S&P Global Ratings

RatingsDirect®

Connecticut; Gas Tax

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Credit Profile		
US$1000.0 mil spl transp oblig bnds transp infrac purps ser 2024A due 07/01/2045		
Long Term Rating	AA/Stable	New
US$380.0 mil spl tax oblig bnds transp infrac purp ser 2024B due 07/01/2030		
Long Term Rating	AA/Stable	New
Connecticut GASTAX		
Long Term Rating	AA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AA' long-term rating to Connecticut's $1 billion senior-lien special tax obligation (STO) bonds, 2024 series A, and approximately $380 million STO refunding bonds, 2024 series B.
- At the same time, S&P Global Ratings affirmed its 'AA' long-term and underlying (SPUR) ratings on the state's $7.79 billion senior-lien STO bonds outstanding.
- The outlook is stable.

Security

The state's 2024 series A, 2024 series B, and STO bonds outstanding are secured by a first-lien pledge of revenues collected statewide that are credited to and deposited into the state's special transportation fund (STF). In accordance with the enabling act and bond provisions, pledged revenues are appropriated and do not require further legislative approval. Pledged revenues include:

- A portion of the state's general retail sales and use tax, as specified under state statutes;
- Motor fuels taxes (including gasoline, special fuels, and motor carrier road taxes);
- Taxes on oil companies;
- Motor vehicle receipts (registration fees for motor vehicles, license, permit, and fee revenue); and
- Other transportation-related receipts, funds, and moneys.

The 2024 series A and B bonds will be the first issued under an amended and restated indenture, approved by the State Bond Commission on Oct. 22, 2024. Notably, the amended and restated indenture does not require the state to fund a debt service reserve fund (DSRF) at maximum annual debt services (MADS), and it permits the state to establish a DSRF on a series-by-series basis where it deems appropriate. The series 2024 bonds will not be secured by a DSRF, which we view as neutral within our credit analysis due to the strong-to-very strong coverage and low volatility of pledged revenues. In addition, the indenture enables the state to elect, on a series-by-series basis, the timing of debt service deposits with the trustee, including up to the date they are due. However, Connecticut will continue to make monthly deposits to the trustee for principal and interest on the series 2024 bonds. Some future indenture amendments and modifications require the consent of 60% of bondholders of the debt outstanding, which the state does not expect to occur until at least 2028.

Proceeds from the 2024 series A bonds will finance various projects of the Connecticut Department of Transportation's (DOT) transportation infrastructure program and proceeds from the 2024 series B refunding bonds will be used to refund various STO bonds outstanding for debt service savings and elimination of sequestration risk from Build America Bonds (BABs) subsidies.

Credit overview

The 'AA' rating incorporates our view of Connecticut's very strong economic fundamentals, anchored by a large statewide taxing base from which pledge revenues are collected, and the diverse composition of pledged revenues deposited into the STF that have exhibited low volatility across economic cycles. While we anticipate Connecticut will continue to issue debt to fund its transportation infrastructure program, the state has demonstrated active management of the STF, both in its sizing of debt issuances associated with the DOT's large transportation capital program, its front-loaded debt service schedule, and its periodic expansion of revenues deposited to the fund, which we believe will continue to provide strong-to-very strong coverage above 2.0x.

In response to inflation pressures, Connecticut was one of two states that suspended the motor fuel tax for portions of fiscal years 2022 and 2023 to provide taxpayer relief. After resuming full-year collection of the state's 25-cent per gallon motor fuels tax, actual fiscal 2024 pledged revenues (S&P Global Ratings-calculated net of federal payments and interest income) totaled $2.3 billion (or 16.4% over the previous year). The state also benefitted partially from better-than-forecasted growth in motor vehicle license, permit, and fee receipts. Based on actual fiscal 2024 pledged revenues, we calculate annual debt service coverage (DSC) of approximately 2.7x in 2024 and MADS coverage of 2.5x, occurring in 2025.

Following stronger-than-anticipated revenue performance in the previous four fiscal years, the state accumulated an excess STF balance of $972 million (or 45.9% of fiscal 2024 debt service and operating expenditures). During the 2024 legislative session, Connecticut's legislature approved the one-time use of cumulative excess balances held in the STF (above 18% of expenditures) to redeem several transportation-related obligations outstanding. As of Nov. 1, 2024, the state estimates approximately $526.9 million will be available for bond redemptions or cash defeasances of STO bonds, which will generate approximately $689.4 million in total debt service savings (or approximately $60.3 million of present value savings) between fiscal years 2025 and 2036. In our view, these one-time measures will provide the state with some additional capacity to accommodate increased borrowing and debt service costs to fund the DOT's five-year transportation capital program.

We generally expect DSC will remain resilient despite the state's forecasted expectations that pledged revenues will dip below the 7.2% average annual growth rate achieved between fiscal years 2017 and 2024. Connecticut's Office of Policy and Management's (OPM) projects out-year pledged revenues growth rates in the STF will decline by 1.3% in fiscal 2025 and gradually normalizing of revenue growth at 1.2%, 1.6%, and 1.5% between fiscal years 2026 and 2028, respectively. At the same time, the state projects cumulative fiscal year-end surplus balances in the STF will rebound to $583.0 million through the end of fiscal 2026. However, structural out-year gaps could materialize in fiscal years 2026, 2027, and 2028 as revenue growth slows and debt service expenditures increase. Assuming no revenue enhancements or adjustments to the state's $5.1 billion in prospective transportation bond financing needs over this period, OPM projects a revenue-expenditure imbalance that will need to be addressed pursuant to the state's constitutional requirement to adopt a balanced budget. Therefore, a key credit consideration will be the state's ability to identify alternative and sustainable revenue sources and raise revenue when necessary to fund the state's transportation infrastructure program and maintain steady coverage levels.

Key considerations in our assessment of the credit quality of the pledged STF revenues include:

- Very strong and diverse statewide economic base of more than 3.6 million people generating pledged revenues, coupled with recent demonstrated resilience of the state's economic profile, which has contributed to a 57.5% cumulative growth rate in pledged revenues between fiscal years 2017 and 2024.
- Sales, motor fuel, and other motor vehicle activity that has historically demonstrated low volatility of pledged STF revenues, coupled with the state's regular forecasting of conditions within the fund, and its history of implementing periodic increases to motor fuel tax rates, fees, and allocations of pledged revenues or approval of new revenue streams dedicated to the STF.
- Strong-to-very strong coverage and liquidity, with senior-lien MADS coverage of 2.5x (occurring in fiscal 2025), incorporating both fiscal 2024 actual pledged revenues and estimated debt service following the current bond issuances.
- Good bond provisions and Connecticut's strong commitment to its transportation program, including a 2.0x additional bonds test (ABT) for both first- and second-lien bonds and establishment of a 2.0x rate covenant, which we view as credit stabilizing factors and likely to limit coverage dilution as the state funds additional transportation debt issuances in its capital improvement plan (CIP).
- A close linkage to the Connecticut general obligation (GO) rating, and in our view, any rating action on the state's general creditworthiness would also have a corresponding effect on the rating of the state's STO bonds.

Environmental, social, and governance

We consider Connecticut's environmental and governance factors to have a neutral influence on our credit analysis and are consistent with similar obligations secured by sales, motor fuels, and other related taxes. Connecticut's strong management and comprehensive long-term capital planning incorporates hardening of transportation assets and other infrastructure helps to mitigate exposure to physical risks--including severe weather events, coastal, and inland flooding risks. In addition, we consider the state's social capital risks to have a neutral influence in our credit analysis for Connecticut, although we recognize demographic trends--including an aging population with slow growth--could present long-term social capital considerations to Connecticut's economy, consumption trends, and changing transportation needs that could affect growth in pledged revenues and service levels. We believe the broad taxing base and diversity of pledged revenue, coupled with forecasting the potential effects of long-term revenue pressures and adjusting revenue to reduce volatility in the STF help manage these risks.

Outlook

The stable outlook reflects our expectation that DSC could experience modest fluctuations as Connecticut issues additional debt to support substantial transportation-related capital needs, but we believe the state's diverse economic base and demonstrated timely adjustments to taxes and fees to sustain pledged revenue growth and stave off periodic cyclical pressures should keep DSC at levels that we consider strong to very strong over the outlook period.

Downside scenario

Based on our view that the STO bonds exhibit a close linkage to Connecticut's general creditworthiness, if we lower the state GO rating, it will likely result in a corresponding negative rating action on the STO. Alternatively, we could lower the rating if a significant or sustained deterioration of pledged revenues or a substantial increase in the STO debt burden materially weakens our view of coverage.

Upside scenario

The application of our priority-lien tax revenue debt criteria limits the STO bonds to no more than one notch above Connecticut's general creditworthiness. Therefore, raising the STO rating would correspond with our raising the state GO rating.

For more information regarding Connecticut's long-term credit fundamentals, see our full analysis, published Sept. 20, 2024, on RatingsDirect.

Credit Opinion

Economic fundamentals: very strong

In our view, Connecticut's very strong economic fundamentals are supported by its large, statewide economic base from which pledged revenues are derived. Very strong wealth and income levels continue to anchor the state's economy, although we continue to monitor gross state product (GSP) and population trends, which have typically lagged the nation and could limit future growth prospects and economic activity in the state.

In 2023, Connecticut's per capita personal income was $89,899, or approximately 129% of the nation, ranking highly among states. However, we continue to monitor the state's personal income growth trends over the long-term and how that could translate to economic activity, particularly as its compounded annual personal income growth rate (CAGR) of 3.8% (2015-2023) continues to lag the U.S. CAGR (5.2%). Over the past 10 years, Connecticut's real GSP grew at just a 1.0% CAGR, well below that of the nation (2.4%) over the same period. S&P Global Market Intelligence projects the state's GSP growth (5.6% cumulative increase) could continue a slower path over the next four years compared with the nation (8.3% cumulative increase).

Revenue volatility: low

We believe pledged revenue securing the STO bonds will continue to exhibit low volatility based on a broad-and-well-diversified mix of pledged transportation-related revenues that have remained resilient across economic cycles, increasing by an average annual growth rate of approximately 7.2% from 2017-2024.

Sales and use tax allocations to the STF (36.5% of fiscal 2024 pledged revenues) comprise the leading share pledged revenues, while oil consumption-based taxes, including motor fuels taxes (21.8%) and oil companies' tax payments (15.5%) represent the next largest revenue sources. In our view, sales taxes, particularly those derived from auto sales, could exhibit greater sensitivity to changing economic conditions compared with per-gallon-fuel taxes or motor vehicle license fees, but we expect this revenue source will remain a relatively small share (approximately 5%) of pledged revenues over the long term. Connecticut projects a 0.7% average annual decline in motor fuel tax receipts between

2025 and 2028, while sales and use tax receipts are estimated to average 2.0% over the same period, which we view as reasonable relative to our expectations for U.S. and state economic growth, as well as increased fuel efficiency standards and changes in consumer trends..

In addition, we view Connecticut as actively managing the capacity of its transportation capital program, with regular forecasting of pledged revenues incorporated into OPM's forecasting, review of bonding requests by the state's bonding commission, and the legislature enacting revenue enhancements for transportation-related purposes, when necessary. The state increased allocations or introduced new sources that have supported growth in STO-pledged revenue to long-term debt associated with its statewide transportation improvement plan. Recent policy actions that have diversified and supported continued revenue growth include:

- In 2016, Connecticut made a statutory dedication of a 0.5% statewide general sales tax to the STF, and the legislature added dedicated sales and use taxes collected on the sale of new and used motor vehicles, which was fully phased in during fiscal 2023.
- In 2021, the state approved a highway use fee (effective Jan. 1, 2023) on certain heavy, multi-unit motor vehicles based on the weight and number of miles driven on public roads in the state. The state reported highway user fees generated approximately $60 million in 2024, and will grow modestly thereafter, although the state could continue to adjust projected annual growth rates from this source as additional use fee collection data becomes available.

Overall, state highway user receipts rebounded following a slight dip due to the COVID-19 pandemic. As more drivers transition to electric vehicles (EVs) or other vehicles with higher fuel efficiency, we expect that pledged revenues for state highway user tax revenue bonds will recognize shifts in revenue reliance over the long term, but we believe the overall sector will remain resilient. If motor fuel tax revenue losses become significant, we believe states will consider transportation-related revenue alternatives, but, to date, these industry shifts have not affected our ratings.

Coverage and liquidity: strong-to-very strong

We calculate actual pledged revenues for the fiscal year ended June 30, 2024--excluding pledged Build America Bonds interest subsidy or interest earnings for our DSC calculations--covered proposed future senior-lien MADS of $910.7 million, occurring in fiscal 2025, to be a strong-to-very strong 2.5x. Our MADS calculation also factors in the state's planned use of $526.9 million in cumulative excess from the STF to redeem certain bonds in fiscal year 2025.

The state projects annual DSC will remain above 2.0x over the ensuing five fiscal years, which we view as strong to very strong. Pro forma projections between fiscal years 2025 and 2028, which incorporate modest average annual growth of 0.6% in pledged revenue and factors in potential debt issuance of $5.1 billion (subject to approval by the state's bond commission), indicated coverage will decline to approximately 2.0x-2.1x. Estimated annual STO bond issuances range from $1.0 billion-$1.4 billion between fiscal years 2025 and 2028, but projected debt financing plans could change as the volume of projects, shifts in federal support, and lingering inflation-fueled effects augment project costs. Nevertheless, we view Connecticut's rapid debt amortization schedule--with nearly 66% of existing STO principal retired within the next 10 years, frontloaded debt service requirements, and conservative annual average pledged revenue growth projections from 2024-2028 should support stable DSC despite a potentially higher debt load.

Linkage to state general creditworthiness: close

Because the state collects the pledged revenues, we view the rating on the transportation revenue bonds as linked to Connecticut's creditworthiness. In our establishment of a one-notch upward limitation on the transportation revenue bond rating compared with the state GO rating, we factored into our analysis that Connecticut provides critical public services. In 2018, Connecticut voters approved a state constitutional amendment that continues directing any funding sources to the STF, including motor fuels and oil company and sales tax revenues, as long as the law authorizing the state to collect or receive them remains in existence. The amendment added state constitutional restrictions on the use of pledged transportation revenue once deposited to the STF in accordance with state statute against potential diversion of a portion of the pledged revenue stream. However, we believe it does not sufficiently mitigate the exposure of the STO rating from the operating risk of the state--as collector of the pledged taxes--to rate it above our one-notch upward limitation from the state rating.

In addition, Connecticut does not, in our view, benefit from a limited scope of operations or extraordinary expenditure flexibility, which we believe still exposes it to some operating risk in the collection and distribution of pledge revenues.

Connecticut--Key credit metrics	
	Metric
Economic data	
Economy	Very strong
EBI level per capita % of U.S.	121
Population (obligor)	3,603,982
Broad and diverse MSA	Statewide
Population (MSA)	
Financial data	
Revenue volatility	Low
Coverage and liquidity	Strong - very strong
Baseline coverage assessment	ABT
MADS coverage (x)	2.54
MADS year	2025
Annual debt service coverage (x)	2.68
Three-year pledged revenue change (%)	16.58
Bond provisions	
ABT (x)	2.00
ABT type	MADS
ABT period	Historical
DSRF type	None
Obligor relationship	
Obligor linkage	Close
PL rating limit (number of notches above OC)	1

Data points and ratios may reflect analytical adjustments. EBI--Effective buying income. MSA--Metropolitan statistical area. MADS-Maximum annual debt service. ABT--Additional bonds test. DSRF--Debt service reserve fund. PL--Priority lien. OC--Obligor creditworthiness.N/A--Not available. 3-pronged test--MADS, 10% of principal, or 125% of average annual debt service.

Ratings Detail (As Of November 13, 2024)		
Connecticut GASTAX		
Long Term Rating	AA/Stable	Affirmed
Connecticut GASTAX		
Long Term Rating	AA/Stable	Affirmed
Connecticut GASTAX (BAM)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut GASTAX (BAM)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut GASTAX (BAM) (SECMKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut GASTAX (BAM) (SECMKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut GASTAX (BAM) (SECMKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Connecticut GASTAX (BAM) (SECMKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.