22 NOV 2022

Fitch Rates Connecticut's $900 Million GO Bonds 'AA-'; Outlook Stable

Fitch Ratings - San Francisco - 22 Nov 2022: Fitch Ratings has assigned a 'AA-' rating to $900 million in State of Connecticut general obligation (GO) bonds, consisting of:

--$400 million GO Bonds (2022 Series E);

--$250 million GO Bonds (2022 Series F) (Social Bonds);

--$250 million GO Refunding Bonds (2022 Series G).

Par amounts are subject to change pending final sale.

The bonds are expected to be offered by negotiated sale the week of Nov. 28, 2022.

In addition, Fitch has affirmed the state's Issuer Default Rating (IDR) and outstanding GO bonds at 'AA-' and affirmed the ratings on bonds linked to the IDR as listed at the end of this release.

The Rating Outlook is Stable.

SECURITY

The GO bonds are supported by the full faith and credit of the state pledged to payment of principal and interest.

ANALYTICAL CONCLUSION

Connecticut's 'AA-' IDR reflects its superior gap-closing capacity, as well as its wealthy and diverse, yet slow-growing economic profile. The rating also incorporates the state's elevated liability burden, carrying costs and expenditure growth trends, which are likely to remain comparatively high over time.

Economic Resource Base

Connecticut has a diverse and mature economic base anchored by a large finance sector and important manufacturing and education and health sectors. Post-pandemic economic growth trails national trends. Connecticut has the highest per capita personal income of any state, though income growth slowed in the prior decade.

KEY RATING DRIVERS

Revenue Framework: 'a'

The state's largest tax revenue source, personal income tax (PIT), is subject to considerable cyclicality, although the state instituted measures to shield the general fund from its volatility. Sales and corporate income taxes further diversify the revenue base. Absent tax policy changes, underlying revenues are expected to grow only modestly over time, consistent with the state's wealthy and diverse but slow-growing economic profile. The state has unlimited legal ability to levy taxes.

Expenditure Framework: 'aa'

Connecticut's natural pace of spending growth is expected to outpace revenues, requiring ongoing budget controls. The state has consistently demonstrated the ability to cover its comparatively high fixed costs, including making full actuarial contributions to pensions for more than a decade, and it benefits from the large degree of budget autonomy common to states.

Long-Term Liability Burden: 'a'

The state's long-term liability burden is elevated and among the highest for U.S. states, but still considered moderate relative to personal income. Long-term debt consists primarily of GO and transportation borrowings, with much of GO borrowing undertaken on behalf of local schools. Net pension liabilities are a more significant burden, with the state carrying obligations for state retirees as well as for local school teachers. OPEB is also a significant liability, although one the state has been able to modify.

Operating Performance: 'aaa'

Resilience is bolstered by strong mechanisms that set aside in the budget reserve fund (BRF) volatile revenue collections over specific thresholds and a required excess margin of revenues over budgeted spending, enabling rapid accumulation of balances. Budget management powers and strong fiscal monitoring, including frequent revenue and budget forecasting, allow the state to identify budget under-performance and address emerging gaps.

RATING SENSITIVITIES

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

--Consistent economic and revenue growth at or above Fitch's long-term expectations for national inflation over the medium term, raising Fitch's assessment for revenue growth prospects;

--Material and sustained success in gradually lowering its elevated liability burden to less than 10% of personal income, while actively managing a comparatively high fixed cost burden.

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

--Weakening of budget management policies and practices that materially amplifies structural challenges;

--Actions that elevate the state's liability burden closer to or above 40% of personal income.

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.

CURRENT DEVELOPMENTS

Connecticut Budgetary Update

Strong budgetary management policies, including relatively recent mechanisms that accelerate deposits to the budget reserve fund (BRF), and robust revenue performance have facilitated marked improvement to the state's financial position. Specific tools include a volatility cap that shifts non-withholding PIT and pass-through entities tax receipts above a threshold to the BRF, and a revenue cap mechanism that shifts a required excess of budgeted revenues over spending to the BRF.

State revenue collections have exceeded prudent budgetary expectations since the pandemic's onset. The state ended fiscal 2022 with a $4.3 billion surplus, around 20% of fiscal 2022 general fund appropriations. The state added $200 million to the BRF balance in fiscal 2022, bringing it to the full cap of 15% of appropriations ($3.3 billion).

In fiscal 2022, the state also transferred an additional $5.5 billion in revenues above the volatility and revenue caps to state teacher and employee pensions to lower the state's liabilities: $3.4 billion in fiscal 2022 and $2.1 billion in fiscal 2023. Higher baseline spending for debt service, pensions and healthcare, among other needs, are partly offset by administrative efficiencies from an anticipated wave of state employee retirements.

Connecticut's fiscal 2023 budget includes some sizeable one-time and recurring tax cuts totaling $643 million in fiscal 2023. One-time policies include a $250 child tax credit funded from fiscal 2022 surplus ($125 million), as well as expansions to the state earned income tax credit ($43 million) and reductions to state unemployment insurance taxes ($40 million). Recurring tax cuts include expended property tax credits ($60 million per year) and reduced car tax mill rates ($100 million per year).

Connecticut is also one of a handful of states implementing a gas tax holiday. The nine-month gasoline tax break is projected to reduce Special Transportation Fund (STF) revenue by a combined $240 million in fiscal 2022 and 2023. Lost gas tax revenues were offset by larger-than-anticipated revenues in other streams, especially Gross Receipts Taxes on Oil Companies, which rose sharply amidst elevated petroleum prices. While affordable, this gas tax holiday nonetheless results in less funding available for transportation needs.

Federal Relief Provides Critical Support

Under the $1.9 trillion American Rescue Plan Act of 2021 (ARPA), Connecticut received $2.8 billion in direct federal aid to the state. The state projects it will spend or allocate all but $200 million of these funds by the end of fiscal 2023. While the enacted budget and outyear forecasts incorporate use of federal stimulus aid for operating needs, they also anticipate budget surpluses and sizable one-time spending, thereby lessening the risk of a fiscal cliff as federal aid rolls off.

Connecticut Economic Update

Connecticut's economy was affected by the pandemic and related public health measures in early 2020, and recovery has been uneven. The state's 13% decline in nonfarm payrolls from February through April 2020 was somewhat less than the national decline of 15%, and Connecticut's rebound in nonfarm payrolls has now surpassed the national recovery after lagging through the first quarter of 2022. By September 2022, 89% of lost state jobs have been recovered compared to the national rate of 104%.

Connecticut's unemployment rate has nonetheless improved to near all-time lows. The monthly unemployment rate for September 2022 was 4.0% versus the 3.5% national rate. The state's employment-to-population ratio (EPOP) of 62.0% in September 2022 is almost three percentage points below its pre-pandemic ratio of 64.6% in February 2020. Connecticut's September 2022 EPOP places it somewhat higher than the national EPOP of 60.1%. See "U.S. States - Labor Market Quarterly Tracker - 2Q22 (Employment Recovery Resilient Despite Recession Concerns and Inflation)" on fitchratings.com.

CREDIT PROFILE

Related Ratings

In conjunction with the affirmation of the state's IDR, Fitch has affirmed the ratings on bonds that are notched off of the IDR based on various appropriation structures:

--University of Connecticut state debt service commitment bonds, subject to annual appropriation, at 'A+';

--Connecticut Higher Education Supplemental Loan Authority state supported revenue bonds at 'A+';

--Capital Region Development Authority (formerly known as the Capital City Economic Development Authority) appropriation-backed parking and energy fee revenue bonds, 2004 series B and series 2018 refunding bonds at 'A+';

--Connecticut Development Authority general fund obligation bonds series 2004A at 'A+';

--Connecticut Innovations general fund obligation bonds series 2014A at 'A+'.

The Rating Outlook is Stable.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

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.

Fitch Ratings Analysts

Bryan Quevedo
Director
Primary Rating Analyst
+1 415 732 7576
Fitch Ratings, Inc. One Post Street, Suite 900 San Francisco, CA 94104

Douglas Offerman
Senior Director
Secondary Rating Analyst
+1 212 908 0889

Karen Krop
Senior Director
Committee Chairperson
+1 212 908 0661

Media Contacts

Sandro Scenga
New York
+1 212 908 0278
sandro.scenga@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Connecticut, State of (CT)	LT IDR	AA-	Affirmed		AA-

ENTITY/DEBT	RATING			RECOVERY	PRIOR
[General Government]					
• Connecticut, State of (CT) /General Obligation - Unlimited Tax/ 1 LT	LT	AA-	Affirmed		AA-
• Connecticut, State of (CT) /Special Capital Reserve Fund/ 1 LT	LT	A+	Affirmed		A+
• Connecticut, State of (CT) /State Appropriation/ 1 LT	LT	A+	Affirmed		A+
• Connecticut, State	LT	A+	Affirmed		A+

ENTITY/DEBT	RATING			RECOVERY	PRIOR
of (CT) /State Contract/ 1 LT					
• Connecticut, State of (CT) /UConn State Debt Service Commitment/ 1 LT	LT	A+	Affirmed		A+

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (pub.04 May 2021) (including rating assumption sensitivity)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

Connecticut, State of (CT)	EU Endorsed, UK Endorsed

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