

REVISED

FY 2009 ASSESSMENT OF FINANCIAL STRENGTH

OF

ARIZONA STATE UNIVERSITY

NORTHERN ARIZONA UNIVERSITY

THE UNIVERSITY OF ARIZONA



NORTHERN
ARIZONA
UNIVERSITY



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TABLE OF CONTENTS

	Page
EXECUTIVE SUMMARY	iii
INTRODUCTION	
Methodology	1
Linkage to 2020 Vision	2
PRIMARY RESERVE RATIO	
Ratio Description	3
ASU/NAU/UA Ratios, FY 2004-2009	6
ASU/NAU/UA Bullet Analysis	7
VIABILITY RATIO	
Ratio Description	10
ASU/NAU/UA Ratios, FY 2004-2009	12
ASU/NAU/UA Bullet Analysis	13
RETURN ON NET ASSETS RATIO	
Ratio Description	16
ASU/NAU/UA Ratios, FY 2004-2009	18
ASU/NAU/UA Bullet Analysis	19
NET OPERATING REVENUES RATIO	
Ratio Description	21
ASU/NAU/UA Ratios, FY 2004-2009	22
ASU/NAU/UA Bullet Analysis	23
COMPOSITE FINANCIAL INDEX (CFI)	
CFI Description	25
ASU/NAU/UA CFI, FY 2004-2009	28
ASU/NAU/UA Bullet Analysis	29
BENCHMARKING	
Four Ratios	30
Composite Financial Index	31
ARIZONA STATE UNIVERSITY DATA	
NORTHERN ARIZONA UNIVERSITY DATA	
THE UNIVERSITY OF ARIZONA DATA	
APPENDIX A: COMMENTARY BY CAROL CAMPBELL	
APPENDIX B: “TRADITIONAL” FY 2009 FINANCIAL RATIO ANALYSIS	

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EXECUTIVE SUMMARY

NOTE: In response to Regent requests at the January 28, 2010, meeting of the Audit Committee, this document has been revised since its first publication on January 15, 2010, to include the following:

1. FY 2009 data for the peer institutions of Arizona State University, Northern Arizona University, and The University of Arizona. The original document contained only FY 2007 and FY 2008 peer data because FY 2009 data was not yet available. This FY 2009 peer data is reflected in the following places in this document:
 - a. In the small peer data tables in this Executive Summary. The FY 2008 peer data has been replaced with FY 2009 peer data for each of the four CFI ratios and for the CFI.
 - b. In the graphs for the four ratios and the CFI. A data point has been added to each graph to reflect the FY 2009 peer median. All graphs now show three years of peer data.
 - c. Behind the university “Data” tabs. The complete detail of the FY 2009 peer data, showing ratios for each peer institution, has been added behind each university’s “Data” tab. The FY 2007 and FY 2008 peer data that appeared in the original document has been retained.
2. In Appendix B, “FY 2009 Traditional” Financial Ratio Analysis. Bar charts showing the composition of Total Revenue for each university over the 8-year reporting period have been added at pages 14-19 of Appendix B. This data reflects university revenues only and does not include the revenue of component units, e.g., Foundations, Alumni Associations, Capital Facilities Finance Corporations. These charts break out the federal fiscal stabilization funds received in FY 2009.

The Arizona Board of Regents annually prepares an analysis of the financial condition of Arizona State University, Northern Arizona University, and The University of Arizona using data from the universities’ audited financial statements. For the second year, this FY 2009 Assessment of Financial Strength uses the methodology developed by KPMG, BearingPoint, et al. and used by university governing boards and accreditation agencies across the country.

The methodology employs four financial ratios and a single indicator of financial health—the Composite Financial Index—and provides a scale against which to benchmark our universities. The analysis is for each university’s entire enterprise, which includes their component units.

PRIMARY RESERVE RATIO

The Primary Reserve Ratio provides a snapshot of financial strength and flexibility by indicating how long the institution could function using its expendable net assets (those assets that the university can access relatively quickly to satisfy its debt obligations) without relying on additional net assets generated by operations. ASU's ratio of 22% (11 weeks of spending), NAU's of 34% (18 weeks), and UA's of 32% (17 weeks) fall below the methodology's 40% (20 weeks) threshold for moderate financial health but are above the 10-15% (5-8 weeks of spending) potential problem range. ASU's and UA's ratios are virtually unchanged from prior year, while NAU's ratio improved significantly from 24% to 34%. Factors contributing to the FY 2009 ratios include losses on endowment investments due to the downturn in the financial markets, thus reducing net assets; and significant capital expansion programs using debt financing. A lower Primary Reserve Ratio is anticipated during such expansions.

FY 2009 benchmarking data:

	FY 2009 Ratio	Peer Median	Rank of Peers*
ASU	22%	56%	12/13
NAU	34%	25%	7/12
UA	32%	56%	12/14

*Each university compiles data for its 15-institution peer set. However, not all peer institutions had released their FY 2009 audited financial statements as of our publishing date. Therefore, ASU is reporting for 12 peers, and rankings are for those 12 plus ASU. NAU is reporting for 11 peers, and rankings are for those 11 plus NAU. UA is reporting for 13 peers, and rankings are for those 13 plus UA.

VIABILITY RATIO

The Viability Ratio measures one of the most basic determinants of clear financial health: the availability of expendable net assets to cover debt should the institution need to settle its obligations as of the financial statement date. Although a ratio of 100% or greater indicates that an institution has sufficient expendable net assets to satisfy debt obligations, this value should not serve as an objective. While there is no absolute threshold indicating whether the institution is no longer financially viable, the Viability Ratio, along with the Primary Reserve Ratio, can help define an institution's "margin for error."

ASU's ratio of 24.3%, NAU's of 34.7%, and UA's of 46.0%, while falling below the methodology's 125% threshold for moderate financial health, are not unexpected. All three universities and their component units have incurred significant debt for research infrastructure, student housing, and other capital projects over the last six years. However, all three universities are "going concerns" and expect to receive additional revenues subsequent to June 30, 2009, including state General Fund appropriations that included appropriated debt service for

research buildings. ASU receives state support for debt service for 41% of its outstanding long-term debt; NAU for 26%; and UA for 18%. This ongoing state support is not reflected in the universities' expendable net assets and, therefore, cannot be included in the calculation of this ratio. The Viability Ratio has remained relatively stable at NAU and UA over the last six years but has trended downward at ASU.

FY 2009 benchmarking data:

	FY 2009 Ratio	Peer Median	Rank of Peers
ASU	24.3%	192%	13/13
NAU	34.7%	42%	9/12
UA	46.0%	186%	14/14

RETURN ON NET ASSETS RATIO

The Return on Net Assets Ratio determines whether the institution is financially better off than in previous years by measuring total economic return. It provides the most comprehensive measure of the growth or decline in total wealth of an institution over a specific time. NAU's ratio of 8.3%, although down slightly from the 11% reported in FY 2008, is well above the 6% threshold, demonstrating a strong commitment to balanced budgets along with an ability to respond to financial and budgetary changes. ASU's ratio of -4.8% and UA's of -3.6% were heavily impacted by the challenging financial market conditions in FY 2009 that resulted in significant decreases in endowment market values and large decreases in net assets of their component units—\$130 million decrease at ASU and \$60 million decrease at UA. All three universities (excluding their component units) reported increases in net assets. However, only NAU (university only) would still have reported an increase in net assets had it not been for the FY 2009 Federal Fiscal Stabilization Funds distributed to the universities.

FY 2009 benchmarking data:

	FY 2009 Ratio	Peer Median	Rank of Peers
ASU	-4.8%	-4%	9/13
NAU	8.3%	-7%	1/12
UA	-3.6%	-4%	7/14

NET OPERATING REVENUES RATIO

A positive Net Operating Revenues Ratio indicates that the institution experienced an operating surplus for the year. Generally speaking, the larger the surplus, the stronger the institution's financial performance as a result of the year's activities. A negative ratio indicates a loss for the year. NAU's FY 2009 Net Operating Revenues Ratio of 7.2% indicates that the university and its component units experienced an operating surplus for the year, and the ratio exceeds the

methodology's 4% threshold. NAU has recorded a positive Net Operating Revenues Ratio for six consecutive years, indicating strong revenue growth accompanied by strong spending controls. ASU's -2.2% ratio and UA's -1.4% ratio indicate an operating deficit for the year—total expenses exceeded total revenues from all sources. Because ASU and UA Foundations hold significantly larger endowments than the NAU Foundation, they were more significantly impacted by decreases in endowment market values and investment losses.

FY 2009 benchmarking data:

	FY 2009 Ratio	Peer Median	Rank of Peers
ASU	-2.2%	-3%	6/13
NAU	7.2%	-5%	2/12
UA	-1.4%	-8%	5/14

COMPOSITE FINANCIAL INDEX (CFI)

After looking at the relative strengths and weaknesses of each of the four core ratios, it is useful for an institution to be able to combine them into a single score. This combination, using a reasonable weighting plan, allows a weakness or strength in a specific ratio to be offset by another ratio result, thereby allowing a more holistic approach to understanding the total financial health of the institution. The Composite Financial Index (CFI) is useful in helping governing boards and senior management understand the financial position that the institution enjoys in the marketplace.

The CFI is one indicator of the financial health of an institution and must be combined with nonfinancial indicators, such as enrollment growth, national recognition of academic and research programs, and construction of new facilities, in determining the overall health of the university. The CFI scale ranges from -1 to +10, a -1 indicating the need to assess the institutional ability to survive, and a +10 indicating the ability to deploy resources to achieve robust mission. All three universities fall on the lower end of this scale.

NAU's FY 2009 CFI of 2.6 is up slightly from the prior year 2.4, indicating a strengthening of its financial position. NAU's CFI has remained in the 1.6 to 3.2 range over the past six years, with the highest CFI reported in FY 2007 and the lowest in FY 2006. ASU's CFI of 0.5 and UA's of 0.9 have both been cut in half from prior year. ASU's CFI has fluctuated in the 0.5 to 2.4 range over the last six years, with the highest CFI reported in FY 2007 and the lowest in FY 2009. UA's CFI has fluctuated in the 0.9 to 2.8 range over the last six years, with the highest CFI reported in FY 2007 and the lowest in FY 2009.

The fluctuation of the universities' CFIs within a relatively narrow range over the last six years indicates that in both good financial times and in bad, our universities fall rather low on this scale, necessitating analysts to look at other nonfinancial indicators of a university's overall health.

The methodology cautions against applying the CFI as a peer group measure as it is the combination of four ratios and the underlying reasons for differences may be indiscernible because of a number of possible variations. This differs from the four ratios which, analyzed individually, could reveal a limited number of most likely reasons for differences. However, the methodology recommends analyzing the CFI over an extended period of time, at least five years, to effectively understand the financial direction of the institution. With this caveat, we provide this benchmarking data:

FY 2009 benchmarking data:

	FY 2009 CFI	Peer Median	Rank of Peers
ASU	0.5	3.0	13/13
NAU	2.6	1.6	3/12
UA	0.9	2.9	14/14

COMMENTARY BY CAROL CAMPBELL

These ratios and CFI's are not unexpected for reasons presented by Carol Campbell, former ASU Executive Vice President and Chief Financial Officer, to the Board's Audit Committee during its January 22, 2009, meeting. These reasons continue to apply to the universities' FY 2009 financial results:

- Structural revenue deficits:
 - Low tuition as required by ABOR's current policy that resident undergraduate tuition cannot exceed the top of the lower one-third of a 50-state survey of senior institutions.
 - State General Fund instructional and capital support are well below national averages.
 - Our universities are young Western universities lacking the endowments and legacy of financial stewardship found among alumni of older Eastern and Midwestern universities.

- Structural expense deficits:
 - All long-term debt for capital constructions sits on the universities' financial statements. While the state will sometimes appropriate funds for debt service, the impact of this is higher expenses flowing through the universities servicing a far greater debt burden without the offsetting asset base. Our universities are striving to meet a growing enrollment demand while most of the nation enjoys stable enrollment.

- With the exception of the Arizona Financial Aid Trust (AFAT) Fund, no state-supported student financial aid, requiring our universities to use tuition and other revenues for financial aid.
- Structural operating margin deficit:
 - Despite the limited revenue base and mandatory funding of both facilities and financial aid as described above, our universities operate in a competitive national marketplace where the national academic pool, lab supplies, academic journals, and other components of the Higher Education Price Index (HEPI) are the same as for all other universities. The historical annual increase in the HEPI averages about 1% higher than the CPI. This combination of factors puts intense pressure on operating margins, especially when enrollment increases must be absorbed.
- Looking ahead, deep cuts in state General Fund appropriations, combined with unprecedented endowment losses, present very challenging circumstances for our universities, who already have very little financial flexibility.

Carol Campbell's complete commentary is provided in Appendix A.

“TRADITIONAL” FY 2009 FINANCIAL RATIO ANALYSIS

The Arizona University System FY 2009 Financial Ratio Analysis (the “traditional” analysis), presenting 10 ratios for the 8-year period FY 2002-FY 2009, is provided in Appendix B.

INTRODUCTION

METHODOLOGY

This assessment of the financial strength of Arizona State University, Northern Arizona University, and The University of Arizona for the fiscal year ending June 30, 2009, is based on methodology presented in *Strategic Financial Analysis for Higher Education*, Sixth Edition, a project jointly developed and sponsored by Prager, Sealy & Co., LLC; KPMG LLP; and BearingPoint, Inc. This methodology is the continuation of work begun in the 1970's by Peat Marwick Mitchell & Co., predecessor to KPMG, and updated and refined over a period of almost 35 years. For our purposes, we will refer to this methodology as the "KPMG" methodology.

While the methodology is comprehensive, our analysis will focus on four ratios arising from the four questions under the overarching question, "What is the overall measurement of financial health?"

- **PRIMARY RESERVE RATIO:** Are resources sufficient and flexible enough to support the mission?
- **VIABILITY RATIO:** Are financial resources, including debt, managed strategically to advance the mission?
- **RETURN ON NET ASSETS RATIO:** Does asset performance and management support the strategic direction?
- **NET OPERATING REVENUES RATIO:** Do operating results indicate the institution is living within available resources?

These ratios will then be used to develop a **COMPOSITE FINANCIAL INDEX (CFI)** for each university. To quote from the KPMG methodology:

"Having one overall financial measurement of an institution helps governing boards and senior management understand the financial status of the institution. The Composite Financial Index (CFI) combines four core high-level ratios into a single score. This permits a strength or weakness in a specific ratio to be offset by another ratio, resulting in a more holistic approach to financial measurement. The CFI is best used as a component of financial goals of the strategic plan and should be calculated over a long time horizon, both historically and projected to the future."

LINKAGE TO 2020 VISION

2020 Vision, the Arizona University System’s long-term strategic plan, has four strategic goals:

- Educational Excellence
- Research Excellence
- Community Engagement and Workforce Impact
- Productivity

Strategies for achieving each of these goals have been developed by the universities, and metrics—key indicators—have been identified to measure progress toward each goal. While none of the four goals can be achieved in the absence of financial strength for each of our universities, this analysis will be done in the context of the Productivity goal. The Productivity component of 2020 Vision has two major components: (1) Producing greater numbers of degrees more efficiently, and (2) linking resources to strategic goals and objectives. A subset of the latter is an evaluation of the overall financial strength of the system and of each university. In this regard, 2020 Vision uses a key indicator, the Composite Financial Index (CFI), to assess this aspect. Again, to quote from the KPMG methodology:

“The CFI is useful in helping governing boards and senior management understand the financial position that the institution enjoys in the marketplace. Moreover, this measurement will also prove valuable in assessing future prospects of the institution, functioning as an ‘affordability index’ of a strategic plan.”

ATTRIBUTION

The explanations of the methodology contained in this document are summarized from *Strategic Financial Analysis for Higher Education*, Sixth Edition, 2005, Prager, Sealy & Co., LLC; KPMG LLP; and BearingPoint, Inc.

PRIMARY RESERVE RATIO

- Can resources be increased sufficiently in order to realize objectives?
- Does the institution need to reevaluate and perhaps modify its mission and priorities in light of its current and future resources?

The Primary Reserve Ratio is the key indicator for these specific questions. This indicator helps determine both whether there are sufficient resources and whether the net assets have enough flexibility. The formula for this ratio is:

$$\frac{\text{EXPENDABLE NET ASSETS (UNIVERSITY AND COMPONENT UNITS)}}{\text{TOTAL EXPENSES (UNIVERSITY AND COMPONENT UNITS)}}$$

The Primary Reserve Ratio measures the financial strength of the institution by comparing expendable net assets to total expenses. Expendable net assets represent those assets that the institution can access relatively quickly and spend to satisfy its debt obligations. This ratio provides a snapshot of financial strength and flexibility by indicating how long the institution could function using its expendable reserves without relying on additional net assets generated by operations. Trend analysis indicates whether an institution has increased its net worth in proportion to the rate of growth in its operating size.

It is reasonable to expect expendable net assets to increase at least in proportion to the rate of growth in operating size. If they do not, the same dollar amount of expendable net assets will provide a smaller margin of protection against adversity as the institution grows in dollar level of expenses. The trend of this ratio is important. A negative or decreasing trend over time indicates a weakening financial condition.

The Primary Reserve Ratio is useful from both an historical and a prospective review point. Historically, showing the relationship of expendable net assets to total expenses gives insight into whether the institution has been able to retain expendable resources at the same rate of growth as its commitments. Over time, total expenses demonstrate the impact of both inflation and programmatic changes on the institution. Once an item is part of the core spending pattern of the institution, it is, in many cases, difficult to change and therefore significantly reduces an institution's operating flexibility. From a prospective viewpoint, when applied to expected spending patterns, this ratio can help an institution understand the affordability of its strategic plan.

The Primary Reserve Ratio also serves as a counterpoint to the Viability Ratio presented later. An institution may have insignificant expendable net assets and little or no debt and therefore produce an acceptable value for the Viability Ratio. But low expendable net assets in relation to operating size signals a weak financial condition. In these cases, the Primary Reserve Ratio will be a much more valid measure of financial strength.

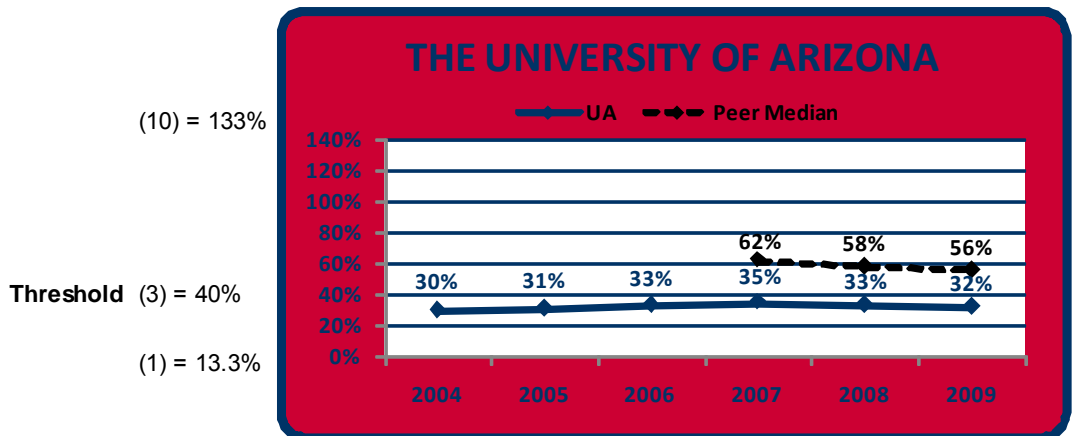
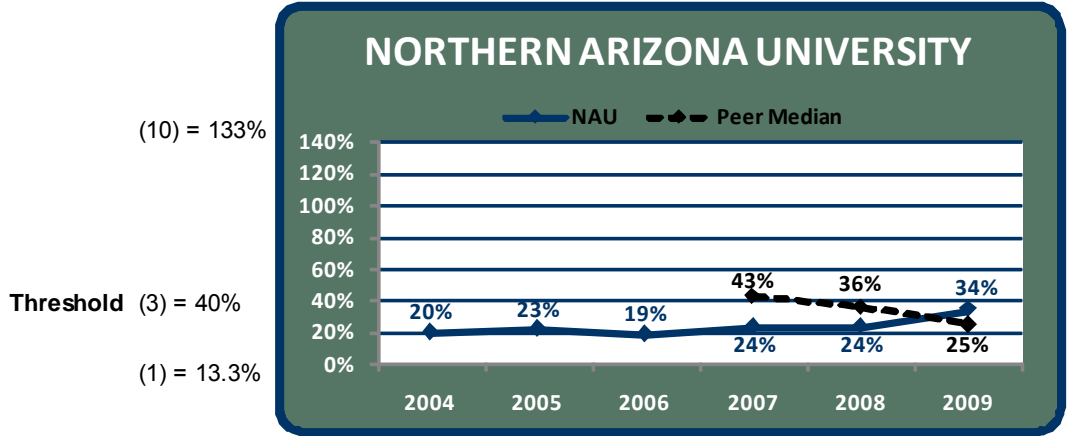
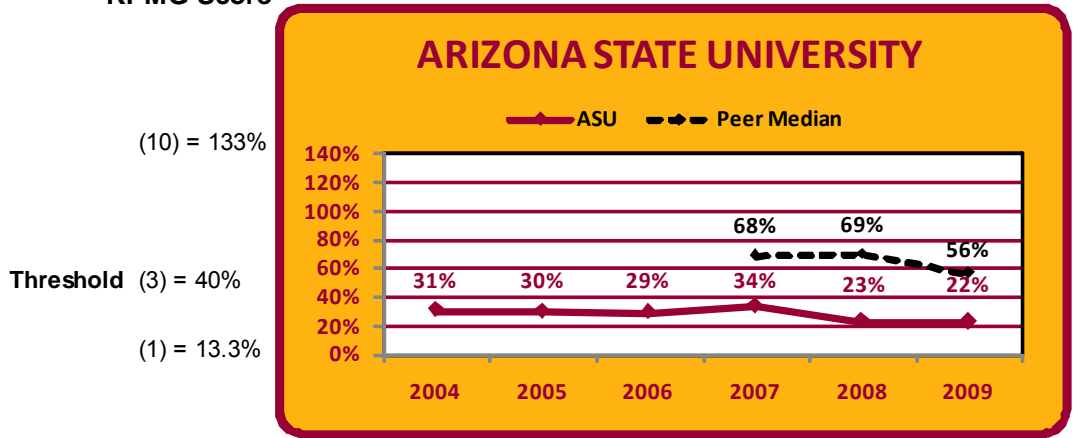
An analysis of financial statements suggests that a Primary Reserve Ratio of 40% or better is advisable to give institutions the flexibility to transform the enterprise. The implication of 40% is that the institution would have the ability to cover about 20 weeks of expenses (40% of 52 weeks) from reserves. Generally, institutions operating at this ratio level rely on internal cash flow to meet short-term cash needs, are able to carry on a reasonable level of facilities maintenance, and appear capable of managing modest unforeseen adverse financial events. Reserves are often required for capital expansion or to implement change in the institution's mission. Should these actions be in process, it would be appropriate to expect a temporary decline in this ratio. A ratio below 10% to 15% indicates that the institution's expendable net asset balances are in a position that generally requires short-term borrowing on a regular basis, since resources cover only 1 to 2 months of expenses, and that the institution tends to struggle to have sufficient resources for reinvestment. In addition, institutions with a low Primary Reserve Ratio generally lack sufficient resources for strategic initiatives and may have less operating flexibility.

The Primary Reserve Ratios for Arizona State University, Northern Arizona University, and The University of Arizona, along with each university's analysis, are presented on the next two facing pages.

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PRIMARY RESERVE RATIO

KPMG Score



- (1) = Very little financial health.
- (3) = Threshold; moderate financial health.
- (10) = Top score within range.

PRIMARY RESERVE RATIO

ASU BULLET ANALYSIS

- ASU's FY 2009 Primary Reserve Ratio of 22.0% indicates that at June 30, 2009, the university and its component units had approximately 11 weeks of annual spending available from year-end expendable balances (ASU and component units), down slightly from 12 weeks the prior year. ASU's ratio falls below the 40% threshold (representing 20 weeks of annual spending in year-end expendable balances) that indicates moderate financial health but is above the 10-15% potential problem range.
- ASU's component units reported a \$59 million decrease in temporarily restricted net assets at June 30, 2009, primarily due to losses on endowment investments.
- Total expenses of ASU and its component units remained essentially the same between FY 2008 and FY 2009.
- Absent the \$69.8 million in Federal Fiscal Stabilization Funds, ASU's FY 2009 Primary Reserve Ratio would be 17.7%, an indication of the magnitude—\$87.4 million—of the FY 2009 General Fund budget cuts.

NAU BULLET ANALYSIS

- NAU's FY 2009 Primary Reserve Ratio of 34.1% indicates that at June 30, 2009, the university and its component units had approximately 18 weeks of annual spending available from year-end expendable balances.
- NAU's ratio approaches the 40% threshold (20 weeks) that indicates moderate financial strength and flexibility and is well above the 10% to 15% potential problem range.
- NAU's FY 2009 Primary Reserve Ratio of 34.1% increased significantly over the prior year's 23.8% and has trended upward for 4 consecutive years, a sign of increasing financial strength. This has occurred in spite of significant capital improvements and expansion over the past 6 years. A lower Primary Reserve Ratio during such an expansion period would be expected.
- Absent the \$23.5 million in Federal Fiscal Stabilization Funds, NAU's FY 2009 Primary Reserve Ratio would be 28.0%, an indication of the magnitude—\$29.2 million—of the FY 2009 General Fund budget cuts.

UA BULLET ANALYSIS

- UA's FY 2009 Primary Reserve Ratio of 32.0% indicates that at June 30, 2009, the university and its component units had approximately 17 weeks of annual spending available from year-end expendable balances.
- UA's ratio approaches the 40% threshold (20 weeks) that indicates moderate financial strength and flexibility and is well above the 10% to 15% potential problem range.
- UA's Primary Reserve Ratio has remained stable over the past 6 years, fluctuating in the range of 28% to 33%. This has occurred in spite of a significant capital expansion program to add

infrastructure. Net investment in capital assets increased due to spending for leasehold improvements, new and ongoing construction projects, and equipment acquisitions. A lower Primary Reserve Ratio during such an expansion period would be expected.

- Absent the \$60.8 million in Federal Fiscal Stabilization Funds, UA's FY 2009 Primary Reserve Ratio would be 30.3%, an indication of the magnitude—\$75.9 million—of the FY 2009 General Fund budget cuts.

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VIABILITY RATIO

The Viability Ratio measures one of the most basic determinants of clear financial health: the availability of expendable net assets to cover debt should the institution need to settle its obligations as of the balance sheet date. The formula for this ratio is:

$$\frac{\text{EXPENDABLE NET ASSETS (UNIVERSITY AND COMPONENT UNITS)}}{\text{LONG-TERM DEBT (PROJECT RELATED) (UNIVERSITY AND COMPONENT UNITS)}}$$

The denominator is defined as all amounts borrowed for long-term purposes from third parties and includes all notes, bonds, and capital leases payable that impact the institution's credit, whether or not the institution directly owes the obligation. Long-term debt includes both the current and long-term portions. This would include debt of the institution's affiliated foundations, partnerships, and other special-purpose entities. It would also include amounts owed to a system or state-financing agency as it represents debt issued on the institution's behalf.

Although a ratio of 100% or greater indicates that, as of the balance sheet date, an institution has sufficient expendable net assets to satisfy debt obligations, this value should not serve as an objective. Many public institutions can operate effectively at a ratio far less than 100%, partially because the ongoing benefit of state support is not reflected in the institution's expendable net assets. Institutions with a ratio of less than 100% are, similar to those with a low Primary Reserve Ratio, less self-reliant and have significantly less operating flexibility but can function, and often function well.

The level that is "right" for the Viability Ratio is institution specific; the institution should develop a target for this ratio and others that balances its financial, operating, and programmatic objectives.

There is no absolute threshold that will indicate whether the institution is no longer financially viable. However, the Viability Ratio, along with the Primary Reserve Ratio, can help define an institution's "margin for error." As the Viability Ratio's value falls below 100%, an institution's ability to respond to adverse conditions from internal resources diminishes, as does its ability to attract capital from external sources and its flexibility to fund new objectives. If an institution is in the middle of a major capital expansion program, this ratio may well fall to a lower level than an institution that is not. However, all institutions will have limits on how much debt is affordable; establishing targets and thresholds specific to the institution will be helpful in guiding decisions on affordability of debt.

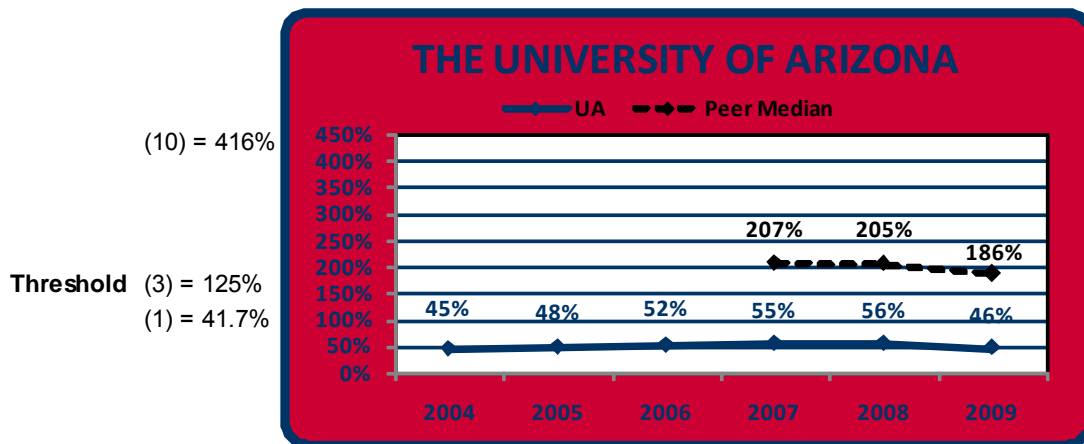
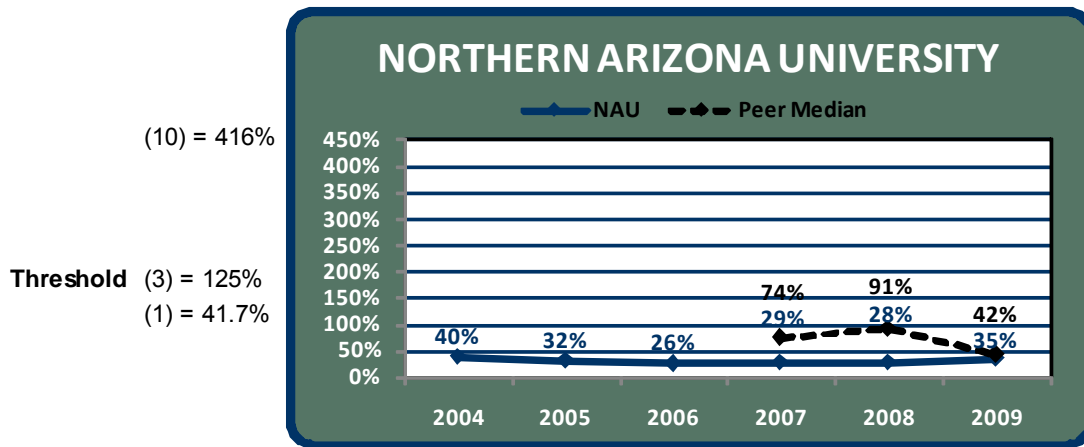
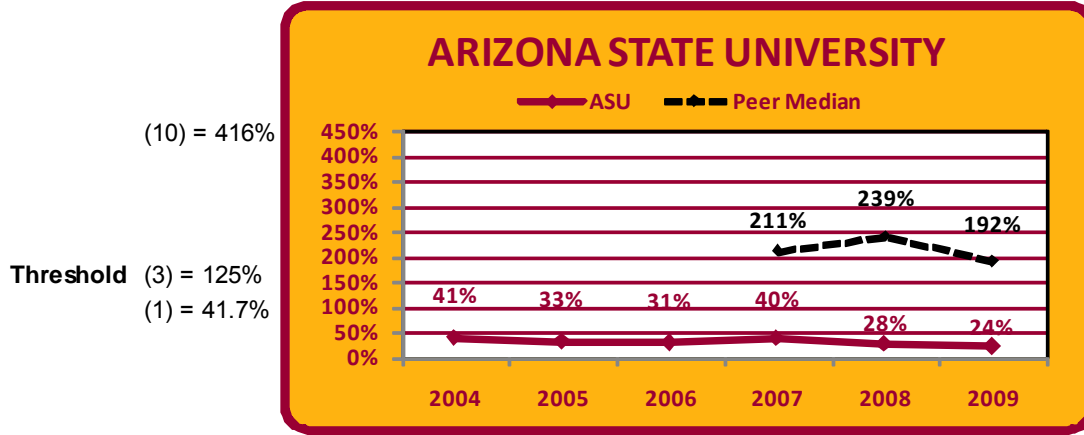
In addition, most debt relating to plant assets is long term and does not have to be paid off at once. Payments of other liabilities may similarly be delayed. Analysts should be aware that institutions often show a remarkable resiliency that permits them to continue long beyond what appears to be their point of financial collapse. In fact, institutions have been known to survive for a time with high debt levels and no expendable net assets—or even negative net

asset balances. Frequently, this means living with no margin for error and meeting severe cash flow needs by obtaining short-term loans.

The Viability Ratios for Arizona State University, Northern Arizona University, and The University of Arizona, along with each university's analysis, are presented on the next two facing pages.

VIABILITY RATIO

KPMG Score



1 = Very little financial health.
 3 = Threshold; moderate financial health.
 10 = Top score within range.

VIABILITY RATIO

ASU BULLET ANALYSIS

- ASU's FY 2009 Viability Ratio of 24.3% is below the 125% threshold and reflects the significant debt incurred by ASU and its component units, most recently for research infrastructure and student housing. This ratio means that at June 30, 2009, ASU had Expendable Net Assets sufficient to pay 24.3% of its long-term debt. A ratio of 100% would indicate the ability to satisfy all debt obligations at June 30, 2009, but should not serve as an objective. It is unlikely the university would ever be required to make debt repayments over a shorter time span than the current repayment schedule.
- The decline in this ratio from 28.1% in FY 2008 to 24.3% in FY 2009 is primarily due to the \$140 million in long-term debt issued by ASU during FY 2009.
- Approximately \$359 million, or 41%, of ASU's capital debt outstanding at June 30, 2009 (exclusive of capital leases), is financed by a separate research infrastructure state appropriation or by a share of state sales tax appropriated for this purpose. This ongoing support from the state is not reflected in the university's Expendable Net Assets at June 30, 2009, and, therefore, is not included in the calculation of this ratio.
- Absent the Federal Fiscal Stabilization Funds, this ratio would be 19.5% at June 30, 2009.

NAU BULLET ANALYSIS

- NAU's FY 2009 Viability Ratio of 34.7% is below the 125% threshold and reflects the significant debt that the university incurred over the past years for its capital expansion. This ratio means that at June 30, 2009, NAU had Expendable Net Assets sufficient to pay 34.7% of its long-term debt.
- Approximately \$86 million, or 26%, of NAU's capital debt outstanding at June 30, 2009 (exclusive of capital leases), is financed by a separate research infrastructure state appropriation. This ongoing support from the state is not reflected in the university's Expendable Net Assets at June 30, 2009, and, therefore, is not included in the calculation of this ratio.
- NAU's Viability Ratio is offset by the fact that the university receives 35% of its total annual revenues from state General Fund appropriations.
- Absent the Federal Fiscal Stabilization Funds, this ratio would be 28.4% at June 30, 2009.

UA BULLET ANALYSIS

- UA's FY 2009 Viability Ratio of 46.0% is below the 125% threshold and reflects the significant debt that the university incurred over the past years for its capital expansion. This ratio indicates that at June 30, 2009, UA had Expendable Net Assets sufficient to pay 46% of its long-term debt.
- Approximately \$193 million, or 18%, of UA's capital debt outstanding at June 30, 2009 (exclusive of capital leases), is financed by a separate research infrastructure state appropriation. This ongoing support from the state is not reflected in the university's Expendable Net Assets at June 30, 2009, and, therefore, is not included in the calculation of this ratio.

- Although there is a slight decrease from the 56.0% ratio in the prior year, UA's net assets increased by \$9.8 million due to the receipt of Federal Fiscal Stabilization Funds and increased tuition revenues, contracts and grants activity, and restricted gift donations.
- Absent the Federal Fiscal Stabilization Funds, this ratio would be 40.3% at June 30, 2009.

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RETURN ON NET ASSETS RATIO

The Return on Net Assets Ratio determines whether the institution is financially better off than in previous years by measuring total economic return. This ratio furnishes a broad measure of the change in an institution's total wealth over a single year and is based on the level and change in total net assets, regardless of asset classification. Thus, the ratio provides the most comprehensive measure of the growth or decline in total wealth of an institution over a specific period of time. The formula for this ratio is:

$$\frac{\text{CHANGE IN NET ASSETS (UNIVERSITY AND COMPONENT UNITS)}}{\text{TOTAL NET ASSETS (UNIVERSITY AND COMPONENT UNITS)}}$$

A decline in this ratio may be appropriate and even warranted if it reflects a strategy to better fulfill the institution's mission. On the other hand, an improving trend in this ratio indicates that the institution is increasing its net assets and is likely to be able to set aside financial resources to strengthen its future financial flexibility.

The Return on Net Assets Ratio, like all the others, is better applied over an extended period so that the results of long-term plans are measured. Long-term returns are quite volatile and vary significantly based on the prevailing level of inflation in the economy. Therefore, establishing fixed nominal return targets is not possible. Rather, institutions should establish a real rate of return target in the range of approximately 3-4 percent. The real return plus the actual inflation index, either the Consumer Price Index (CPI) or the Higher Education Price Index (HEPI), will produce the nominal rate of return. A useful proxy to measure changes specific to an institution from the impact of both inflation and programmatic commitments may be the growth of total expenses over a long period of time. However, as with each ratio, there are no absolute measures. For example, if an institution's strategic plan calls for activities that will consume substantial resources, such as program expansion, a high return on net assets may be required in order to maintain a properly capitalized institution.

Because the Return on Net Assets Ratio is affected by a number of potentially volatile items, it is important that the institution understand the causes of the change in this ratio from year to year. If, for example, large investment returns or nonrecurring gains are providing a substantial percentage of the increase in net assets, any market correction could have negative implications, possibly impacting program financing.

It is important that an institution project this ratio under various future assumptions. In years of high investment returns, net assets can increase substantially over the short term, thereby improving the ratio. However, positive external developments may imply that an institution has the capacity to defer cost-reducing activities or postpone necessary adjustments to tuition levels. Then, when market conditions become relatively flat or turn negative, the institution could find its financial performance inadequate. If so, an extended period may be spent attempting to recover, possibly at the expense of necessary programmatic initiatives.

For institutions with sizable investments, it is advisable to smooth the results of this ratio by looking at Return on Net Assets over time, for example, 5-10 years. Changes in market performance can also significantly impact the numerator of this ratio from year to year. For this reason, each institution will need to set its own goal for this ratio.

The Return on Net Assets Ratios for Arizona State University, Northern Arizona University, and The University of Arizona, along with each university's analysis, are presented on the next two facing pages.

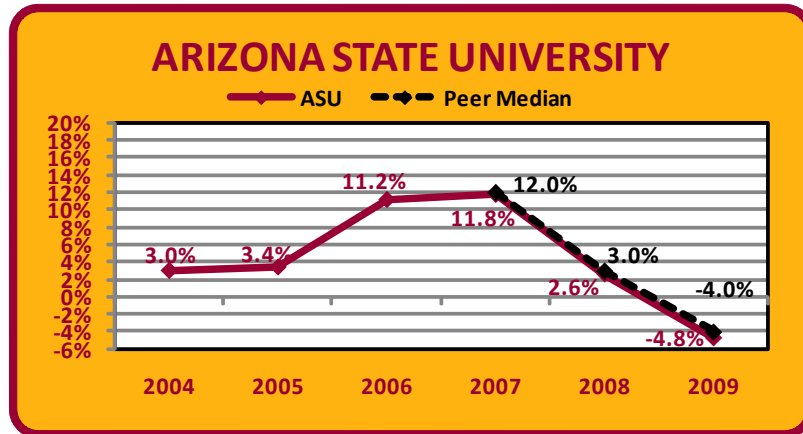
RETURN ON NET ASSETS RATIO

KPMG Score

(10) = 20%

Threshold (3) = 6%

(1) = 2%

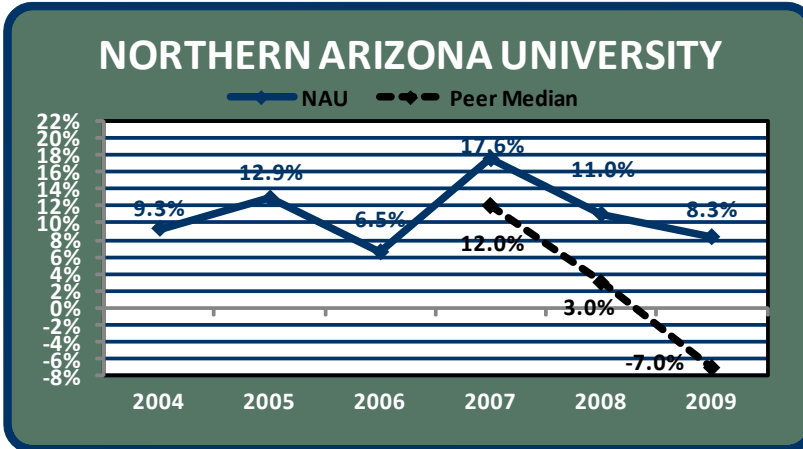


NORTHERN ARIZONA UNIVERSITY

(10) = 20%

Threshold (3) = 6%

(1) = 2%

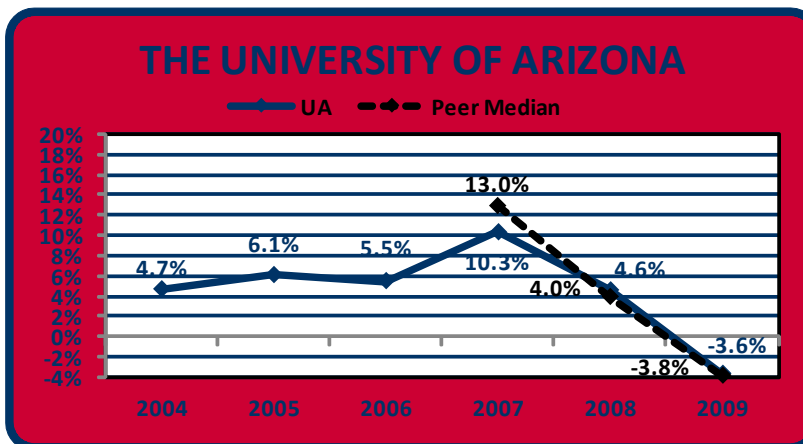


THE UNIVERSITY OF ARIZONA

(10) = 20%

Threshold (3) = 6%

(1) = 2%



- (1) = Very little financial health.
- (3) = Threshold; moderate financial health.
- (10) = Top score within range.

RETURN ON NET ASSETS RATIO

ASU BULLET ANALYSIS

- ASU's FY 2009 Return on Net Assets Ratio was -4.8%, well below the 6% threshold. This is lower than the prior year ratio of 2.6%.
- In FY 2009 the net assets of ASU's component units decreased by \$130 million, primarily due to significant decreases in endowment market values at the ASU Foundation. In comparison, the component units reported a \$33 million increase in net assets in FY 2008.
- ASU (university only) reported an increase in net assets of \$57.6 million. It should be noted that ASU received \$69.8 million in FY 2009 Federal Fiscal Stabilization Funds. Absent these federal stimulus funds, ASU (university only) would have reported a \$12.2 million decrease in net assets.
- Absent the \$69.8 million in Federal Fiscal Stabilization Funds, ASU's FY 2009 Return on Net Assets Ratio would be -9.5%.

NAU BULLET ANALYSIS

- NAU's FY 2009 Return on Net Assets Ratio was 8.3%, well above the 6% threshold. This is lower than the prior year ratio of 11%.
- NAU's component units reported a \$10.2 million decrease in net assets, primarily at the NAU Foundation, that resulted from investment losses. This compares to a \$4.4 million increase in net assets of the component units in FY 2008.
- NAU (university only) reported a \$39.5 million increase in net assets for FY 2009. NAU received \$23.5 million of FY 2009 Federal Fiscal Stabilization Funds; NAU (university only) would have reported a \$13.5 million increase in net assets had it not received the federal stimulus funds.
- NAU has steadily increased its net assets over the 6-year period FY 2004-2009, demonstrating a strategic direction of budget controls and building reserves.
- Absent the \$23.5 million in Federal Fiscal Stabilization Funds, NAU's FY 2009 Return on Net Assets Ratio would be 1.7%.

UA BULLET ANALYSIS

- UA's FY 2009 Return on Net Assets Ratio was -3.6%, well below the 6% threshold. This is down from the prior year ratio of 4.6%.
- UA's component units reported a \$60.0 million decrease in net assets, primarily at the UA Foundation, due to a net loss on endowment investments. This compares to a \$17.7 million increase in net assets of the component units in FY 2008.

- UA (university only) reported a \$9.8 million increase in net assets for FY 2009. UA received \$60.8 million in FY 2009 Federal Fiscal Stabilization Funds. Absent these federal stimulus funds, UA (university only) would have reported a \$51.0 million decrease in net assets.
- Absent the \$60.8 million in Federal Fiscal Stabilization Funds, UA's FY 2009 Return on Net Assets Ratio would be -8.4%.

NET OPERATING REVENUES RATIO

The Net Operating Revenues Ratio is a primary indicator, explaining how the surplus from operating activities affects the behavior of the other three core ratios. A large surplus or deficit directly impacts the amount of funds an institution adds to or subtracts from net assets, thereby affecting the Primary Reserve Ratio, the Return on Net Assets Ratio, and the Viability Ratio. The formula for this ratio is:

$$\frac{\text{OPERATING INCOME (LOSS) + NET NONOPERATING REVENUES (EXPENSES) + COMPONENT UNIT CHANGE IN UNRESTRICTED NET ASSETS}}{\text{OPERATING REVENUES + NONOPERATING REVENUES + COMPONENT UNIT TOTAL UNRESTRICTED REVENUE}}$$

A positive Net Operating Revenues Ratio indicates that the institution experienced an operating surplus for the year. Generally speaking, the larger the surplus, the stronger the institution's financial performance as a result of the year's activities. However, as a note of caution, if surpluses are obtained by underspending on mission-critical investments, then the surplus achieved should be questioned. A negative ratio indicates a loss for the year. A small deficit in a particular year may be relatively unimportant if the institution is financially strong, is aware of the causes of the deficit, and has an active plan in place that cures the deficit.

Large deficits and structural deficits are almost always a bad sign, particularly if management has not identified initiatives to reverse the shortfall. A pattern of large deficits can quickly sap an institution's financial strength to the point where it may have to make major adjustments to programs. A continuing decline or a pattern of deficits is a warning signal that management and the governing board should focus on restructuring the institution's income and expense streams to return to an acceptable Net Operating Revenues Ratio.

A key for institutions establishing a benchmark for this ratio would first be the anticipated institutional growth in total expenses. A ratio in the 2 to 4 percent range may appear somewhat low. However, the determination of net operating revenues includes depreciation expense as a component, indicating that a positive return in this area would suggest the institution lived within its means.

The Net Operating Revenues Ratios for Arizona State University, Northern Arizona University, and The University of Arizona, along with each university's analysis, are presented on the next two facing pages.

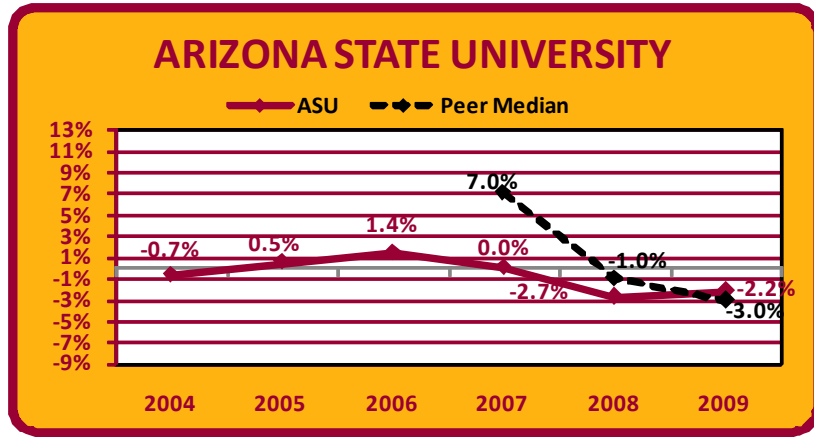
NET OPERATING REVENUES RATIO

KPMG Score

(10) = 13%

Threshold (3) = 4%

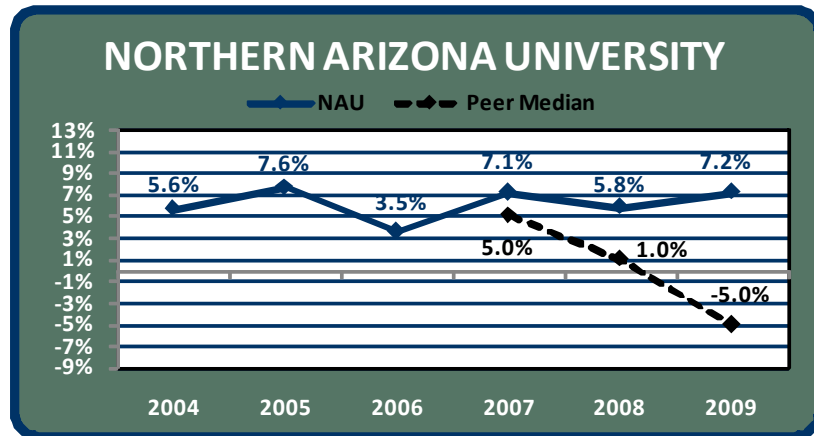
(1) = 1.3%



(10) = 13%

Threshold (3) = 4%

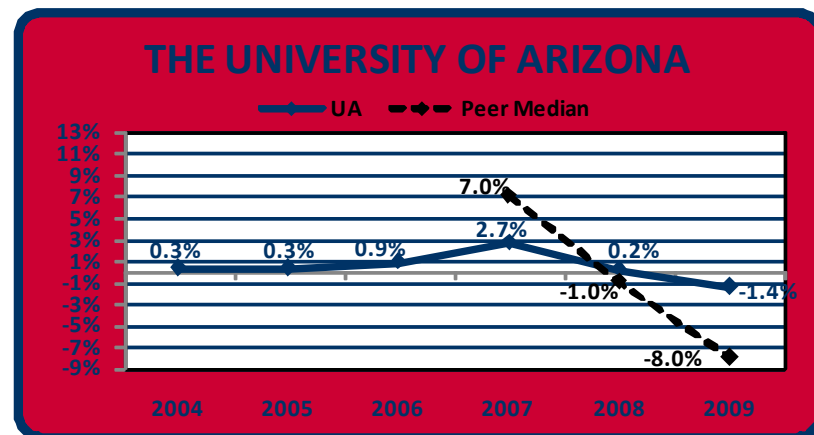
(1) = 1.3%



(10) = 13%

Threshold (3) = 4%

(1) = 1.3%



- 1 = Very little financial health.
- 3 = Threshold; moderate financial health.
- 10 = Top score within range.

NET OPERATING REVENUES RATIO

ASU BULLET ANALYSIS

- ASU's FY 2009 Net Operating Revenues Ratio of -2.2% indicates an operating deficit for the year—operating expenses exceeded operating revenues. Up slightly from -2.7% for the prior year, this ratio is well below the 4% threshold.
- This ratio was impacted by the decrease in endowment market values between FY 2008 and FY 2009, impacting both ASU's net nonoperating revenues and the change in unrestricted net assets for the component units (primarily the ASU Foundation).
- Combined revenues—ASU operating revenues, ASU nonoperating revenues, and the component units' unrestricted revenues—remained essentially the same in total between FY 2008 and FY 2009, although there were changes within categories.
- Absent the \$69.8 million in Federal Fiscal Stabilization Funds, ASU's FY 2009 Net Operating Revenues Ratio would be -6.9%.

NAU BULLET ANALYSIS

- NAU's FY 2009 Net Operating Revenues Ratio of 7.2% indicates that the university and its component units experienced an operating surplus for the period—operating revenues exceeded operating expenses. Up from 5.8% the prior year, this ratio is well above the 4% threshold.
- NAU has recorded a positive Net Operating Revenues Ratio for 6 consecutive years, indicating strong revenue growth accompanied by strong spending controls. This reflects good management of budget and fiscal operations and demonstrates that the university is living within its means.
- Absent the \$23.5 million in Federal Fiscal Stabilization Funds, NAU's FY 2009 Net Operating Revenues Ratio would be 1.6%.

UA BULLET ANALYSIS

- UA's FY 2009 Net Operating Revenues Ratio of -1.4% indicates that the university and its component units experienced an operating deficit for the period—operating expenses exceeded operating revenues. Down from 0.2% the prior year, this ratio is well below the 4% threshold.
- UA has recorded a positive Net Operating Revenues Ratio for 5 consecutive years, recording a negative ratio in FY 2009 for the first time since FY 2004. The state of Arizona continues to experience weak economic conditions, negatively impacting UA's budget.
- Absent the \$60.8 million in Federal Fiscal Stabilization Funds, UA's FY 2009 Net Operating Revenues Ratio would be -5.7%.

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COMPOSITE FINANCIAL INDEX (CFI)

After looking at the relative strengths and weaknesses of each of the four core ratios, it is useful for an institution to be able to combine them into a single score. This combination, using a reasonable weighting plan, allows a weakness or strength in a specific ratio to be offset by another ratio result, thereby allowing a more holistic approach to understanding the total financial health of the institution.

The Composite Financial Index (CFI) is useful in helping governing boards and senior management understand the financial position that the institution enjoys in the marketplace. Moreover, this measurement will also prove valuable in assessing future prospects of the institution, functioning as an “affordability index” of a strategic plan. The KPMG methodology has been adopted by many leading institutions and has found great acceptance by senior management and governing boards. It is a valuable tool for senior managers and boards to help understand not only the state of an institution’s financial situation at a point in time but also serve as a valuable tool that can provide insight into the trends of an institution’s key financial indicators.

KPMG recommends that each institution develop the CFI that is tailored to the institutional needs and then apply it over an extended period of time—both historically and as a planning tool as the institution develops a prioritized and priced strategic plan. By tailoring the CFI in this way, the institution will have insight into the financial impact of different activities.

As an example, if an institution has just completed a significant investment in new facilities with a significant debt component, the expectation that both the CFI and the Viability Ratio will be depressed is reasonable. Similarly, if the institution has recently completed a major capital campaign, the CFI may well have improved, and the governing board and senior management have the opportunity to consider whether the amount of the increase matched overall expectations.

As with any financial analysis, KPMG believes a long period of time, at least 5 years, represents enough measurement points to effectively understand the financial direction of the institution. They also believe that once developed, the schema should be fixed; and if there is a compelling reason for a change, that all information be restated so that comparative data is consistent. However, the weighting should not be revised as a response to changes or deterioration in certain financial indicators but should only be done if the institution’s financial or programmatic objectives have fundamentally changed over the long term.

KPMG has also found, however, that applying the CFI as a peer group measure has some limitations. This is different from the comparison of an individual ratio, where senior managers of an institution believe they have the capability to understand the action to take if an individual ratio is different from another institution. This relates to the fact that there are a limited number of most likely reasons for movement in a selected ratio. However, when the

ratios are combined, the underlying reasons for change may be indiscernible because of the number of possible variations.

The weightings used for each ratio in the CFI calculation represent what KPMG believes is an appropriate assessment of the relative importance of each ratio and a reasonable assessment of balance between an institution's short- and long-term needs. However, weighting of the ratios becomes the key variable that would reflect differences in institutional philosophy and approach to financial planning.

Under the KPMG methodology, the 4 ratios are weighted as follows in calculating the CFI:

RATIO	WEIGHTING IN CFI
Primary Reserve	35%
Return on Net Assets	20%
Net Operating Revenues	10%
Viability Ratio	35%

The four-step methodology is as follows:

- Compute the values of the four core ratios;
- Convert these figures to strength factors along a common scale;
- Multiply the strength factors by specific weighting factors; and
- Total the resulting four numbers to reach the single CFI score.

The CFI measures only the financial component of an institution's well-being. It must be analyzed in context with other associated activities and plans to achieve an assessment of the overall health, not just financial health, of the institution. As an example, if two institutions have identical CFI scores but one requires substantial investments to meet its mission-critical issues and the other has already made those investments, the first institution is less healthy than the second. In fact, an institution's CFI can become too high as well as too low. When put in the context of achievement of mission, a very high CFI with little achievement of mission may indicate a failing institution.

The scale accompanying the CFI graphs presented on page 28 is KPMG's scale for charting CFI performance. These CFI scores do not have absolute precision. They are indicators of ranges of financial health that can be indicators of overall institutional well-being, when combined with nonfinancial indicators. This would be consistent with the fact that there are a large number of variables that can impact an institution and influence the results of these ratios. However, the ranges do have enough precision to be indicators of the institutional financial health; and the CFI as well as its trend line, over a period of time, can be the single most important measure of the financial health for the institution.

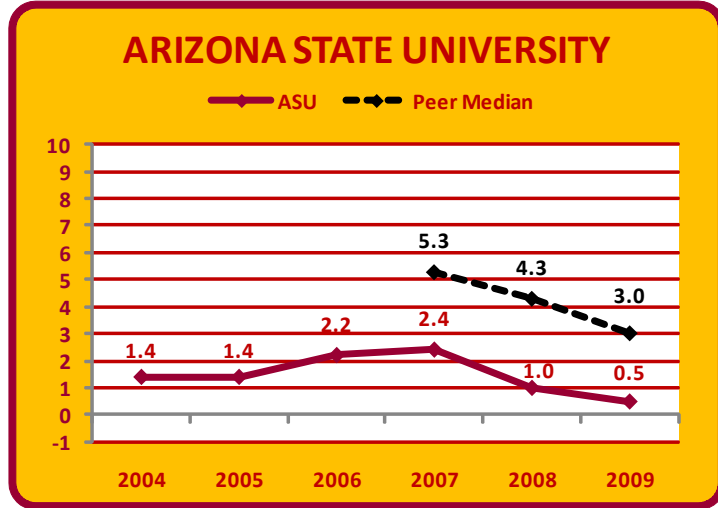
The overlapping of the scores on the CFI scale represents the ranges of measurement that an institution may find useful in assessing itself. There is little discernible difference between the financial position of an institution with a 3.3 or one with a 3.4 CFI. In this case, the nonfinancial indicators will be a stronger differentiator between the institutions. However, there are readily discernible financial differences between an institution scoring 3.4 and 5.5 on the CFI. An institution with a significantly low or declining CFI will be disadvantaged when competing with institutions with a higher or improving CFI.

The Composite Financial Indices (CFI) for Arizona State University, Northern Arizona University, and The University of Arizona, along with each university's analysis, are presented on the next two facing pages.

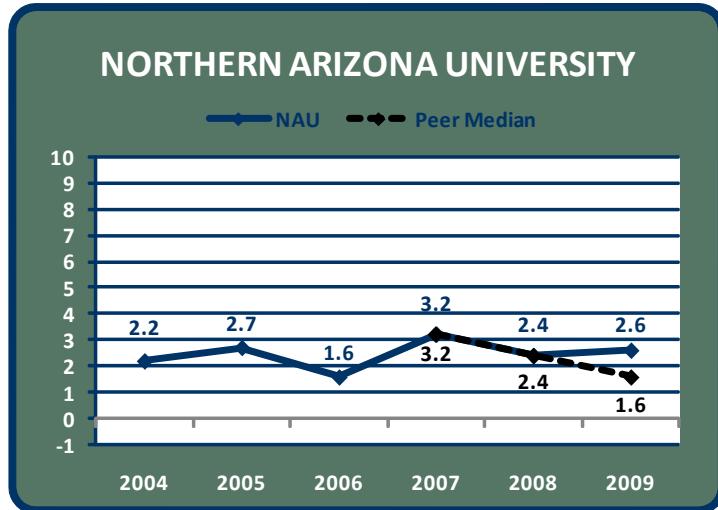
COMPOSITE FINANCIAL INDEX (CFI)

KPMG Scale

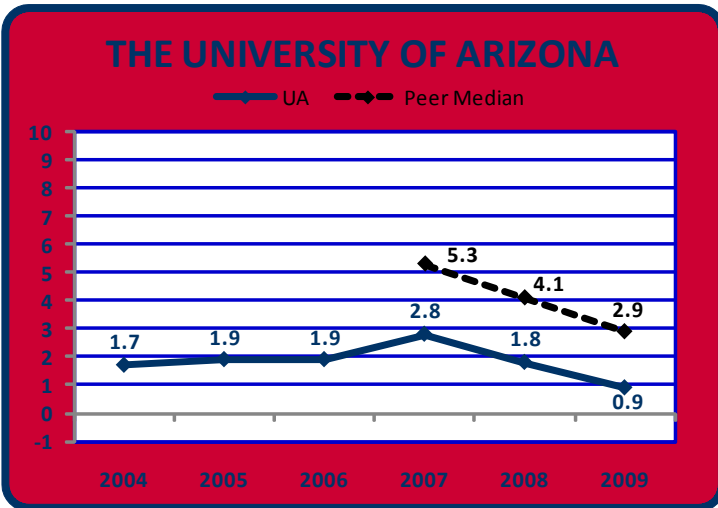
- 8 to 10 Deploy resources to achieve robust mission
- 6 to 9 Allow experimentation with new initiatives
- 4 to 7 Focus resources to compete in future state
- 2 to 5 Direct institutional resources to allow transformation
- 0 to 3 Re-engineer the institution
- 1 to +1 Assess institutional ability to survive



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- 8 to 10 Deploy resources to achieve robust mission
- 6 to 9 Allow experimentation with new initiatives
- 4 to 7 Focus resources to compete in future state
- 2 to 5 Direct institutional resources to allow transformation
- 0 to 3 Re-engineer the institution
- 1 to +1 Assess institutional ability to survive



COMPOSITE FINANCIAL INDEX (CFI)

ASU BULLET ANALYSIS

- ASU reports a Composite Financial Index (CFI) of 0.5 for the fiscal year ended June 30, 2009, down from the 1.0 for the prior year. This decline is due to the factors mentioned earlier, most notably the challenging investment markets that prevailed throughout FY 2009.
- ASU's CFI is significantly weakened by its Viability Ratio, which is negatively impacted by its total long-term debt.
- The CFI is one indicator of financial health for an institution but must be combined with non-financial indicators, such as enrollment growth, national recognition of academic and research programs, and construction of new facilities, in determining the overall health of the university.
- Absent the Federal Fiscal Stabilization Funds, ASU's CFI would be 0.3 at June 30, 2009.

NAU BULLET ANALYSIS

- NAU reports a CFI of 2.6 for the fiscal year ended June 30, 2009, an improvement from the FY 2008 ratio of 2.4.
- NAU's CFI is significantly weakened by its Viability Ratio, which is negatively impacted by its total long-term debt. NAU is in a very aggressive and unprecedented capital improvement and expansion program, resulting in an almost \$200 million increase in the long-term debt of the university and its component units. The new facilities constructed from this tax-exempt debt are a combination of auxiliary, academic, and research. An additional \$178 million in debt is planned for FY 2010.
- NAU has grown its enrollment to historical highs. The university has also grown the accompanying tuition and research revenues, replenished reserves, and reported excellent Returns on Net Assets over this expansion period.
- Absent the Federal Fiscal Stabilization Funds, NAU's CFI would be 1.3 at June 30, 2009.

UA BULLET ANALYSIS

- UA reports a CFI of 0.9 for the fiscal year ended June 30, 2009, the lowest CFI in the last 6 years, dropping from the 1.8 reported in the prior year.
- UA's CFI is significantly weakened by its Viability Ratio (reflecting the magnitude of total long-term debt), along with a negative Net Operating Revenues Ratio and a negative Return on Net Assets Ratio, offset somewhat by a Primary Reserve Ratio that approaches the desired threshold.
- UA's capital expansion and improvements added \$212 million to long-term debt in FY 2009. Of this amount, \$202 million is attributable to student life projects, which include construction and building renewal necessary to support the university's instructional mission.
- Absent the Federal Fiscal Stabilization Funds, UA's CFI would be 0.8 at June 30, 2009.

BENCHMARKING

FOUR RATIOS

The KPMG methodology provides a scale against which to benchmark the universities' four ratios. This scale is based on industry experience.

- 1 represents very little financial health;
- 3, the threshold level, represents a relatively stronger financial position (moderate financial health); and
- 10 represents the top score within range for an institution.

SCORING SCALE	1	3	10
Primary Reserve Ratio	13.3%	40%	133%
Viability Ratio	41.7%	125%	416%
Return on Net Assets Ratio	2%	6%	20%
Net Operating Revenues Ratio	1.3%	4%	13%

A strength factor of 1 on each of the four ratios, which is also a CFI of 1, indicates an institution under financial stress. This institution has a Primary Reserve Ratio of 13.3%, indicating that expendable resources are available to cover about 7 weeks of annualized expenses (13.3% of 52), and that while some Net Operating Revenues and Return on Net Assets exist, the amounts of 1.3% and 2%, respectively, are too small to allow replenishment of reserve levels and may well not equal even modest growth in total expenses. Finally, a Viability Ratio of 41.7% indicates long-term debt exceeding expendable resources by 2.4 times ($1 / .417$).

A strength factor of 3 on each of the four ratios indicates that an institution is relatively financially healthy in that approximately 20 weeks of annualized expenses are retained in expendable resources (40% of 52); the Net Operating Revenues generated are sufficient to keep pace with, and will likely exceed the growth of, moderate expense levels; the Return on Net Assets would appear reasonable for the overall investment activity of the institution; and expendable net assets (Viability Ratio) exceed the institutional debt levels, although not by excessive amounts. Institutions with this profile generally have enough wealth and access to capital resources to finance modest program improvements and address a modest financial challenge; however, a significant institutional transformation may be difficult to realize without additional resources.

At a strength factor of 10 on each ratio, about 69 weeks of annualized expenses exist in expendable resources (Primary Reserve Ratio); Net Operating Revenues indicate the margin from operating activities will exceed normal increases in expense levels; the Return on Net Assets will provide marginal resources that may be used to support institutional initiatives; and the institution has substantial expendable resources in excess of debt (Viability Ratio).

COMPOSITE FINANCIAL INDEX (CFI)

The KPMG methodology uses the scale presented on page 28 to interpret the CFI scores. The language associated with the scale is directly from the KPMG methodology

BENCHMARKING TO PEERS

It is instructive to consider these thoughts from the KPMG methodology on comparing an institution's financial ratios to a peer group:

“Prior editions (of this work) have noted the use of financial ratios to make peer comparisons. Publications have increased the use of peer rankings over time, especially concerning the quality of academic programs and the institution as a whole. These peer comparisons have benefited many institutions and provided management a way to communicate an institution's goals and progress toward those goals to its various stakeholders. Institutions have also used peer comparisons successfully by establishing an aspirant peer group. However, it has also become evident that some institutions have over-used peer comparisons and have forgotten three basic principles of financial analysis—one, ratios should be used to measure success factors in order to improve the institution financially to achieve its mission; two, that the information being compared must be on a fairly consistent basis; and three, that peer comparisons are only a weak relative indicator and do not measure attainment of an institution's unique mission. Therefore, common sense, qualitative interpretation, and longitudinal interpretation are required.”

The KPMG methodology continues, stating:

“Longitudinal comparisons are generally more important than peer comparisons since the institution can adapt the ratios over time to meet institutional needs and reflect changing conditions. In addition, . . . many ratio calculations can be modified to better reflect the objectives of the particular institution. The institution is generally assured of a consistent basis and availability of information sources, not all of which are reported in the institution's annual financial report. Causes of changes in ratios can also be identified more easily. Internal comparisons can be used over a longer time horizon to monitor historical institutional performance, establish prospective targets and, combined with nonfinancial drivers, present a more thorough analysis and evaluation.”

The KPMG methodology also discusses limitations of comparisons among public institutions. Some public institutions rely on the sponsoring government for a credit rating for debt, whereas others obtain their own credit rating. In some instances, debt related to a public institution's plant assets does not reside at the institution level—where it resides for ASU, NAU, and UA—but rather at a higher level such as a state system or the state. In some states, public institutions are not permitted to maintain expendable net asset balances above a certain level;

institutions that incur operating surpluses or have significant expendable net assets may find future operating support reduced.

The KPMG methodology comments that:

“Many public institutions may find the threshold values (for the four core ratios) too high or cannot attain them due to operating and governance restrictions; however, the values indicate that these institutions possess minimal operating and financial flexibility independent of the state, which we believe limits the institutions’ ability to adapt to a changing market and invest in significant new strategic initiatives, absent the identification of a specific new funding source.”

In February 2009, the Board’s Strategic Planning, Budget and Finance Committee approved the new sets of peer institutions for Arizona State University, Northern Arizona University, and The University of Arizona. The universities compiled the four ratios and the CFI of their peer institutions based on the published audited financial statements for FY 2007-2009. Because some institutions had not released their FY 2009 audited financial statements as of our publishing date, the universities were limited, for purposes of this assessment, to available comparative FY 2009 peer data. For ASU, 12 of their 15 peers had released their FY 2009 financial statements; 13 of UA’s 15 peers; and 11 of NAU’s 15 peers.

The FY 2007-2009 peer data provided on the ratio graphs, and detailed for each university’s peers behind the university “Data” tabs, provides additional context for this assessment of financial strength. As stated previously, the analytical value of peer comparisons is limited but could give the Board some additional information as financial health is monitored over time.

ASU DATA

ARIZONA STATE UNIVERSITY

FINANCIAL RATIOS		FY 2009				FY 2008				FY 2007				FY 2006				FY 2005				FY 2004			
		Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI
Primary Reserve Ratio calculation:																									
Institution unrestricted net assets	+	165,914				27,368				155,702				145,128				160,275				149,725			
Institution expendable restricted net assets	+	75,384				99,214				76,908				62,854				55,914				63,096			
C.U. unrestricted net assets	+	(57,447)				6,512				32,802				38,154				27,250				9,488			
C.U. temporary restrict net assets	+	174,586				233,668				219,495				115,184				94,275				81,016			
C.U. net investment in plant	-	-				-				-				-				-				-			
Numerator-Total		358,437				366,762				484,907				361,320				337,714				303,325			
Institution operating expenses	+	1,419,929				1,393,530				1,263,699				1,115,768				1,013,571				881,316			
Institution nonoperating expenses	+	45,637				53,421				46,823				42,788				35,035				45,620			
C.U. total expenses	+	163,219				158,433				137,843				103,421				92,676				68,976			
Denominator- Total		1,628,785				1,605,384				1,448,365				1,261,977				1,141,282				995,912			
PRIMARY RESERVE RATIO	÷	0.220	1.655	0.35	0.58	0.228	1.718	0.35	0.60	0.335	2.517	0.35	0.88	0.286	2.153	0.35	0.75	0.296	2.225	0.35	0.78	0.305	2.290	0.35	0.80
Net Operating Revenue Ratio calculation:																									
Institution operating Income (loss)	+	(571,575)				(599,453)				(476,057)				(405,607)				(390,314)				(337,790)			
Institution net nonoperating revenues	+	598,326				582,936				482,391				412,185				373,633				329,442			
C.U. change in unrestricted net assets	+	(61,911)				(25,750)				(5,655)				10,904				22,653				1,753			
Elimination of inter-entity amounts	+	-				-				-				-				-				-			
Numerator-Total		(35,160)				(42,267)				679				17,482				5,972				(6,595)			
Institution operating revenues	+	848,354				794,077				787,642				710,161				623,257				543,526			
institution nonoperating revenues	+	643,963				636,357				529,214				454,973				408,668				375,062			
C.U. total unrestricted revenues	+	101,308				132,683				132,188				114,325				115,329				70,729			
Elimination of inter-entity amounts	+	-				-				-				-				-				-			
Denominator- Total		1,593,625				1,563,117				1,449,044				1,279,459				1,147,254				989,317			
NET OPERATING REVENUES RATIO	÷	-0.022	-1.000	0.1	-0.10	-0.027	-1.000	0.1	-0.10	0.000	0.036	0.1	0.00	0.014	1.051	0.1	0.11	0.005	0.400	0.1	0.04	-0.007	-0.513	0.1	-0.05
Return on Net Assets Ratio calculation:																									
Change in net assets + C.U. change in net assets		(72,049)				37,286				153,438				130,457				37,817				33,556			
Divided by total net assets + C.U. total net assets		1,486,985				1,449,699				1,296,682				1,165,922				1,128,105				1,109,823			
RETURN ON NET ASSETS RATIO	÷	-0.048	-1.000	0.2	-0.20	0.026	1.286	0.2	0.26	0.118	5.917	0.2	1.18	0.112	5.595	0.2	1.12	0.034	1.676	0.2	0.34	0.030	1.512	0.2	0.30
Viability Ratio calculation:																									
Numerator- Expendable net assets		358,437				366,762				484,907				361,320				337,714				303,325			
Institution long-term debt (total project-related debt)	+	874,100				765,272				796,474				742,714				743,805				557,674			
C.U. long-term debt (total project-related debt)	+	603,843				540,121				416,703				417,311				279,212				191,646			
Denominator- total long-term debt		1,477,943				1,305,393				1,213,177				1,160,025				1,023,017				749,320			
VIABILITY RATIO	÷	0.243	0.582	0.35	0.20	0.281	0.674	0.35	0.24	0.400	0.959	0.35	0.34	0.311	0.747	0.35	0.26	0.330	0.792	0.35	0.28	0.405	0.971	0.35	0.34
COMPOSITE FINANCIAL INDEX (CFI)					0.5				1.0				2.4				2.2				1.4				1.4

ARIZONA STATE UNIVERSITY

FY 2009 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
Texas at Austin (University of)	92%	1	-3%	6	-59%	13	8202%	1	5.6	1
Pennsylvania State University	91%	2	-4%	7	-4%	8	303%	2	4.6	2
California, Los Angeles (University of)	44%	9	-1%	4	2%	2	251%	3	3.3	3
Michigan State University	66%	3	-13%	12	-28%	12	221%	4	3.3	4
Indiana University	57%	5	-5%	8	3%	1	182%	8	3.1	6
Iowa (University of)	57%	6	0%	3	0%	3	194%	6	3.1	5
Minnesota, Twin Cities (University of)	57%	4	-13%	13	-17%	10	196%	5	2.8	7
Washington (University of)	56%	7	-7%	10	-20%	11	191%	7	2.8	8
Maryland, College Park (University of)	44%	10	-3%	5	-2%	5	181%	9	2.4	9
Rutgers (The State University of New Jersey)	55%	8	0%	2	-3%	7	117%	11	2.3	10
Ohio State University	41%	11	-7%	11	-12%	9	124%	10	1.8	11
Wisconsin - Madison (University of)	11%	13	8%	1	-1%	4	51%	12	1.4	12
Arizona State University	22%	12	-5%	9	-2%	6	24%	13	0.5	13
*Connecticut (University of)										
*Florida State University										
*Illinois (University of)										
Mean (excluding ASU)	56%		-4%		-12%		851%		3.0	
Median (excluding ASU)	56%		-4%		-3%		192%		3.0	
KPMG Threshold	40%		6%		4%		125%			

* Audited financial statements unavailable as of February 24, 2010.

ARIZONA STATE UNIVERSITY

FY 2008 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
Texas at Austin (University of)	124%	1	4%	6	-13%	16	9635%	1	7.0	1
Pennsylvania State University	106%	2	4%	5	5%	2	361%	2	6.6	2
Florida State University	83%	4	7%	2	5%	1	234%	9	5.2	3
Michigan State University	92%	3	2%	12	-1%	8	297%	3	5.0	4
California, Los Angeles (University of)	54%	10	9%	1	4%	6	281%	4	4.9	5
Indiana University	77%	6	4%	7	4%	5	243%	7	4.7	6
Iowa (University of)	69%	8	3%	9	4%	4	239%	8	4.4	7
Maryland, College Park (University of)	53%	11	7%	3	5%	3	221%	10	4.3	8
Minnesota, Twin Cities (University of)	82%	5	0%	13	-3%	12	254%	5	4.2	9
Washington (University of)	72%	7	3%	8	-1%	9	248%	6	4.2	10
Rutgers (The State University of New Jersey)	56%	9	4%	4	4%	7	162%	11	3.5	11
Ohio State University	40%	12	-1%	14	-5%	15	144%	12	2.1	12
Arizona State University	23%	13	3%	10	-3%	11	28%	15	1.0	13
Illinois (University of)	21%	14	-3%	15	-2%	10	50%	13	0.7	14
Wisconsin - Madison (University of)	10%	16	2%	11	-5%	14	43%	14	0.7	15
Connecticut (University of)	20%	15	-3%	16	-4%	13	18%	16	0.4	16
Mean (excluding ASU)	64%		3%		0%		829%		3.9	
Median (excluding ASU)	69%		3%		-1%		239%		4.3	
KPMG Threshold	40%		6%		4%		125%			

ARIZONA STATE UNIVERSITY

FY 2007 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
Texas at Austin (University of)	140%	1	17%	1	15%	1	11000%	1	9.7	1
Pennsylvania State University	110%	2	15%	3	14%	2	391%	2	8.7	2
Minnesota, Twin Cities (University of)	91%	4	15%	4	8%	7	284%	3	7.2	3
Michigan State University	99%	3	11%	10	12%	4	266%	4	7.0	4
Indiana University	76%	7	16%	2	7%	8	252%	6	6.6	5
Florida State University	84%	5	13%	7	5%	11	236%	7	6.3	6
Washington (University of)	78%	6	14%	5	12%	3	211%	8	6.2	7
Iowa (University of)	68%	8	9%	13	7%	10	201%	9	5.3	8
California, Los Angeles (University of)	53%	10	8%	14	5%	12	256%	5	5.0	9
Maryland, College Park (University of)	46%	11	14%	6	7%	9	169%	10	4.5	10
Ohio State University	41%	12	12%	8	10%	5	134%	12	4.4	11
Rutgers (The State University of New Jersey)	56%	9	9%	12	9%	6	142%	11	4.2	12
Arizona State University	34%	13	11%	9	0%	15	38%	15	2.4	13
Wisconsin - Madison (University of)	14%	16	11%	11	1%	13	53%	14	2.1	14
Illinois (University of)	22%	15	7%	15	1%	14	56%	13	1.9	15
Connecticut (University of)	24%	14	3%	16	-4%	16	19%	16	1.0	16
Mean (excluding ASU)	67%		11%		7%		911%		5.3	
Median (excluding ASU)	68%		12%		7%		211%		5.3	
KPMG Threshold	40%		6%		4%		125%			

NAU DATA

NORTHERN ARIZONA UNIVERSITY

FINANCIAL RATIOS	FY 2009				FY 2008				FY 2007				FY 2006				FY 2005				FY 2004						
	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI			
Primary Reserve Ratio calculation:																											
Institution unrestricted net assets	124781				80149				70716				47337				45075				37244						
Institution expendable restricted net assets	18918				22951				19801				20193				18345				14367						
C.U. unrestricted net assets	17464				20139				15944				10030				7373				5061						
C.U. temporary restrict net assets	17146				22845				25025				15668				14533				12656						
C.U. net investment in plant	48615				49254				44574				30313				16443				12547						
Numerator-Total	129694				96830				86912				62915				68883				56781						
Institution operating expenses	354804				355565				330633				310766				278917				273455						
Institution nonoperating expenses	13480				13967				10541				10433				8345				5781						
C.U. total expenses	11506				37869				28202				7000				18206				6907						
Denominator- Total	379790				407401				369376				328199				305468				286143						
PRIMARY RESERVE RATIO	0.341	2.568	0.35	0.90	0.238	1.787	0.35	0.63	0.235	1.769	0.35	0.62	0.192	1.441	0.35	0.50	0.225	1.695	0.35	0.59	0.198	1.492	0.35	0.52			
Net Operating Revenue Ratio calculation:																											
Institution operating Income (loss)	-176727				-193222				-136057				-129198				-107381				-108300						
Institution net nonoperating revenues	208955				214139				158678				138397				130045				122134						
C.U. change in unrestricted net assets	-2675				4195				5816				2657				2446				3175						
Elimination of inter-entity amounts	0				0				0																		
Numerator-Total	29553				25112				28437				11856				25110				17009						
Institution operating revenues	178077				162343				194576				181568				171536				165155						
institution nonoperating revenues	223686				228106				169218				148829				138390				127915						
C.U. total unrestricted revenues	8830				42063				34018				9657				20653				10082						
Elimination of inter-entity amounts	0				0				0				0														
Denominator- Total	410593				432512				397812				340054				330579				303152						
NET OPERATING REVENUES RATIO	0.072	5.537	0.1	0.55	0.058	4.466	0.1	0.45	0.071	5.499	0.1	0.55	0.035	2.682	0.1	0.27	0.076	5.843	0.1	0.58	0.056	4.316	0.1	0.43			
Return on Net Assets Ratio calculation:																											
Change in net assets + C.U. change in net assets	29355				34842				46646				16322				28543				18924						
Divided by total net assets + C.U. total net assets	351960				317119				264815				249904				221068				202862						
RETURN ON NET ASSETS RATIO	0.083	4.170	0.2	0.83	0.110	5.494	0.2	1.10	0.176	8.807	0.2	1.76	0.065	3.266	0.2	0.65	0.129	6.456	0.2	1.29	0.093	4.664	0.2	0.93			
Viability Ratio calculation:																											
Numerator- Expendable net assets	129694				96830				86912				62915				68883				56781						
Institution long-term debt (total project-related debt)	325786				292740				252201				240221				181903				128008						
C.U. long-term debt (total project-related debt)	47737				48519				47423				35391				35480				15726						
Denominator- total long-term debt	373523				341259				299624				240221				217383				143734						
VIABILITY RATIO	0.347	0.833	0.35	0.29	0.284	0.680	0.35	0.24	0.290	0.696	0.35	0.24	0.262	0.628	0.35	0.22	0.317	0.760	0.35	0.27	0.395	0.947	0.35	0.33			
COMPOSITE FINANCIAL INDEX (CFI)				2.6				2.4				3.2				1.6				2.7				2.2			

NORTHERN ARIZONA UNIVERSITY

FY 2009 Financial Statement Data for Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
George Mason	12%	11	4%	3	-4%	8	11%	11	0.7	10
Georgia State University	23%	10	0%	5	-2%	7	24%	10	0.7	11
Kent State University	52%	3	-12%	12	-15%	12	112%	4	2.0	4
*Northern Illinois University										
University of Alabama	72%	1	2%	4	0%	4	103%	5	2.9	1
University of Akron - Main Campus	25%	8	-8%	9	9%	1	50%	8	1.6	9
University of Nevada Las Vegas	59%	2	-2%	6	3%	3	126%	2	2.7	2
*University of North Carolina Greensboro										
University of Maine	38%	6	-7%	8	-2%	6	121%	3	1.7	7
Ohio University - Main Campus	39%	5	-3%	7	-6%	9	102%	7	1.6	8
Bowling Green State University	40%	4	-9%	10	-14%	11	142%	1	1.9	6
*Old Dominion University										
*Southern Illinois University Carbondale										
Wichita State University	24%	9	6%	2	0%	5	103%	6	2.0	5
Western Michigan University	4%	12	-11%	11	-14%	10	5%	12	-0.2	12
Northern Arizona University	34%	7	8%	1	7%	2	35%	9	2.6	3
Mean	35%		-3%		-4%		82%		1.6	
Median	25%		-7%		-5%		42%		1.60	
KPMG Threshold	40%		6%		4%		125%			

* Audited financial reports unavailable at February 24, 2010.

NORTHERN ARIZONA UNIVERSITY

FY 2008 Financial Statement Data for Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
George Mason	20%	13	6%	6	3%	4	24%	15	1.6	13
Georgia State University	28%	9	1%	11	-9%	14	46%	12	1.1	14
Kent State University	50%	7	0%	12	-5%	13	96%	8	2.1	10
Northern Illinois University	16%	15	1%	10	0%	9	31%	13	0.8	15
University of Alabama	91%	1	-3%	15	-18%	16	140%	5	3.3	4
University of Akron - Main Campus	28%	10	0%	13	9%	1	50%	11	1.9	11
University of Nevada Las Vegas	70%	2	14%	1	3%	5	147%	3	4.8	1
University of North Carolina Greensboro	58%	3	3%	9	0%	8	138%	6	2.9	6
University of Maine	56%	4	7%	5	2%	7	171%	2	3.7	2
Ohio University - Main Campus	51%	6	12%	3	-2%	11	145%	4	3.6	3
Bowling Green State University	53%	5	0%	14	-3%	12	190%	1	2.8	7
Old Dominion University	43%	8	12%	2	3%	6	66%	10	3.1	5
Southern Illinois University Carbondale	22%	13	5%	7	4%	3	113%	7	2.3	9
Wichita State University	23%	12	3%	8	0%	10	90%	9	1.6	12
Western Michigan University	15%	16	-5%	16	-10%	15	18%	16	0.3	16
Northern Arizona University	24%	11	11%	4	6%	2	28%	14	2.4	8
Mean	42%		4%		-1%		98%		2.4	
Median	36%		3%		1%		91%		2.35	
KPMG Threshold	40%		6%		4%		125%			

NORTHERN ARIZONA UNIVERSITY

FY 2007 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
George Mason	24%	12	19%	2	7%	7	33%	14	3.3	7
Georgia State University	36%	10	8%	11	5%	9	61%	11	2.7	12
Kent State University	66%	3	15%	4	8%	3	119%	5	4.9	3
Northern Illinois University	19%	16	8%	12	2%	14	34%	13	1.7	15
University of Alabama	125%	1	12%	9	18%	1	177%	2	7.0	1
University of Akron - Main Campus	33%	11	12%	8	9%	2	50%	12	3.2	9
University of Nevada Las Vegas	58%	5	7%	13	5%	8	120%	4	3.6	6
University of North Carolina Greensboro	88%	2	19%	1	8%	4	110%	7	5.7	2
University of Maine	64%	4	14%	5	4%	11	173%	3	4.8	4
Ohio University - Main Campus	43%	9	6%	14	2%	15	112%	6	2.8	11
Bowling Green State University	56%	6	10%	10	7%	5	180%	1	4.6	5
Old Dominion University	44%	8	13%	6	2%	13	63%	10	3.1	10
Southern Illinois University Carbondale	23%	15	13%	7	2%	12	76%	8	2.7	13
Wichita State University	23%	14	4%	16	0%	16	18%	16	1.2	16
Western Michigan University	46%	7	4%	15	4%	10	72%	9	2.5	14
Northern Arizona University	24%	13	18%	3	7%	6	29%	15	3.2	8
Mean	50%		11%		6%		93%		3.6	
Median	43%		12%		5%		74%		3.20	

UA DATA

THE UNIVERSITY OF ARIZONA

FINANCIAL RATIOS	FY 2009				FY 2008				FY 2007				FY 2006				FY 2005				FY 2004				
	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	Data	Str	Wt	CFI	
Primary Reserve Ratio calculation:																									
Institution unrestricted net assets	+	179821			157,234				165,775				149,522				101,265				106,895				
Institution expendable restricted net assets	+	140,375			158,554				133,550				122,003				105,429				96,758				
C.U. unrestricted net assets	+	25,095			30,371				27,784				24,484				19,498				19,264				
C.U. temporary restrict net assets	+	141,096			147,555				153,653				148,317				155,679				137,253				
C.U. net investment in plant	-	0			0				0				0				0				0				
Numerator-Total		486,387			493,714				480,762				444,326				381,871				360,170				
Institution operating expenses	+	1,405,886			1,375,060				1,284,787				1,230,857				1,163,410				1,109,931				
Institution nonoperating expenses	+	40887			41,121				38,426				31,407				26,769				23,984				
C.U. total expenses	+	74779			87,471				70,816				72,635				54,688				60,684				
Denominator- Total		1,521,552			1,503,652				1,394,029				1,334,899				1,244,867				1,194,599				
PRIMARY RESERVE RATIO	÷	0.320	2.403	0.35	0.84	0.328	2.469	0.35	0.86	0.345	2.593	0.35	0.91	0.333	2.503	0.35	0.88	0.307	2.306	0.35	0.81	0.301	2.267	0.35	0.79
Net Operating Revenue Ratio calculation:																									
Institution operating Income (loss)	+	-545,837			-568,259				-472,502				-446,264				-393,457				-380,061				
Institution net nonoperating revenues	+	530,536			569,170				507,584				453,026				397,113				381,737				
C.U. change in unrestricted net assets	+	-5,276			2,587				3,301				4,986				234				1,581				
Elimination of inter-entity amounts	+	0			0				0				0				0				0				
Numerator-Total		-20,577			3,498				38,383				11,748				3,890				3,257				
Institution operating revenues	+	860,049			806,801				812,285				784,693				769,953				729,870				
institution nonoperating revenues	+	571,423			610,291				546,010				484,433				423,882				405,721				
C.U. total unrestricted revenues	+	69,900			89,924				74,253				77,039				54,251				61,816				
Elimination of inter-entity amounts	+	0			0				0				0				0				0				
Denominator- Total		1,501,372			1,507,016				1,432,548				1,346,165				1,248,086				1,197,407				
NET OPERATING REVENUES RATIO	÷	-0.014	-1.000	0.1	-0.10	0.002	0.332	0.1	0.03	0.027	3.828	0.1	0.38	0.009	0.671	0.1	0.07	0.003	0.240	0.1	0.02	0.003	0.209	0.1	0.02
Return on Net Assets Ratio calculation:																									
Change in net assets + C.U. change in net assets		-50,153			60,623				124,132				63,125				66,208				48,767				
Divided by total net assets + C.U. total net assets		1,382,711			1,322,088				1,209,185				1,146,062				1,079,854				1,030,344				
RETURN ON NET ASSETS RATIO	÷	-0.036	-1.000	0.2	-0.20	0.046	2.293	0.2	0.46	0.103	5.133	0.2	1.03	0.055	2.754	0.2	0.55	0.061	3.066	0.2	0.61	0.047	2.367	0.2	0.47
Viability Ratio calculation:																									
Numerator- Expendable net assets		486,387			493,714				480,762				444,326				381,871				360,170				
Institution long-term debt (total project-related debi)	+	1,047,709			876,339				867,240				842,388				778,448				777,063				
C.U. long-term debt (total project-related debi)	+	9,109			9,829				10,559				11,265				10,476				30,669				
Denominator- total long-term debt		1,056,818			886,168				877,799				853,653				788,924				807,732				
VIABILITY RATIO	÷	0.460	1.104	0.35	0.39	0.557	1.336	0.35	0.47	0.548	1.313	0.35	0.46	0.520	1.248	0.35	0.44	0.484	1.161	0.35	0.41	0.446	1.069	0.35	0.37
COMPOSITE FINANCIAL INDEX (CFI)					0.9				1.8				2.8				1.9				1.9			1.7	

THE UNIVERSITY OF ARIZONA

FY 2009 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
*University of California - Davis										
University of California - Los Angeles	43.87%	9	-0.53%	4	1.57%	2	251.24%	3	3.4	4
University of Florida	31.58%	13	-7.51%	11	-48.89%	13	166.73%	9	1.9	11
*University of Illinois - Urbana										
University of Iowa	56.61%	7	-0.32%	3	0.36%	3	193.93%	6	3.1	6
University of Maryland - College Park	43.69%	10	-3.10%	5	-1.52%	6	180.95%	8	2.4	10
Michigan State University	66.26%	4	-12.46%	13	-27.67%	12	221.05%	4	3.3	5
University of Minnesota - Twin Cities	57.23%	6	-13.19%	14	-16.54%	9	195.69%	5	2.8	8
University of North Carolina at Chapel Hill	79.00%	3	-8.37%	12	-19.06%	10	149.57%	10	3.0	7
Ohio State University	41.38%	11	-7.34%	10	-12.15%	8	124.03%	11	1.8	12
Pennsylvania State University - Main Campus	91.13%	1	-4.05%	8	-3.78%	7	302.85%	2	4.6	2
Texas A&M	58.89%	5	3.67%	2	83.25%	1	108.29%	12	3.8	3
University of Texas - Austin	90.74%	2	-3.23%	6	-58.15%	14	8202.07%	1	5.6	1
University of Washington - Seattle	55.71%	8	-7.29%	9	-20.43%	11	190.74%	7	2.8	8
University of Wisconsin - Madison	11.25%	14	7.60%	1	-0.95%	4	50.58%	13	1.4	13
University of Arizona	31.97%	12	-3.63%	7	-1.37%	5	46.02%	14	0.9	14
Mean	54.24%		-4.27%		-8.95%		741.70%		2.9	
Median	56.16%		-3.84%		-7.97%		185.84%		2.9	
KPMG Threshold	40%		6%		4%		125%			

* Audited financial statements unavailable as of February 24, 2010.

THE UNIVERSITY OF ARIZONA

FY 2008 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
University of California - Davis	34.60%	13	10.06%	1	2.19%	6	78.35%	13	2.90%	11
University of California - Los Angeles	54.25%	9	8.61%	2	3.57%	4	280.85%	3	5.20%	4
University of Florida	53.67%	10	5.02%	5	-2.70%	11	227.54%	6	3.70%	10
University of Illinois - Urbana	20.80%	15	-2.55%	16	-1.70%	10	49.35%	15	0.70%	16
University of Iowa	69.39%	7	3.23%	10	3.50%	5	193.33%	9	4.30%	7
University of Maryland - College Park	52.46%	11	6.61%	4	4.70%	3	220.95%	7	4.60%	6
Michigan State University	91.71%	4	1.72%	12	-0.61%	8	277.85%	4	4.80%	5
University of Minnesota - Twin Cities	82.39%	5	0.37%	13	-3.36%	12	253.97%	5	4.20%	8
University of North Carolina at Chapel Hill	105.66%	2	8.04%	3	5.96%	1	192.29%	10	6.00%	3
Ohio State University	39.63%	12	-0.88%	15	-4.82%	14	143.93%	11	2.10%	13
Pennsylvania State University - Main Campus	105.26%	3	4.20%	7	5.01%	2	361.20%	2	6.90%	2
Texas A&M	60.86%	8	-0.80%	14	-8.67%	15	130.90%	12	2.50%	12
University of Texas - Austin	123.69%	1	3.86%	8	-12.80%	16	9634.65%	1	7.00%	1
University of Washington - Seattle	72.27%	6	3.28%	9	-0.94%	9	216.37%	8	3.90%	9
University of Wisconsin - Madison	10.40%	16	1.80%	11	-4.49%	13	42.89%	16	0.70%	15
University of Arizona	32.83%	14	4.59%	6	0.23%	7	55.71%	14	1.80%	14
Mean	63%		4%		-1%		773%		3.8	
Median	58%		4%		-1%		205%		4.1	
KPMG Threshold	40%		6%		4%		125%			

THE UNIVERSITY OF ARIZONA
FY 2007 Financial Statement Data for Select Proposed Peers Using KPMG Methodology for CFI Analysis

Peer University	PRIMARY RESERVE		RETURN ON NET ASSETS		NET OPERATING REVENUES		VIABILITY		COMPOSITE FINANCIAL INDEX	
	Ratio	Rank	Ratio	Rank	Ratio	Rank	Ratio	Rank	CFI	Rank
University of California - Davis	34.74%	13	2.72%	1	1.50%	6	77.11%	13	2.00%	11
University of California - Los Angeles	54.02%	9	7.69%	2	4.97%	4	258.87%	3	5.10%	4
University of Florida	54.39%	10	13.65%	5	7.44%	11	257.58%	6	6.00%	10
University of Illinois - Urbana	23.60%	15	6.88%	16	0.77%	10	58.28%	15	1.90%	16
University of Iowa	68.99%	7	8.55%	10	6.55%	5	203.97%	9	5.30%	7
University of Maryland - College Park	53.84%	11	13.37%	4	7.24%	3	190.42%	7	5.40%	6
Michigan State University	100.19%	4	11.07%	12	11.66%	8	268.28%	4	7.00%	5
University of Minnesota - Twin Cities	92.62%	5	14.55%	13	7.58%	12	288.74%	5	7.30%	8
University of North Carolina at Chapel Hill	105.17%	2	17.43%	3	11.61%	1	212.91%	10	7.30%	3
Ohio State University	40.88%	12	12.12%	15	9.60%	14	133.79%	11	4.40%	13
Pennsylvania State University - Main Campus	110.42%	3	14.66%	7	14.45%	2	391.17%	2	8.70%	2
Texas A&M	76.75%	8	9.17%	14	4.76%	15	157.27%	12	4.90%	12
University of Texas - Austin	140.07%	1	16.58%	8	15.24%	16	10999.88%	1	9.70%	1
University of Washington - Seattle	77.69%	6	13.60%	9	12.05%	9	210.84%	8	6.20%	9
University of Wisconsin - Madison	14.04%	16	10.61%	11	1.22%	13	53.10%	16	2.10%	15
University of Arizona	34.49%	14	10.27%	6	2.68%	7	54.77%	14	2.80%	14
Mean	72%		12%		8%		864%		5.5	
Median	62%		13%		7%		207%		5.3	
KPMG Threshold	40%		6%		4%		125%			

APPENDIX A

APPENDIX A

**COMMENTARY ON FY 2008 ASSESSMENT OF FINANCIAL STRENGTH
CAROL N. CAMPBELL
PRESENTED TO THE ARIZONA BOARD OF REGENTS AUDIT COMMITTEE
JANUARY 22, 2009**

Past experience with KPMG/Prager Ratio Analysis:

In the late 1990's, the Department of Education revamped the Title IV (Federal Financial Aid Programs) financial eligibility criteria. As part of the process, I was asked to serve as a consultant to the ED. We looked at a number of possible tools that would serve the purpose and settled on the four ratios previously developed by KPMG/Prager as the most robust and descriptive indicators available. I actively participated in the public commentary process that followed the introduction of the ratios and once they were adopted, I also served as faculty, presenting the ratios and at a series of educational sessions for university business officers.

PURPOSE OF THE RATIOS:

The ratios are indicators of institutional financial strengths and weaknesses. They are not a report card; rather they are tools to understand individual institutions and to serve as a basis for future decision-making. They help answer questions such as, "Does an institution have the financial flexibility to broaden its mission?" Or in present circumstances in Arizona, "How do we best manage through a severe revenue shortfall?"

The ratios should NOT be used to compare the Arizona universities against one another. We are three distinct entities, each coping with a very different set of dynamics and each having distinctly different composite revenues, growth patterns, and research focus.

The ratios are best used to study each university individually and most importantly, the trend of each ratio over time.

BACKGROUND:

That said, there are certain commonalities among the Arizona Universities because of the environment in which we all exist that have an overwhelming influence on the relatively weakness of the ratios in comparison with national results. These common factors include:

❖ Structural Revenue Deficits

- Tuition. ABOR and case law have determined that compliance with state constitutional requirements that "education be as free as possible" means that in-state tuition cannot exceed the "top of the bottom third," nationally and, indeed, ABOR has a history of

reducing requests to raise tuition even when the requests have been at or below that threshold. Recently adopted tuition guarantee programs lag the national rankings by one year for incoming freshmen and do not keep pace over the student's subsequent years of enrollment. Currently, the Universities all rank well below the top of the bottom third.

- State Support. While State instructional and capital support per student differs among the three institutions, it is well below national averages as well. In 2007, the most recent year for which data was available from IPEDS, the Universities ranked 16th (U of A), 30th (NAU), and 36th (ASU) out of the 50 states when combining state appropriations and state capital appropriations per FTE. Results were similar if only state appropriations per FTE are measured.
- Fund-Raising and Endowment Support. Taking a look across the United States, one will find a marked cultural differentiation between the East Coast, which is dominated by private universities and the Rocky Mountain region which is dominated by public universities. The much older, established Eastern and Midwestern universities have built a strong legacy of financial stewardship among alumni that is lacking in the West. Thus, private support and, more importantly, the endowments that result from many years of such support, are considerably lower in the West, and especially in Arizona where both institutional youth and a culture that does not prize education are in effect.

❖ Structural Expense Deficits

- Debt Service. Unlike many other states, the State of Arizona does not bond for University academic facilities. While the State will sometimes appropriate funds for debt service, the impact of this is higher expenses flowing through the Universities and a far greater debt burden without the offsetting asset base. Lack of State responsibility for academic facilities is exacerbated because while enrollments, and therefore facility needs, are growing in Arizona, most of the rest of the nation is enjoying stable enrollment.
- Financial Aid. Unlike many other states, the State of Arizona does not have a state-sponsored financial aid program for Arizona students. Therefore ABOR had mandated that the Universities set aside a minimum of 17% of tuition to fund financial aid. In fact, the Universities exceed this requirement to maintain access to as many students as possible. In general, financial aid expenses are considerably higher for the Arizona Universities than at many other universities, unless such Universities have depth in endowed scholarships.

❖ Structural Operating Margin Deficit

Despite the limited revenue base and mandatory funding of both facilities and financial aid as described above, the Arizona Universities still operate in a competitive national marketplace where academic journals, lab supplies, the national academic labor pool, and other components of the Higher Education Price Index (HEPI) are the same as all other universities. And the historical annual increase in the HEPI averages about 1% higher than the CPI. The combination of factors puts intense pressure on operating margins, especially when enrollment increases must be absorbed.

All of these factors combine to create an operating environment in which reserves are thin and building reserves, as reflected in growth of net assets, is a long, slow, process. This is well-reflected in all of the following ratios which are calculated on the basis of revenues, expenses, net assets, operating margins, outstanding debt, and debt service.

SUMMARY:

The threshold and comparative ratio scales are useful to illustrate that the Arizona Universities are much higher leveraged and under-reserved and operate on thinner margins compared to national norms. This means that the Arizona Universities have considerably less capacity than their national peers with which to ride out an economic downturn.

Because of the unique set of structural revenue and expense deficits that impact the Arizona Universities, it is difficult to find peer comparisons that operate in a similar economic environment.

In general, the Universities' ratios trended upward from 2004 through 2007 and declined somewhat in 2008. Reasons include increased debt as facilities to manage enrollment growth and research infrastructure were built, declining financial market returns, and a decline in state appropriation.

Nevertheless, it is important to note that the Universities have generally held their own with essentially stable trends over the past five years while at the same time they have absorbed thousands of additional students, added tens of thousands of gross square feet new space, improved student access and financial aid, all the while raising academic quality and research productivity.

Looking ahead, deep cuts in state appropriations combined with unprecedented endowment losses present very challenging circumstances for Universities with so little financial flexibility.

The next section provides supplemental commentary on each of the individual ratios and should be read in conjunction with the commentary provided in the January 12, 2009 FY 2008 Assessment of Financial Strength document.

PRIMARY RESERVE RATIO

The purpose of this ratio is to determine if spendable reserves are keeping pace with the growth in operations. A stable trend over time, which all Universities exhibit, indicates that this is the case.

Expect the ratio to decline when:

- Enrollment growth requires facility expansion which converts expendable assets to non-expendable assets due to investment in additional facilities.
- Sudden financial market decline reduces the value of endowments which are reflected in expendable net assets without proportional and precipitous reduction of expenses.

Expect the ratio to increase when:

- Revenues regularly exceed expenses creating additional reserves.
- Financial markets rise creating additional endowment value in excess of current endowment spending.

Given the investment in facilities and growth in operations due to increasing enrollment, the stable trends of all Universities are quite an achievement.

The future implications are that financial market declines following June 30, 2008 will likely erode the ratios in 2009 and given that 2008 values are below the advised threshold level, the Board needs to question how much of the reduction in state support can be absorbed by further eroding reserves.

RETURN ON NET ASSETS RATIO

This ratio reflects the productive use of assets over time. It is sensitive to the absolute value of the annual increase in net assets (all revenue minus all expenses) in proportion to the size of the asset base. In the case of the Arizona Universities, UA and ASU have four times the asset base of NAU. To achieve a 10% return on net assets, UA and ASU would need consistent revenues of \$130 to \$140 million in excess of all expenses including the depreciation generated by their large investment in fixed assets. Results of this magnitude are unlikely, especially under current economic conditions.

Since all revenues and expenses are included in determining this ratio, volatility may be caused by nonrecurring events such as land sales, write-downs, or dramatic swings in financial markets. The Board should understand the reasons for such annual volatility.

Over time, the ratio will reflect the budgetary philosophy and financial environment of an institution, including considerations such as whether it is operating at break-even or is building or consuming reserves. The Board should understand the reasons underlying these results.

NET OPERATING REVENUES RATIO

This ratio focuses on the results of recurring operations. By definition, it excludes “other income,” capital gifts and grants, most gifts to the endowment, and, importantly, the annual state appropriation for research infrastructure. Since operating expenses such as debt service and depreciation for these research facilities are included in the calculation, excluding the offsetting revenue artificially depresses this ratio with the effect most pronounced for UA and ASU.

This ratio is an even stronger indicator of budget philosophy over time and it should reflect lower volatility than the Return on Net Asset ratio.

Given the structural revenue and expense deficits note previously, it is no surprise that the Arizona Universities have relatively low operating margins and therefore low ratio values on a national scale. Only NAU has met the threshold level over the past five years, and has done so consistently.

This ratio also reflects the relatively poor financial market returns in fiscal 2008, and probably some erosion of reserves as state appropriation cuts were absorbed late in the fiscal year. To the extent that current year expenses are paid from reserves, which accumulated from prior years’ revenues, a current year financial operating deficit is incurred.

Looking ahead, this ratio will likely fall further due to the precipitous financial market decline in fall 2008 and as reserves may be further eroded to meet anticipated state appropriation cuts.

VIABILITY RATIO

As a ratio of expendable net assets to debt, this ratio is an indicator of debt capacity and financial flexibility. The ratios of the Arizona Universities reflect their rather unique situation under which the state will not bond for academic facilities but will, on occasion, provide legislative appropriations for debt service. Note that legislative appropriations support 35% (41% in FY 2009) of ASU debt, 30% (26% in FY 2009) of NAU debt, and over 20% (18% in FY 2009) of UA debt. If either the state carried the debt or the Universities carried net assets sufficient to service the debt, then the ratios would be considerably higher.

The rating agencies recognize and give the Universities credit for this situation. The average AA rated public university has two dollars of net assets for every dollar of debt. Both UA and ASU have AA ratings even though their balance sheets reflect just one dollar of net assets for every two dollars of debt. However, investment in enrollment growth and research facilities has taken its toll and institutional debt capacity, at current ratings, is limited.

APPENDIX B

APPENDIX B

ARIZONA UNIVERSITY SYSTEM FY 2009 FINANCIAL RATIO ANALYSIS

EXECUTIVE SUMMARY

BACKGROUND:

Board policy 3-410 requires Arizona State University, Northern Arizona University, and The University of Arizona to provide the Arizona Board of Regents with audited annual financial reports and a 10-year ratio analysis of selected data from the financial reports.

With the implementation of GASB 34/35 and 39 in 2002 and 2004, respectively, and the associated changes in financial reporting requirements, the universities and central office staff developed 10 new financial ratios. At its December 2005 meeting, the Board's Audit Committee approved these ratios and requested the universities to report them beginning with FY 2005 financial data, even though implementing the new ratios at that time would result in presentation of only four years of comparative data.

Accordingly, this FY 2009 annual financial ratio analysis uses data from the universities' FY 2009 audited financial statements, together with data from 7 previous annual reports, covering the period July 1, 2001, through June 30, 2009. An additional year of information will be added to this ratio analysis each year until 10 years of comparable information is again provided.

Each university presents 10 ratios over the 8-year period (pages 8-25). The ratios serve as indicators of the universities' financial strengths and weaknesses. Ratio formulas are presented on page 26, and ratios are presented by university on pages 27-29.

ANALYSIS:

Ratio 1: State General Fund Appropriations to Total Revenue

State General Fund Appropriations as a percentage of Total Revenue decreased significantly at all three universities—approximately 5 percentage points—from FY 2008 to FY 2009. This reverses a 5-year stabilization and reflects the massive General Fund cuts—a total of \$192.5 million—dealt to the universities in FY 2009. ASU's ratio decreased from a high of 39% in FY 2002 to the current 8-year low of 27%. NAU's ratio decreased from a high of 42% in FY 2002 to the current 8-year low of 35%. UA's ratio decreased from a high of 33% in FY 2002 to the current 8-year low of 24%.

[Note: The universities' FY 2009 ratios for Ratio 1 do not agree with the ratios for "Reliance on State Funding" in Moody's January 5, 2010, Special Comment (pages 30-33) primarily because Moody's included the FY 2009 Federal Fiscal Stabilization Funds

in their calculation of state support to the universities. Although the federal stimulus funds were intended to backfill the reductions in state General Fund support, they are federal, not state, funds and, consistent with treatment of other federal funds, are included in the universities' calculations of Ratio 3 below.]

Ratio 2: Net Tuition and Fees Revenue to Total Revenue

Net Tuition and Fees as a percentage of Total Revenue increased 2-3 percentage points over the prior year. The steady 8-year increase at ASU (23% to 33%), NAU (19% to 28%), and at UA (14% to 18%) shows an increasing reliance on Tuition and Fees as a revenue source—a continuing shift from state support to student support—a trend continuing in public universities around the country. Historically, UA's reliance on tuition and fees is less due to higher levels of research funding and, while at an 8-year high of 18% in FY 2009, has remained in the 14-16% range over the previous 7 years.

Ratio 3: Gifts, Grants, Contracts, TRIF Revenue, and Federal Fiscal Stabilization Funds to Total Revenue

Total Gifts, Grants, Contracts, TRIF Revenue, and Federal Fiscal Stabilization Funds (FFSF) as a percentage of Total Revenue increased 3-6 percentage points over the prior year. Over the 8-year period, this percentage remained relatively stable until FY 2009 when it took a significant uptick, reflecting receipt of FY 2009 FFSF and the changing nature of the composition of Total Revenue resulting from the severe FY 2009 state budget cuts. ASU's ratio of 28% is up from the prior year 22%; NAU's 26% up from 23%; and UA's 44% up from 39%. UA's greater restricted funding from the federal government and private donors causes its ratio to diverge from ASU's and NAU's.

Ratio 4: Other Revenue to Total Revenue

Other Revenue (auxiliary enterprises revenues, net investment income, and educational department sales and services revenues) as a percentage of Total Revenue in FY 2009 decreased 1-3 percentage points from the prior year, continuing a trend first noted in FY 2008 with the downturn in the financial markets. ASU reported an FY 2009 ratio of 12%; NAU, 12%, and UA, 13%. Over the 8-year period, this ratio has fluctuated between 12% and 18% at all three universities. In any given year, this ratio can be significantly impacted by irregular transactions such as land sales.

In FY 2009 this ratio was negatively impacted by the global economic collapse and the dramatic downturn in the financial markets that resulted in net losses on the universities' endowments.

Ratio 5: Net Revenue (University Only) to Total Revenue (University Only)

Because of the receipt of FY 2009 federal stimulus funds, all three universities managed to cover their current year expenses with current year revenue in FY 2009, thus avoiding the need to deplete net assets to operate the universities. However, without the stimulus funds, ASU and UA would have reported decreases in their net assets of

\$12 million and \$51 million, respectively. On the other hand, even without federal stimulus funds, NAU would have reported positive Net Revenues of \$15.5 million.

Ratio 6: Net Revenue (University + Component Units) to Total Revenue (University + Component Units)

This ratio, indicating the ability of the universities and their component units (see page 7) to operate within current year revenue, decreased from prior year at all three universities. However, ASU and UA suffered especially large decreases—moving into negative numbers—because their Foundations hold significantly larger endowment investments than does the NAU Foundation. ASU and its component units reported Net Revenues of -\$72 million, while UA and its component units reported -\$50 million. Significant losses occurred in the component units, whose endowment investments were significantly and negatively impacted by the global economic collapse and the dramatic downturn in the financial markets. NAU and its component units combined reported positive Net Revenues of \$29 million, but that number also was dragged down by a loss of over \$4 million on Foundation endowment investments.

Ratio 7: Expendable Net Assets to Total Expenses

Ratio 7 indicates the ability of expendable net assets (those assets available for use for operations) to keep pace with total expenses. ASU's ratio has remained relatively stable over the 8-year reporting period (adjusting FY 2008 for a reimbursement that occurred shortly after June 30, 2008). The current 16% ratio (8.5 weeks of spending coverage) would be 12% (6 weeks) without federal stimulus funds. NAU's ratio of 39% (20 weeks of spending coverage) would be 33% (17 weeks) without stimulus funds, but increased significantly over the prior year 28%, continuing an upward trend and reflecting an increasing ability to respond to emergencies or unforeseen needs. UA's 22% ratio (11.5 weeks of spending coverage) would be 18% (9 weeks) without stimulus funds has remained relatively stable over the 8-year reporting period.

Ratio 8: Unrestricted Net Assets to Total Expenses

Ratio 8 indicates the ability of unrestricted net assets (the subset of expendable net assets that can most quickly be converted to cash) to keep pace with total expenses. ASU's ratio of 11% (6 weeks spending coverage) remains within a relatively stable range of 11%-16% over the 8-year period (adjusting for anomaly in FY 2008 ratio). NAU's FY 2009 ratio of 34% (18 weeks spending coverage) continues an 8-year upward trend from 10% in FY 2002 to 34% in FY 2009, indicating continued increasing operating flexibility. UA's ratio of 12% (6 weeks spending coverage) remains within a relatively stable range of 8%-13% over the 8-year period.

It should be noted that the booking by the universities of the FY 2009 federal stimulus funds at the end of FY 2009 resulted in a temporary increase in Unrestricted Net Assets at June 30, 2009. Without these federal stimulus funds, ASU's ratio would be 7% (4 weeks spending coverage); NAU's, 28% (14 weeks); and UA's, 8% (4 weeks).

Ratio 9: Debt Service Payment (Interest + Principal) to Total Expenses

The universities consistently earn solid investment bond ratings by showing adequate capacity to pay interest and to repay principal on debt. The universities continue to maintain strong ratings for both System Revenue Bonds (SRBs) and Certificates of Participation (COPs) from Moody's and from Standard & Poor's.

It should be noted, however, that on January 5, 2010, Moody's issued a Special Comment on Arizona's three public universities, explaining why Moody's is not immediately taking any rating action following its downgrade of the state of Arizona's issue rating by one notch from Aa3 to A1 and maintained the negative outlook. Quoting from the Special Comment:

“Our decision to not take rating action at this point in time heavily rests on our belief that the universities have healthy student market positions and tuition setting flexibility which could help offset future pressure on state funding.

We will also continue to monitor these universities' abilities to maintain balance sheet strength, with significant borrowing absent growth of financial resources and cash flow a possible contributor to rating pressure. The Arizona public universities have a shorter history of fundraising for endowment, and balance sheet resources are thin compared to medians for similar-sized institutions. Further, the state provides modest levels of capital support and the public universities have significantly ramped up borrowing levels in order to fund capital investment. As a result, capital ratios for these three universities are relatively weak for their rating categories. An inability to grow revenue to support debt service and bolster their financial resource bases to better support growing debt levels could contribute to rating pressure.”

The universities' current ratings and outlooks are:

- ASU and UA maintained an AA SRB rating and an AA- COPs rating from S&P; and an Aa3 rating on SRBs and an A1 rating on COPs from Moody's. These ratings are in the upper half of the investment grade rating categories. The rating outlook for ASU and UA remains stable, meaning that based upon present debt levels in relation to net assets, a rating is not likely to change in the near future. However, in light of Moody's recent downgrade of the state of Arizona's rating as noted above, further deterioration of the state's financial position could have a chain reaction on the universities' bond ratings.
- NAU maintained an A+ SRB rating and an A COPs rating from S&P; and an A2 SRB rating and an A3 COPs rating from Moody's. The rating outlook for NAU from S&P remains stable, while Moody's moved their rating down a notch from positive to stable, the same outlook as is held by ASU and UA.

The most recent Moody's and Standard & Poor's analyses are available upon request from the universities. Moody's January 5, 2010, Special Comment is included on pages 30-33.

ASU's FY 2009 debt ratio of 5.4% increased slightly over its 5.0% ratio the prior year, remaining in the 3-5% range during this 8-year reporting period. NAU's FY 2009 debt ratio of 6.5% decreased slightly from its 6.8% ratio at prior year-end and remains in the 4-7% range. UA's FY 2009 debt ratio of 5.7% decreased slightly from its 5.9% at prior year-end, remaining in the 4-6% range over the 8-year reporting period.

Ratio 10: Total Financial Resources (University + Component Units) to Direct Debt (University + Component Units)

This ratio measures coverage of debt by all resources available to the university, including those of its component units. A larger percentage indicates the availability of more resources to cover total university and component unit debt. ASU's ratio of 51%, (although down from 58% the prior year), NAU's ratio of 89% (remaining stable for 4 years), and UA's ratio of 81% (although down from 102% in the 2 prior years), reflect the ability of each university and its component units to repay all outstanding debt without undue financial hardship.

Explained differently, at June 30, 2009, ASU and its component units had sufficient financial resources to pay 51% of the total debt of the university and component units; NAU, 89%; and UA, 81%.

CONCLUSION:

The Arizona University System suffered draconian state General Fund budget cuts during FY 2009—\$192.5 million, or 16% of its initial budget—challenging university management to reevaluate priorities and to increase productivity. Management made difficult decisions to lay off and furlough staff; consolidate, eliminate, and/or reduce colleges, schools, academic departments, programs, and class offerings; and implement other cost-cutting measures. This financial analysis indicates that were it not for FY 2009 Federal Fiscal Stabilization Funds, ASU and UA would have reported decreases in net assets instead of reporting increases. Key observations made by all three universities are:

- Universities are reporting a continued trend toward increasing reliance on revenue sources other than state General Fund support. State appropriations have not kept pace proportionally with overall university revenues. These dramatic decreases in state support as a percentage of total university revenues are being offset with increases in net tuition and fees and other revenues such as research grants and contracts, and gifts. Fortunately, \$154.1 million of the FY 2009 reduction of \$192.5 million in state General Fund appropriations was offset by Federal Fiscal Stabilization Funds. However, General Fund cuts of this magnitude cannot be sustained in the absence of such stimulus funds.

- Both ASU and UA anticipate that their research grants and contracts revenues will continue to be a significant revenue source due to recently opened research facilities and other commitments made in the research area. It should be noted that these research revenues are not available to support core university operations. However, they do have a significant, positive impact on the state's economy.
- ASU and UA generate relatively small or essentially breakeven net revenues each year. Although total revenues have increased significantly over the last 8 years, these revenues are used to grow the universities to meet enrollment demand, especially at ASU. Given these relatively small net revenues in any given fiscal year, the universities have a more limited ability to react to emergencies or unforeseen needs. NAU, who relies more heavily on state General Fund support than ASU or UA, has positioned itself to generate increasing net revenues through strict budgetary controls, balanced budgets, and growing its enrollment. This gives NAU the financial flexibility to react to emergencies or unforeseen needs.
- All three universities, while carrying large amounts of long-term debt for capital expansion, can repay their current levels of debt and have the capacity for future additional debt financings. However, Standard & Poor's and Moody's will also continue to monitor the universities' abilities to maintain balance sheet strength, with significant borrowing absent growth of financial resources and cash flow a possible contributor to rating pressure.
- The long-term financial health of the universities will depend on securing continuing revenue streams at a level necessary for the universities to realize their missions.

UNIVERSITY COMPONENT UNITS AS DEFINED BY GASB 14 AND GASB 39

Arizona State University:

- ASU Foundation
- Arizona Capital Facilities Finance Corporation (ACFFC)
- ASU Alumni Association
- Collegiate Golf Foundation
- Mesa Student Housing, LLC
- Arizona State University Research Park, Inc.
- Sun Angel Endowment
- Sun Angel Foundation
- Downtown Phoenix Student Housing, LLC
- University Public Schools, Inc.

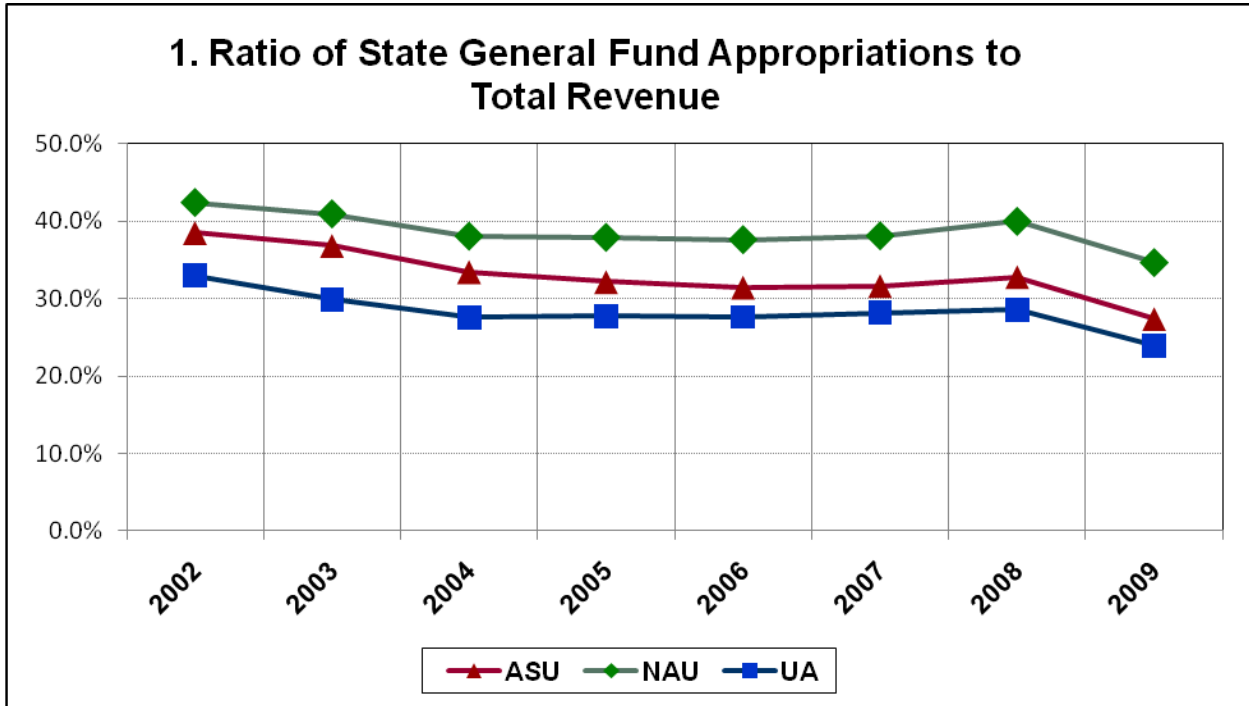
Northern Arizona University:

- Northern Arizona University Foundation, Inc.
- Northern Arizona Capital Facilities Finance Corporation (NACFFC)

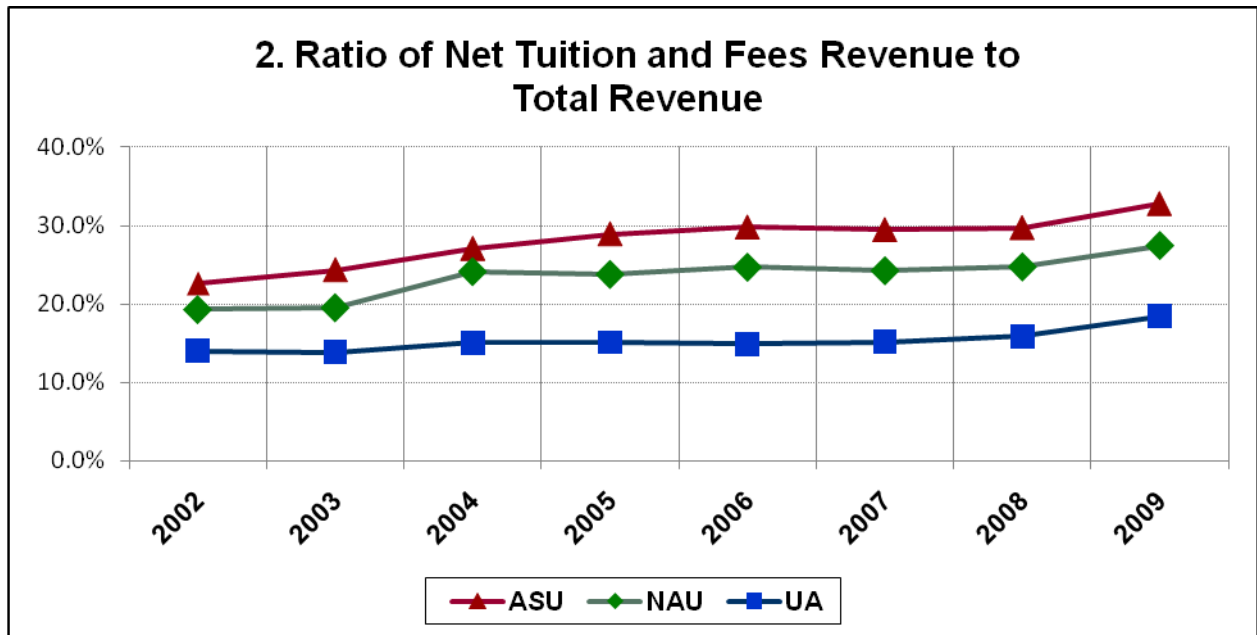
The University of Arizona:

- The University of Arizona Foundation, Inc.
- The University of Arizona Alumni Association
- Law College Association of The University of Arizona
- Campus Research Corporation

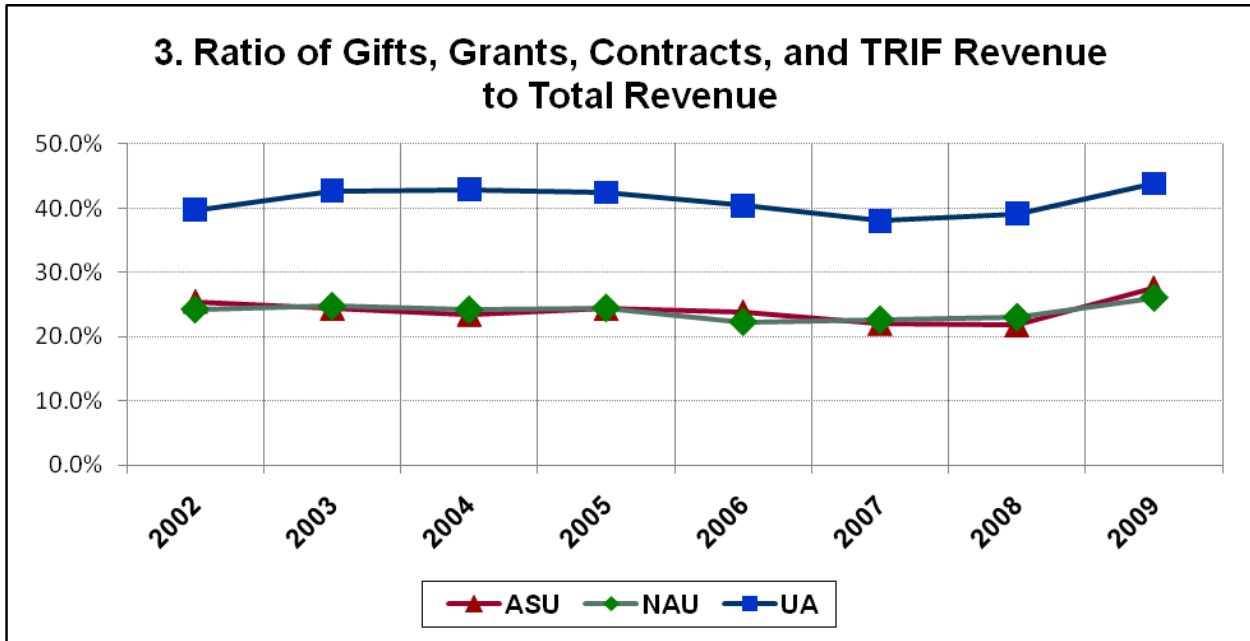
Ratio 1	Description of Ratio
<p data-bbox="191 268 380 401">State General Fund Appropriations Total Revenue</p> <p data-bbox="172 436 399 468">FY 2009 RATIOS</p> <p data-bbox="159 514 412 577"> $\frac{\text{ASU}}{27\%}$ $\frac{\text{NAU}}{35\%}$ $\frac{\text{UA}}{24\%}$ </p>	<p data-bbox="443 264 1468 430">Element definition: State General Fund Appropriations are state of Arizona legislative General Fund appropriations to the universities and do not include university tuition collections remitted to the state by the universities and then appropriated back to the universities. Total Revenue includes operating, nonoperating, and other revenue and gains.</p> <p data-bbox="443 468 1468 730">State General Fund Appropriations as a percentage of Total Revenue decreased significantly at all three universities—5 percentage points—from FY 2008 to FY 2009. This reverses a 5-year stabilization and reflects the massive General Fund cuts—a total of \$192.5 million—dealt to the universities in FY 2009. ASU’s ratio decreased from a high of 39% in FY 2002 to the current 8-year low of 27%. NAU’s ratio decreased from a high of 42% in FY 2002 to the current 8-year low of 35%. UA’s ratio decreased from a high of 33% in FY 2002 to the current 8-year low of 24%.</p> <p data-bbox="443 768 1468 867">This ratio shows the divergence among the three universities in the extent to which they rely on the state of Arizona for funding, with 35% of NAU’s support coming from the state while only 24% of UA’s support comes from the state.</p> <p data-bbox="443 905 1468 1029">State General Fund appropriations have increased over the 8-year period by \$96 million (30%) at ASU, by \$30 million (27%) at NAU, and by \$20 million (6%) at UA. General Fund appropriations decreased at all three universities between FY 2008 and FY 2009.</p>



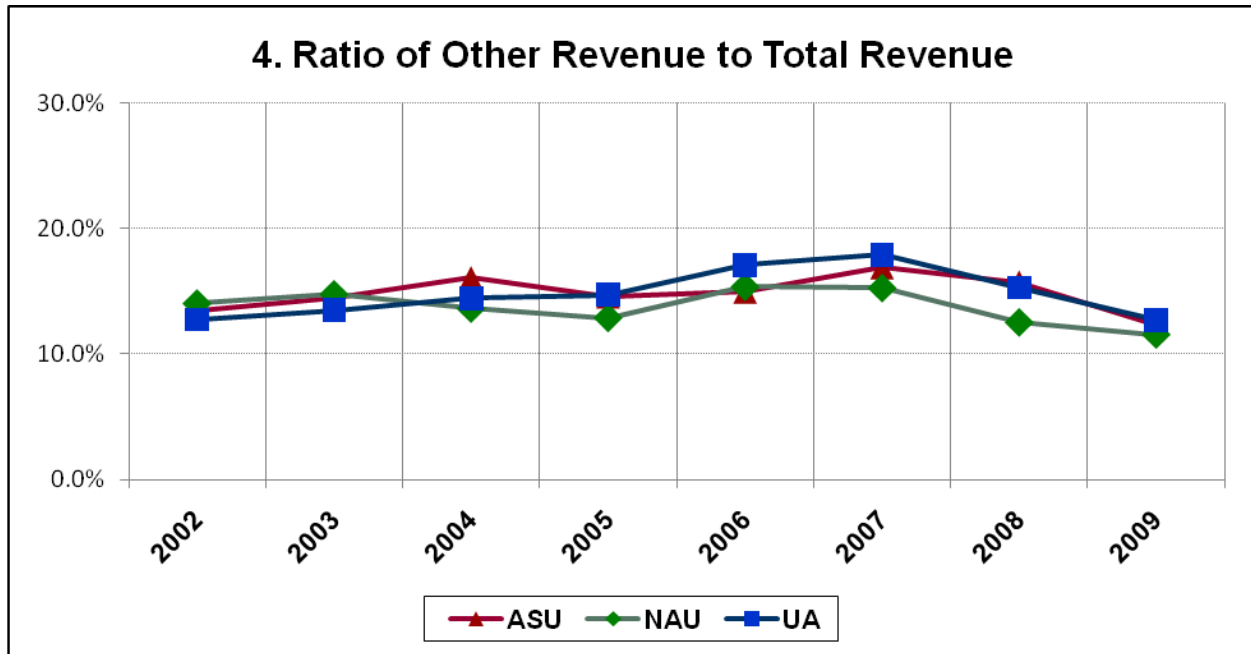
Ratio 2	Description of Ratio						
<p data-bbox="159 268 412 331">Net Tuition & Fees Total Revenue</p> <p data-bbox="168 369 402 401">FY 2009 RATIOS</p> <table data-bbox="159 443 412 506"> <tr> <td>ASU</td> <td>NAU</td> <td>UA</td> </tr> <tr> <td>33%</td> <td>28%</td> <td>18%</td> </tr> </table>	ASU	NAU	UA	33%	28%	18%	<p data-bbox="444 268 1468 369">Element definition: <i>Net Tuition and Fees</i> are tuition and fees paid by students and are net of scholarship allowances. <i>Total Revenue</i> includes operating, nonoperating, and other revenue and gains.</p> <p data-bbox="444 405 1468 636">Net Tuition and Fees as a percentage of Total Revenue increased 2-3 percentage points over the prior year. The steady 8-year increase at ASU (23% to 33%), NAU (19% to 28%), and at UA (14% to 18%) shows an increasing reliance on Tuition and Fees as a revenue source—a continuing shift from state support to student support—as reflected in the decrease in state General Fund appropriations as a percentage of total revenues (Ratio 1) over the same period.</p> <p data-bbox="444 672 1468 800">As with Ratio 1, this ratio shows the divergence among the three universities in the extent to which they rely on tuition and fees to operate the university. Student tuition and fees provide 33% of total revenues at ASU but only 18% at UA.</p>
ASU	NAU	UA					
33%	28%	18%					



Ratio 3	Description of Ratio
<p data-bbox="164 268 407 401">Gifts, Grants, Contracts, TRIF & FFSF Revenue Total Revenue</p> <p data-bbox="172 436 399 468">FY 2009 RATIOS</p> <p data-bbox="159 512 412 573"><u>ASU</u> <u>NAU</u> <u>UA</u> 28% 26% 44%</p>	<p data-bbox="443 268 1468 468"><i>Element definition:</i> Gifts, Grants, and Contracts come from private donors, additions to endowments, and government (primarily federal) and private research grants and contracts. TRIF Revenue is ABOR's share of state sales tax revenue approved under Proposition 301 (November 2000). Total Revenue includes operating, nonoperating, and other revenue and gains.</p> <p data-bbox="443 506 1468 705">Total Gifts, Grants, Contracts, and TRIF Revenue as a percentage of Total Revenue increased 3-6 percentage points over the prior year. Over the 8-year period, this percentage remained relatively stable until FY 2009 when it took a significant uptick, reflecting receipt of FY 2009 Federal Fiscal Stabilization Funds and the changing nature of the composition of Total Revenue resulting from the severe FY 2009 state budget cuts.</p> <p data-bbox="443 741 1468 940">UA's greater restricted funding from the federal government and private donors causes its ratio to diverge dramatically from ASU's and NAU's. This greater reliance on restricted funding somewhat limits UA's financial flexibility. As research continues to ramp up in FY 2010 and thereafter in new research buildings at all three universities, more federal and other research grants and contracts should generate increased funding, especially at UA and ASU.</p>

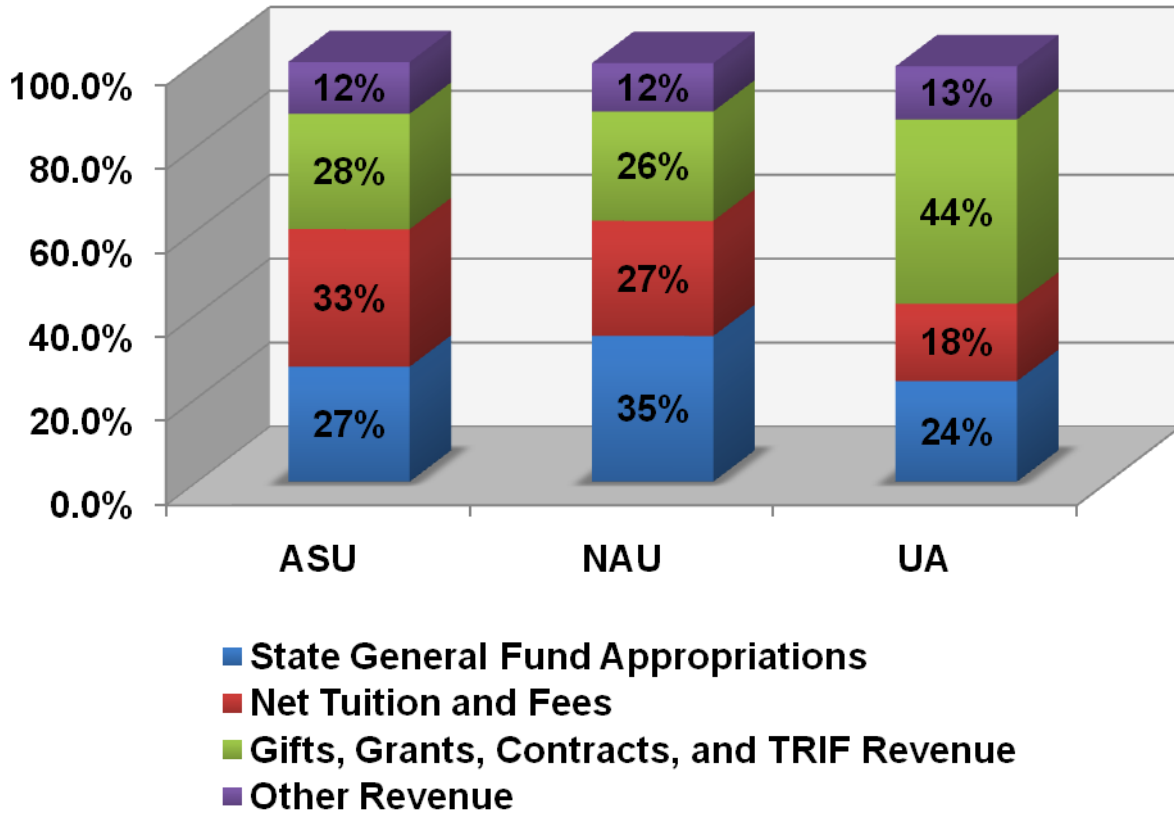


Ratio 4	Description of Ratio
<p data-bbox="180 268 391 331"><u>Other Revenue</u> <u>Total Revenue</u></p> <p data-bbox="168 369 402 401">FY 2009 RATIOS</p> <p data-bbox="159 443 412 506"><u>ASU</u> <u>NAU</u> <u>UA</u> 12% 12% 13%</p>	<p data-bbox="443 260 1471 394">Element definition: <i>Other Revenue</i> includes auxiliary enterprises revenue, investment income, and all other revenue, both operating and nonoperating, not included in the numerators of Ratios 1, 2, and 3. <i>Total Revenue</i> includes operating, nonoperating, and other revenue and gains.</p> <p data-bbox="443 426 1471 594">Other Revenue as a percentage of Total Revenue in FY 2009 decreased 1-3 percentage points from the prior year, continuing a downward trend first noted in FY 2008 with the downturn in the financial markets. Over the 8-year period, this ratio has fluctuated between 12% and 18%. In any given year, this ratio can be significantly impacted by irregular transactions such as land sales.</p> <p data-bbox="443 625 1471 722">In FY 2009 this ratio was significantly and negatively impacted by the global economic collapse and the downturn in the financial markets that resulted in net losses on the universities' endowments.</p>



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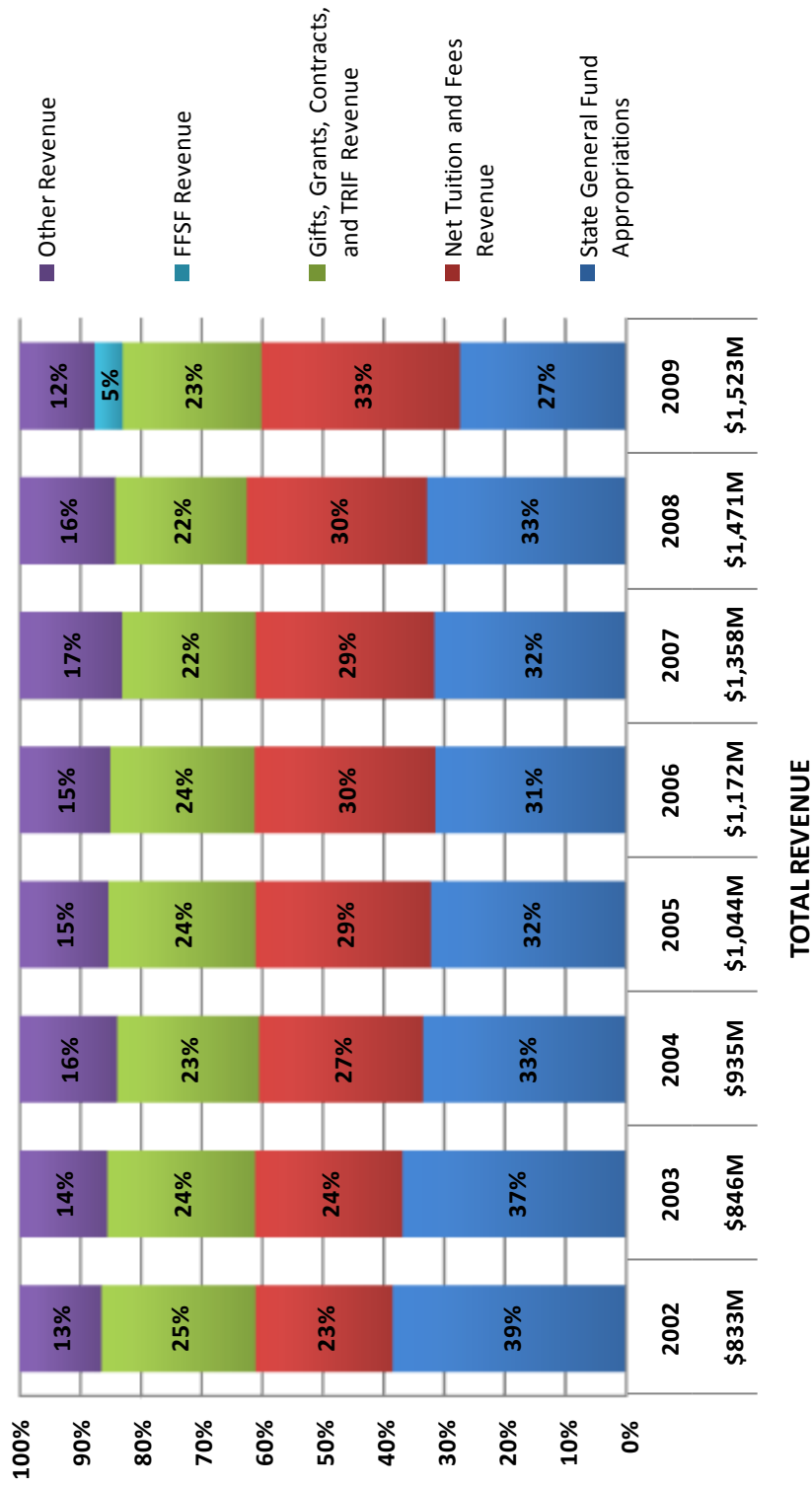
Composition of University Total Revenue Ratios 1, 2, 3, and 4 Combined



Note: University totals may not equal 100% due to rounding.

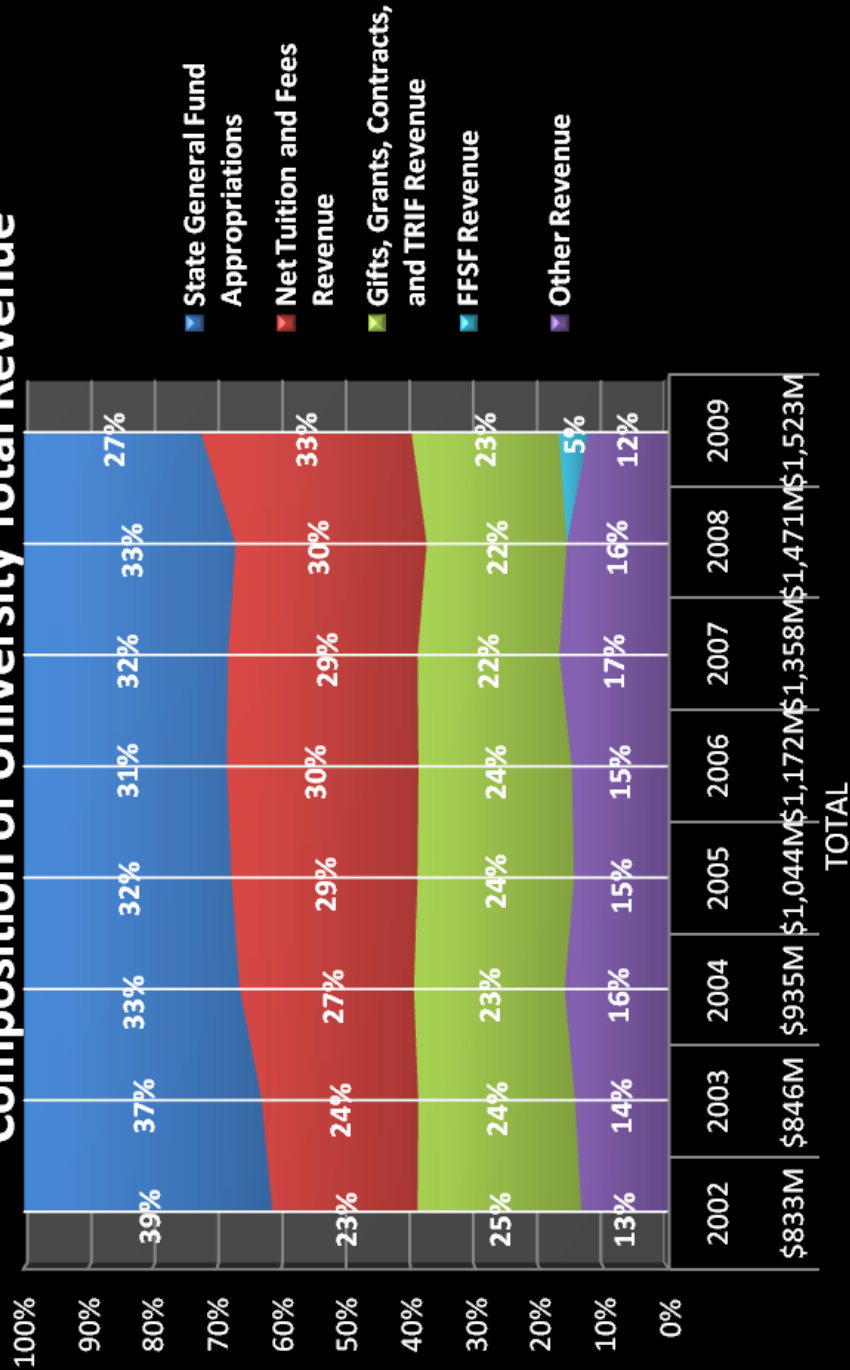
ARIZONA STATE UNIVERSITY

Composition of University Total Revenue



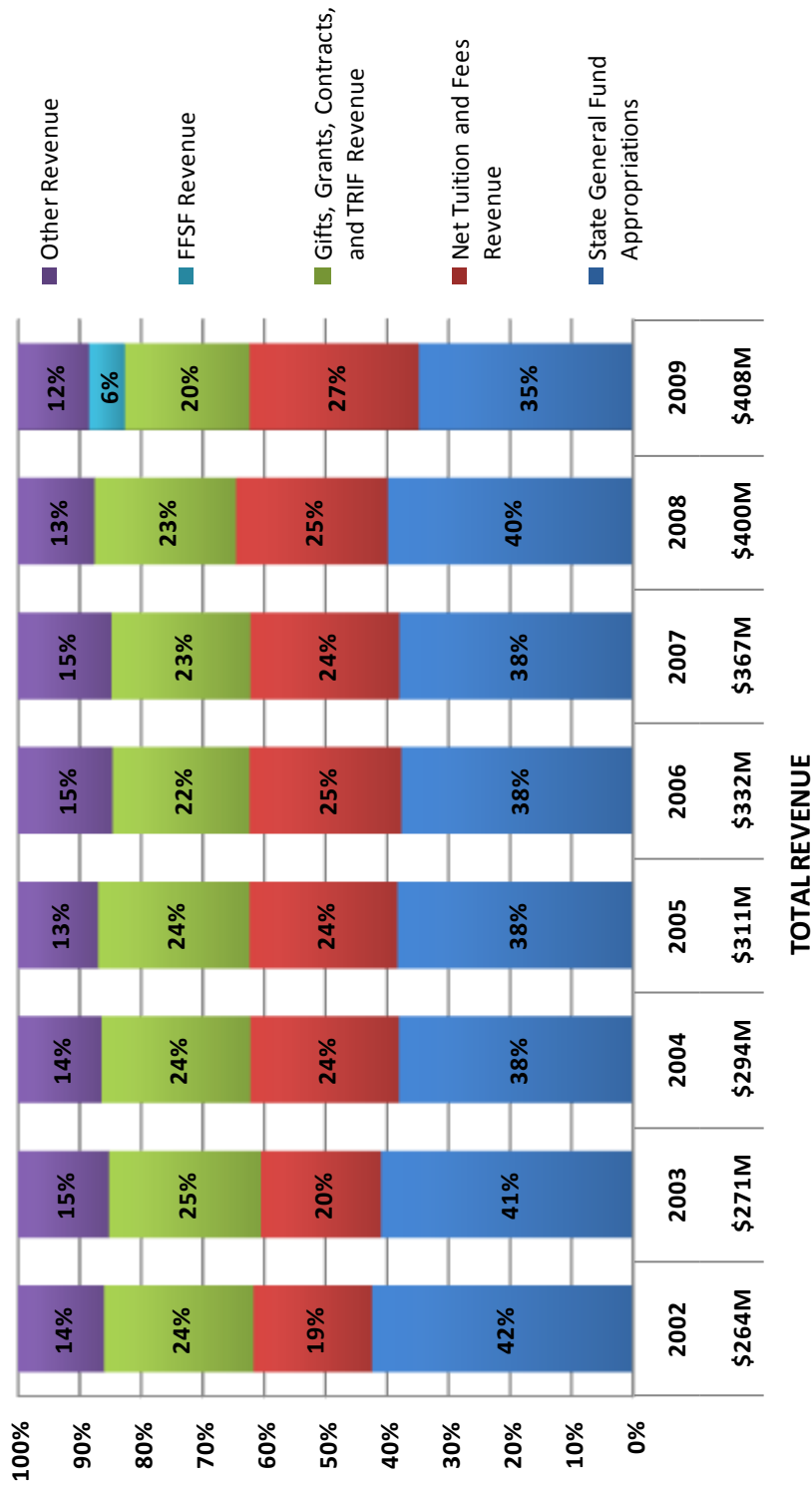
ARIZONA STATE UNIVERSITY

Composition of University Total Revenue



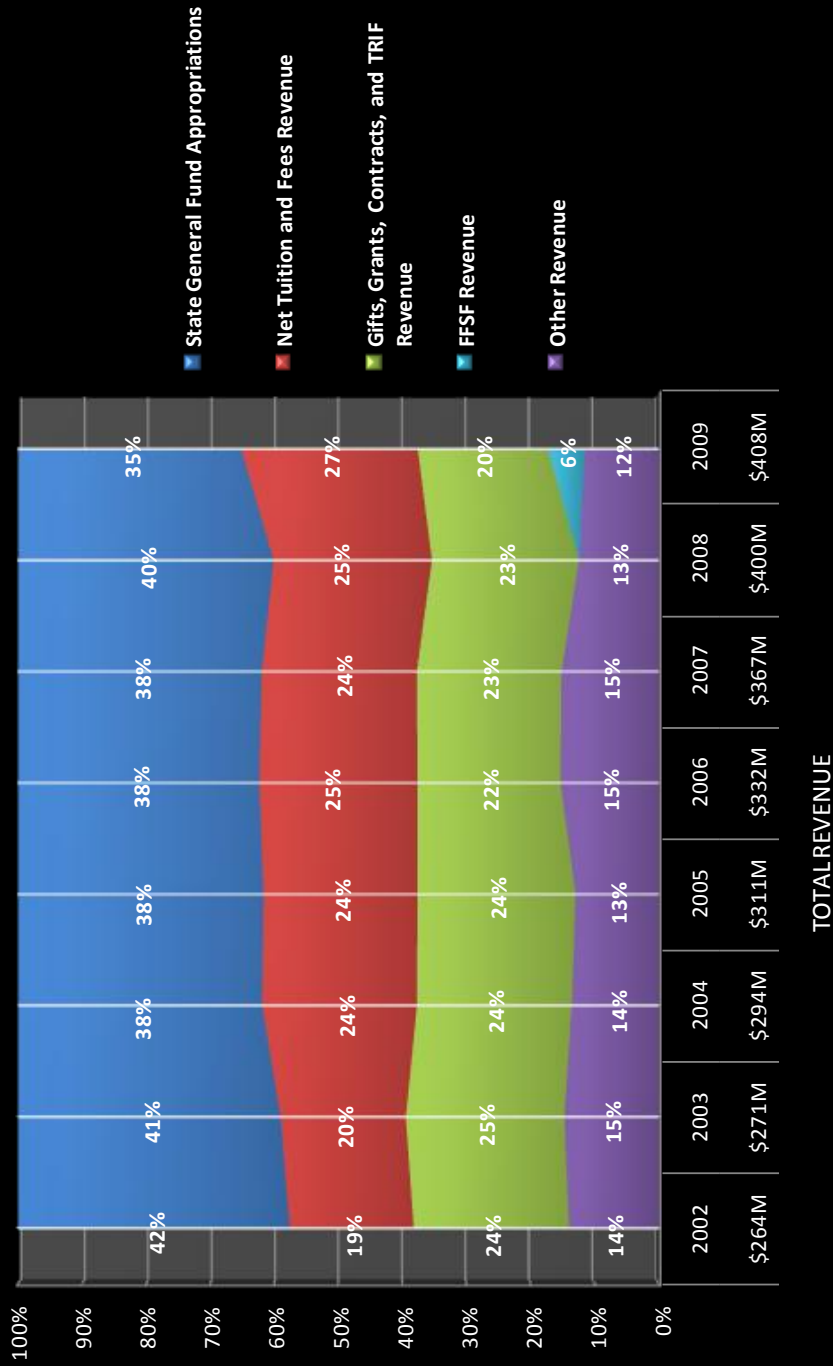
NORTHERN ARIZONA UNIVERSITY

Composition of University Total Revenue



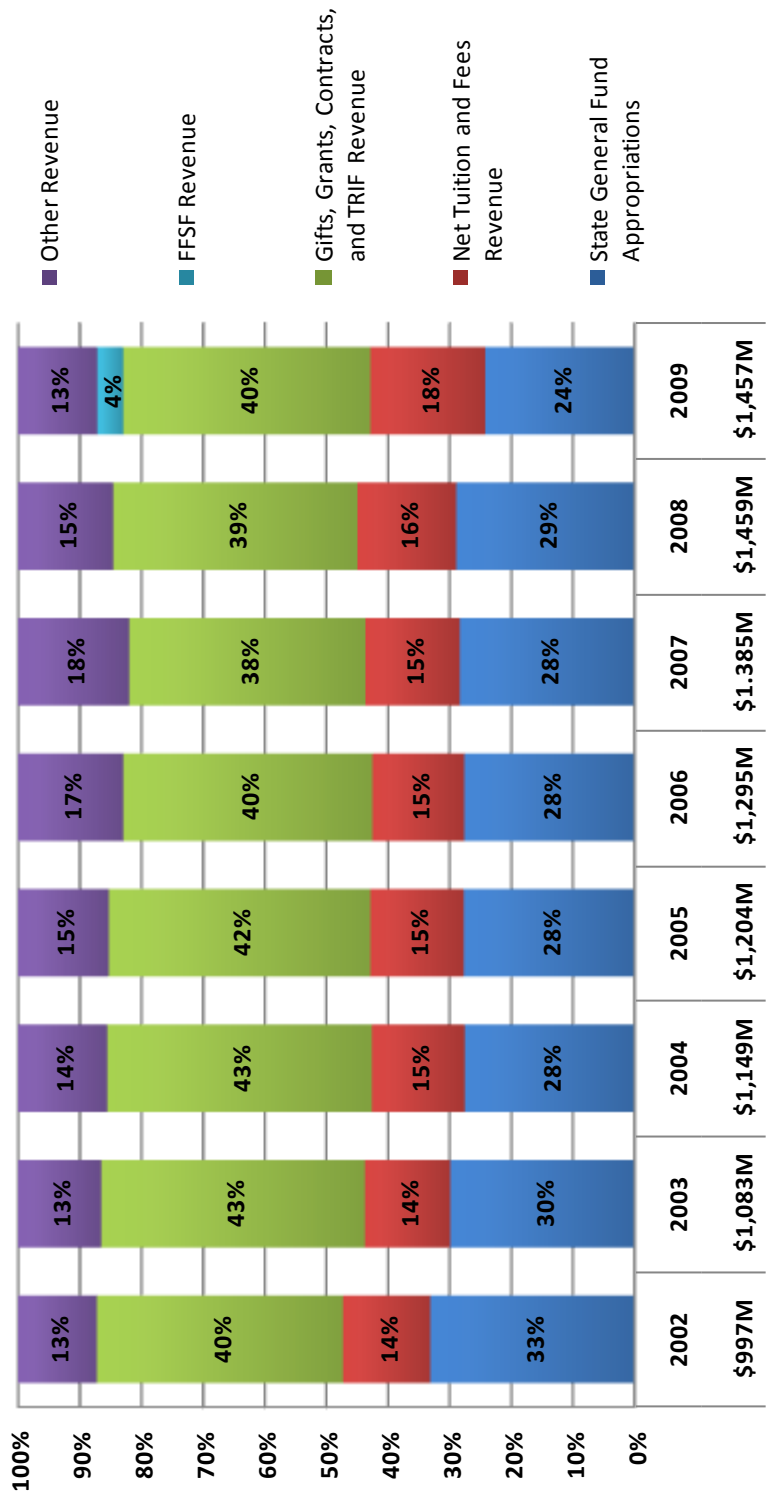
NORTHERN ARIZONA UNIVERSITY

Composition of University Total Revenue



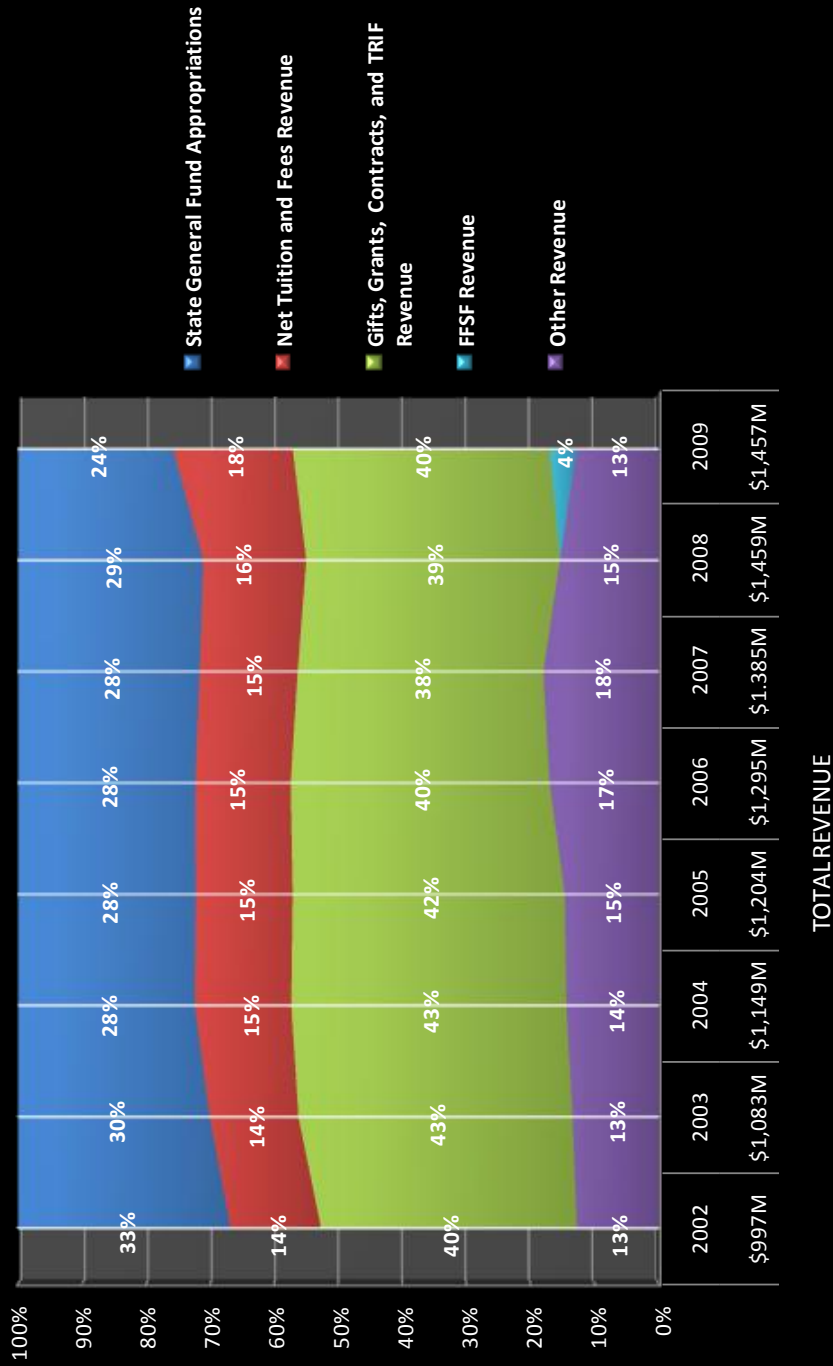
THE UNIVERSITY OF ARIZONA

Composition of University Total Revenue

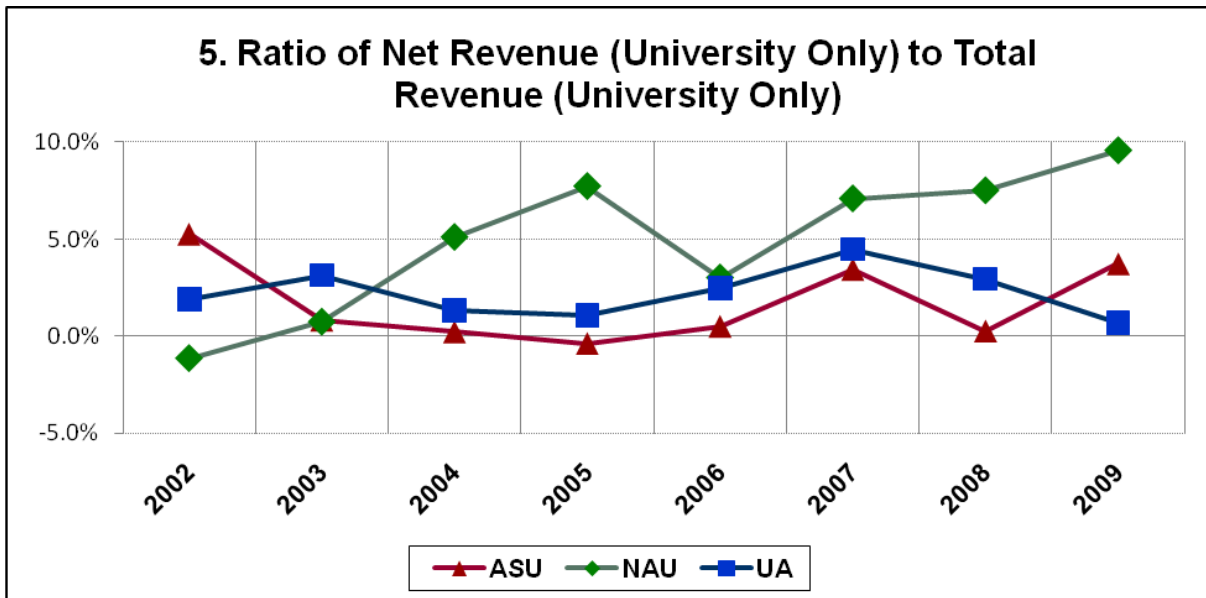


THE UNIVERSITY OF ARIZONA

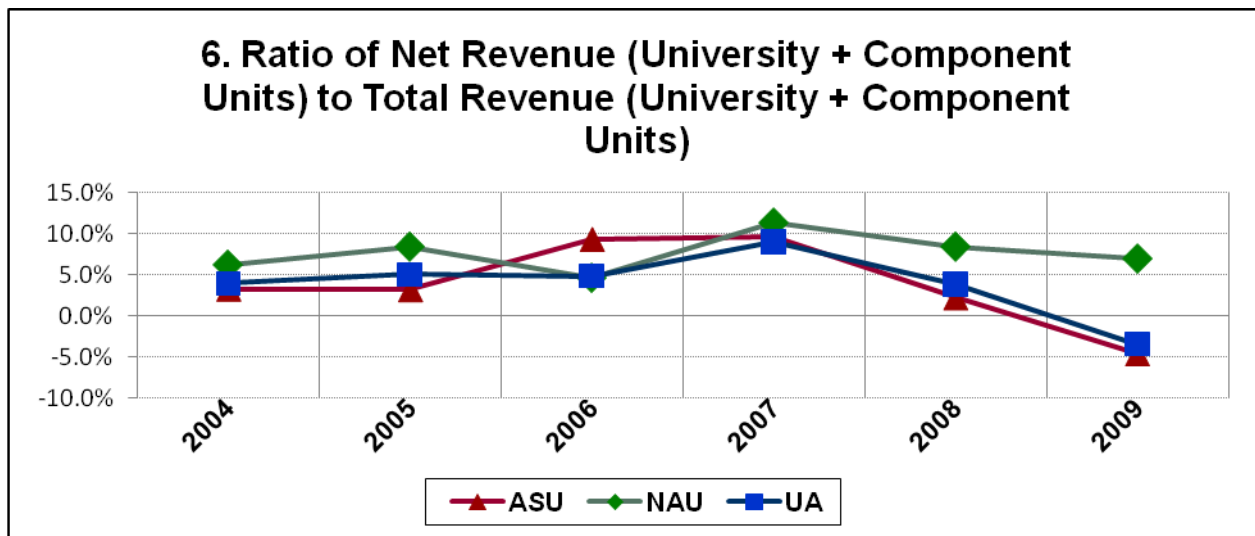
Composition of University Total Revenue



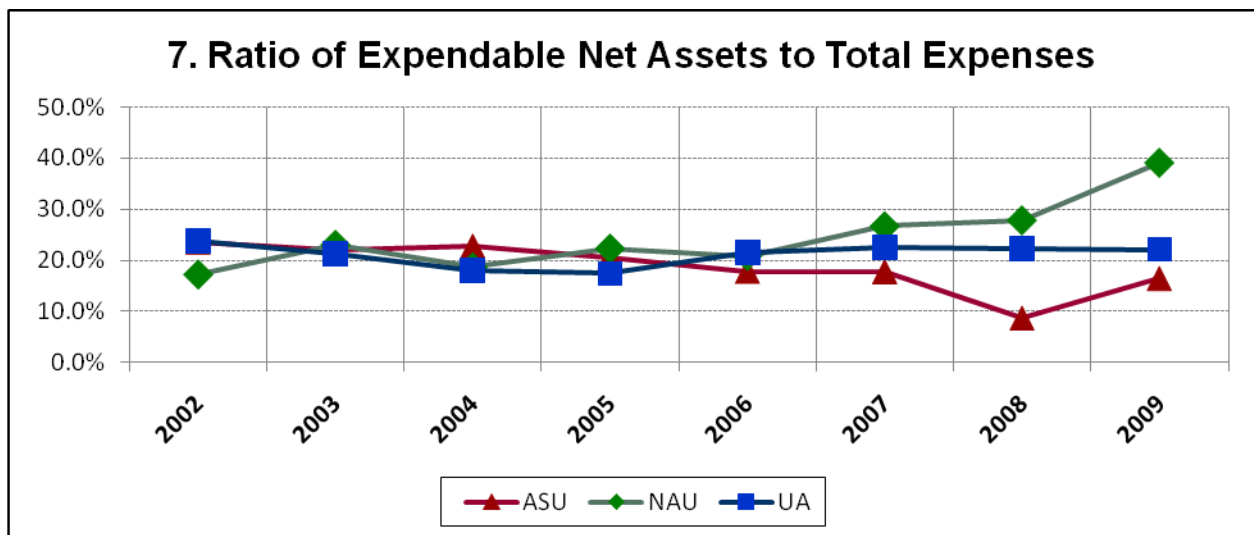
Ratio 5	Description of Ratio
<p data-bbox="167 268 406 405">Net Revenue (University Only) Total Revenue (University Only)</p> <p data-bbox="167 436 406 468">FY 2009 RATIOS</p> <p data-bbox="155 510 417 573">ASU 3.7% NAU 9.6% UA 0.7%</p>	<p data-bbox="440 268 1471 405"><i>Element definition:</i> Net Revenue equals total revenue less total expenses. Total Revenue includes operating, nonoperating, and other revenue and gains. Both figures are for the university only and do not include component units.</p> <p data-bbox="440 436 1471 537">This ratio indicates whether current year revenues were sufficient to cover current year expenses, thereby avoiding the need to deplete net assets to operate the university.</p> <p data-bbox="440 569 1471 905">This ratio has fluctuated over the 8-year reporting period at all three universities, but all three operated within their current year revenues in FY 2009. Without FY 2009 federal stimulus funds, both ASU and UA would have finished FY 2009 with negative ratios, indicating that current year revenues were not sufficient to cover current year expenses. ASU would have reported a negative \$12 million in Net Revenues while UA would have reported a negative \$51 million. Without federal stimulus funds, NAU would still have finished FY 2009 with positive Net Revenues of \$15.5 million, indicating increasing financial strength and flexibility that has been trending upward since FY 2006.</p> <p data-bbox="440 936 1471 1270">ASU's FY 2009 ratio increased to 3.7% from 0.3% in FY 2008, finishing FY 2009 with a \$57 million excess of Total Revenue (\$1.523 billion) over Total Expenses (\$1.466 billion). NAU's FY 2009 ratio increased to 9.6% from 7.5% in FY 2008, finishing the year with a \$39 million excess of Total Revenue (\$408 million) over Total Expenses (\$368 million). NAU continues to demonstrate its commitment to a balanced budget and to building reserves, a significant portion of which will be used to outfit and operate new research and other buildings. UA's FY 2009 ratio decreased to 0.7% from 3% in FY 2008, finishing FY 2009 with a \$10 million excess of Total Revenue (\$1.457 billion) over Total Expenses (\$1.447 billion).</p>



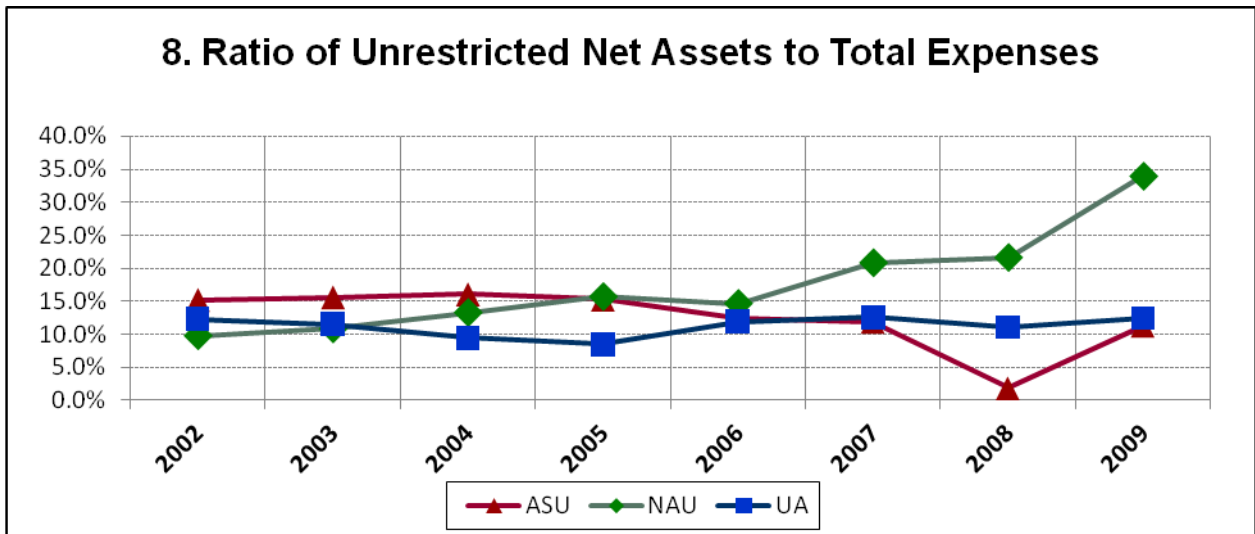
Ratio 6	Description of Ratio
<p data-bbox="159 268 407 470">Net Revenue (University + Component Units) Total Revenue (University + Component Units)</p> <p data-bbox="170 506 396 537"><u>FY 2009 RATIOS</u></p> <p data-bbox="151 579 418 642"><u>ASU</u> <u>NAU</u> <u>UA</u> -4.6% 7.0% -3.4%</p>	<p data-bbox="448 268 1474 470"><i>Element definition:</i> Net Revenue equals total revenue less total expenses. Total Revenue includes operating, nonoperating, and other revenue and gains. Both figures are for the university <u>and</u> its component units. Reporting of financial data for component units is required under GASB 39 beginning with FY 2004 financial statements. Each university's component units are listed on page 7.</p> <p data-bbox="448 506 1474 667">This ratio indicates whether current year revenues of the university and its component units as defined by GASB 14 and 39 were sufficient to cover current year expenses of the university and the component units, thereby avoiding the need to deplete net assets to operate the university and the component units.</p> <p data-bbox="448 705 1474 1104">This ratio decreased from prior year at all three universities, but ASU and UA suffered especially large decreases—moving into negative numbers—because their Foundations hold significantly larger endowment investments than does the NAU Foundation. ASU and its component units reported Net Revenues of -\$72 million, while UA and its component units reported -\$50 million. Noting the positive Net Revenues numbers in Ratio 5 for ASU and UA (university only), it is clear that the losses have occurred in the component units and result from the global economic collapse and the downturn in the financial markets that caused significant net losses on endowment investments. NAU and its component units combined reported positive Net Revenues of \$29 million, but that number also was dragged down by a loss of over \$4 million on Foundation endowment investments.</p> <p data-bbox="448 1142 1474 1241">Not surprisingly, in light of the economic downturn and the fact that Arizona is one of states hit hardest by the recession that began in December 2007, this ratio has trended downward at all three universities for the last two years.</p>



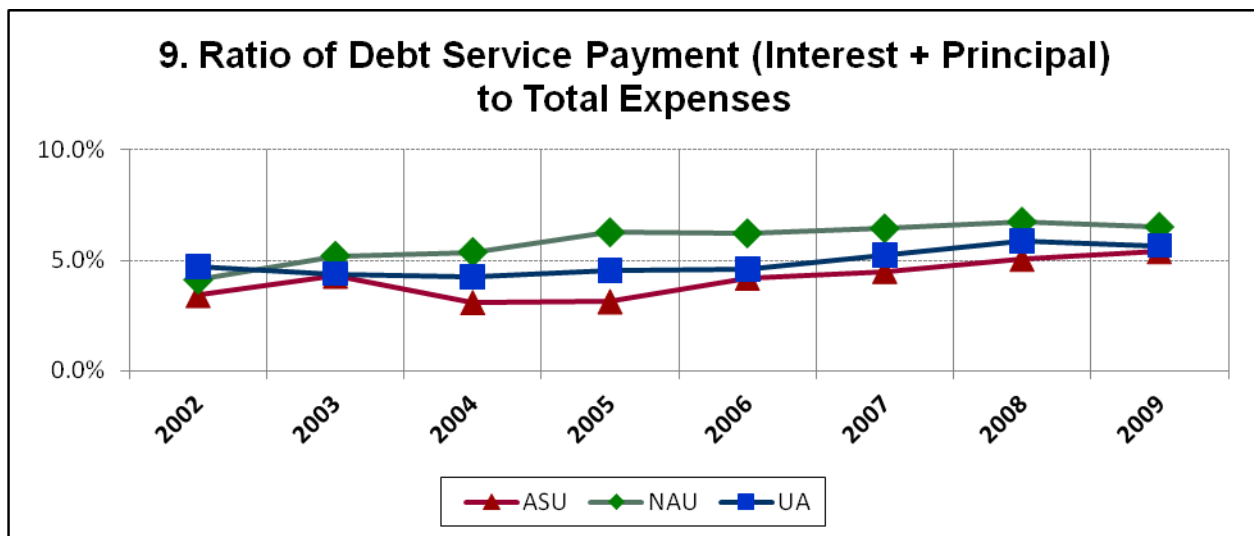
Ratio 7	Description of Ratio
<p data-bbox="175 268 396 369">Expendable Net Assets Total Expenses</p> <p data-bbox="175 405 396 436">FY 2009 RATIOS</p> <p data-bbox="159 478 412 541">ASU NAU UA 16% 39% 22%</p>	<p data-bbox="444 260 1468 426"><i>Element definition: Expendable Net Assets</i> are assets available for use for operations. They include both unrestricted and expendable restricted net assets; they exclude endowments and net assets invested in property. <i>Total Expenses</i> include operating, nonoperating, and other expenses and losses.</p> <p data-bbox="444 453 1468 583">This ratio measures whether or not expendable net assets have kept pace with total expenses and the financial strength of the universities by indicating the percentage of usable net assets at the end of the year to total expenses.</p> <p data-bbox="444 611 1468 877">ASU's ratio has remained relatively stable over the 8-year reporting period (adjusting FY 2008 for a reimbursement that occurred shortly after June 30, 2008). The 16% ratio would be 12% if the federal stimulus funds are removed. NAU's ratio of 39% (33% without stimulus funds) increased significantly over prior year, continuing an upward trend and an increasing ability to respond to emergencies or unforeseen needs. UA's ratio has remained relatively stable over the reporting period, with a reported 22% (18% without stimulus funds) in FY 2009.</p> <p data-bbox="444 911 1468 1108">Explained differently, at June 30, 2008, ASU had approximately 8.5 weeks (up from 5 weeks at prior year-end), but 6 weeks without federal stimulus funds, of annual spending available from year-end expendable net assets. NAU reported 20 weeks (up from 14 at prior year-end), but 17 weeks without stimulus funds. UA had approximately 11.5 weeks (down slightly from 12 weeks at prior year-end), but 9 weeks without stimulus funds.</p> <p data-bbox="444 1140 1468 1232">This ratio, as is the case for all ratios in this analysis, is valid as of June 30, 2009, only. The universities are "going concerns" and, therefore, can expect to receive additional revenues in subsequent years.</p>



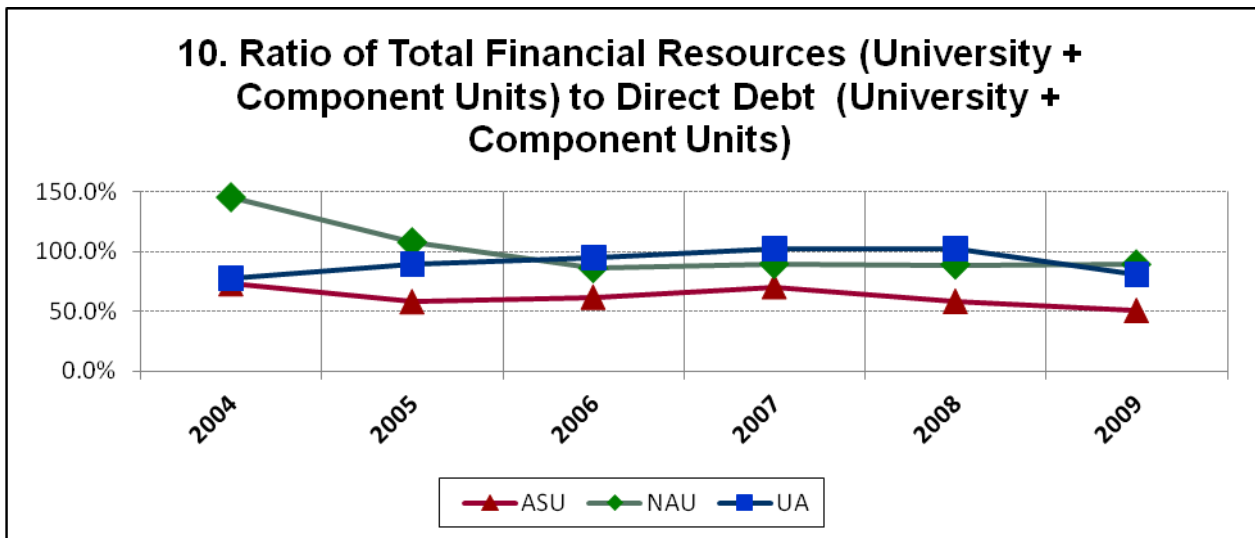
Ratio 8	Description of Ratio						
<p data-bbox="175 268 402 369">Unrestricted Net Assets Total Expenses</p> <p data-bbox="175 405 402 436">FY 2009 RATIOS</p> <table data-bbox="159 478 412 546"> <tr> <td><u>ASU</u></td> <td><u>NAU</u></td> <td><u>UA</u></td> </tr> <tr> <td>11%</td> <td>34%</td> <td>12%</td> </tr> </table>	<u>ASU</u>	<u>NAU</u>	<u>UA</u>	11%	34%	12%	<p data-bbox="444 268 1468 405"><i>Element definition: Unrestricted Net Assets</i> are a subset of expendable net assets (see Ratio 7) and represent those net assets that can most quickly be converted to cash. <i>Total Expenses</i> include operating, nonoperating, and other expenses and losses.</p> <p data-bbox="444 436 1468 573">This ratio measures the coverage of annual operations by the university's most liquid assets, those unrestricted net assets than can be the most quickly converted to cash. A higher percentage indicates more operating flexibility by the university.</p> <p data-bbox="444 604 1468 835">ASU's ratio of 11% (6 weeks spending coverage) remains within a relatively stable range of 11%-16% over the 8-year period (adjusting for anomaly in FY 2008 ratio). NAU's FY 2009 ratio of 34% (18 weeks spending coverage) continues an 8-year upward trend from 10% in FY 2002 to 34% in FY 2009, indicating continued increasing operating flexibility. UA's ratio of 12% (6 weeks spending coverage) remains within a relatively stable range of 8%-13% over the 8-year period.</p> <p data-bbox="444 867 1468 966">This ratio, as is the case for all ratios in this analysis, is valid as of June 30, 2009, only. The universities are "going concerns" and, therefore, can expect to receive additional revenues in subsequent years.</p>
<u>ASU</u>	<u>NAU</u>	<u>UA</u>					
11%	34%	12%					



Ratio 9	Description of Ratio						
<p data-bbox="191 268 396 436">Debt Service Payments (Interest + Principal) Total Expenses</p> <p data-bbox="168 470 402 506">FY 2009 RATIOS</p> <table data-bbox="152 541 418 611"> <tr> <td><u>ASU</u></td> <td><u>NAU</u></td> <td><u>UA</u></td> </tr> <tr> <td>5.4%</td> <td>6.5%</td> <td>5.7%</td> </tr> </table>	<u>ASU</u>	<u>NAU</u>	<u>UA</u>	5.4%	6.5%	5.7%	<p data-bbox="440 268 1471 405">Element definition: <i>Debt Service Payments</i> include the interest and principal payments for the university's System Revenue Bonds (SRBs) and Certificates of Participation (COPs). <i>Total Expenses</i> include operating, nonoperating, and other expenses and losses.</p> <p data-bbox="440 436 1471 636">This ratio measures the burden of debt service payments relative to, or as a proportion of, overall expenses of the university. This is one of the key ratios considered by rating agencies to determine ratings for SRBs and COPs. Rating agencies generally view 10% or less as a significant indicator of satisfactory creditworthiness, thus allowing debt instruments to be sold at more favorable interest rates.</p> <p data-bbox="440 667 1471 1035">At June 30, 2009, all three universities are well within the acceptable debt ratio range and demonstrate that they have adequate resources to meet existing debt requirements. Moody's and Standard & Poor's bond ratings and outlooks remain unchanged from prior year-end for all three universities with the exception that in July 2009 Moody's edged NAU down to stable from positive, the same outlook as is held by ASU and UA. As discussed earlier, in light of its December 23, 2009, downgrading of the state of Arizona's issuer rating one notch, Moody's issued a Special Comment on January 5, 2010, cautioning, "We will also continue to monitor these universities' (ASU, NAU, UA) abilities to maintain balance sheet strength, with significant borrowing absent growth of financial resources and cash flow a possible contributor to rating pressure."</p> <p data-bbox="440 1066 1471 1297">ASU's FY 2009 debt ratio of 5.4% increased slightly over its 5.0% ratio the prior year largely due to the state-funded research infrastructure debt service payments. ASU's debt ratio remained in the 3-5% range during this 8-year reporting period. NAU's FY 2009 debt ratio of 6.5% decreased slightly from its 6.8% ratio at prior year-end and remained in the 4-6% range. UA's FY 2009 debt ratio of 5.7% decreased slightly from its 5.9% at prior year-end and remained in the 4-6% range over the 8-year reporting period.</p>
<u>ASU</u>	<u>NAU</u>	<u>UA</u>					
5.4%	6.5%	5.7%					



Ratio 10	Description of Ratio						
<p data-bbox="162 268 415 506">Total Financial Resources (University + Component Units) Direct Debt (University + Component Units)</p> <p data-bbox="162 535 415 573"><u>FY 2009 RATIOS</u></p> <table data-bbox="159 611 415 678"> <tr> <td><u>ASU</u></td> <td><u>NAU</u></td> <td><u>UA</u></td> </tr> <tr> <td>51%</td> <td>89%</td> <td>81%</td> </tr> </table>	<u>ASU</u>	<u>NAU</u>	<u>UA</u>	51%	89%	81%	<p data-bbox="448 268 1468 535">Element definition: <i>Total Financial Resources</i> include restricted and unrestricted expendable and nonexpendable net assets of the university, plus permanently and temporarily restricted and unrestricted net assets of the component units, excluding net property and equipment of the component units. <i>Direct Debt</i> is the total outstanding capital debt of the university and its component units. Reporting of financial data for component units is required under GASB 39 beginning with FY 2004 financial statements.</p> <p data-bbox="448 554 1468 688">This ratio measures coverage of debt by all resources available to the university, including those of its component units. A larger percentage indicates the availability of more resources to cover total university and component unit debt.</p> <p data-bbox="448 707 1468 974">ASU's ratio of 51%, although down from 58% at prior year-end, reflects the ability of ASU and its component units to repay all outstanding debt without undue financial hardship. NAU's ratio of 89% has remained stable for 4 years and reflects the ability of NAU and its component units to repay all outstanding debt without undue financial hardship. UA's FY 2009 ratio of 81%, although down from 102% in the 2 prior years, also reflects the ability of UA and its component units to repay all outstanding debt without undue financial hardship.</p> <p data-bbox="448 993 1468 1089">Explained differently, at June 30, 2009, ASU had sufficient financial resources to pay 51% of the total debt of the university and component units; NAU, 89%; and UA, 81%.</p> <p data-bbox="448 1108 1468 1243">This ratio, as is the case for all ratios in this analysis, is valid as of June 30, 2009, only. The universities are "going concerns" and, therefore, payment of the total direct debt is not required as of June 30, 2009, but will be paid off over time.</p>
<u>ASU</u>	<u>NAU</u>	<u>UA</u>					
51%	89%	81%					



FINANCIAL RATIO FORMULAS

Ratio 1 ASU only	State general fund appropriations Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 2 ASU only	Tuition and Fees, net of scholarship allowance Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 3 ASU only	Gifts, additions to endowments, grants, contracts, and state sales tax share (technology and research initiatives funding)- (Operating/Nonoperating/Capital) Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 4 ASU only	Auxiliary enterprises revenues, investment income, and all other revenues (operating and nonoperating) not in the other revenue categories. Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 5 ASU only	Net revenues (Total revenues less total expenses) Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 6 ASU and component units	Net revenues (Total revenues less total expenses) Total Revenue (Operating/Nonoperating/Other Revenues and Gains)
Ratio 7 ASU only	Expendable Net Assets (Unrestricted and expendable restricted net assets) Total Expenses (operating, nonoperating and other expenses and losses)
Ratio 8 ASU only	Unrestricted net assets Total Expenses (operating, nonoperating and other expenses and losses)
Ratio 9 ASU and component units	Debt service payments (interest payments per SRECNA and principal payments per cash flow) Total Expenses (operating, nonoperating and other expenses and losses)
Ratio 10	Total financial resources (unrestricted and restricted - expendable and nonexpendable - net assets of the Univ, plus permanently and temporarily restricted and unrestricted net assets of the component units) Total direct debt (total outstanding capital debt of the Univ and component units, excluding the University's capital leases.

Note: all ASU capital leases have related debt included in the total debt of the component units, and therefore are not included in the Total direct debt.

ARIZONA STATE UNIVERSITY
Financial Ratios for Fiscal Years: 2002 to 2009
(dollars in millions)

Ratio	2002	2003	2004	2005	2006	2007	2008	2009
1 <u>State General Fund Appropriations</u>	321	312	313	336	369	430	483	417
Total Revenues	833	846	935	1,044	1,172	1,358	1,471	1,523
ASU only. Fiscal 2007 includes \$7 million in building renewal (capital) appropriations. Fiscal 2008 and 2009 includes \$14 million in research infrastructure debt service funding.	38.5%	36.9%	33.5%	32.2%	31.5%	31.7%	32.8%	27.4%
2 <u>Net Tuition and Fees Revenue</u>	188	206	253	302	349	400	437	499
Total Revenues	833	846	935	1,044	1,172	1,358	1,471	1,523
ASU only	22.6%	24.3%	27.1%	28.9%	29.8%	29.5%	29.7%	32.8%
3 <u>Gifts, Grants & Contracts, FFSF, and TRIF Revenue</u>	212	206	219	254	279	299	320	419
Total Revenues	833	846	935	1,044	1,172	1,358	1,471	1,523
ASU only. FFSF - Federal Fiscal Stabilization Funds TRIF - Technology & initiative research fund. ASU's share of the state education sales tax.	25.5%	24.3%	23.4%	24.3%	23.8%	22.0%	21.8%	27.5%
4 <u>Other Revenues</u>	112	122	150	152	175	229	231	188
Total Revenues	833	846	935	1,044	1,172	1,358	1,471	1,523
ASU only	13.4%	14.5%	16.0%	14.6%	14.9%	16.8%	15.7%	12.3%
5 <u>Net Revenues</u>	44	7	2	(4)	6	47	4	57
Total Revenues	833	846	935	1,044	1,172	1,358	1,471	1,523
ASU only	5.3%	0.8%	0.2%	-0.4%	0.5%	3.5%	0.3%	3.7%
6 <u>Net Revenues</u>			34	38	131	153	37	(72)
Total Revenues			1,036	1,182	1,400	1,602	1,663	1,559
ASU and component units			3.3%	3.2%	9.4%	9.6%	2.2%	-4.6%
7 <u>Expendable Net Assets</u>	186	184	213	216	208	233	127	241
Total Expenses	789	839	934	1,049	1,166	1,311	1,467	1,466
ASU only	23.6%	21.9%	22.8%	20.6%	17.8%	17.8%	8.7%	16.4%
8 <u>Unrestricted net assets</u>	120	131	150	160	145	156	27	166
Total expenses	789	839	934	1,049	1,166	1,311	1,467	1,466
ASU only	15.2%	15.6%	16.1%	15.3%	12.4%	11.9%	1.8%	11.3%
9 <u>Debt Service Payments (int & princ)</u>	27	36	29	33	49	59	74	79
Total Expenses	789	839	934	1,049	1,166	1,311	1,467	1,466
ASU only	3.4%	4.3%	3.1%	3.1%	4.2%	4.5%	5.0%	5.4%
10 <u>Total financial resources , net</u>			545	593	716	854	761	749
Direct debt			749	1,023	1,160	1,213	1,305	1,478
ASU and component units			72.8%	58.0%	61.7%	70.4%	58.3%	50.7%

NORTHERN ARIZONA UNIVERSITY
Financial Ratios for Fiscal Years: 2002 to 2009
(dollars in millions)

Ratio	2002	2003	2004	2005	2006	2007	2008	2009
1 <u>State General Fund Appropriations</u>	112	111	112	118	125	140	160	142
Total Revenues	264	271	294	311	332	367	400	408
NAU only. Fiscal 2008 includes \$5.9 million in research infrastructure debt appropriations.	42.4%	41.0%	38.1%	37.9%	37.7%	38.1%	40.0%	34.7%
2 <u>Net Tuition and Fees Revenue</u>	51	53	71	74	82	89	99	112
Total Revenues	264	271	294	311	332	367	400	408
NAU only	19.3%	19.6%	24.1%	23.8%	24.7%	24.3%	24.8%	27.5%
3 <u>Gifts, Grants & Contracts, and TRIF Revenue</u>	64	67	71	76	74	83	92	106
Total Revenues	264	271	294	311	332	367	400	408
NAU only	24.2%	24.8%	24.1%	24.4%	22.3%	22.6%	23.0%	26.1%
TRIF - Technology & Research Initiative Fund. NAU's share of the state education sales tax.								
4 <u>Other Revenues</u>	37	40	40	40	51	56	50	47
Total Revenues	264	271	294	311	332	367	400	408
NAU only	14.0%	14.8%	13.6%	12.9%	15.4%	15.3%	12.5%	11.5%
5 <u>Net Revenues</u>	(3)	2	15	24	10	26	30	39
Total Revenues	264	271	294	311	332	367	400	408
NAU only	-1.1%	0.7%	5.1%	7.7%	3.0%	7.1%	7.5%	9.6%
6 <u>Net Revenues</u>			19	28	16	47	35	29
Total Revenues			305	333	344	416	416	416
NAU and component units			6.2%	8.4%	4.7%	11.3%	8.4%	7.0%
7 <u>Expendable Net Assets</u>	46	62	52	64	67	91	103	144
Total Expenses	267	269	279	287	321	341	370	368
NAU only	17.2%	23.0%	18.6%	22.3%	20.9%	26.7%	27.8%	39.1%
8 <u>Unrestricted net assets</u>	26	29	37	45	47	71	80	125
Total expenses	267	269	279	287	321	341	370	368
NAU only	9.7%	10.8%	13.3%	15.7%	14.6%	20.8%	21.6%	34.0%
9 <u>Debt Service Payments (int & princ)</u>	11	14	15	18	20	22	25	24
Total Expenses	267	269	279	287	321	341	370	368
NAU only	4.1%	5.2%	5.4%	6.3%	6.2%	6.5%	6.8%	6.5%
10 <u>Total financial resources , net</u>			209	233	236	267	303	332
Direct debt			144	217	276	300	342	374
NAU and component units			145.1%	107.4%	85.5%	89.0%	88.6%	88.8%

THE UNIVERSITY OF ARIZONA
Financial Ratios for Fiscal Years: 2002 to 2009
(dollars in millions)

	Ratio	2002	2003	2004	2005	2006	2007	2008	2009
1	State General Fund Appropriations	329	324	317	334	358	390	417	349
	Total Revenues	997	1,083	1,149	1,204	1,295	1,385	1459	1457
	UA only	33.0%	29.9%	27.6%	27.7%	27.6%	28.2%	28.6%	24.0%
2	Net Tuition and Fees Revenue	140	150	173	182	193	210	232	269
	Total Revenues	997	1,083	1,149	1,204	1,295	1,385	1459	1457
	UA only	14.0%	13.9%	15.1%	15.1%	14.9%	15.2%	15.9%	18.5%
3	Gifts, Grants & Contracts, and TRIF Revenue	396	463	493	511	523	527	571	639
	Total Revenues	997	1,083	1,149	1,204	1,295	1,385	1459	1457
	UA only	39.7%	42.8%	42.9%	42.4%	40.4%	38.1%	39.1%	43.9%
	TRIF - Technology & initiative research funding. UA's share of the state education sales tax.								
4	Other Revenues	127	146	166	177	221	248	223	185
	Total Revenues	997	1,083	1,149	1,204	1,295	1,385	1459	1457
	UA only	12.7%	13.5%	14.4%	14.7%	17.1%	17.9%	15.3%	12.7%
5	Net Revenues	19	34	15	13	32	62	43	10
	Total Revenues	997	1,083	1,149	1,204	1,295	1,385	1459	1,457
	UA only	1.9%	3.1%	1.3%	1.1%	2.5%	4.5%	2.9%	0.7%
6	Net Revenues			49	66	63	124	61	-50
	Total Revenues			1,244	1,311	1,295	1,385	1564	1472
	UA and component units			3.9%	5.0%	4.9%	8.0%	3.9%	-3.4%
7	Expendable Net Assets	232	222	204	207	272	299	316	320
	Total Expenses	978	1,049	1,134	1,190	1,262	1,323	1416	1447
	UA only	23.7%	21.2%	18.0%	17.4%	21.6%	22.6%	22.3%	22.1%
8	Unrestricted net assets	120	121	107	101	150	166	157	180
	Total expenses	978	1,049	1,134	1,190	1,262	1,323	1416	1447
	UA only	12.3%	11.5%	9.4%	8.5%	11.9%	12.5%	11.1%	12.4%
9	Debt Service Payments (int & princ)	46	46	48	54	58	69	83	82
	Total Expenses	978	1,049	1,134	1,190	1,262	1,323	1416	1,447
	UA only	4.7%	4.4%	4.2%	4.5%	4.6%	5.2%	5.9%	5.7%
10	Total financial resources , net			628	707	806	896	907	851
	Direct debt			808	789	854	878	886	1057
	UA and component units			77.7%	89.6%	94.4%	102.1%	102.4%	80.5%

SPECIAL COMMENT

 Table of Contents:

INTRODUCTION	1
MOODY'S RELATED RESEARCH	3

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No Immediate Rating Actions Taken on Arizona Public Universities in Conjunction with Downgrade of State Rating; Pressure on State Funding Remains a Challenge

 Introduction

Moody's maintains ratings on three public universities in Arizona—University of Arizona (rated Aa3), Arizona State University (Aa3) and Northern Arizona University (A2). On December 23, Moody's lowered the state of Arizona's issuer rating one notch from Aa3 to A1 and maintained the negative outlook. Moody's has not immediately taken rating action on any of the rated four-year public universities following downgrade of the state's rating. However, we believe that the state's economic and financial difficulties will create both near and longer-term challenges for the public higher education system and the university ratings could face pressure in the near-term, especially if funding delays from the state extend well into the spring and operating cash balances tighten.

Moody's decision to not immediately take rating action following downgrade of the state is largely due to a variety of university credit strengths that are independent of the state's budget situation. These universities generally have diverse revenue bases and histories of positive operating performance, healthy market positions and tuition setting flexibility, and adequate cash balances to cushion a short-term delay in receipt of state funding.

The recent downgrade of the state's issuer rating reflects Arizona's ongoing economic and financial deterioration, leading to significant revenue underperformance, a sizeable budget gap (\$1.5 billion in FY 2010 or 24% of general fund recurring revenues), and tightened liquidity, requiring internal and external borrowing for cash flow. Arizona's economy has slowed significantly reflecting considerable weakening in the housing sector. For more information on the state's credit profile, please read our report published on the state on December 23, 2009.

Although the Arizona public universities have diverse revenue bases, they do receive a sizeable amount of funding from the state in support of annual operations. In FY 2009, state appropriations represented approximately 30% of University of Arizona's operating revenue, 34% for Arizona State University, and 41% for Northern Arizona University. Although the state implemented cuts in appropriations to the three universities in FY 2009, state funding amounts may be protected in FY 2010 as a result of federal stimulus funding helping to compensate for cuts that otherwise would have been made. These universities will face the longer term challenge of balancing their budgets if state funding declines when federal stimulus funding comes to an end.

Near-term the universities may have to wrestle with temporary funding delays due to the state's cash flow challenges. According to university management, state general fund appropriations to the three public universities for the month of December have been delayed and timing of their receipt is uncertain. Moody's has been in contact with all three universities, and we believe that all three have adequate cash balances to cushion this particular funding delay. Further, the universities expect to receive spring semester tuition payments over the next few weeks helping to bolster cash balances. However, a longer term pattern of multiple months of state funding delays could create liquidity concerns. We will continue to monitor the state's timely provision of general fund appropriations to the universities and the impact of any delays on university operating cash balances.

As the state faces significant economic challenges, Moody's believes that the Arizona public universities will be required to grow alternative revenue streams, including net tuition revenue and fundraising. Our decision to not take rating action at this point in time heavily rests on our belief that the universities have healthy student market positions and tuition setting flexibility which could help offset future pressure on state funding. All three have large enrollment bases and have demonstrated steady growth of net tuition per student over the past five years. Further, University of Arizona and Arizona State University draw a meaningful proportion of their student bodies from outside of Arizona with out-of-state tuition comprising an important piece of the revenue base. The universities do not currently have any state-mandated limitations on tuition increases, and we believe they have moderate flexibility to implement tuition increases in coming semesters.

We will also continue to monitor these universities' abilities to maintain balance sheet strength, with significant borrowing absent growth of financial resources and cash flow a possible contributor to rating pressure. The Arizona public universities have a shorter history of fundraising for endowment, and balance sheet resources are thin compared to medians for similar-sized institutions. Further, the state provides modest levels of capital support and the public universities have significantly ramped up borrowing levels in order to fund capital investment. As a result, capital ratios for these three universities are relatively weak for their rating categories. An inability to grow revenue to support debt service and bolster their financial resource bases to better support growing debt levels could contribute to rating pressure.

Moody's also maintains ratings on revenue bonds issued by three Arizona community colleges—Pinal County (revenue bond rating of A3), Maricopa County (Aa2), and Cochise County (A3) Community Colleges. These community college districts rely on state appropriations for a much smaller proportion of their revenue bases and are more heavily dependent on tax revenues which could also be pressured in the medium term.

In conclusion, although we have chosen not to immediately take rating action on Arizona State University, University of Arizona, or Northern Arizona University in conjunction with the state's rating downgrade, we believe that the state's economic challenges could have a meaningful trickle-down effect to the public universities both near and longer-term. Although we believe the universities have adequate cash balances to buffer against a short-term delay in state funding for operations, longer-term delays or ongoing major cuts in funding and an increased pace of borrowing could pressure the Arizona public universities' credit profiles over the next few years.

Moody's Rated Arizona Public Universities

	UNIVERSITY OF ARIZONA (FY 2009)	ARIZONA STATE UNIVERSITY (FY 2009)	NORTHERN ARIZONA UNIVERSITY (FY 2009)
Operating Revenue	\$1.4 B	\$1.4 B	\$390 M
Total Financial Resources (including foundations and other component units)	\$863 M	\$748 M	\$231 M
Pro-Forma Direct Debt Outstanding (FY 2009 plus debt issued during FY 2010 to-date)	\$1.04 B	\$1.5 B	\$504 M
Three-Year Average Operating Margin	1.2%	1.2%	5.6%
Reliance on State Funding (including federal fiscal stabilization funds)	30%	34%	41%

Moody's Related Research

- » [Public University Governance Faces New Challenges as U.S. Public Higher Education Becomes Increasingly Market-Driven \(105943\)](#)
- » [Moody's Fiscal Year 2008 Public College and University Medians \(119172\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

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