



RATING ACTION COMMENTARY

Fitch Affirms Fellowship Senior Living's (NJ) Rev Bonds at 'BBB+'; Outlook Negative

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Fitch Ratings - New York - 24 Nov 2020: Fitch Ratings has affirmed the 'BBB+' rating assigned to approximately \$88.5 million of series 2019A, 2019B, 2013A, and 2013B revenue bonds issued by the Wisconsin Public Finance Authority on behalf of Fellowship Senior Living (FSL).

The Rating Outlook is Negative.

SECURITY

The bonds are secured by a revenue pledge, mortgage, and a debt service reserve fund.

KEY RATING DRIVERS

EXECUTION RISK: The Negative Outlook reflects higher execution risk as FSL continues to rebuild its independent living (IL) occupancy after a large construction project in the center of its campus. Following the 2019 debt issuance, FSL's balance sheet weakened to 47.8% cash to debt, which is below Fitch's 'BBB' category median of 67.1%. However, Fitch

expects that FSL's campus repositioning projects will help rebuild balance sheet and debt service coverage metrics as IL occupancy returns to historical levels above 90%. Failure to improve the balance sheet over the next two years will likely lead to a downgrade.

STRONG MARKET POSITION: FSL is located in Basking Ridge, NJ, a desirable and affluent suburb, with household income levels and housing prices well above state and national averages. Prior to the construction project, FSL had IL occupancy in the mid-90% range, despite the presence of competition. IL occupancy has softened over the last few years, falling to 85% in fiscal 2019 and 80% through the first nine months of fiscal 2020, due to various on-going construction projects and coronavirus pandemic induced disruptions which have hindered marketing efforts. However, IL occupancy was improving before the coronavirus pandemic and IL move ins have resumed their positive momentum over the last two quarters. Fitch believes that FSL's extensive capital repositioning projects, including common space renovations, a new health center, and additional skilled nursing beds and assisted living units (ALU) will help the campus rebuild IL occupancy closer to historical averages. Ongoing projects include the second phase of the SNF project and the AL renovations which are expected to be completed in 2021.

IMPROVING OPERATIONAL PERFORMANCE: Operations have improved in 2020 despite disruptions from the pandemic. FSL had an operating ratio of 86.3%; 16.1% net operating margin (NOM); and 28.8% NOM-adjusted, which are better than Fitch's 'BBB' category medians, and are improved compared to the 95.6% operating ratio, 3.9% NOM, and 16.2% NOM-adjusted in fiscal 2019. Operations were supported by \$5.3 million in pandemic-related government funding, which helped reduce the impact of pandemic induced disruptions. Fitch expects FSL to maintain recently improved operating metrics going forward.

MIXED LONG-TERM LIABILITY PROFILE: FSL's debt burden is mixed as of Sept. 30, 2020, with a cash-to-debt of 47.8% compared to Fitch's 'BBB' category median of 67.1% and debt to net available of 5.8x compared to Fitch's 'BBB' category median of 6.7x. However, debt service coverage metrics remain strong compared to Fitch's 'BBB' category medians with maximum annual debt service (MADS) making up 10.3% of revenues through the first three quarters of 2020 and a MADS coverage of 3.0X, both of which are better than the Fitch category medians of 12.4% and 2.2%, respectively.

ASYMMETRIC RISK FACTORS: There are no asymmetric risk factors considered in this rating determination.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Given FSL's financial position as it rebuilds IL occupancy following the large construction projects, an upgrade is considered unlikely over the outlook period.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Failure to improve IL occupancy to near 90%;

--Failure to improve balance sheet metrics, with cash to debt remaining below 60% over the next two years;

--Weakened cash flow such that debt service coverage is consistently below 2.0x and unrestricted liquidity growth flattens.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [<https://www.fitchratings.com/site/re/10111579>].

CREDIT PROFILE

Located in Basking Ridge, NJ, FSL is a senior living organization with several distinct service lines. Fellowship Village (FV) is FSL's continuing care retirement community, which offers Type-A (Lifecare) contracts. FSL offers traditional contracts which become non-refundable after 50 months and 90% refundable contracts; however, most have chosen the traditional option. FV currently has 256 independent living residences/units (ILUs), 81 assisted living

suites/units (ALUs; includes 17 memory care units), and 54 skilled nursing (SN) beds. FSL's other service lines includes Fellowship Freedom Plans, which is a CCRC "without walls," Fellowship Helping Hands, a home health agency, and a Hospice program which was accredited in December 2017.

All service lines of FSL are included in the obligated group. FSL's total operating revenues in fiscal 2019 were approximately \$45.5 million.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means 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 Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING	PRIOR
Fellowship Senior Living (NJ)		
● Fellowship Senior Living (NJ) /General Revenues/1 LT	LT	BBB+ Rating Outlook Negative Affirmed BBB+ Rating Outlook Negative

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[U.S. Public Finance Not-For-Profit Continuing Care Retirement Community Rating Criteria \(pub. 29 Mar 2018\) \(including rating assumption sensitivity\)](#)

[Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 27 Mar 2020\) \(including rating assumption sensitivity\)](#)

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Wisconsin Public Finance Authority

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