STANDARD & POOR'S RATINGS SERVICES
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Summary:
University of Connecticut; General Obligation; General Obligation Equivalent Security

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Summary:

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Credit Profile		
US$300.0 mil GO rfdg bnds (Connecticut) ser 2016 A due 06/30/2036		
Long Term Rating	AA/Negative	New
US$42.0 mil GO rfdg bnds (Connecticut) ser 2016B due 06/30/2036		
Long Term Rating	AA/Negative	New

Rationale

Standard & Poor's Ratings Services has assigned its 'AA' long-term rating, and negative outlook, to the University of Connecticut's $300 million series 2016A general obligation (GO) bonds, and approximately $42 million series 2016A refunding GO bonds. At the same time, Standard & Poor's has affirmed its 'AA' rating, with a negative outlook, on the university's $1.1 billion parity debt outstanding.

We base the rating on the security provided by the state debt service commitment, which is defined by Public Act 95-230 (UCONN 2000), and the master indenture. The State of Connecticut ('AA/Negative' GO rating) is obligated to pay an annual amount sufficient to cover debt service on any state debt service commitment-authorized GO debt of the university. As part of the state's contract with bondholders, the funds necessary to meet the debt service commitment are paid by the state treasurer to the trustee from Connecticut's general fund and these payments are not subject to further legislative authorization or appropriation. Although the bonds are secured by a GO pledge of the university and do not carry a GO pledge of the state, in our view the debt service payment mechanism established by the statute and bond documents, which mandates and obligates the state to make annual payments without further legislative approval, provides strong bondholder security similar to Connecticut's GO pledge. Under the UCONN 2000 legislation enacted in 1995, the debt service commitment extends for the life of the bonds. The 2016A bonds will fund various capital projects for the university and a health center, while the refunding series 2016A bonds will refund debt outstanding for interest cost savings.

Connecticut has a long track record of supporting investments in the university. In 1995, the legislature approved the UCONN 2000 program to strengthen the university and the overall economic development prospects of the state. Since that time it has been expanded and extended by the legislature (21st Century UCONN) and includes three phases of investment to modernize, expand, and rehabilitate the university's physical plant. The current program extends through 2024 and totals $4.6 billion including $4.3 billion of bond authorization secured by the debt service commitment, of which $2.2 billion has been issued to date. The most recent expansion/extension was during the 2013 legislative session.

The University of Connecticut was founded in 1881, has 31,624 students, and offers seven undergraduate and 23 graduate and professional degree programs at 14 colleges and schools. In addition to the main campus in Storrs, Conn., there are five undergraduate regional campuses located throughout the state. A sixth campus houses the university's health center, which includes the school of medicine, the school of dental medicine, medical and dental clinics, and John Dempsey Hospital in Farmington; a seventh campus houses the School of Law. The university is the flagship institution of the State of Connecticut. The university has received a significant amount of support from the state in the form of operating appropriations and the issuance of the debt service commitment bonds to modernize, enhance, and expand its physical plant. (For more information on the University, please see our analysis published March 6, 2015, on RatingsDirect).

The state's 'AA' GO rating reflects what we view as Connecticut's:

- High wealth and income levels;
- Diverse economic base, which has experienced cyclical performance over time;
- Ongoing revenues and expenditures that are near structural alignment, assuming the governor's recommended mid-biennium cuts are enacted;
- Active monitoring of revenues and expenditures to identify and correct mid-fiscal year budget gaps, as exemplified by midyear budget adjustments made in fiscal years 2015 and 2016, and proposed for fiscal 2017; and
- Adequate operating liquidity, which has improved following the state's move to budgeting based on generally accepted accounting principles (GAAP), and issuance of GAAP conversion bonds in 2014 to provide liquidity to assist in the transition.

Offsetting factors, in our opinion, include a history of cyclical state budget performance and currently weak revenue trends. We expect revenue growth to remain slow for the next several years, the result of economic weakness in the state's high paying financial sector; however, our rating assumes the state will adjust for this in a structurally sound manner, as it has since coming out of the financial crisis. Connecticut previously issued debt to cover operating deficits during recessions, some of which remains outstanding from the last economic downturn. In our opinion, the state's current budgetary reserve is relatively small and would likely provide only a slim cushion in the event of another recession. Further offsetting factors include Connecticut's above-average debt levels, high unfunded pension liabilities, and large unfunded other postemployment benefit (OPEB) liabilities. These represent a significant fixed-cost pressure, which we expect to remain high for the foreseeable future.

(For additional information on the state of Connecticut's GO rating, see the article published March 9, 2016, on RatingsDirect.)

Outlook

The negative outlook mirrors our negative outlook on Connecticut's GO bonds. The negative outlook on the state reflects our view of budget pressures that could lead the state budget to fall out of structural alignment. Connecticut has been experiencing weak revenue growth, but enacted budget solutions to date have been largely structural, in our opinion. However, we see at least a one-in-three chance that the magnitude of future cuts needed, if current weak revenue trends continue, could lead to unstructural budget solutions--particularly due to high liabilities and low budget reserve balances that leave little margin in the event of an unexpected national economic slowdown. Spearheading the weak revenue growth is an economic concentration in the finance industry, which has been shedding jobs. Total state employment is back to its pre-recession peak, but high-paying financial industry jobs have been replaced by lower wage employment.

In our view, state budget pressure is evidenced in the multiple rounds of midyear budget cuts in fiscal years 2015 and 2016, substantial midyear budget adjustments needed for fiscal 2017, and the relatively sizable budget gap the state previously closed when it first enacted its fiscal 2016-2017 biennium budget. We believe budget pressure has contributed to the inability to add to modest reserve levels at a time of national economic growth. In addition, we believe projected out-year gaps beyond the current biennium, and a proposal by the governor, now tabled, to defer a portion of the state's pension liabilities through 2032, indicate potential out-year stress as well. Although enacted and proposed midyear adjustments to the enacted fiscal 2016-2017 biennium budget would leave Connecticut largely structurally balanced, we believe the state's flexibility to adjust to potential further midyear shortfalls may be constrained by several factors. These include budget reserve levels that are expected to remain modest through fiscal 2018; the potential difficulty in raising tax rates further, after already increasing them multiple times in recent years; and cost pressures due to high debt, pension, and OPEB liabilities. Should we believe the state is likely to fall out of structural budget alignment or adopt significant deferrals to its pension liabilities, we could lower our rating. However, if Connecticut appears able to implement structural budget solutions to future revenue shortfalls, we could potentially revise the outlook to stable during the remaining year of our two-year negative outlook horizon.

Related Criteria And Research

Related Criteria

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Bank Liquidity Facilities, June 22, 2007
- USPF Criteria: Standby Bond Purchase Agreement Automatic Termination Events, April 11, 2008
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011
- General Criteria: Methodology: Not-For-Profit Public And Private Colleges And Universities, Jan. 6, 2016

Ratings Detail (As Of March 22, 2016)		
University of Connecticut, Connecticut		
Connecticut		
University of Connecticut (Connecticut)		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GO		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GO		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GOEQUIV		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GOEQUIV		
Long Term Rating	AA/Negative	Affirmed

Ratings Detail (As Of March 22, 2016) (cont.)		
University of Connecticut (Connecticut) GO rfdg bnds (Connecticut)		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GO rfdg bnds		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut (Connecticut) GO (AGM) (SEC MKT)		
Unenhanced Rating	AA(SPUR)/Negative	Affirmed
Univ of Connecticut		
Long Term Rating	AA/Negative	Affirmed
University of Connecticut GO		
Unenhanced Rating	AA(SPUR)/Negative	Affirmed
Univ of Connecticut GO		
Unenhanced Rating	AA(SPUR)/Negative	Affirmed
Univ of Connecticut (Connecticut) GO		
Unenhanced Rating	AA(SPUR)/Negative	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.