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Investment Insights

State of the State: New Jersey

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Overview

The state of New Jersey continues to demonstrate fiscal strength and resilience. With three consecutive years of full pension contributions and strong levels of reserves, New Jersey continues to offer valuable opportunities for investors.

New Jersey's credit rating trajectory will depend on the state's ability to sustain balanced operations and adequate reserves.

This piece highlights the Passaic Valley Water Commission, New Jersey's fourth largest water supplier and the largest publicly owned water supplier in the state.

State overview

New Jersey continues to demonstrate near-term strength following its recovery from the COVID-19 pandemic. The improvement in credit quality earned the state rating upgrades by all three public agencies during the 2023 calendar year. This positive momentum has largely been the result of record levels of revenue, federal stimulus, and an economy that has rebounded exceptionally well post-pandemic. Combined with levels of inflation that have not been observed since the 1980s, sales tax receipts have been an important source of increased tax revenue that for the budgeted 2026 fiscal year is anticipated to reach over $14.4 billion alone, or 25% of budgeted revenues.[1] The state's undesignated fund balance has also risen as a result. Historically before the onset of COVID, New Jersey's fund balance as a percent of annual appropriations was low compared to other states at below 6%. For fiscal year 2026, that figure is projected at 13% of expenditures.[2] This level does represent a decline from the state's peak fund balance of 20% in fiscal 2023, a sign that stimulus efforts and revenue generation have begun to slow. This observation signals the need for New Jersey to maintain fiscal responsibility in order to manage its budget and costs appropriately moving forward, as extraordinary federal support diminishes.

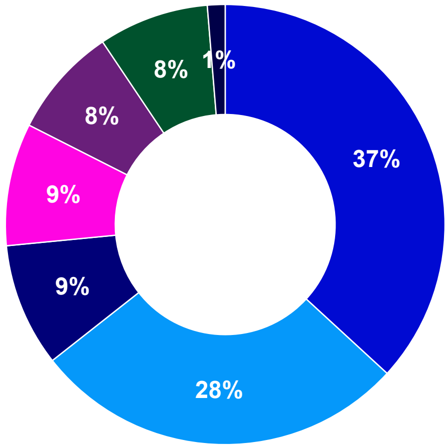
Encouragingly, New Jersey has used this opportunity to prioritize the overall fiscal health of its accounts and reserves, particularly as it relates to addressing the state's large liability burden. As part of that effort, the fiscal 2026 budget will represent New Jersey's fifth consecutive year of making its full actuarial contribution to the state's pension plans.[1] New Jersey also benefits from a large economy with high wealth levels, as illustrated by an average personal income that is 116% of the national average.[3] Its proximity to the New York City metro area further provides for access to a diverse set of employment opportunities, with a cost of living that is lower than residing in Manhattan itself. For these reasons, the investment team believes debt issued by the state of New Jersey has continued to offer opportunity for municipal investors.

Despite recent progress, we believe New Jersey faces longer-term challenges from its exposure to high levels of debt and retirement liabilities, which could become more pronounced as the state looks to sustain balanced operations and adequate reserves. As such, the state's credit trajectory will hinge on its demonstrated ability to achieve a balanced budget financed by tax collections and other recurring revenues, while ensuring policies are in place to sustain its debt management program. Without these controls and policy measures, New Jersey could face the politically unpopular decision to either cut expenses or incur additional deficit financing. Either outcome would be a negative for the credit, especially following a period where the governor has otherwise expanded the budget to cover increased levels of educational spending and pension contributions. Additionally, New Jersey's already-high tax rates restrict the state's ability to further increase revenues absent a continued rebound in post-pandemic economic activity. Ultimately, the direction of future credit ratings will largely depend on New Jersey's ability to address these fiscal concerns in a timely and sustainable fashion.

Fiscal update: Revenues

As shown in Figure 1 on the following page, New Jersey revenues are heavily dependent on gross income and sales taxes, followed by the corporate business tax. Combined, these three income streams account for 73% of budgeted revenues.[2]

Figure 1: Fiscal Year 2025 Budgeted Revenues (%)

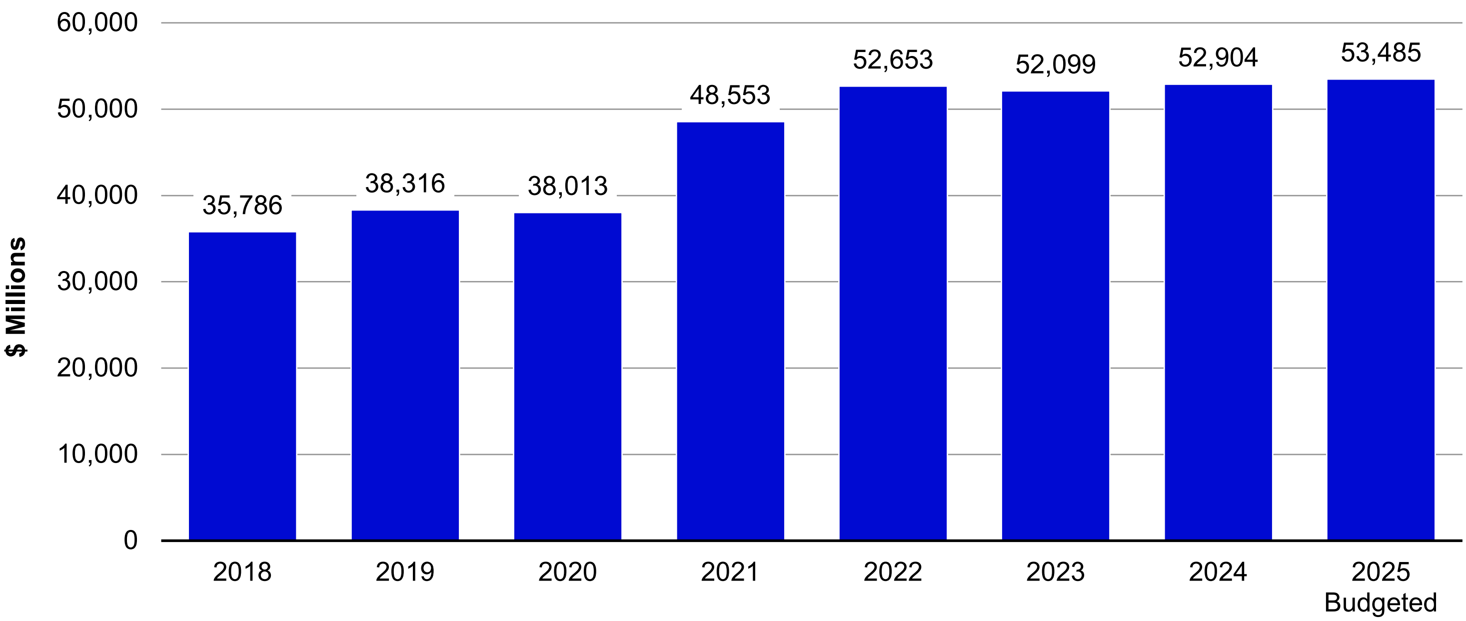


Gross Income Tax	**36.82**
Sales and Use Tax	**27.57**
Misc. Tax and Fees	**9.06**
Other Major Taxes	**9.00**
Corporation Business Tax	**8.12**
Pass-Through Business Alternative Income Tax	**8.11**
Casino Taxes and Fees	**1.30**

Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024

New Jersey's financial health has continued to recover and grow post-pandemic. Although revenue growth in the state has begun to slow following the rapid growth over the past three years, revenues are in line with original budgeted figures and are expected to increase 3.5% in fiscal 2026 according to the New Jersey Office of Legislative Services.[4] The main drivers of the year-over-year growth in estimated revenues are increases in two of the state's largest revenue sources, gross income tax and sales and use tax revenues. These revenue streams are expected to increase 4.2% and 5.2% in fiscal 2026, respectively. Offsetting this growth are projections for the third largest revenue source, corporation business tax (CBT) revenues, to decline by 5.2% in the same fiscal year. The decline in CBT revenues can be largely attributed to the calendar-year end 2023 expiration of a 2.5% surcharge on the state's corporate business tax. This loss of revenue will pressure the state's the ability to maintain a structurally balanced budget to a degree.[4]

Figure 2: Historical and Estimated Revenues

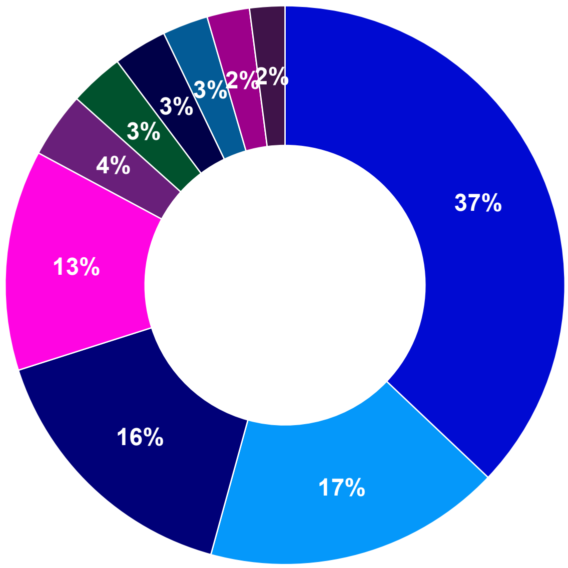


Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024

Fiscal update: Expenses

Except for fiscal 2023, which saw a 2% decline, the state's budgeted appropriations have increased year over year as far back as fiscal 2015. For context—the state's annual pre-pandemic budget in fiscal 2019 was approximately $38 billion. Fiscal 2025's budget of more than $53 billion represents material growth of 40%. While annual spending continues to flow to several areas, education remains the largest component of the proposed budget and is reported to have a 5-year compound annual growth rate of 6%.[2] Total spending for education is expected to top $21 billion, or approximately 36% of total 2025 budgeted appropriations. Other significant expense drivers include employee benefits and human services, the ramp-up of which is the result of New Jersey's increased pension contributions in recent years.

Figure 3: Fiscal Year 2025 Budgeted Expenses (%)

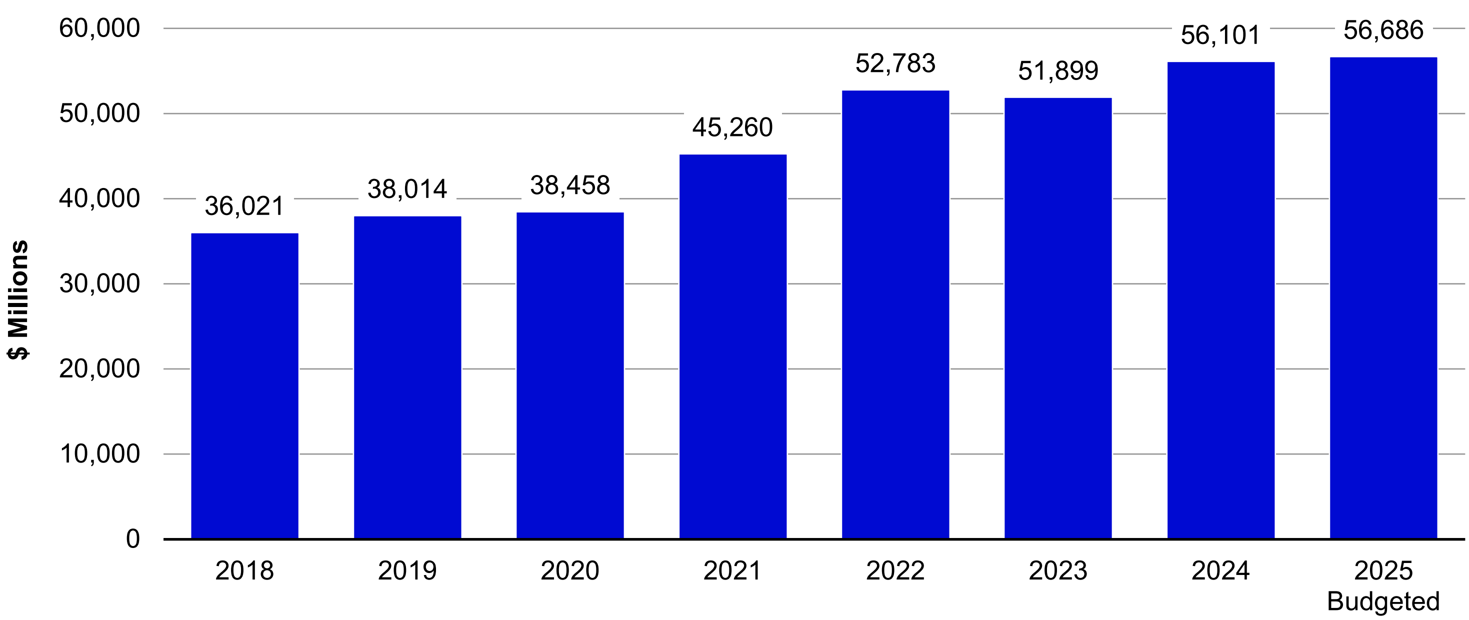


	Education	**37.08**
	Other	**17.19**
	Human Services	**15.81**
	Employee Benefits (Health)	**12.77**
	State	**3.79**
	Transportation	**3.14**
	Treasury	**3.10**
	Children & Families	**2.64**
	Health	**2.46**
	Corrections	**2.03**

Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024

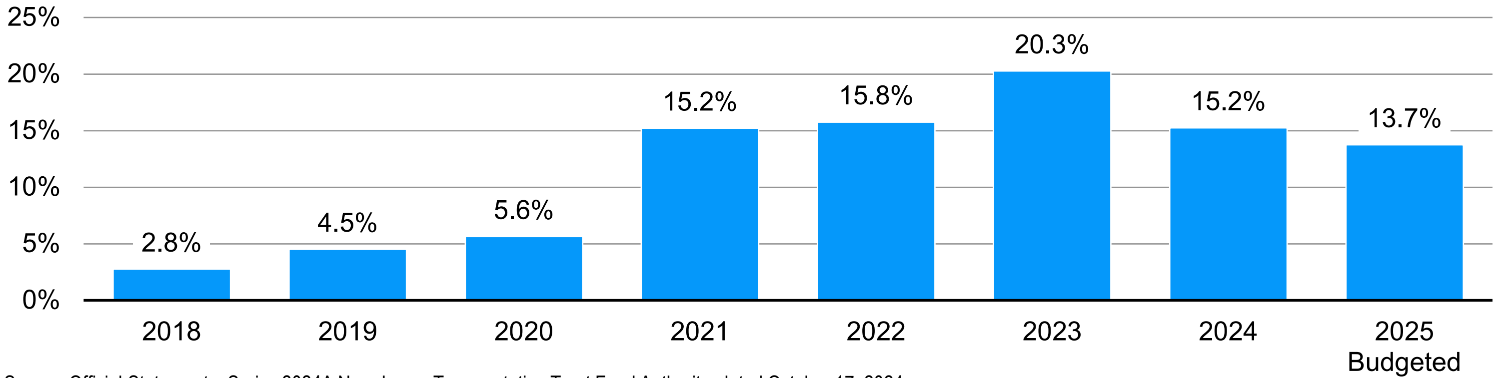
While the potential for slower future revenue growth is something that New Jersey will need to manage in the coming years, the state's fund balance is stronger than pre-pandemic levels. This level remains strong at more than twice the pre-pandemic balance in 2019 and with a 5-year CAGR of 19% in the same time period. However, most recent estimates show evidence of forthcoming moderation. Since our last update, the fiscal 2025 budget is to decline to $5.1 billion, or roughly 9% of budgeted expenditures.[2] In the meantime, conservative budgeting and the ability to match revenues to expenditures will be key to the state's creditworthiness going forward.

Figure 4: Historical and Estimated Expenses



Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024

Figure 5: Historical Budgetary Fund Balance as a % of Expenses



Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024.

New Jersey pension funding

New Jersey's retirement obligations remain a significant hurdle and account for a far greater portion of the state's long-term liabilities than its outstanding bonds. According to Moody's investor service, the pension liability alone represents about half of the state's total long-term liabilities, increasing to over 80% when including post-employment benefit costs (OPEB).[5] Funding ratios remain low but improved year-over-year at approximately 47% for state and local employees,[2] and New Jersey has made progress in addressing this liability in the form of contributing its full annual pension payment in fiscal since fiscal 2022 and is expected to contribute its full annual pension payment in fiscal 2025.[8] These payments represent the first full contributions to the plans in 25 years. The state's ability and willingness to sustain this practice of full funding will be a credit risk to monitor moving forward, especially amid rising costs and slowing revenue growth. The plans' assets also remain vulnerable to swings in market performance as has been experienced in both positive and negative directions over the past three years (see Figure 6).

Figure 6: Historical New Jersey Pension Funding

	Fiscal 2017	Fiscal 2018	Fiscal 2019	Fiscal 2020	Fiscal 2021	Fiscal 2022	Fiscal 2023	Fiscal 2024
Valuation Date	July 1, 2016	July 1, 2017	July 1, 2018	July 1, 2019	July 1, 2020	July 1, 2021	July 1, 2022	July 1, 2023
Assets	75,348	79,313	81,433	82,293	79,867	98,110	90,055	96,857
Liabilities	243,591	221,601	209,560	207,123	208,173	195,927	200,139	205,513
UAAL*	(168,243)	(142,289)	(128,127)	(124,830)	(128,307)	(97,817)	(110,084)	(108,655)
Percent Funded	30.9%	35.8%	38.9%	39.7%	38.4%	50.1%	45.0%	47.1%

Source: Official Statement – Series 2024A New Jersey Educational Facilities Authority, dated November 20, 2024
*UAAL: Unfunded Actuarial Accrued Liability

Economic update

A major factor supporting New Jersey is the state's significant wealth characteristics, as reflected in the state's per capita personal income (PCPI) that is 116% of national levels.[3] This level, which is among the highest in the nation, is supported by the state's proximity to the New York City metro area as a major employment center. While New Jersey's tax structure is high, especially for earners making above $1 million per year, housing remains more affordable than comparable New York City options (See Figure 7).

Figure 7: Historical Per Capita Personal Income

	2016	2017	2018	2019	2020	2021	2022	2023	2024
NJ Per Capita Personal Income	62,213	64,410	67,142	69,626	73,460	74,805	78,700	80,724	84,071
US Per Capita Personal Income	49,812	51,811	54,098	56,047	59,510	63,444	65,423	68,531	72,425
NJ/US PCPI	125%	124%	124%	124%	123%	118%	120%	118%	116%

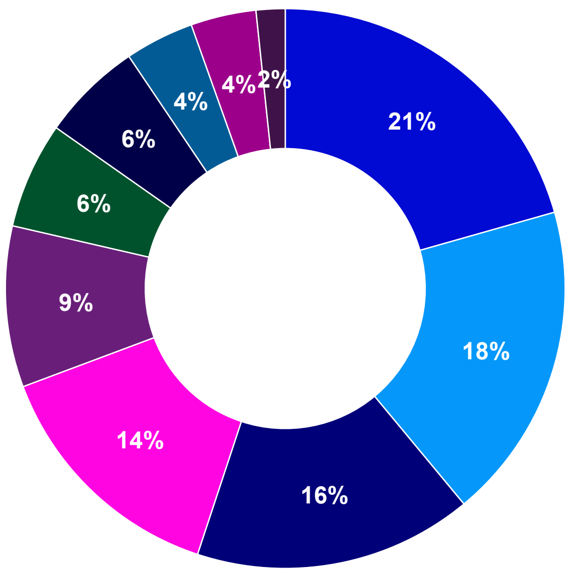
Source: Bureau of Economic Analysis, as of December 31, 2024

Labor and unemployment

New Jersey's employment base is generally diverse, with no sector representing greater than 21% of the whole. Leisure and hospitality, a sector that was particularly vulnerable to pandemic-related job losses, has now effectively fully recovered and represents 9.3% of employment as of February 2025. This level illustrates a rebound from a low of 3.1% reported in June 2020. Unemployment remains significantly lower than at the height of the pandemic but has been on a steadily increasing recently. As of February 2025, the unemployment rate stood at 4.6%.[3]

The overall economic recovery following the onset of the COVID-19 pandemic has been strong. This positive momentum has been supported by an improving job market and a strong demand for workers. Easing pandemic restrictions has also allowed for a return to in-office work for many businesses, as well as domestic and international travel.

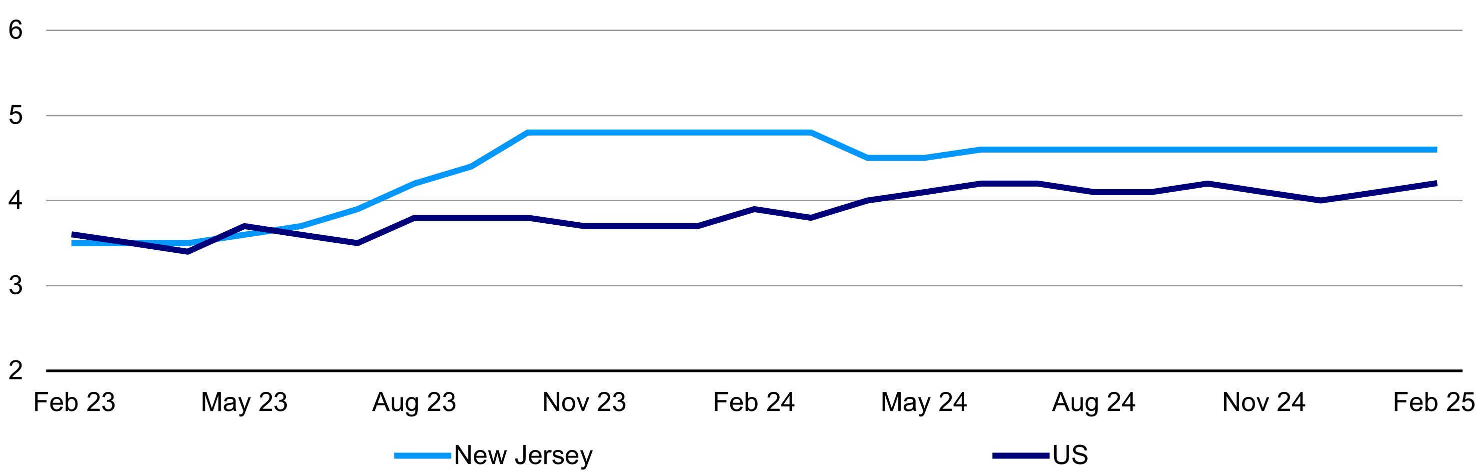
Figure 8: New Jersey Employment by Industry



Trade, Transportation, Utilities	**20.60**
Education and Health Services	**18.38**
Professional and Business Services	**16.09**
Federal, State, Local Government	**14.23**
Leisure and Hospitality	**9.30**
Financial Activities	**6.14**
Manufacturing, State	**5.82**
Other Services	**3.98**
Logging, Mining & Construction	**3.78**
Information	**1.67**

Source: Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024.

Figure 9: Historical Seasonally Adjusted Unemployment Rate (%)



Source: Bureau of Labor Statistics, February 28, 2023 through February 28, 2025

New Jersey General Obligation Update

Moody's: A1 / Positive as of August 16, 2024
S&P: A / Stable as of September 18, 2024
Fitch: A+ / Stable as of November 27, 2024

Moody's has assigned a rating of A1 to the state's general obligation bonds since 2023 and revised the outlook to positive from stable on August 14, 2024, citing solid economic and revenue performance that are expected to maintain strong reserve levels and the state's improvements to its pension funding practices. Moody's notes credit challenges in managing the state's large long-term liability and fixed cost burden.[8]

S&P affirmed the state's general obligation rating at A with stable outlook on September 18, 2024. The report claims the rating reflects a diverse and wealthy tax base, strategic position between New York City and Philadelphia, as well as a high long-term debt, pension and OPEB liabilities.[9]

Fitch also affirmed the state's general obligation at A+ with stable outlook as of its report dated April 26, 2024. Fitch notes that "state has effectively leveraged recent fiscal momentum to accelerate progress on its long-term fiscal and liability challenges. Economic and revenue performance remains solid despite slowing from the pace immediately following the pandemic. More rapid revenue growth helped New Jersey to shrink its liabilities and maintain ending balances well in excess of recent historical experience. Despite recent improvements, high liabilities and elevated carrying costs are likely to remain longer-term constraints on its budget choices." [10]

Spotlight on a New Jersey Revenue Bond: Passaic Valley Water Commission

Moody's: Aa3 / Stable as of March 30, 2023
S&P: A+ / Stable as of March 27, 2023

Passaic Valley Water Commission is New Jersey's fourth largest water supplier and the largest publicly owned water supplier in the State. Moody's rates them Aa3 (no outlook). Drawing from the Passaic River system, the Commission is responsible for the collection, treatment, and delivery of drinking water to approximately 800,000 customers and twenty-four wholesale water suppliers in the Northern region of the state, delivering nearly 83 million gallons of drinking water per day. Their retail customer base spans six municipalities, twenty-five municipal customers, and several private utilities.

The Commission's fundamental financials are very strong, boasting a strong historical track record of debt service coverage, debt management, and margin performance. The Commission has kept their water rates relatively affordable compared to other water purveyors in the area, a benefit to portions of their service district that remain socioeconomically weak. Conservative management will allow the Commission to remain strong and adaptable as they prepare for future improvements to their operations.

Going forward, the Commission's strategic plan[11] encompasses several key projects to ensure they stay ahead of regulations. The plan includes a variety of proactive measures to provide more affordable, cleaner, water to their district, including: measuring and addressing new PFAs regulations (if needed), convert open-air storage reservoirs to more sanitary storage tanks, convert distribution methods to more cost-effective in-house options where available, developing a watershed management plan, maintaining cybersecurity programs, and creating more data-driven and systematic budgets, training programs, performance evaluations, and education opportunities for employees. This proactive approach should allow them to keep rates affordable and set the Passaic Valley Water Commission on a path for long-term stability and growth.

Sources:

1. State of New Jersey Budget in Brief, Fiscal 2026, as of February 25, 2025
2. Official Statement – Series 2024A New Jersey Transportation Trust Fund Authority, dated October 17, 2024
3. Bureau of Economic Analysis, as of December 31, 2024
4. Office of Legislative Services Tax and Revenue Outlook, April 1, 2025
5. Moody's, as of April 12, 2023
6. Official Statement – Series 2024A New Jersey Educational Facilities Authority, dated November 20, 2024
7. Moody's, as of November 1, 2024
8. Moody's, as of August 16, 2024
9. S&P, as of September 18, 2024
10. Fitch, as of November 27, 2024
11. Passaic Valley Water Commission 2023-2027 Strategic Plan, dated March 20, 2023

About risk

Municipal securities are subject to the risk that legislative or economic conditions could affect an issuer’s ability to make payments of principal and/or interest.

Junk bonds involve greater risk of default or price changes due to changes in the issuer’s credit quality.

The values of junk bonds fluctuate more than those of high quality bonds and can decline significantly over short time periods.

All fixed income securities are subject to two types of risk: credit risk and interest rate risk. Credit risk refers to the possibility that the issuer of a security will be unable to make interest payments and/ or repay the principal on its debt. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa. .

Municipal bonds are issued by state and local government agencies to finance public projects and services. They typically pay interest that is a tax in their state of issuance. Because of their tax benefits, municipal bonds usually offer lower pre-tax yields than similar taxable bonds. The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

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Past performance does not guarantee future results.

A credit rating is an assessment provided by a nationally recognized statistical rating organization (NRSRO) of the creditworthiness of an issuer with respect to debt obligations, including specific securities, money market instruments or other debts. Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest); ratings are subject to change without notice. NR indicates the debtor was not rated and should not be interpreted as indicating low quality.

For more information on Standard and Poor's rating methodology, please visit www.standardandpoors.com and select 'Understanding Credit Ratings' under 'About Ratings' on the homepage.

For more information on Moody's rating methodology, please visit https://ratings.moodys.io/ratings and select 'Rating Methodologies' on the homepage.

For more information on Fitch Ratings rating methodology, please visit www.fitchratings.com and select 'Criteria' under 'Resources' on the homepage. Then select 'Rating Definitions' under 'Resources' on the 'Contents' menu.

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*Source: Simfund as of March 31, 2025.