MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns Baa3 to St. Joseph's Healthcare System's (NJ) Ser. 2017; outlook negative

Global Credit Research - 07 Aug 2017

New York, August 07, 2017 -- Issue: Taxable Bonds, Series 2017; Rating: Baa3; Rating Type: Underlying LT; Sale Amount: $80,000,000; Expected Sale Date: 08/14/2017; Rating Description: Revenue: Other;

Summary Rating Rationale

Moody's Investors Service has assigned a Baa3 to St. Joseph's Healthcare System's (NJ) (SJHS) proposed $80 million Series 2017 Revenue Bonds to be issued through the New Jersey Health Care Facilities Financing Authority. The proposed Series 2017 bonds are expected to be fixed rate, taxable securities with balloon maturities in 2022 and 2027. At this time, we are also affirming the Baa3 on the system's outstanding revenue bonds. The rating outlook is revised to negative.

The Baa3 reflects SJHS's large scale and essentiality as a safety net provider, and acknowledges strong operating cash flow generation in recent years that has contributed to a steadily improved unrestricted absolute and relative liquidity position through FY 2016. They system continues to demonstrate reduced reliance on state subsidies despite its location in a demographically challenged service area. However, the rating may be under pressure as SJHS reports unexpected operating pressures in FY 2017 which will continue to present financial headwinds given expenses associated with the installation of a new electronic medical record (EMR) clinical platform and ongoing charity care subsidy reductions from the state. While the proposed debt issuance will reduce the organization's annual contributions to the sizable defined benefit pension plan liability, it will require stronger cash flow generation to fund debt service and annual sinking fund payments as the debt structure adds risk to the system with the presence of bullet maturities in 5 and 10 years.

Rating Outlook

The negative outlook reflects weaker than anticipated operating performance in FY 2017 and incorporates an expectation that operating performance will remain suppressed as the system also enters into a period of elevated capital spend, which includes the implementation of a new clinical IT platform.

Factors that Could Lead to an Upgrade

Growth in unrestricted liquidity

Material improvement in operating performance

Significant reduction of total adjusted leverage relative to medians

Factors that Could Lead to a Downgrade

Material reduction in state subsidies that results in weaker operations and inability to meet projections

Meaningful decline in financial reserves

Increase in leverage or greater than anticipated capital spending

Prolonged contraction in operations stemming from EMR implementation

Legal Security

Bonds are secured by a gross revenue pledge of the obligated group and a mortgage security interest in the Paterson and Wayne campuses. Required covenants include annual debt service coverage of 1.25 times and cushion ratio of 1.25, both measured quarterly. A 60 days cash on hand covenant is present only if either of the other two required ratios are not met for two consecutive quarters. Failure to meet covenants results in the required engagement of a consultant. The documents include a substitution of notes provision as well.

Use of Proceeds

The Institution will use the proceeds of the Series 2017 Bonds to: (i) provide moneys to finance the general corporate purposes of the Institution and the other Members of the Obligated; and (ii) pay the costs of issuance of the Series 2017 Bonds. According to management, proceeds will be used to reimburse for recent contributions made to the pension plan ($45 million; see Pensions and OPEB) and contribute remaining proceeds ($35 million) to the pension.

Obligor Profile

SJHS is a not-for-profit two acute-care-hospital health system sponsored by the Sisters of Charity of Saint Elizabeth. The financial statistics above include other subsidiaries, including employed physicians, two foundations, and various outpatient care facilities.

Methodology

The principal methodology used in this rating was Not-For-Profit Healthcare Rating Methodology published in November 2015. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Regulatory Disclosures

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