

FITCH AFFIRMS UNITED METHODIST RETIREMENT COMMUNITY (MICHIGAN) BONDS AT 'BBB'

Fitch Ratings-New York-19 November 2009: Fitch Ratings affirms the 'BBB' rating on the \$14,065,000 Economic Development Authority of the Village of Chelsea revenue and refunding bonds, series 1998 (United Methodist Retirement Communities, Inc.). The Rating Outlook is Stable.

The rating affirmation is based on United Methodist Retirement Communities' (UMRC) historically solid occupancy levels, management's strategic decision to dispose of underperforming skilled nursing facility (SNF) assets and invest in independent living units (ILU), and a manageable debt position. Credit concerns include adequate, but reduced liquidity, and softened profitability.

UMRC's Chelsea Retirement Community's (CRC) ILU occupancy averaged 97% from fiscal year (FY) 2005-FY2008, but fell to 87% in FY2008 and 88% through Sept. 30, 2009. Furthermore, CRC's assisted living unit (ALU) and residential dementia facility (RDF) occupancy also softened in FY2008 and through Sept. 30, 2009, but remains above 90%. Occupancies are softer as UMRC is finding it challenging to re-sell its smaller studio apartments and are taking some of them out of service as it consolidates and converts them into larger one bedroom deluxe units. UMRC's stand alone nursing facility, Boulevard Temple, enjoyed occupancy of 92% and 91%, respectively during the last two fiscal years. Regardless, Boulevard Temple continues to produce operating losses from inadequate reimbursement and UMRC's inability to properly align operating expenses. As a result of the poor performance, UMRC is in the process of selling the SNF and expects to net about \$2 million of sale proceeds. The SNF sale is expected to close by Dec. 1, 2009.

UMRC is also in the process of developing its Cedars of Dexter (Cedars) project. Cedars is expected to be a 60-unit refundable entrance fee facility located about eight miles east of CRC and 10 miles northwest of Ann Arbor, MI in a desirable community. As of Sept. 30, 2009, UMRC collected 25 10% deposits and spent about \$5 million to acquire and improve the land. The expected weighted average entrance fee of \$240,000 is about the same as median home values in the primary market area. Management also reports that the average net worth of its depositors is well in excess of that amount. The project's total development cost is estimated between \$18 million-\$20 million and is expected to be temporarily funded with a five-year \$9 million construction loan, \$2 million SNF sale proceeds, UMRC equity, and initial entrance fee proceeds that are projected to total \$14 million. While Fitch views UMRC's SNF disposition and ILU investments favorably, Fitch will closely monitor Cedars' construction and fill-up and evaluate the project's permanent financing plans over the next 24 months.

UMRC's liquidity is satisfactory, with \$17 million of cash and investments amounting to 190 days of operating expenses or 122% of long-term debt as of Sept. 30, 2009. These levels are down slightly from \$18 million or 203 days cash on hand in FY2007 due to investment losses and increased capital spending for Cedars. UMRC also used a \$3 million line of credit to fund the initial expenses for Cedars, but this line was eliminated with the construction loan. UMRC's current debt position is manageable with 3.6% maximum annual debt service as a percent of revenues and 26.2% debt to capitalization as of Sept. 30, 2009. Fitch views the \$9 million construction loan as an acceptable amount of debt that should not impact the 'BBB' rating, but remains moderately concerned with its five-year term.

UMRC's operating profitability suffered in FY2007, FY2008, and the nine month period ending Sept. 30, 2009 mostly from the aforementioned losses at Boulevard Temple. The SNF lost \$891,000 in FY2007, \$1.36 million in FY2008, and another \$607,000 through Sept. 30, 2009. CRC remains profitable, with \$864,000 of operating earnings in FY2007, \$1.2 million in FY2008, and a weakened \$222,000 operating profit through Sept. 30, 2009 due to the lighter occupancy levels and an increasing charity care burden, especially in its ALU. However, CRC has not yet received its restricted fund donations for FY2009 that typically amounts to several hundred thousand dollars.

Management expects the charity care costs to pressure operating earnings through FY2010, but revised its charity care policy to moderate this burden. Moreover, the disposal of Boulevard Temple and development of Cedars should improve overall earnings in the medium and longer term.

The Stable Outlook reflects Fitch's expectation that UMRC will continue to maintain solid operations and adequate cash balances. Fitch views the Cedars project and disposition of Boulevard Temple positively; however, Fitch will review the rating at the time of the permanent plan of finance.

UMRC now consists of two facilities, Chelsea Retirement Community and Cedars of Dexter. CRC is a rental-only continuing care retirement community (type C) with 125 ILUs, 49 ALUs, 102 RDF beds, and 85 SNF beds located in Chelsea, MI, about 15 miles west of Ann Arbor. Cedars is expected to be 60 unit type C ILU facility located in Dexter, MI about 10 miles northwest of Ann Arbor. Disclosure is good in terms of content and timeliness and is viewed favorable by Fitch. Quarterly disclosure includes a balance sheet, income statement, and statement of cash flows.

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