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Update

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Howard University, DC

Rating Update - Moody's Assigns Ba1 Bank Bond Rating to Howard University's (DC) Series 2016; Outlook Negative

Summary Rating Rationale

Moody's Investors Service has assigned a Ba1 bank bond rating to Howard University's Taxable Bonds, Series 2016. The $160 million bonds are supported by a letter of credit from Barclays. At the same time the Ba2 rating on the Series 2011 A and Series 2011 B bonds issued through the District of Columbia has been affirmed. The bank bond rating is one notch higher because of the materially stronger legal security.

The secured Ba1 and unsecured Ba2 ratings reflect Howard's federal funding, District of Columbia location and real estate value, and market reputation as a large Historically Black College and University. These strengths are offset by thin operating performance and revenue pressures from a patient care enterprise with high Medicaid exposure and price sensitive student market. The university also has thin working capital and significant deferred maintenance. Additionally, the university has significant fixed costs including debt service, pension and healthcare benefits.

Credit Strengths

» Ongoing federal support, accounting for 26% of fiscal 2016 revenue

» Significant scale and program reach with near $800 million revenue base

» Clear commitment by newer management team to move to operating equilibrium

» Real estate and broadcast spectrum holdings that may allow monetization

» New debt structure unlocks over $130 million of collateral required under prior agreement

Credit Challenges

» Fundamental strain on both tuition and patient care revenues will require ongoing expense management

» Era of weak liquidity and deficit operations saw material increase in accounts payable and accrued expenses

» Substantial deferred maintenance

» Vulnerability to federal funding delays and expectations of ongoing thin working capital

» Considerable financial leverage with pro forma total adjusted debt of $648 million

» While improved, the debt structure still includes reliance on bank supported demand debt

Rating Outlook

The negative outlook reflects the sustained market challenges impacting Howard's student and patient care markets. Ongoing revenue deterioration will negatively impact cash flow and the resulting debt service coverage, making it difficult to meaningfully rebuild operating liquidity.

Factors that Could Lead to an Upgrade

» Significant and sustained improvement in operating performance

» Material improvement in hospital's competitive profile or successful spin off of hospital

» Demonstrated strengthening of student demand

» Ongoing gains in unrestricted liquidity

Factors that Could Lead to a Downgrade

» Inability to generate sufficient cash flow from operations to cover debt service

» Material decline in tuition and auxiliary revenue

» Rising losses from health care operations and/or a cut in the federal appropriation

» Marked decline in total cash and investments including unrestricted cash and investments

» Significant increase in debt

Key Indicators

Exhibit 1

HOWARD UNIVERSITY, DC

	2011	2012	2013	2014	2015	2015 Pro Forma
Total FTE Enrollment	9,917	9,294	9,515	9,530	9,351	9,351
Operating Revenue ($000)	832,612	854,634	836,522	799,596	796,598	796,598
Annual Change in Operating Revenue (%)	-1.3	2.6	-2.1	-4.4	-0.4	-0.4
Total Cash & Investments ($000)	440,432	445,906	508,130	549,529	559,885	559,885
Total Debt ($000)	374,795	381,989	393,328	413,537	430,822	493,913
Spendable Cash & Investments to Total Debt (x)	0.9	0.9	1.0	1.0	1.0	0.9
Spendable Cash & Investments to Operating Expenses (x)	0.4	0.4	0.5	0.5	0.5	0.5
Monthly Days Cash on Hand (x)	141	136	153	163	172	172
Operating Cash Flow Margin (%)	8.4	10.3	9.3	3.7	3.9	3.9
Total Debt to Cash Flow (x)	5.4	4.3	5.1	13.9	14.0	16.0

Enrollment is for fall of indicated year
Source: Audited financial statements and Moody's Investors Service

Recent Developments

On June 23, 2016, Howard successfully priced the $160 million Taxable Bonds, Series 2016. The proceeds will be used primarily to repay the $95 million outstanding under the Multi-bank credit agreement. That agreement required collateral posting of approximately $130 million. Simultaneously, the university plans to enter into a $75 million operating line of credit to support seasonal cash needs as well as buffer against potential delays or reductions in federal funding. The new debt structure unlocks over $130 million of collateral that supported the prior multi-bank agreement and will reduce other short-term liabilities including accounts payable. By replacing a shorter dated bank agreement with a longer dated bank agreement, the new structure will allow management more time for its financial turnaround to progress. While the new structure will result in lower short-term liabilities, long-term debt will increase by approximately 15% over the amount outstanding as of June 30, 2015.

Detailed Rating Considerations

Market Profile: Fundamental Challenges at Both Academic and Health Care Enterprises

Howard will continue to confront fundamental challenges in both its core academic programs and its hospital that will make it difficult to maintain fiscal balance without ongoing determination to closely control expenses. Although Howard is federally chartered and is one of the largest of the Historically Black Colleges and Universities, the university has struggled to maintain fiscal balance while providing a high quality education and medical care for price-sensitive patients.

The administration is determined to adjust its academic expenses to enrollment and more effectively manage enrollment given market limits. It reports plans to reduce expenses by another $28 million in FY 2017 which is necessary given the net tuition revenue declines. Net tuition revenue is down by approximately 6% in FY 2016, from FY 2014. Across those two years, enrollment edged down and discounting increased.

Despite its important role in the district, the hospital is financially challenged by a myriad of issues including a high Medicaid population, tightening reimbursement, increasing market consolidation and intensifying competition, and past disruptions resulting from changes in hospital leadership.

The university engaged Paladin Healthcare Management in fall 2014 to implement an operational improvement program. Based on preliminary results for the first 11 months of FY 2016, the hospital has produced close to $25 million improvement in net income, moving to a slightly positive net income for the period.

Howard has a long-standing history of federal support, which enables it to offer a higher cost and quality academic program than would be supported by its own independent pricing ability. The federal appropriation is expected to level out at $222 million for FY 2016 after having been $4 million less in FY 2015.

Operating Performance: Revenue Softness Creates Need for Strategic Expense Management

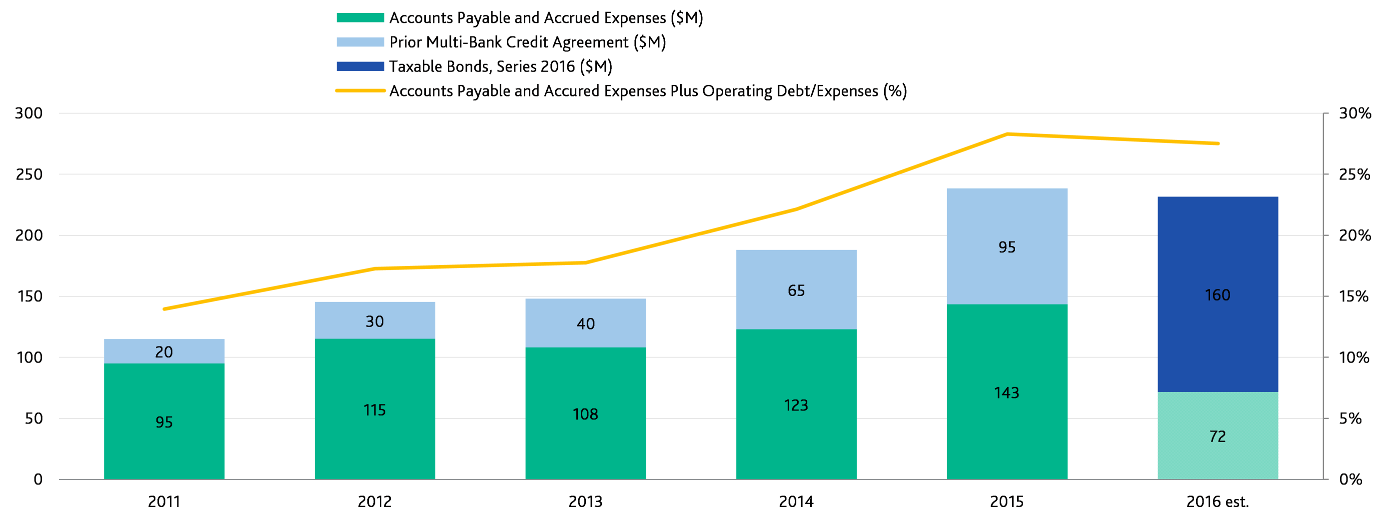
With soft prospects for revenue growth, Howard will likely have to manage through a sustained period of careful expense management without harming its reputation and programmatic strategies. Preliminary results for the first 11 months of FY 2016 show a 5% reduction in operating expenses, with approximately 60% of the reductions from the hospital division. Importantly, management has stated that to fulfill its mission as an academic medial center, it does not need to own a hospital and will seek various approaches to spinning off the hospital operations.

The university is seeking to monetize some assets. The asset monetization strategy includes certain non-core real estate holdings with property tax assessed valuations of approximately $400 million as well as the potential transfer of broadcast spectrum rights. In a credit positive move, management has committed to not use any of those one time gains to plug operations. Instead, the gains will primarily be used to make capital investments or debt reduction. Asset monetization is one potential source of capital renewal funding that does not require incremental debt.

Wealth and Liquidity: Substantial Overall Wealth But Thin Working Capital and Accounts Payable Backlog

With total cash and investments of $560 million as of June 30, 2016, Howard has substantial wealth relative to its size, but 45% of the total is subject to donor or grantor restrictions and is not, therefore, readily available to support operations. In order to manage liquidity over the FY 2013 to FY 2015 period, the university delayed vendor payments. During that period, accounts payable and accrued expenses grew by 33% to $143 million. In addition the university became increasingly reliant on external bank facilities for working capital needs.

Exhibit 2
New Taxable Bonds Will Help Reduce Accounts Payable That Had Been Ramping Up



2016 estimate reflects expected reduction of vendor invoices through June 30, 2016
Source: Howard University, audited financial statements and Moody's Investors Service

LIQUIDITY

The university's liquidity is weak especially given its negative operating performance history. While the FY 2015 monthly days cash on hand of 172 days seems substantial for the rating category, this amount was artificially high through the deferral of vendor payments and reliance on external liquidity. In addition, a portion of those funds were encumbered by collateral posting requirements in the past.

With the retirement of the prior multi-bank agreement, the university will no longer have to post the over $130 million of collateral required under that agreement. This yields a material increase in effective liquidity, although working capital will still remain thin, especially as management intends to use a portion of the proceeds from the taxable borrowing to meaningfully reduce accounts payable. By June 30, 2016, the university reports that it will have paid down $28-30 million of accounts payable and that no payable will be more than 60 days in arrears.

The university is planning to enter into a $75 million line of credit to manage seasonal working capital needs and any potential timing delays or reductions in federal funding. The proposed line of credit will be secured by the same tuition revenue and mortgage pledge supporting the Series 2016 reimbursement agreement as discussed below.

Leverage: Considerable Ongoing Costs Including Cost From $160M Deficit Financing

The university has pro forma total debt of $494 million. The primary components are the taxable Series 2016 bonds ($160 million), the Series 2011 A and 2011 B bonds ($289 million) and $33 million of capital leases.

Currently, our calculation of total debt does not include debt associated with College Hall, a $107 million student residence for 1,400 students opened in August 2014, enabling the university to close older dormitories and favorably offer more attractive student housing options. Management reports healthy net revenue performance over the first two years of operations. However, should project performance falter, prompting direct university financial support, the project could negatively impact the college's credit profile.

DEBT STRUCTURE

Of total pro forma debt of $494 million, 68% is fixed rate. The $160 million of new variable rate demand debt exposes the university to interest rate and potential demand risk. Under some scenarios the reimbursement agreement would allow for a multi-year term out period. Affirmative covenants include the commitment to redeem $8.2 million in 2018 and $8.6 million in 2019. The agreement includes a rating trigger, under which a rating on any debt below BB by S&P or Ba3 by Moody's would be an event of default. The reimbursement agreement also includes a most favored nation clause that would incorporate potential future covenants.

DEBT-RELATED DERIVATIVES

None.

PENSIONS AND OPEB

Howard's defined benefit pension plan and post retirement benefits add considerable debt-like liabilities to the credit. The substantial $669 million projected benefit obligation for Howard University's noncontributory defined benefit pension plan was 81% funded at June 30, 2015. Fiscal 2015 contributions were $16 million, or 2% of operating expenses.

Howard provides post-retirement medical benefits and life insurance to certain employees. As of June 30, 2015, the unfunded projected benefit obligation was $63 million. Employer contributions for the pay-go plan were $4 million in fiscal 2015.

Governance and Management: Focus on Operating Stability Requires Investments in Institutional Control

Stabilization of senior management and demonstration of effective implementation of financial and operational strategies will be critical as the leadership remains focused on achieving operating stability in the face of potential revenue declines and constrained resources. The current president began his role in July 2014 and has recruited and replaced most senior officers. FY 2016 is the first year when the new management team had substantial control of the budget. Based on preliminary results, operating performance did improve markedly. The ability to reduce debt, build working capital and invest in facilities will require ongoing operating discipline. The asset monetization strategy, discussed above, could help propel those goals.

Legal Security

Howard's obligation to repay Barclays Bank PLC under the Reimbursement Agreement supporting the Taxable Bonds, Series 2016 is secured by pledged revenues including student tuition and fees and a mortgage pledge on certain real estate to be executed by September 30, 2016. The same pledge secures a proposed new $75 million line of credit with JPMorgan Chase Bank. The university has covenanted to provide an executed mortgage equal to at least $237.4 million (or lesser amount subject to bank approval) by September 30, 2016. Failure to provide the mortgage by that date would constitute an event of default, granting the bank rights and remedies including demanding immediate repayment.

The Series 2011A and 2011B Revenue Bonds are unsecured general obligations, additionally secured by a debt service reserve fund and other funds created under the indenture. The debt service reserve fund for the Series 2011A bonds only, holds approximately $12.6 million and was established at 50% of maximum annual debt service. There is a rate covenant of 1.1 times and an additional bonds test that requires a certificate of the university's chief financial officer concluding that projected debt service coverage will be at least 1.1 times upon issuance and, on a pro forma basis for the following fiscal year. If the debt service coverage falls below 1.1 times, the university will not be in default as long as it hires a consultant and does not drop below 1 times coverage as defined in the Loan Agreement.

Use of Proceeds

Proceeds from the $160 million taxable borrowing will primarily be used to repay the $95 million multi-bank credit agreement and to meaningfully reduce accounts payable.

Obligor Profile

Howard University is a private not-for-profit historically black college and university in Washington, D.C. with approximately 9,400 full-time equivalent students and $800 million in operating revenue. It is known for its undergraduate health sciences, business, marketing, and communication programs as well as its graduate programs in business, law, and medicine. The university owns the Howard University Hospital where medical students do their internships, residencies, and/or fellowships and where members of its faculty practice provide clinical services. The university has several subsidiaries engaged in international initiatives such as technical assistance programs in Malawi.

Methodology

The principal methodology used in this rating was Global Higher Education published in November 2015. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

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