

Higher Education
New Issue

Wartburg College, Iowa

Iowa Higher Education Loan Authority

Ratings

New Issues

Iowa Higher Education Loan Authority
Private College Facility Revenue
Bonds (Wartburg College Project)
\$50,490,000 Refunding
Series 2005A BBB-
\$35,285,000 Series 2005B NR

Outstanding Debt

Iowa Higher Education Loan Authority
Private College Facility Revenue
Bonds (Wartburg College Project)
\$50,000,000 Refunding Series 2002* .. BBB-
\$963,647 Various Loans NR

Rating Outlook Stable

*To be refunded with the issuance of the series 2005A bonds. NR – Not rated.

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Profile

Type: Private, four-year college

Location: Waverly, IA

Use of Proceeds: Series 2005A bond proceeds will be used to refund the outstanding series 2002 bonds. Series 2005B bond proceeds will be used to construct a wellness center, fund capitalized interest, and pay costs of issuance.

Sale Information: Bonds are scheduled to sell on or about Dec. 13 through negotiation by Griffin, Kubik, Stephens & Thompson, Inc.

■ Outlook

The 'BBB-' rating and Stable Outlook are supported by Wartburg College's (Wartburg, or the college) increasing enrollment, demonstrated history of consistent fundraising, and liquidity levels appropriate for the rating level. Fitch Ratings expects enrollment to continue to grow, which should provide additional opportunities for fundraising prospects.

■ Rating Considerations

Fall 2005 headcount enrollment was 1,811, up 13.2% since fall 2000. The college has maintained a moderate level of liquidity, with fiscal 2005 unrestricted and temporarily restricted cash and investments of \$23.8 million. For fiscal 2005, the liquidity level would cover 64.3% of the year's operating expenses. The Fitch median for colleges rated in the 'BBB' category is 40%. Maintenance of liquidity levels is due partially to annual fundraising, which has been consistent over the past six years, and nearing completion of an \$88 million capital campaign.

Credit concerns include negative operating margins for three of the last six years and a high debt burden. The primary revenue source for the college, representing 83.7% of fiscal 2005 revenue, is student-generated revenue, which includes tuition, fee, and auxiliary revenues. Annual tuition and fees for fall 2005 was \$21,130. While tuition and fee revenue has increased each year for the past six years, the operating margins have been negative for three of those years. The operating margin for fiscal 2005 was (8.7%). Fitch does not include unrealized investment gains/losses or assets released from restriction for capital improvements in its calculation of operating margin. The operating margin has been negatively affected by the increase in depreciation for two new buildings and higher interest expense on the outstanding series 2002 bonds. Prior to fiscal 2005, the interest was capitalized. The college expects operating expenses to stabilize and revenues to continue to rise with enrollment growth and fundraising.

Wartburg's existing debt burden is high. For fiscal 2005, debt service consumed 8.7% of unrestricted revenues. The debt burden is above the Fitch 'BBB' median of 4.9%. Debt service on the series 2005B bonds, which is to be paid from Wellness Center revenues, is expected to be at least break even. After the issuance of the series 2005A and 2005B bonds (collectively, the 2005 bonds), the college has no plans for any additional debt in the near term.

■ Strengths

- Liquidity consistent with other private universities rated in the 'BBB' category.
- Demonstrated history of fundraising.
- Financial support from the community for the Wellness Center.

■ Risks

- High debt burden.
- Negative operating margins for three of the last six years.
- Lack of revenue diversity.

■ New Issue Details

The 2005 bonds will be issued by the Iowa Higher Education Loan Authority (the authority). The bonds will be issued pursuant to an indenture of trust agreement dated Dec. 1, 2005 between the authority and Wells Fargo Bank, N.A. (based in Des Moines, IA). The authority will loan the proceeds to Wartburg as specified in a loan agreement dated Dec. 1, 2005.

The college's loan payments to the trustee will equal the annual debt service on the 2005 bonds. The loan payments are a general obligation of Wartburg. In addition, for the series 2005A bonds, Wartburg will grant to the authority a first lien mortgage on certain real property of the college, excluding the Wellness Center, and a second lien on the Wellness Center. For the series 2005B bonds, Wartburg will grant to the authority a first lien mortgage on the Wellness Center and a second lien on certain real property of the college. Both series of bonds will be secured by a reserve fund.

The series 2005A bonds will be repaid from available revenues of the college. The series 2005B bonds will be repaid from revenues generated by the Wellness Center, primarily community membership fees and city contributions. Revenues of the college are also available if payments on the series 2005A bonds have been made.

The bonds are expected to sell on or about Dec. 13 through negotiation by Griffin, Kubik, Stephens & Thompson, Inc. The series 2005A bond proceeds will be used to refund the outstanding series 2002 bonds. The series 2005B bonds will be used to construct a Wellness Center, fund capitalized interest and a reserve fund, and pay costs of issuance.

The series 2005 tax-exempt fixed-rate bonds are expected to have a final maturity in fiscal 2038. Projected debt service on the series 2005A bonds is relatively flat at \$3.1 million. Projected debt service on the series 2005B bonds increases from \$949,573 in fiscal 2008 to \$1.9 million in fiscal 2009, gradually rising to \$2.96 million in fiscal 2024 but remaining flat through fiscal 2038.

The college covenants to generate net income available for debt service at a level sufficient to cover 1.1 times (x) annual debt service or for total cash and investments to debt to be equal to or greater than 0.75x. If both ratios are below their required levels for any fiscal year, the college must employ an independent consultant.

For additional debt to be issued, historical pro forma debt service coverage for the two most recently ended fiscal years must not be less than 1.1x or, if historical debt service coverage (not including pro forma debt) was not less than 1.1x, one of the two following reports must be received: a consultant report stating that the projected debt service coverage ratio for each of the first three years following completion of the new project will not be less than 1.25x after giving effect to the incurrence of such additional debt and additional net revenues; or a certificate or a report from the chief financial officer of the college that debt service coverage would be at least 1.4x on a pro forma basis.

■ Wellness Center

The series 2005B bond proceeds will be used to construct a Wellness Center of approximately 200,000 square feet. The Wellness Center will be used by both Wartburg students and the local community, primarily residents of the city of Waverly. The Wellness Center will include gymnasiums, an arena, running tracks, a pool, exercise rooms, racquetball courts, and classrooms. The Wellness Center is expected to open in fall 2007.

Revenues generated by community membership fees and contributions from Waverly are pledged to repayment of the debt. The largest revenue source is expected to be community membership fees. Community membership fees will be \$600 per year and are expected to generate net revenues of \$1.145 million in fiscal 2008. The first full year of operations will be fiscal 2009. To generate the \$1.145 million in revenues, approximately 1,900 community memberships are needed. Waverly has a population of 9,271.

Community memberships are expected to come from community residents that currently use the public parks and

Wellness Center Projections*

(\$, Fiscal Years Ending May 31)

	2008	2009	2010	2011	2012	2013	2014	2015	2016
Net Community									
Memberships	1,145,607	1,179,975	1,215,374	1,251,836	1,289,391	1,328,072	1,367,915	1,408,952	1,451,221
Guest Fees	81,987	84,447	86,980	89,589	92,277	95,045	97,897	100,834	103,859
Non Membership Revenues	627,099	655,251	683,912	712,554	728,868	707,609	724,338	741,568	759,315
Discounts and Collection									
Costs	(879,906)	(114,525)	(68,391)	(71,255)	(72,887)	(70,761)	(72,434)	(74,157)	(75,931)
City Contribution	150,000	150,000	150,000	150,000	150,000	150,000	150,000	150,000	0
Net Revenues	1,124,787	1,955,148	2,067,875	2,132,724	2,187,649	2,209,965	2,267,716	2,327,197	2,238,464
Series 2005B Annual Debt									
Service	949,573	1,899,146	1,899,146	1,933,359	1,975,727	2,011,051	2,049,243	2,085,111	1,972,330
Debt Service Coverage (x)	1.18	1.03	1.09	1.10	1.11	1.10	1.11	1.12	1.13

*Based on low revenue estimates from the feasibility study and excludes college contributions and student fees.

recreational programs, which are expected to be curtailed, and from private employers. Private employers in the area with the largest number of employees include CUNA Mutual Life Insurance Company (with 750 employees), Nestle USA (300), Lutheran Services in Iowa (200), and Bartels Lutheran Retirement Community (200).

The second largest revenue source is nonmembership revenue, which includes primarily program revenues and space rental and special events income. The college may lease space in the Wellness Center to the hospital. The hospital services in the center will function as a health center for students. Other medical professionals might also use space for physical therapy, which could result in additional revenues for the Wellness Center. The health center services provided by the hospital will reduce expenses for the college, which currently provides these services to its students. Nonmembership revenues are expected to be \$627,099 in fiscal 2008.

While Fitch believes that some of the revenue projections are optimistic, additional revenues for the first eight years of operations have been committed by Waverly. Through an agreement between the city and the college, the city will pay \$150,000 annually to the college for eight years for the benefit of the Wellness Center. In addition, the city guarantees annually starting in June 2008 for eight years, up to \$600,000, if revenues fall below specified projections. Furthermore, the city covenants to transfer all indoor recreation programs to the Wellness Center and not to build a competing wellness center or health center while the bonds are outstanding.

The operating costs of the Wellness Center will be covered by the college. In fiscal 2008, the college will begin collecting a \$400 student fee instituted on

Wartburg students to be applied to the Wellness Center. The fees are expected to generate \$680,000 of revenues in the first year.

Based on projections for the Wellness Center provided to Fitch by the underwriter, total estimated revenues for fiscal 2008 are \$1.11 million. Revenues are expected to grow to \$1.9 million in fiscal 2009 as fewer discounts are offered and the center will have had a full year of operations. After fiscal 2009, estimated revenues are expected to increase annually by approximately 3%. In fiscal 2008, debt service on the series 2005B bonds is expected to be \$949,573. Debt service is estimated to increase to 1.9 million in fiscal 2009 and then rise slightly each year until fiscal 2024 when debt service reaches \$2.96 million. Based on the projections provided, it appears that debt service coverage should be at least 1.1x for most years. If revenues from the Wellness Center were not sufficient to cover debt service, series 2005B bondholders would have a second lien on revenues of Wartburg after payment of debt service on the series 2005A bonds.

■ Background and Governance

Wartburg College is a private college serving primarily undergraduate students. The campus is located in Waverly, IA in northeastern Iowa near Waterloo. The college, founded in 1852, is governed by a 28-member board of regents. During the past several years, the board has taken a more active role in fundraising and overseeing investment policies and has established various committees.

Day-to-day operations at Wartburg are managed by the college's senior administrators, including the president and vice presidents of advancement, enrollment management, academic affairs, student development, and financial affairs. Wartburg's

Demand and Enrollment Data

(Fall Term)

	2000	2001	2002	2003	2004	2005
Freshmen						
Applicants	1,740	1,741	1,828	1,976	1,931	1,795
Acceptances	1,453	1,420	1,454	1,554	1,532	1,483
Acceptance Rate (%)	83.5	81.6	79.5	78.6	79.3	82.6
Matriculants	538	512	551	553	535	560
Matriculation Rate (%)	37.0	36.1	37.9	35.6	34.9	37.8
Enrollment (Headcount)						
Undergraduate	1,600	1,649	1,695	1,775	1,804	1,811
Full-Time Equivalent	1,561	1,602	1,652	1,743	1,761	1,772
Average ACT	—	24.1	23.8	23.7	23.7	23.7
ACT National Average	—	21.0	20.8	20.9	21.0	20.9
Tuition (\$)	15,765	16,565	17,530	18,550	19,700	21,130
Room and Board (\$)	4,500	4,600	4,800	5,080	5,350	6,185
Total Cost (\$)	20,265	21,165	22,330	23,630	25,050	27,315
Annual Increase (%)	—	4.4	5.5	5.8	6.0	9.0

ACT – American College Testing.

principal administrative personnel reflect strong experience in academia and higher education administration. The president has been with the college since 1998, while the vice president for administration has been there since 1996. In fiscal 2002, the college hired its first vice president of enrollment management.

■ Student Demand

Fitch views a school's ability to attract students as a critical factor in the rating process for a private college since the majority of funding is from student tuition and fees.

Fall 2005 headcount enrollment totaled 1,811, up 13.2% since fall 2000. Most students attend full time, as reflected by the full-time equivalent figure of 1,772 for fall 2005.

The number of freshmen students applying to Wartburg increased by 11%, from 1,740 applicants in fall 2000 to 1,931 for fall 2004. However, there was a 7% decline in freshmen applications for fall 2005. The decrease was partially attributed to a new enrollment management staff. When reviewing application data, it should be noted that applicants are not required to deposit any funds with their application. Considering the net number of student deposits, which Fitch believes provides a better indication of student demand, the number of deposits has been fairly stable over the past six years.

The percentage of student applications accepted has ranged from 78.6%–83.5% for the last six years. For fiscal 2005, the rate was 82.6%. The matriculation rate has been fairly stable; it was 37.0% in fall 2000, and 37.8% in fall 2005. The matriculation rate is consistent with most private universities rated in the 'BBB' category by Fitch. Wartburg has been able to retain 80% of its freshmen and has a student graduation rate (based on six years) of 67%.

Approximately 74% of the college's students are from Iowa. Based on a study conducted by the Western Interstate Commission for Higher Education, the number of high school graduates in Iowa through 2011 is expected to decline by 8%. Fitch views this as a limiting factor for enrollment growth at Wartburg.

Wartburg's primary competitors include the University of Northern Iowa, Iowa State University, Luther College, Central College, University of Iowa, Simpson College, and Buena Vista University.

Tuition and fees for fall 2005 at Wartburg were \$21,130. Room and board were an additional \$6,185. Fall 2005 tuition, fees, and room and board were 9% higher than the prior fall semester. The 9% increase for fall 2005 was higher than the rise for the prior five years, which ranged from 4%–6%. However, this increase for fall 2005 did not have a negative impact on enrollment or create a pricing disadvantage with competing private schools.

Financial Summary

(\$000, Audited Fiscal Years Ended May 31)

	2000	2001	2002	2003	2004	2005
Statement of Operating Activities (Unrestricted)						
Gross Tuition and Fees	22,119	23,964	25,673	28,329	31,520	33,880
Less Student Aid	8,419	9,236	10,330	11,719	13,294	14,669
Net Tuition and Fees	13,700	14,728	15,343	16,610	18,226	19,211
Endowment Income	436	397	255	339	230	273
Investment Income	223	330	138	281	324	460
Private Gifts, Grants, and Bequests	2,776	2,347	2,386	2,158	2,474	2,661
Auxiliary Enterprises	6,695	7,421	7,856	8,197	8,725	9,325
Other	400	411	372	425	509	472
Net Assets Released from Restrictions	1,292	1,969	940	832	3,576	1,688
Total Revenues	25,522	27,603	27,290	28,842	34,064	34,090
Instruction	9,792	11,191	11,860	12,799	14,483	15,886
Institutional Support	4,356	4,927	5,293	5,354	5,778	5,997
Public Service	378	438	634	562	635	538
Academic Support	1,707	1,883	2,016	2,393	2,578	2,701
Student Services	2,621	2,942	3,239	3,453	3,730	3,970
Auxiliary Enterprises	5,001	5,754	6,060	6,293	6,763	7,952
Total Operating Expenses	23,855	27,135	29,102	30,854	33,967	37,044
Increase/(Decrease) in Unrestricted Net Assets from Operations	1,667	468	(1,812)	(2,012)	97	(2,954)
Net Assets Released from Restrictions for Capital Improvements	4,946	301	1,260	—	1,229	1,468
Total Non-Operating Revenue/(Expense)	844	770	(1,754)	(1,424)	1,271	529
Increase/(Decrease) in Unrestricted Net Assets	7,457	1,539	(2,306)	(3,436)	2,597	(957)
Operating Income Available for Debt Service						
Net Increase/(Decrease) In Net Assets from Operations	1,667	468	(1,812)	(2,012)	97	(2,954)
Add Back: Depreciation Expense	1,822	2,118	2,397	2,517	2,906	3,582
Add Back: Interest Expense	401	559	604	1,047	1,603	2,671
Net Available Revenues	3,890	3,145	1,189	1,552	4,606	3,299
Debt Service	853*	1,097	1,197	1,423**	1,886	2,972
Historical Debt Service Coverage (x)	4.6	2.9	1.0	1.1	2.4	1.1
Maximum Annual Debt Service (MADS)	3,116	3,116	3,116	3,116	3,116	3,116
MADS on Wellness Center	N.A.	N.A.	N.A.	N.A.	N.A.	2,970
Total MADS	N.A.	N.A.	N.A.	N.A.	N.A.	6,086
Pro Forma MADS Coverage – Excluding Wellness (x)	1.25	1.01	0.38	0.50	1.48	1.06
Statement of Financial Position						
Total Cash and Investments	41,634	45,902	41,005	44,630	49,251	49,344
Available Funds (Unrestricted and Temporarily Restricted Cash and Investments)	22,118	25,069	19,621	22,971	26,054	23,836
Endowment (Included in Cash and Investments)	35,514	37,725	36,038	34,622	35,048	36,770
Land, Buildings, and Equipment, Net	39,609	43,955	46,986	45,944	72,960	81,514
Unrestricted Net Assets	54,073	55,612	53,307	50,570	53,168	52,210
Temporarily Restricted Net Assets	2,362	3,456	3,565	5,974	6,046	7,866
Permanently Restricted Net Assets	19,516	20,833	21,384	21,659	23,197	25,508
Total Net Assets	75,951	79,901	78,256	78,203	82,411	85,584
Bonds Payable	441	404	366	340	314	287
Loans Payable	6,045	10,344	9,188	51,108	50,671	49,869
Total Debt	6,486	10,748	9,554	51,448	50,985	50,156
Series 2005B Bonds (New Money)	0	0	0	0	0	35,000
Pro Forma Debt	6,486	10,748	9,554	51,448	50,985	85,156

*Debt service for fiscal 2000 adjusted to reflect payment of \$3.7 million repayment on line of credit. **Debt service for fiscal 2003 adjusted to reflect payment of \$1.0 million repayment on line of credit. N.A. – Not applicable.

■ Financial Performance

The table on page 5 reflects the historical performance of Wartburg College based on the independently audited financial statements.

Operating Margin

The largest source of unrestricted revenues for the college is tuition, which was 56.4% of fiscal 2005 revenues. An additional 27.3% of revenues is derived from auxiliary enterprises, which consist primarily of student room and board revenues and other student-generated revenues. The reliance on tuition, fees, and auxiliary revenues to support operations requires the college to manage its enrollment. A decline in enrollment without an offsetting reduction in expenditures could adversely affect the financial performance of the college.

Fitch measures financial performance by the operating margin, which is calculated by dividing the change in unrestricted net assets from operations by the operating revenues. In calculating the operating margin, Fitch does not include any unrealized or realized investment gains or losses as investment income for operating purposes. Additionally, when comparing the college's financial statements to Fitch's report, it should be noted that for the line item "net assets released from restrictions," Fitch does not include as operating revenue any funds that are to be used to fund capital improvements. Four of the last six years have been greatly affected by excluding these revenues. In fiscal 2000, \$4.9 million of net assets released from restrictions were used to fund capital improvements. In fiscal years 2002, 2004, and 2005, the amounts released for capital improvements were \$1.3 million, \$1.2 million, and \$1.5 million, respectively.

The operating margin was positive for fiscal years 2000, 2001, and 2004 but was negative for fiscal years 2002, 2003, and 2005. While revenues have grown by \$8.5 million, or 33.3%, since fiscal 2000, expenses have risen by \$13.2 million, or 55.3%. A portion of the increase in expenses, \$4 million, can be attributed to a \$1.7 million increase in depreciation expenses and \$2.3 million in interest expense. The rise in interest expense was due to the issuance of the series 2002 bonds. The college expects operating expenses to stabilize and revenues to continue to increase along with enrollment growth and fundraising.

Liquidity

Fitch includes unrestricted and temporarily restricted cash and investments as available funds, which represent a measurement of liquidity. Fitch views liquidity as providing flexibility, which, in turn, allows the school to handle a disruption in operating revenues or unexpected increases in operating expenses.

For fiscal 2005, available funds were \$23.8 million, which covers the \$85.4 million of debt outstanding after the issuance of the 2005 bonds by 0.28x. Fiscal 2005 available funds would cover 64.3%, or over seven months of unrestricted operating expenses. The median coverage of 'BBB' category colleges rated by Fitch is 40%. While the level of liquidity to operations is better than the median, liquidity to debt is low, reflecting the college's high debt burden.

Debt Burden/Capital Improvement Plan

Wartburg's existing debt burden is high. For fiscal 2005, debt service consumed 8.7% of unrestricted revenues.

Financial Ratios

(Audited Fiscal Years Ended May 31)

	2000	2001	2002	2003	2004	2005
Operating Ratios						
Operating Margin (%)	6.5	1.7	(6.6)	(7.0)	0.3	(8.7)
Historical Debt Service as % of Unrestricted Revenue	3.3	4.0	4.4	4.9	5.5	8.7
MADS on Existing Debt as % of Unrestricted Operating Revenue	12.2	11.3	11.4	10.8	9.1	9.1
Flexibility Ratios						
Net Tuition and Fees to Revenues (%)	53.7	53.4	56.2	57.6	53.5	56.4
Net Tuition, Fees, and Auxiliary to Revenues (%)	79.9	80.2	85.0	86.0	79.1	83.7
Tuition Discount Rate (%)	38.1	38.5	40.2	41.4	42.2	43.3
Liquidity Ratios						
Available Funds to Pro Forma Debt (x)	3.41	2.33	2.05	0.45	0.51	0.28
Available Funds to Operating Expenses (%)	92.7	92.4	67.4	74.5	76.7	64.3
Months of Available Funds on Hand	11.1	11.1	8.1	8.9	9.2	7.7
Available Funds to MADS – Excluding Wellness Center (x)	7.1	8.0	6.3	7.4	8.4	7.6
Available Funds to MADS – Including Wellness Center (x)	—	—	—	—	—	3.9

MADS – Maximum annual debt service.

The debt burden is above the Fitch 'BBB' median of 4.9%.

Debt service on the 2005B bonds, which is paid from Wellness Center revenues, combined with the debt service on the series 2005A bonds, is expected to increase Wartburg's maximum annual debt service (MADS) to \$6.1 million in fiscal 2032. Based on fiscal 2005 revenues, MADS of \$6.1 million would consume 17.9% of revenues. However, fiscal 2005 revenues do not include any additional revenues to be generated by the project or those from the community to support the project (*see Wellness Center, page 2*). After the issuance of the 2005 bonds, the college has no plans to issue any additional debt in the near term.

Endowment and Fundraising

Wartburg had an endowment of \$36.7 million as of May 31, 2005, with approximately 41.3% of the endowment being unrestricted. Income from the endowment, along with other investment income, is less than 1% of unrestricted revenues.

Annual fundraising for Wartburg has been consistent and at significant levels over the past six years. The annual amount has ranged from \$4.0 million–\$7.3 million. When reviewing the college's revenue data in this report, it should be noted that only unrestricted revenues are included. For example, in fiscal 2005, \$7.2 million of gifts, grants, and bequests were recorded. However, only \$2.2 million was recorded as unrestricted. The remaining amount was recorded as \$3.6 million to temporarily restricted assets and \$2.1 million to permanently restricted assets. Each year, after certain conditions have been met, funds from temporarily restricted assets are transferred to unrestricted assets.

Wartburg currently has an \$88 million capital campaign under way. The campaign is intended to provide \$41 million for financial aid and technology enhancements, \$40 million for facilities, and \$7 million for operations. The campaign is scheduled to be completed by October 2006. As of October 2005, \$81 million had been collected or pledged. Fitch viewed the college's demonstrated history of successful and consistent fundraising as a positive credit factor in the rating process.

■ Participants

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