FITCH DOWNGRADES THE COLLEGE OF NEW JERSEY, NJ REVS TO 'A+'; OUTLOOK REVISED TO STABLE

Fitch Ratings-Chicago-22 November 2019: Fitch Ratings has downgraded to 'A+' from 'AA-' the ratings on approximately $402 million of New Jersey Educational Facilities Authority revenue bonds issued on behalf of The College of New Jersey (TCNJ) and has removed the bonds from Under Criteria Observation. Fitch has also assigned an Issuer Default Rating (IDR) of 'A+' to TCNJ.

The Rating Outlook is revised to Stable from Negative.

SECURITY

The bonds are an unsecured general obligation of TCNJ.

ANALYTICAL CONCLUSION

The downgrade to 'A+' reflects TCNJ's mild cash flow declines and vulnerability to further operating variability coupled with largely flat operating support from the state of New Jersey (rated A/Stable). TCNJ's financial flexibility is limited by a relatively high debt burden, resulting in a financial profile that is inconsistent with a higher rating. The 'A+' is supported by noted strength in demand characteristics and stable enrollment, in a challenging and competitive market which tempers TCNJ's pricing flexibility somewhat. The outlook reflects an expectation of steady to growing available fund levels supported by steady operating cash flow.

KEY RATING DRIVERS

Revenue Defensibility: 'aa'; Strong Demand Profile in Competitive Market

TCNJ's strong demand characteristics anchor the 'aa' assessment, supporting very steady enrollment trends in a competitive and challenging market. Very high student quality and retention are tempered by somewhat midrange matriculation, indicative of the competitive environment.

Operating Risk: 'aa'; Manageable Capital Needs; Strong Cash Flow

Cash flow margins should remain strong going forward, and TCNJ's stated capital plans are relatively modest and flexible. TCNJ has been successful utilizing fundraising and other external sources for some of its capital needs.

Financial Profile: 'a'; Relatively High Leverage Softened by State Pension Support

With 24% available funds to adjusted debt (including net pension liabilities) ratio in fiscal 2018, TCNJ maintains a financial profile through Fitch's scenario analysis consistent with an 'a' assessment. Consideration for this metric is strengthened by the state's consistent operating and pension support, which lessens the burden of adjusted debt relative to the calculated value and supports a financial profile assessment of 'a' as it relates to the 'A+' IDR.

Asymmetric Additional Risk Considerations
No asymmetric risk factors affected the rating.

RATING SENSITIVITIES

STATE SUPPORT: The explicit and thus far consistent level of state support for TCNJ's pension contributions and general operations are noted considerations in Fitch's leverage assessment and 'A+' rating. As the state has no statutory requirement to fund its higher education employer pension costs, indications of diminishing state support for either pension benefits or operating support could result in rating pressure.

EROSION IN DEMAND CHARACTERISTICS: Fitch considers TCNJ's strong demand profile to be integral in preserving its revenue growth and operating flexibility going forward in the face of a competitive and demographically challenging operating environment. Enrollment pressure or material shifts in demand characteristics could pressure the rating.

CREDIT PROFILE

TCNJ, founded in 1855 and located in the Trenton suburb of Ewing, NJ, is a public institution of higher education in the state. The college's strong liberal arts core forms the foundation for over 50 majors offered throughout seven schools. Full time equivalent (FTE) enrollment was 7,465 for fall 2019. Most students attend full-time and enter as freshmen.

Revenue Defensibility

Revenue defensibility is supported by generally favorable demand characteristics, some pricing flexibility against consistent enrollment, and a meaningful amount of state operating support. Challenging demographic characteristics in a competitive environment temper the assessment, though very stable enrollment is indicative of TCNJ's steady role in the market.

TCNJ maintains very high student quality, strong retention of over 90%, a very good graduation rate approaching 90%, steadily growing applications, and solid selectivity (near 50% in fall 2019). Matriculation is comparatively weaker at just over 20%, evidencing the challenging market TCNJ operates within. The school reports that its primary cross-application schools are Rutgers University, the University of Delaware, Stevens Institute of Technology, Rowan University, Villanova University, Ramapo College, and Seton Hall University.

State appropriations are a key revenue source for TCNJ, accounting for 23% of fiscal 2018 operating revenues. While providing a base of support, state funding has generally not kept pace with growth in TCNJ's enrollment or expense base and is unlikely to materially offset potential volatility in other revenue sources going forward. Support consists of base operating appropriations and fringe benefit appropriations, which are either reimbursed or paid on TCNJ's behalf by the state. After years of effectively flat operating support, the state increased TCNJ's operating appropriation by 5.6% in fiscal 2020. However, Fitch's baseline expectation is that funding will remain flat and somewhat politically sensitive, particularly at times of economic decline.
In addition to state support, TCNJ has a limited but consistent level of grant and contract revenue near 9% of its operating revenues. Still, Fitch expects that over time TCNJ will become incrementally more reliant on student-fee generated revenues (66% of total revenues in fiscal 2018), which will likely grow at a modest pace between 0%-2% annually.

Operating Risk

Broadly, TCNJ's operating risk assessment of 'aa' reflects an expectation that cash flow margins will stabilize near 14% going forward and its capital needs will be relatively flexible and manageable to absorb.

TCNJ's cash flow has diminished in recent years, driven in part by shifts in pension and other post-employment benefit (OPEB) expenses as well as operating pressure. Performance in fiscal 2018 was weaker as reported, reflecting the full recognition of OPEB expense (and associated revenue), as well as increased fringe benefit costs and O&M expenditures. Fitch excludes OPEB expenses from its related operating calculations given the obligatory and explicit funding provided by the state for the full expense (reported as non-operating revenue), rendering it effectively non-cash in its entirety. Fitch expects generally balanced operations to continue at levels sufficient to produce steady coverage and incremental improvement in leverage.

Future capital needs are expected to remain modest, as suggested by TCNJ's only slightly elevated age of plant near 13 years and modest level of internally funded outlays planned. TCNJ has been successful at securing external funding in support of some capital needs, including capital grants and gifts. It also has a solid fundraising platform; it's first ever comprehensive campaign was successful, surpassing the $40 million goal with $63million contributed/committed through closure of the campaign in 2018. Fitch believes TCNJ retains some flexibility on necessary expenditures but will need to maintain a competitive operating platform to preserve its strong recruitment and retention expectations.

Financial Profile

Leverage remains a key credit consideration. Available fund (AF) levels have incrementally increased over time, but remain relatively light against the college's bonded debt and adjusted debt burden. TCNJ had approximately $402 million in debt outstanding as reported at fiscal 2018 YE, all of which is fixed rate. This figure includes approximately $37 million in series 2010B crossover refunded debt, which was redeemed on July 1, 2019. Excluding this debt increases AF to long-term debt by approximately 4%. TCNJ's debt structure is front-loaded, with a substantial portion amortizing over the next 10-15 years. Fitch expects the college to preserve its AF and slowly reduce its leverage over time.

While the state has consistently provided operating support for the full contractual (not actuarial) contribution, that support is not protected by statute and TCNJ's financial profile assessment, and rating, is at risk of exposure should the state change its current practice of supporting pension benefits. The state has taken some action to improve funding of its pension obligations, including reducing cost of living adjustments and incrementally increasing contributions to the actuarial level, which Fitch expects will crowd other state funding priorities over time, but otherwise lower the reported liabilities of the plans. OPEB for higher education institutions is an explicit liability of the state, and thus its related liability and associated expenses are excluded from Fitch's analysis of leverage and cash flow.

Asymmetric Additional Risk Considerations
No asymmetric additional risk considerations apply to TCNJ's rating.

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Sources of Information
In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

ESG Considerations
Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg.

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Additional information is available on www.fitchratings.com

Applicable Criteria
Public Sector, Revenue-Supported Entities Rating Criteria (pub. 07 Nov 2019)
https://www.fitchratings.com/site/re/10099396
U.S. Public Finance College and University Rating Criteria (pub. 03 Jun 2019)
https://www.fitchratings.com/site/re/10075131