State of Connecticut – G.O.

Issuer: State of Connecticut		
Assigned	**Rating**	**Outlook**
General Obligation Bonds (2024 Series F)	AA+	Stable
General Obligation Bonds (2024 Series G) (Social Bonds)	AA+	Stable
General Obligation Refunding Bonds (2024 Series H)	AA+	Stable
Affirmed	**Rating**	**Outlook**
General Obligation Bonds	AA+	Stable

Methodology:

U.S. State General Obligation Rating Methodology

ESG Global Rating Methodology

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Rating Summary: The long-term rating for the State of Connecticut's General Obligation Bonds reflects the State's strong credit profile and its maintenance of certain statutory fiscal guardrails since FY 2017 which have accommodated strong reserves and progress in addressing its large unfunded pension liabilities.

Proceeds of the 2024 Series F Bonds will be used to fund capital projects throughout the State. Proceeds of the 2024 Series G Bonds (Social Bonds) will be used to fund school construction projects. Proceeds of the 2024 Series H Bonds will be used to refund some or a portion of outstanding 2014 Series F and 2014 Series G bonds for present value savings. A portion of the proceeds of each series will additionally be used to pay the costs of issuance.

The State first implemented enhanced statutory fiscal guardrails in FY 2018 which it covenanted to maintain with respect to certain general obligation bondholders through June 30, 2023. Renewed guardrails were enacted and covenanted in FY 2024 that will be in place through at least FY 2028. Among the guardrails is a requirement to annually direct unappropriated general fund balances at fiscal year-end toward the State's budget reserve fund (BRF or rainy day fund) and the maintenance of a revenue volatility cap requiring the most volatile components of personal income tax receipts, in excess of an indexed threshold, to be deposited into the BRF. Any BRF balance exceeding 18% of subsequent-year appropriations at year-end, as well as half of any balance between 15% and 18% of subsequent year-appropriations at year-end, is required to be deposited as supplemental contributions toward the State's unfunded pension liabilities, among other measures. The legislation was passed unanimously by both legislative chambers signaling broad continuing support for the conservative financial practices that have bolstered the State's financial position since FY 2017.

The guardrails resulted in a BRF funded to the statutory limit in each of the last five years and $7.66 billion in supplemental pension contributions since FY 2020. The BRF balance increased from just $213 million at FYE 2017 to an estimated $5.05 billion or 22.1% of current FY 2025 appropriations. The projected BRF balance in excess of the reserve limit at FYE 2024 ($941 million) is to be deposited toward unfunded pension liabilities by the end of the 2024 calendar year, supplementing the $3.60 billion actuarially determined employer contribution (ADEC) already appropriated for FY 2024, marking a fifth consecutive year of pension contributions in excess of the ADEC.

The State's general fund is estimated to have ended FY 2024 with a $404 million surplus. Gross general fund receipts are estimated to have declined 0.8% YoY to $24.0 billion as revenues continue to moderate from the record level achieved in FY 2022 corresponding with broad federal stimulus and particularly strong capital market returns. Personal income and pass-through entity tax proceeds are estimated to have exceeded the revenue volatility cap by $1.33 billion, with this excess directed to the BRF, resulting in estimated general fund revenues available for appropriation of $22.7 billion, a decline of 0.6% YoY. Total appropriations in contrast are expected to have increased 0.3% YoY to $22.3 billion. The FY 2025 budget is the second year of the State's budget biennium and began on July 1, 2024. A $113 million surplus is estimated for FY 2025 based upon August 20, 2024 revenue estimates and adopted expenditures.

Connecticut's economy has recovered significantly from the early months of the pandemic. Seasonally adjusted unemployment in July 2024 was 3.6%, a level lower than the U.S. average at 4.3%. Wealth levels remain very high, with per capita personal income of $87,447 at 128% of the national average in 2023. The longer-term economic growth trends in the State have been sluggish with real gross state product (GSP) growth of just 3.1% between 2017 and 2023, significantly lower than the New England regional growth of 11.7% and National growth of 14.1%.

The State has high debt levels, but this partly reflects its practice of issuing general obligation debt for certain university projects and for purposes that municipal entities and counties fund in other states, such as local school construction. Fixed costs (debt service, OPEB and pension) were 20.2% of general government expenditures in FY 2023, which KBRA views as high. Debt amortization is favorable with about 81% of general obligation principal scheduled to retire within 10 years.

The Stable Outlook reflects Connecticut's diverse and high wealth economic base, strong reserve position, and effective financial management practices, which together provide a solid foundation for future financial performance.

Key Credit Considerations

The rating actions reflect the following key credit considerations:

Credit Positives

- State is estimated to have completed FY 2024 with a BRF balance exceeding the statutory cap at 18% of general fund appropriations and is positioned to direct surplus resources toward supplemental pension contributions for a fifth consecutive year.
- Strong financial management framework and recent extension of enhanced statutory fiscal guardrails through at least FY 2028 position the State for strong operating results.
- Strong wealth levels with the second highest per capita personal income level among all states.

Credit Challenges

- Lower relative growth in the economic indicators of population, employment, and gross state product, although there are recent signs of growth in population.
- Unfunded pension liabilities and tax-supported debt burden are high relative to personal income, each more than 3x the respective U.S. average. However, the State borrows for many local purposes and the comparison on a combined state and local basis is more moderate.

Rating Sensitivities

▪ Significant improvement in the funded ratios for the State's pension systems.	+
▪ Structural operating deficits in the general fund. ▪ Sustained weakening in the State's employment base and economic activity.	-

Rating Highlights	
Per Capita Personal Income (2023) (in dollars)	$87,447
as a % of U.S.	*128%*
Population (2023)	3,617,176
Growth 2010 to 2023	*1.0%*
Real GDP, % Change 2017 to 2023	
Connecticut	3.1%
New England	11.7%
United States	14.1%
Budget Reserve Fund Balance ($ in millions)	
FYE 2019	$2,506
FYE 2020	$3,013
FYE 2021	$3,112
FYE 2022	$3,313
FYE 2023	$3,316
FYE 2024 (Preliminary)[1]	$4,105
Direct Debt (10/1/2024) ($ in millions)	$24,322
Net Pension Liability ($ in millions)	$37,752
Fixed Costs as a % of Governmental Expenditures (FY 2023)	20.2%

(1) Reflects preliminary balance after the expected statutory transfer of $941 million for SERS/TRS pension contributions in excess of the actuarially determined employer contribution.

Rating Determinants (RD)	
1. Management Structure, Budgeting Practices and Policies	AAA
2. Debt and Additional Continuing Obligations	A+
3. Financial Performance and Liquidity Position	AA+
4. State Resource Base	AA-

A discussion of each rating determinant and can be found in prior KBRA reports, the most recent of which is dated July 1, 2024.

RD 3: Financial Performance and Liquidity Position Update

Figure 1

General Fund Revenues and Expenditures
Budgetary Modified Cash Basis (FYE June 30) (dollars in millions)

	Actual										Preliminary / Estimated		
	2019	Δ YOY (%)	2020	Δ YOY (%)	2021	Δ YOY (%)	2022	Δ YOY (%)	2023	Δ YOY (%)	2024 Preliminary	Δ YOY (%)	2025 Estimated
Revenues													
Personal Income Tax	$ 9,640	-2.5%	$ 9,398	10.0%	$ 10,340	17.3%	$ 12,132	-7.5%	$ 11,223	5.2%	$ 11,804	0.7%	$ 11,883
Pass-through Entity Tax	1,172	6.0%	1,242	24.8%	1,550	48.9%	2,308	-11.2%	2,048	-3.8%	1,969	0.0%	1,969
Less: Volatility Cap Deposit	(950)		(530)		(1,241)		(3,047)		(1,322)		(1,326)	-12.3%	(1,164)
Net PIT and Pass-Through Entity Tax	9,862	2.5%	10,109	5.3%	10,649	7.0%	11,392	4.9%	11,950	4.2%	12,447	1.9%	12,688
Federal Grants (excl. ARPA)	2,084	-13.8%	1,797	-16.7%	1,496	29.3%	1,935	3.3%	1,998	3.5%	2,067	-8.4%	1,894
Sales and Use Tax	4,338	-0.5%	4,318	11.0%	4,793	0.5%	4,818	2.6%	4,945	0.5%	4,967	2.7%	5,104
Corporate Income Tax	1,061	-11.9%	934	23.4%	1,153	21.5%	1,401	8.2%	1,517	2.7%	1,557	0.2%	1,561
Excise Taxes (Alcohol and Cigarettes)	421	-0.4%	419	2.6%	430	-5.7%	406	-8.5%	371	-9.3%	336	-3.8%	324
Indian Gaming Payments	255	-35.6%	164	39.4%	229	8.7%	249	12.2%	279	9.6%	306	-0.7%	304
Statutory Transfers from Other Funds	110	24.0%	136	-15.8%	115	10.2%	126	-10.9%	113	-12.0%	99	10.5%	109
Other	1,519	-48.3%	785	112.3%	1,667	-0.2%	1,664	-0.8%	1,652	-45.6%	899	41.2%	1,270
Total Revenues	**19,650**	-2.3%	**19,194**	7.0%	**20,531**	7.1%	**21,991**	3.8%	**22,823**	-0.6%	**22,679**	2.5%	**23,252**
Expenditures													
General Government	653	-2.8%	635	1.8%	646	16.0%	750	24.6%	934				
Public Safety	272	3.2%	281	1.3%	284	6.9%	304	13.9%	346				
Conservation and Development	170	0.9%	172	10.4%	189	23.0%	233	1.5%	237				
Health and Hospitals	1,194	0.7%	1,203	3.4%	1,244	2.6%	1,276	9.3%	1,395				
Human Services	4,312	1.0%	4,357	-2.3%	4,258	4.4%	4,445	11.8%	4,969				
Education, Libraries and Museums	5,208	-1.0%	5,155	2.9%	5,304	7.4%	5,698	6.4%	6,060				
Corrections and Judicial	1,968	1.8%	2,004	-0.5%	1,994	-4.1%	1,912	11.9%	2,139				
Debt Service	2,225	-0.9%	2,205	0.5%	2,216	4.9%	2,325	-5.4%	2,200				
Other	3,247	-2.1%	3,179	3.7%	3,297	12.5%	3,709	5.7%	3,919				
Total Expenditures	**19,249**	-0.3%	**19,189**	1.3%	**19,431**	6.3%	**20,652**	7.5%	**22,199**	0.3%	**22,275**	3.9%	**23,139**

Source: Annual Financial Reports of the State Comptroller, State Comptroller Letters dated August 20, 2024, and September 12, 2024 Credit Presentation

Figure 2

Budget Reserve Fund Summary Operations
Budgetary Modified Cash Basis (FYE June 30) (dollars in millions)

	2019	2020	2021	2022	2023	2024 Preliminary	2025 Estimated
Beginning BRF Balance	$ 1,185	$ 2,506	$ 3,013	$ 3,112	$ 3,313	$ 3,316	$ 4,105
Transfers to General Fund	-	-	-	-	-	-	-
Transfers from General Fund (Outside of Volatility Cap)	371	39	476	1,261	555	404	113
Volatility Cap Deposit	950	530	1,241	3,047	1,322	1,326	1,164
Ending BRF Balance Before Statutory Post-Close Transfers to SERS/TRS	**2,506**	**3,074**	**4,730**	**7,420**	**5,190**	**5,046**	**5,382**
as a % of Ensuing FY Net GF Approps.	*13.1%*	*15.0%*	22.8%	33.4%	23.3%	22.1%	TBD
Statutory Transfer to SERF and TRS Following Year End	-	(62)	(1,618)	(4,107)	(1,875)	(941)	TBD
Ending BRF Balance After Statutory Post-Close Transfer to SERS/TRS	**2,506**	**3,013**	**3,112**	**3,313**	**3,316**	**4,105**	TBD
as a % of Ensuing FY Net GF Approps.	*13.1%*	*15.0%*	*15.0%*	*15.0%*	*15.0%*	*18.0%*	TBD

Source: Annual Financial Reports of the State Comptroller, OPM Letter dated August 20, 2024 and Rating Agency Presentation dated September 12, 2024.

Bankruptcy Assessment

Under Chapter 9 of the U.S. Bankruptcy Code, State governments are not permitted to petition courts for protection from creditors, including holders of their general obligation debt.

ESG Management

KBRA typically analyzes Environmental, Social, and Governance (ESG) factors through the lens of how issuers plan for and manage relevant ESG risks and opportunities. More information on KBRA's approach to ESG risk management in public finance ratings can be found here. Over the medium-term, public finance issuers will likely need to prioritize ESG risk management and disclosure with the likelihood of expansions in ESG-related regulation and rising investor focus on ESG issues.

KBRA analyzes many sector- and issuer-specific ESG issues but our analysis is often anchored around three core topics: climate change, with particular focus on greenhouse gas emissions; stakeholder preferences; and cybersecurity. Under environmental, as the effects of climate change evolve and become more severe, issuers are increasingly facing an emerging array of challenges and potential opportunities that can influence financial assets, operations, and capital planning. Under social, the effects of stakeholder preferences on ESG issues can impact the demand for an issuer's product and services, the strength of its global reputation and branding, its relationship with employees, consumers, regulators, and lawmakers, and, importantly, its cost of and access to capital. Under governance, as issuers continue to become more reliant on technology, cybersecurity planning and information management are necessary for most issuers, regardless of size and industry.

Environmental Factors

Emission Targets: Connecticut has climate-related goals in place: State statute mandates 45% and 80% reductions in greenhouse gas emissions below 2001 levels by 2030 and 2050, respectively, and 10% and 25% decreases in water consumption and waste disposal, respectively, versus 2001 levels by 2030. The Connecticut Department of Energy and Environmental Protection's (DEEP) annual Greenhouse Gas Emissions Inventory, which measures progress toward these targets, noted in 2021 that data through 2018 indicated the State is lagging, particularly because of transportation emissions.

Physical Climate Risk: Connecticut faces risks from sea level rise, flooding, and severe coastal storms, as most of its population lives near the coast. The State has warned that rising sea levels could bring tidal flooding, even without storms, to infrastructure such as rail lines and I-95. In 2019, the Connecticut Institute for Resilience & Climate Adaptation, a joint program of DEEP and the University of Connecticut, recommended that planning incorporate a 20-inch sea level rise by 2050, and considered subsequent increases as likely. CIRCA's work includes its Municipal Resilience Grant Program to fund local resilience projects and involvement in Resilient Connecticut, which aims to craft a long-term resilience plan for the State and is expected to include regional risk assessments.

Social Factors

The State government has both long-running and new initiatives aimed at social equity. The decades-old Commission on Human Rights and Opportunities, for example, enforces civil and human rights law and regulations, including affirmative action plans at state agencies. Recent efforts include the passage of legislation declaring racism as a public health crisis and creation of a Social Equity Council that seeks to compensate neighborhoods most-affected by the "war on drugs" with revenue from the upcoming adult-use cannabis program.

Governance Factors

Cybersecurity: The State has employed a Chief Information Security Officer since FY 2021, evidencing an increased focus in this area. In March 2021, Governor Lamont announced a multi-year initiative intended to centralize how the Department of Administrative Services manages the state government's IT functions. In January 2022 the State began operation of the Department of Administrative Services / Bureau of Information Technology Solutions (DAS/BITS), providing wide-ranging shared services including infrastructure, applications, and user support. The State additional operates under a State Cyber Disruption Response and Plan and a Cyber Incident Response Plan, which was updated in January 2024. The State has not disclosed any notable or significant data breaches in recent years.