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Contacts

Mary Kay Cooney +1.212.553.7815
AVP-Analyst
marykay.cooney@moodys.com

Susan I Fitzgerald +1.212.553.6832
Associate Managing Director
susan.fitzgerald@moodys.com

Debra Roane +1.212.553.6899
VP-Sr Credit Officer
debra.roane@moodys.com

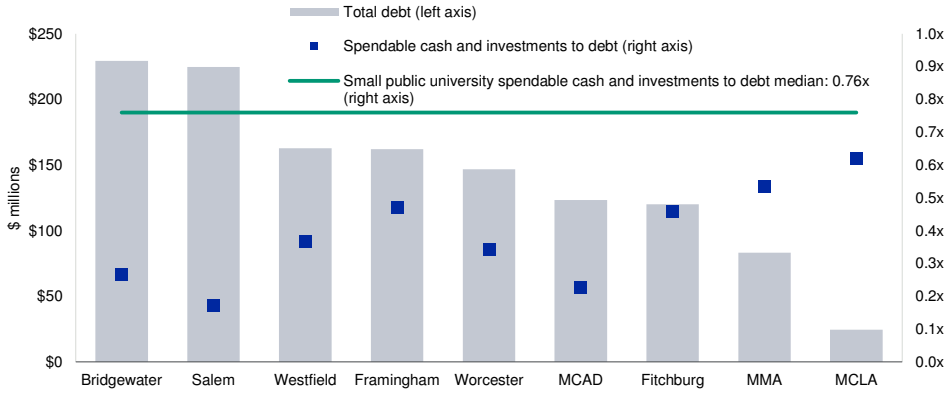
Massachusetts State College Building Authority, MA

Update to credit analysis

Summary

Massachusetts State College Building Authority (Aa2 stable) very good strategic positioning reflects its role as a component unit of the Commonwealth of Massachusetts (Aa1 stable) to design and construct auxiliary facilities across the nine member Massachusetts State University System, with aggregate full-time equivalent (FTE) enrollment of nearly 41,000. Strong oversight and good operating performance of the projects is strengthened by the presence of an aggregate state appropriation intercept mechanism, a debt service reserve fund, and additional available reserves. Offsetting challenges include high leverage, with stagnating enrollment trends and student affordability concerns limiting growth in student charges and operating performance. Slow growth in cash and investments constrains deleveraging, though significant capital plans are not expected through fiscal 2020.

Exhibit 1
High financial leverage across system universities is partially mitigated by strong MSCBA oversight
Fiscal 2017 data



MCAD is Massachusetts College of Art and Design; MMA is Massachusetts Maritime Academy; and MCLA is Massachusetts College of Liberal Arts.
Source: Moody's Investors Service

Credit strengths

» Projects across nine Massachusetts public universities, with total FTE of nearly 41,000 and average student housing occupancy of 93.4%

» Good debt service coverage from project-generated revenue, with no reliance on debt service reserve fund, cash reserves or intercept mechanism to date

» Strong management oversight of the development, construction and maintenance of the bond-financed auxiliary facilities

» Close ties with the state, as MSCBA is a component unit of the Commonwealth of Massachusetts

Credit challenges

» High leverage across all nine institutions based on spendable cash and investments to debt and debt to cash flow

» Highly competitive student market, with lagging demographic projections for in-state high school graduates

» Ongoing pricing sensitivity and focus on affordability limiting significant student and wealth measure growth

Rating outlook

The stable outlook is based on our expectation that pledged revenue will continue to provide good debt service coverage due to strong student demand for the bond-financed facilities and high aggregate occupancy levels. The rating incorporates good reserve levels held at MSCBA and we also expect that the commonwealth appropriations to the nine state universities will remain at least sufficient to cover debt service in the event of a revenue shortfall.

Factors that could lead to an upgrade

» Significant growth and diversification of pledged revenues, providing stronger debt service coverage

» Additional unrestricted liquidity under the control of MSCBA

Factors that could lead to a downgrade

» Sustained weakening of debt service coverage due to reduced housing occupancy

» Decline in credit quality of the Commonwealth

» Material reduction in state appropriations

Key indicators

Exhibit 2

MASSACHUSETTS STATE COLLEGE BUILDING AUTHORITY, MA

	2014	2015	2016	2017	2018
Total Fall FTE Enrollment	41,293	41,182	40,938	40,867	n/a
Total Debt ($000)	1,209,858	1,276,788	1,242,771	1,230,613	1,201,980
Aggregate Occupancy Rate at MSCBA Facilities (%)	99%	98%	98%	96%	94%
Aggregate State Appropriations ($000)	225,670	249,349	260,881	271,266	276,594

During fiscal 2019, MSCBA anticipates issuing approximately $15 million in new money Series 2019A Project Revenue Bonds for projects at Fitchburg State University, Framingham State University, Massachusetts College of Liberal Arts, and Salem State University; FTE refers to full-time equivalent enrollment.
Source: Moody's Investors Service

Exhibit 3
Key indicators by university
Fiscal 2017 data and fall 2017 FTE enrollment

MSCBA University	Fall 2017 FTE	Total Debt ($000)	Spendable Cash & Investments ($000)	Operating Revenue ($000)	Spendable Cash & Investments to Total Debt (x)	Total Debt to Cash Flow (x)	Total Debt to Operating Revenue (x)	Spendable Cash & Investments to Operating Expenses (x)	Operating Cash Flow Margin (%)	Annual Debt Service Coverage (x)
Bridgewater	9,086	229,444	61,504	186,964	.27	26.99	1.23	.32	4.5	3.67
Fitchburg	4,667	120,112	55,142	98,179	.46	8.13	1.22	.57	15.0	3.04
Framingham	4,537	162,019	76,055	104,325	.47	21.88	1.55	.72	7.1	6.71
MCAD	1,839	123,241	27,905	73,567	.23	35.70	1.68	.38	4.7	1.55
MCLA	1,401	24,533	15,210	46,541	.62	17.49	.53	.31	3.0	1.84
MMA	1,781	83,299	44,408	67,504	.53	9.46	1.23	.69	13.1	5.78
Salem	7,105	224,825	38,607	166,565	.17	9.55	1.35	.22	14.1	8.03
Westfield	5,497	162,764	59,947	125,529	.37	12.61	1.30	.50	10.3	5.87
Worcester	4,954	146,741	50,503	96,915	.34	11.31	1.51	.53	13.4	1.56

Fall 2017 full-time equivalent (FTE) enrollment.
Source: Moody's Investors Service

Profile

MSCBA is a component unit of the Commonwealth of Massachusetts and is empowered to design and construct auxiliary facility projects (such as housing, parking, and student activity centers) across the nine state public universities (Bridgewater, Fitchburg, Framingham, Salem, Westfield, and Worcester State (A2 stable) Universities, Massachusetts College of Liberal Arts, Massachusetts College of Art and Design, and Massachusetts Maritime Academy) as well as the state community colleges.

Detailed credit considerations

Market position: MSCBA role for essential auxiliary facilities at nine universities and colleges, with still very good but gradually declining occupancy

MSCBA derives credit strength from the aggregate $1 billion scope of operations among the nine universities and colleges, and the essentiality of and strong demand for the MSCBA-provided auxiliary facilities. All nine campuses host revenue-producing projects financed under this program. These institutions comprise an important sector of the Massachusetts higher education system and enrolled in aggregate an estimated 41,000 full-time equivalent (FTE) students in fall 2017 (roughly 51,000 headcount).

Universities within the authority's oversight will remain challenged by the demographic forecasts for the number of future high school graduates in Massachusetts, as well as the very competitive higher education market leading to softer growth in student charges. Aggregate undergraduate enrollment declined modestly across the nine universities in fall 2017 and is estimated to be similar for fall 2018, reflecting regional demographic trends.

Declining occupancy rates, on an aggregate basis, reflect the challenging demographic market and college affordability concerns. For fall 2018, the aggregate average occupancy for the authority's 16,922 beds was 93.4%, down from 99.1% for fiscal 2014. The lowest occupancy of 72.9% at the Massachusetts College of Liberal Arts is being addressed within a broader strategic plan developed under a new president. The MCLA plan may include reducing and reconfiguring residence options. Though no new residence facilities are expected to be constructed, renovations will be made to improve the use and attractiveness of identified housing.

Growth in MSCBA revenues derived from residence facility rent and auxiliary fees will be limited given lagging residence facility occupancy. MSCBA recorded $103.5 million in payments from the nine institutions in fiscal 2017, up 11% over fiscal 2016. However, for fiscal 2018, net payments were up a low 1% to $105 million. The MSCBA's fiscal 2017 payments were roughly 20% of the combined institutions' student charges - net tuition, fees, room, and board revenues - that totaled $514 million in fiscal 2017.

Operating performance: pledged revenue provides good debt service coverage

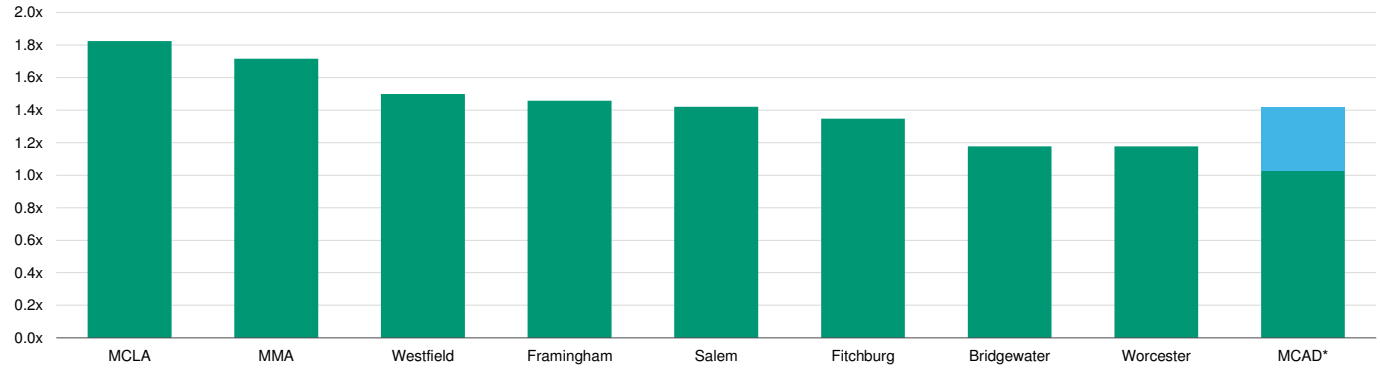
Net revenue generated by the projects is expected to continue to produce good debt service coverage. Coverage based only on net revenues, excluding reserves, exceeded 1.0x across each institution for fiscal 2018 (Exhibit 4). Favorably, to date, MSCBA has not relied

on the debt service reserve fund, available cash reserves, or the intercept mechanism to pay debt service. Based on MSCBA's careful attention to ongoing renovations and maintenance of attractive, well-used facilities, and budgeting oversight to meet debt service requirements, we expect continued good net revenue generation and occupancy.

Exhibit 4

Debt service coverage from net revenues exceeds 1.0x

Fiscal 2018 MSCBA payments and debt service



*MCAD has a contract through fiscal 2032 with Massachusetts College of Pharmacy (Aa3 stable) to lease a minimum of 203 beds of the 493-bed Treehouse Residence Hall. These lease revenues are not included in MCAD's net revenues to MSCBA, but if included would bring coverage to 1.4x.

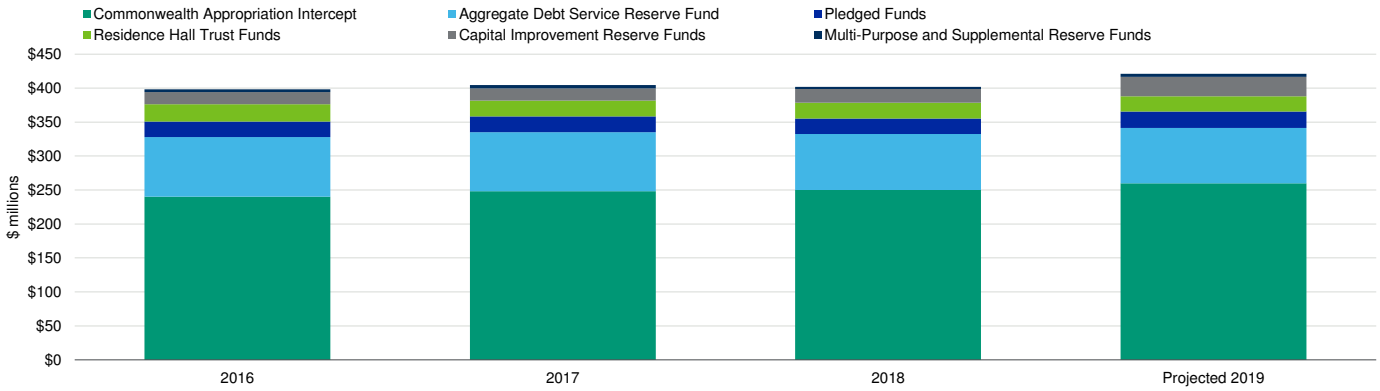
Source: Moody's Investors Service

Wealth and liquidity: ample reserves held by MSCBA and institutions

Multiple reserve funds add credit stability for debt service and plant reinvestment support. Required reserves are held either directly by the authority ($23.3 million at fiscal end 2018 and projected $33.4 million for fiscal 2019) or by the individual institutions ($46.2 million in fiscal 2018 and $46.8 million for fiscal 2019). Another $82 million includes an aggregate debt service reserve fund, bringing total fiscal 2018 reserves to $152 million and projected fiscal 2019 reserves to $161 million, well above the maximum annual debt service total of $104.8 million. Access to Commonwealth appropriations for intercept funds increases the fiscal 2018 total to $402 million (see Exhibit 5).

Exhibit 5

Reserve and interceptable funds are nearly 4x maximum annual debt service of $104.8 million



Residence hall trust funds and pledged funds are held by campuses; capital improvement reserve and multi-purpose reserve funds are held by MSCBA.

Source: Moody's Investors Service

Reserves will weaken when a joint debt service reserve fund (DSRF) legal requirement phases out, which, given continued refunding opportunities, is estimated to occur by 2027. As of June 30, 2018, the DSRF totaled $82.1 million. While no specific plan has been developed for the use of the DSRF at phase out, it is expected to be used for bond redemptions or direct capital investment. The

absence of a reserve fund, relative to current maximum annual debt service (MADS) of $105 million and high financial leverage, could create some credit distinction in the absence of strengthened debt service coverage from operating revenue support.

Cash and investments are modest relative to operations. Combined cash and investments across the nine institutions totaled $563 million for fiscal 2017. Spendable cash and investments of $465 million covered operating expenses by 0.4x, below the public university median of 0.6x.

Liquidity

MSCBA's cash and investments are very liquid, including cash and fixed income securities (such as checking and deposit accounts, money market funds, US treasuries and agencies, commercial paper, and bonds).

Leverage: highly leveraged with very limited debt plans; access to appropriation intercept

Debt issued by MSCBA on behalf of the nine public universities is high with $1.2 billion outstanding as of June 30, 2018. Following a capital-intensive, multi-year period, spending across the system has slowed significantly, as demonstrated by a fiscal 2018 new money issue of $20 million and planned fiscal 2019 new money issue of $15 million. Plans for an additional 150-180 beds at Massachusetts Maritime Academy continue to be reviewed, though no timing has been set at the current time. The Aa2 rating heavily incorporates an expectation that the pace of new money borrowing will remain low in coming years.

The authority receives approval to support projects on Massachusetts community college campuses. The most recent issue was in fiscal 2017. These bonds, currently outstanding in the amount of $5.5 million are backed by auxiliary revenue, reserves, and an intercept of appropriations of only that one community college. The community college debt does not have any claim on the revenue or reserves of the nine state universities.

Debt structure

All of MSCBAs debt is fixed-rate which aids budgeting and provides for predictable annual debt service.

Legal security

Pledged revenues and required reserve funds, in addition to the state appropriation intercept program provide solid support for the bonds. MSCBA maintains a contract with the State Board of Higher Education which empowers the authority to commit the nine state universities to payment of debt service. The authority sets fees and rates for sufficient debt service coverage on each project.

Each university is further required to set aside 25% of its average annual aggregate debt service costs in a Pledged Trust Fund to cover any deficiencies of project revenue for debt service. The pledged trust funds and residence hall trust funds are held by each campus. As of June 30, 2018, aggregate pledged funds and residence hall trust funds totaled $23.2 million and $23.1 million, respectively. A debt service reserve fund, outstanding at $82.1 million, is also available, though is expected to be phased out (see Wealth and liquidity section).

The state appropriation intercept mechanism could be accessed for payment of debt service or replenishment of the joint debt service reserve fund. The authority is required to report on the sufficiency of available funds to pay debt service on its outstanding debt to the Board of Higher Education (BHE) and the state comptroller no later than September 30, in the case of debt service payments due November 1, and no later than January 31, in the case of debt service payments due May 1. Cross-collateralization of state intercept funds to cure any deficiency further strengthens the intercept provision.

Should there be an insufficiency for debt service, the state comptroller transfers amounts from all state universities appropriation accounts (on a pro-rata basis, based on each university's amount of outstanding debt) to cure the shortfall within five days, but in any event no later than the applicable deposit date (October 10 for the November 1 debt service payment and the last business day of February for the May 1 debt service payment). Fiscal 2018 actual appropriations totaled $250.3 million and fiscal 2019 appropriations are budgeted at $260.1 million, and cover current MADS by approximately 2.5x

Debt-related derivatives

None.

Pensions and OPEB

The authority and the nine institutions have moderate exposure to additional debt-like obligations through its participation in the Massachusetts State Employees Retirement System (SERS), which is a cost sharing multiple-employer retirement plan sponsored by the state. The Moody's three-year adjusted net pension liability (ANPL) for the combined MSCBA and institutions is $390 million, and combined with outstanding debt, represents 1.6x operating revenues for fiscal year 2018. In contrast, the public university median is 1.3x.

The authority and universities do not administer OPEB plans, but instead participate in the plan provided by the commonwealth.

Governance and management: sound stewardship by stable leadership and commonwealth oversight

MSCBA's careful management and oversight of capital project development, construction, and delivery add credit strength. The small, although stable, staff has a good track record of delivering projects on time and within budget. Over the past decade, MSCBA has been successful in reducing deferred maintenance needs, favorably positioning itself to meet annual investment largely through current year revenue.

State oversight of the capital program is bolstered by the authority being required to receive project approvals from the Board of Higher Education and the Secretary of the Executive Office for Administration and Finance of the Commonwealth to issue debt for projects at the state universities. The Authority is governed by a nine-member Board that is appointed by the Governor, further strengthening government linkages.

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