million of fixed rate General Receipt Refunding Bonds, 2016 Series A (maturing 2027) and 2016 Series B (maturing 2028). At the same time, Moody's affirmed the A1 underlying and Aa3 enhanced ratings on \$119 million of general receipt bonds outstanding. The outlook on the underlying and enhanced ratings is stable.

The university's underlying A1 rating reflects its moderate scale and proximity to the greater Cincinnati metropolitan area, lending itself to internship and employment opportunities for its primarily commuter student population. Solid liquidity, manageable leverage, and consistently positive operations also support the A1. Challenges facing NKU include softening growth in net tuition revenue and funding or cost pressure that could result from the Commonwealth of Kentucky's (Aa2 stable) budgetary and pension challenges.

The Aa3 enhanced rating is derived from the structure and mechanics of the Kentucky Public University Intercept Program, which is based on the commonwealth's current rating and outlook, combined with the sufficiency of interceptable funds.

Credit Strengths

- » Moderate scale and proximity to the greater Cincinnati metropolitan area provides internship and employment opportunities for its nearly 12,600 full-time equivalent (FTE) students
- » Consistently sound positive operating cash flow margins (11% over fiscal 2013-15 period) providing over 2 times debt service coverage
- » Good liquidity, with 192 monthly days cash on hand
- » Manageable leverage (debt to cash flow of 5.2 times), with no new debt plans
- » Bondholders of the general receipt bonds benefit from Kentucky's public university intercept enhancement program

Credit Challenges

- » Slowed net tuition revenue growth due to weak regional demographics and stiff competition for students (student charges are 60% of operating revenues)
- » Funding or cost pressure likely to result as Kentucky grapples with economic and pension funding challenges

Rating Outlook

The stable outlook reflects our expectation that operating cash flow will remain in the 10%-12% range, providing good coverage of debt service obligations, and liquidity will remain sound.

The stable outlook for the enhanced rating is based on the commonwealth's outlook.

Factors that Could Lead to an Upgrade

- » Underlying rating: Strengthened growth in net tuition revenue leading to sustained improvements in cash flow and financial reserves
- » Enhanced rating: Upgrade in the Commonwealth of Kentucky's rating

Factors that Could Lead to a Downgrade

- » Underlying rating: Erosion of liquidity or substantial increase in leverage
- » Enhanced rating: Deterioration in credit quality of the Commonwealth of Kentucky or insufficient debt service coverage by interceptable funds

Key Indicators

Exhibit 1

| NORTHERN KENTUCKY UNIVERSITY, KY | | | | | |
|--|---------|---------|---------|---------|---------|
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| Total FTE Enrollment | 13,633 | 13,545 | 13,283 | 12,861 | 12,592 |
| Operating Revenue (\$000) | 203,890 | 207,292 | 210,765 | 212,033 | 213,994 |
| Annual Change in Operating Revenue (%) | 5.1 | 1.7 | 1.7 | 0.6 | 0.9 |
| Total Cash & Investments (\$000) | 173,034 | 209,614 | 214,950 | 229,515 | 229,286 |
| Total Debt (\$000) | 98,457 | 103,825 | 94,860 | 137,130 | 128,218 |
| Spendable Cash & Investments to Total Debt (x) | 1.3 | 1.6 | 1.8 | 1.3 | 1.4 |
| Spendable Cash & Investments to Operating Expenses (x) | 0.7 | 0.8 | 0.8 | 0.9 | 0.8 |
| Monthly Days Cash on Hand (x) | 132 | 177 | 180 | 191 | 192 |
| Operating Cash Flow Margin (%) | 16.6 | 13.4 | 11.4 | 11.8 | 11.5 |
| Total Debt to Cash Flow (x) | 2.9 | 3.7 | 4.0 | 5.5 | 5.2 |

Source: Moody's Investors Service

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Recent Developments

On March 31, 2016, Kentucky's governor imposed a 4.5% cut on the fiscal year (FY) 2016 state appropriations on seven of the commonwealth's eight public universities. For NKU, the cut totaled \$2.2 million of its \$48.5 million total FY 2016 operating appropriations. The Kentucky Attorney General filed a lawsuit alleging the governor's cut was not aligned with current legislation requiring a declared budgetary shortfall. As of April 18, 2016, the cut had been implemented but no decision had been made on its legality.

On April 15, 2016, the Executive Branch Biennial Budget (HB 303) was passed by the Kentucky General Assembly and delivered to the Governor. The bill, in its current form, will result in ongoing annual cuts of 4.5% to the seven of eight universities for fiscal years 2017 and 2018. However, NKU's share will be offset by a recurring \$5.3 million funding equity adjustment, commencing in FY 2018, which will begin aligning the university's per student funding with regional peers within the state.

Detailed Rating Considerations

Market Profile: Focus on Employment-Oriented Curriculum To Mitigate Enrollment Challenges

Northern Kentucky University's primarily commuter enrollment will remain sensitive to changing economic conditions, with declines expected to continue in a favorable employment market. This moderate sized regional public university operates in an increasingly competitive market for a declining population of high school graduates in the region. NKU's enrollment declined in each of the last five years, falling nearly 8% from its peak during the recession. Leveraging its proximity to the greater Cincinnati metropolitan area, NKU partners with local corporations to develop an employment-oriented curriculum, yielding a roughly steady incoming class of 2,200 students.

The university's mission for strategic investment in employment-oriented curriculum, with affordable pricing, is favorable for strengthening its student demand profile. NKU's College of Informatics, opened in 2011, has been a fast growing academic segment. The College of Health Professions will be housed in the state-funded Health Innovations Center, furthering NKU's mission. Tuition pricing remains an important attribute to NKU's price sensitive students. The FY 2015 net tuition per student of \$8,800 was among the lowest of the Kentucky public universities, which does provide NKU with some pricing flexibility. Biennium FYs 2017-18 tuition increases have not yet been determined, but are expected to remain modest.

Operating Performance: Sound but Moderating Operating Performance

NKU's operating performance remains sound despite some moderation as revenue stagnates. In FY 2015, annual operating cash flow was sound at 11%, but down from a recent peak of 17% in FY 2011. Continued expected pressure on net tuition revenue and state funding highlight the importance of continued strong budgetary controls and expense flexibility. Top line net tuition revenue grew 12% from FY 2011-13, but since then declined 2.4% due to limited tuition increases and rising student aid. Student charges comprised 60% of Moody's adjusted revenues over the FY 2011-15 period. For FY 2016, management expects a slight decline in operating performance, due primarily to the recent 4.5% state appropriation reduction.

The university will continue to weather state appropriation cuts through careful oversight and expense control. Kentucky has made cuts to its biennial appropriations since 2009, including the very recent 4.5% cut of FY 2016 appropriations instituted this past March. NKU's state operating appropriations (inclusive of the FY 2016 cut) are down 14.6% since FY 2011, to \$46.4 million in FY 2016. State aid comprises a very meaningful 23% of operating revenues. Though, the current state budget for NKU's appropriations for the FYs 2017-18 biennium include the 4.5% cut going forward, the university will be receiving a recurring \$5.3 million in equity funds beginning in FY 2018 to begin realigning NKU's appropriation per student and the other Kentucky comprehensive institutions.

Wealth and Liquidity: Solid Cash and Investments, Strong Liquidity, Mitigate Softer Revenue Growth

NKU's spendable cash and investments covered nearly ten months of expenses, or 0.8 times, in FY 2015. The size and pace of growth of NKU's financial reserves are slightly stronger than similar A1-rated peers, which is favorable given the recent slowing in revenue growth. The university's limited fundraising history has primarily gone to support capital investment, reducing the potential to bolster reserves.

The Northern Kentucky University foundation manages the university's long-term endowment, with assistance from an external advisory firm. For June 30, 2015, the endowment of \$94.9 million recorded a low fiscal year return of 0.9%. As of December 31, 2015, the endowment was \$88.2 million.

LIQUIDITY

NKU's sound liquidity is an important mitigant to state funding uncertainties. The university's monthly liquidity totaled \$101 million at year end FY 2015, which translates to a strong 192 monthly days cash on hand and exceeding the A1-median of 139 days. NKU has limited additional calls on liquidity and all bonds are issued as fixed rate and amortizing.

Leverage: Manageable Leverage; Exploring Partnerships for Capital Investment

NKU's leverage is very manageable at the current time. FY 2015 debt of \$128 million to operating revenues of 0.6 times is slightly stronger than the A1 median of 0.7 times. Spendable cash and investments to debt of 1.4 times exceeded the A1-median of 0.9 times.

State funding for capital, though not frequent, has served as an important component to meeting new academic priorities. The state is directly funding \$97 million toward the cost of NKU's new Health Innovations Center that will house the College of Health Professions. An \$8 million gift from St. Elizabeth Healthcare (Kentucky, not rated) will fund a state-of-the-art healthcare simulation center. The new building is expected to open in summer 2018.

NKU capital structure will become more complicated as it explores a public-private partnership (P3) for development of a student housing/mixed use development on campus land. A request for proposal has been released, with a deadline of June 3, 2016. The university anticipates having FY 2016-18 biennium authorization for up to \$125 million in a development venture that will initially include a 500-bed residence hall. External partnerships for housing will assist NKU in reaching its goal of 3,000 total beds (current capacity is 2,004 beds) within 10 years.

DEBT STRUCTURE

All of the university's bond debt is fixed and amortizing over a 20-year period, providing predictability for budgetary planning.

DEBT-RELATED DERIVATIVES

None.

PENSIONS AND OPEB

Northern Kentucky University has a large and growing exposure to a state multiple-employer cost sharing defined benefit (DB) plan. Significant underfunding of the commonwealth's pension fund presents the potential for escalating costs for NKU and other state agencies. The state does not make any on-behalf payments. The university participates in the Kentucky Employees' Retirement System DB plan (KERS) and one defined contribution (DC) plan. The Moody's adjusted net pension liability (ANPL) for the university is \$324 million, and, combined with outstanding debt, represents 2.1 times operating revenue for fiscal year 2015, which was weaker than the preliminary Moody's public university median of 1.3 times.

The university does not have a direct OPEB liability.

Governance and Management: Milestones in Implementation of Strategic Plan

NKU's leadership is making strides on its 2013-18 Strategic Plan, evidenced in the growth in two of its newer colleges (Informatics and Health Professions). The demonstrated ability to maintain healthy liquidity, manageable leverage, and consistently favorable operating performance in the midst of stagnant state aid and softer enrollment reflects NKU's conservative budgeting priorities. NKU is entering a new stage of capital development as it evaluates third party housing and mixed use development opportunities.

Smooth transitions in senior leadership positions will be essential for NKU's financial stability. A new Senior Vice President for Administration and Finance was appointed in July 2015 and a new position for chief financial officer was established and filled in August 2015.

Legal Security

The General Receipts Bonds are secured by a pledge of substantially all unrestricted revenue, including student tuition and fees, state appropriations, local and private grants and contracts, sales and services of educational activities, and investment income.

The general receipts pledge is subordinate to the university's Housing System Revenue Bonds (the housing bonds) outstanding in the amount of \$1.1 million as of June 30, 2015.

Aggregate pledged revenues totaled \$183 million in FY 2015, with the net pledged revenues (subordinate to the housing bonds) at \$181 million, providing pro forma maximum annual debt service (\$12.5 million) coverage of 14.5 times.

The university's general receipts bonds benefit from the presence of a state intercept program. If the university fails to make debt service payments 10 days in advance of the debt service payment date, the Secretary of the Finance and Administration Cabinet of the Commonwealth is obligated to use any funds that have been appropriated to the university but not yet expended to make debt service payments.

Given that NKU's General Receipts debt service payments are due in September and March, we are reasonably assured that sufficient non-distributed, legislatively adopted state appropriations will be available for intercept. Debt service coverage is calculated by dividing interceptable state aid available to pay the remaining periodic debt service payments. For NKU, this calculation results in a pro forma peak debt service coverage of 3.00 times (accounting for the 4.5% FY 2016 appropriation cut) which is strong sufficiency.

Use of Proceeds

Proceeds of the planned Series 2016A and 2016B bonds will be used to refund all or portions of the Series 2007A and 2008A bonds, and to pay costs of issuance.

Obligor Profile

Northern Kentucky University is a four-year public university with six colleges serving undergraduate and graduate programs, located within the greater Cincinnati metropolitan area. In FY 2015, NKU recorded operating revenues of \$214 million and for fall 2015 served an FTE enrollment of 12,592 students.

Methodology

The principal methodology used in the underlying rating was Global Higher Education published in November 2015. The principal methodology used in the enhanced rating was State Aid Intercept Programs and Financings: Pre and Post Default published in July 2013. Please see the Ratings Methodologies page on www.moody.com for a copy of these methodologies.

Ratings

Exhibit 2

Northern Kentucky University, KY

| Issue | Rating |
|---|--|
| General Receipts Refunding Bonds, 2016 Series A | A1 |
| Rating Type | Underlying LT |
| Sale Amount | \$27,840,000 |
| Expected Sale Date | 04/26/2016 |
| Rating Description | Revenue: Public University Broad Pledge |
| General Receipts Refunding Bonds, 2016 Series A | Aa3 |
| Rating Type | Enhanced LT |
| Sale Amount | \$27,840,000 |
| Expected Sale Date | 04/26/2016 |
| Rating Description | Revenue: Public University Broad Pledge |
| General Receipts Refunding Bonds, 2016 Series B | A1 |
| Rating Type | Underlying LT |
| Sale Amount | \$16,740,000 |
| Expected Sale Date | 04/26/2016 |
| Rating Description | Revenue: Public University Broad Pledge |
| General Receipts Refunding Bonds, 2016 Series B | Aa3 |
| Rating Type | Enhanced LT |
| Sale Amount | \$16,740,000 |
| Expected Sale Date | 04/26/2016 |
| Rating Description | Revenue: Public University Broad Pledge |

Source: Moody's Investors Service

© 2016 Moody's Corporation, Moody's Investors Service, Inc., Moody's Analytics, Inc. and/or their licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. AND ITS RATINGS AFFILIATES ("MIS") ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND CREDIT RATINGS AND RESEARCH PUBLICATIONS PUBLISHED BY MOODY'S ("MOODY'S PUBLICATIONS") MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. MOODY'S PUBLICATIONS MAY ALSO INCLUDE QUANTITATIVE MODEL-BASED ESTIMATES OF CREDIT RISK AND RELATED OPINIONS OR COMMENTARY PUBLISHED BY MOODY'S ANALYTICS, INC. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL, WITH DUE CARE, MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

MOODY'S CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT INTENDED FOR USE BY RETAIL INVESTORS AND IT WOULD BE RECKLESS AND INAPPROPRIATE FOR RETAIL INVESTORS TO USE MOODY'S CREDIT RATINGS OR MOODY'S PUBLICATIONS WHEN MAKING AN INVESTMENT DECISION. IF IN DOUBT YOU SHOULD CONTACT YOUR FINANCIAL OR OTHER PROFESSIONAL ADVISER. ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process or in preparing the Moody's Publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to: (a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc. have, prior to assignment of any rating, agreed to pay to Moody's Investors Service, Inc. for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moody.com under the heading "Investor Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Additional terms for Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657 AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors. It would be reckless and inappropriate for retail investors to use MOODY'S credit ratings or publications when making an investment decision. If in doubt you should contact your financial or other professional adviser.

Additional terms for Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJKK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJKK or MSFJ (as applicable) have, prior to assignment of any rating, agreed to pay to MJKK or MSFJ (as applicable) for appraisal and rating services rendered by it fees ranging from JPY200,000 to approximately JPY350,000,000.

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.

REPORT NUMBER 1023544

Contacts

Mary Kay Cooney
AVP-Analyst
marykay.cooney@moodys.com

212-553-7815

Karen Kedem
VP-Sr Credit Officer/
Manager
karen.kedem@moodys.com

212-553-3614

Joshua M Levine
Associate Analyst
joshua.levine@moodys.com

212-553-4826

CLIENT SERVICES

| | |
|--------------|-----------------|
| Americas | 1-212-553-1653 |
| Asia Pacific | 852-3551-3077 |
| Japan | 81-3-5408-4100 |
| EMEA | 44-20-7772-5454 |