

FITCH RATES CONNECTICUT'S \$200MM GO BONDS 'AA'; OUTLOOK REMAINS NEGATIVE

Fitch Ratings-New York-02 June 2014: Fitch Ratings assigns an 'AA' rating to \$200 million in state of Connecticut general obligation (GO) bonds, 2014 series D.

The bonds are expected to sell via negotiated sale on or about June 11.

In addition, Fitch affirms the following outstanding ratings:

--Approximately \$14.5 billion outstanding GO bonds and notes at 'AA'.

The Rating Outlook remains Negative.

SECURITY

GO bonds to which the full faith and credit of the state will be pledged for payment of principal and interest.

KEY RATING DRIVERS

NEGATIVE OUTLOOK BASED ON BUDGET VULNERABILITY: The Negative Outlook reflects the state's reduced fiscal flexibility at a time of lingering economic and revenue uncertainty. The adopted budget for the current biennium relied on one-time items and anticipated little near-term progress in rebuilding fiscal flexibility. Personal income tax (PIT) revenues have been volatile in the first year of the biennium, with the state taking proactive action to ensure a modest fiscal 2014 budgetary surplus to be deposited to the rainy day fund.

HIGH WEALTH LEVELS: Connecticut is the nation's wealthiest state as measured by per capita personal income. Economic recovery has been slow and uneven since the recession, and the state's large and important finance sector continues to weaken.

CYCLICAL REVENUES AND SPENDING PRESSURE: State revenue performance is cyclical, while high fixed costs limit its ability to respond during revenue downturns.

HISTORICAL WILLINGNESS TO BUILD BALANCES: During past economic recoveries the state has demonstrated a willingness and ability to rapidly repay deficit borrowing and rebuild its rainy day balance. The current slow recovery has hampered rebuilding of reserves in the current biennium.

HIGH DEBT: Tax-supported debt is high for a U.S. state. Most GO bonds, excluding GO bonds issued to fund the teachers' retirement system, amortize rapidly.

SIGNIFICANT PENSION OBLIGATIONS: Unfunded liabilities for employees are significant, including for state employee and teacher pensions. The state fully funds actuarially calculated pension contributions and maintains a fixed amortization date. Additionally, the state has taken steps to reform retirement pension and health liabilities.

RATING SENSITIVITIES

VULNERABILITY TO ECONOMIC AND REVENUE CHALLENGES: An inability to meet or exceed budgeted forecast expectations could lead to a downgrade.

SUCCESS IN RAISING RESERVE BALANCES: Improved fiscal flexibility provided by higher than forecast revenues and material progress in rebuilding reserves could stabilize the state's credit outlook.

CREDIT PROFILE

Connecticut's 'AA' GO rating reflects its vast wealth and income resources, tempered by a comparatively high burden of debt, retirement liabilities and other fixed costs. The Negative Outlook is based on the state's inability in its adopted fiscal 2014-2015 budget to return to more structurally sustainable budgeting and rebuild flexibility at a time of unusually slow economic and revenue recovery. The budget was balanced only through a number of non-recurring resources, including refinancing the outstanding economic recovery notes (ERNs) that were used to fund deficits in the last recession.

Revenues in the first half of fiscal 2014 surged, with solid year-over-year gains in PIT collections prompting the state to elevate its forecast expectations. Following disappointing spring 2014 PIT collections, the state has reversed course, lowering forecast revenue growth down to just below originally budgeted levels and agreeing to a modest package of mid-biennium budget adjustments to ensure a \$43 million deposit to the budget reserve fund (BRF), the state's rainy day fund.

For additional information on the state's GO rating, please see 'Fitch Rates \$650MM Connecticut GO Refunding Bonds 'AA'; Outlook Remains Negative,' May 16, 2014, at www.fitchratings.com.

Contact:

Primary Analyst
Douglas Offerman
Senior Director
+1-212-908-0889
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Marcy Block
Senior Director
+1-212-908-0239

Committee Chairperson
Laura Porter
Managing Director
+1-212-908-0575

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria' (Aug. 14, 2012);

--'U.S. State Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

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Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015

U.S. State Government Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686033

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