

Research Update:

# Connecticut Series 2025 GO Bonds Rated 'AA-'; Outlook Is Stable

April 4, 2025

## Overview

- S&P Global Ratings assigned its 'AA-' long-term rating to the State of Connecticut's \$500 million general obligation (GO) bonds, 2025 series A, \$1.2 billion GO refunding bonds, 2025 series B, and \$300 million GO bonds (taxable), 2025 series A.
- At the same time, we affirmed our 'AA-' long-term rating on the state's GO debt outstanding.
- We also affirmed our 'AA-/A-1' dual rating on the state's series 2016C GO bonds and on the Capital Region Development Authority's series 2004B bonds, with liquidity support provided by Bank of America N.A.
- In addition, we affirmed our 'AA-' rating on debt secured by a special capital reserve fund, which we view to be on par with that of the state GO rating as state-supported GO-equivalent securities, including various issues by the Connecticut Housing Finance Authority, the Connecticut Health & Educational Facilities Authority, and Connecticut Green Bank.
- Lastly, we affirmed our 'A+' rating on the state's appropriation-secured debt and 'A-' rating on obligations secured by the state's moral obligation.
- The outlook on all long-term ratings is stable.

## Rationale

### Security

The state's GO debt is secured by the state's full faith and credit and its taxing power. We rate the state's appropriation debt that is subject to biennial legislative approval one notch below the GO rating reflecting appropriation risk. We also rate certain special obligations of Connecticut for which the state pledges legally available funds to make debt service payments on behalf of various public authorities, institutions, and municipalities. These funds are deemed appropriated by the state and do not require annual legislative approval, which we view as equivalent to Connecticut's GO pledge.

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We rate the moral obligation bonds three notches below the GO rating reflecting the contingent obligation of the state to replenish draws on the debt service reserve fund established for the bonds. Finally, the short-term component of the dual rating reflects the short-term rating on Bank of America N.A., which provides an enhancement for the bonds in the form of a standby bond purchase agreement.

Proceeds from the bonds will fund general government projects authorized under various bond acts of the state and refund existing bonds for refunding savings.

## **Credit highlights**

The rating reflects our view of Connecticut's structurally balanced financial performance and record-high budget reserve fund (BRF) balance, which, in our view, has been achieved through proactive management practices, including long-term financial forecasting to identify potential budget gaps and financial controls to manage expenditure growth and potential cyclical revenue pressures. The state's favorable economic metrics, specifically high per capita income, and gross state product, support our view of Connecticut's underlying credit quality. However, high debt and significantly underfunded pension and other postemployment benefits (OPEB) liabilities, which comprise a large share of its budget, remain a credit pressure. These liabilities could limit budgetary flexibility as the state navigates potentially slower economic and revenue growth conditions.

The state's January 2025 consensus revenue estimate forecasts fiscal 2025 total general fund revenue of \$23.7 billion, representing a 4.2% increase compared with 2024, followed by a 1.1% increase in fiscal 2026 and a 2.8% increase to \$24.6 billion in 2027. The state currently estimates an approximately \$396 million surplus for fiscal 2025, or 1.7% of projected general fund revenue (based on the consensus revenue estimate). The governor has proposed using \$300 million of the projected unappropriated year-end surplus to create and fund a universal preschool endowment (UPE) fund to expand preschool access by increasing availability and subsidizing the cost of offering spaces. The proposal also requires future budget surpluses, after deposits to the BRF up to the statutory maximum of 18% of net general fund appropriations, would be transferred to the UPE fund. Connecticut currently projects a \$1.4 billion volatility cap transfer resulting from certain volatile revenues (including the finals and estimates portion of income tax and pass-through entity taxes) to fund the state BRF up to its 18% statutory maximum. The state will use the remaining revenues above the volatility cap level to pay unfunded liabilities of the state employees retirement system (SERS) or the teacher's retirement system (TERS).

The governor's fiscal 2026-2027 biennial general fund budget proposal totals \$48.8 billion and builds in structural surpluses of \$304 million (1.3% of projected general fund revenue) and \$318 million (1.3%). The proposal also recommends a change to the calculation used to determine the threshold for the volatility cap by adjusting the fiscal 2017 base year (when the volatility cap was first enacted) to a five-year average (fiscal years 2012-2016). This proposed change would provide additional general fund revenues for general fund spending of approximately \$289 million and \$305 million in fiscal years 2026 and 2027, respectively. Nevertheless, we view the volatility cap and other fiscal guardrails enacted by the state as important financial buffers of the state's more volatile revenue streams, and we view the changes as modest relative to the amounts historically available above the cap threshold. However, we believe further efforts to shift more volatile revenues to fund recurring general fund spending could increase the state's exposure to economic downturns and pressures on budgetary performance. At the same time, an eroding commitment by the state to its statutory financial controls could weaken our view of these mechanisms to maintain budget stability and reduce its long-term fixed cost burden.

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The BRF is projected to remain fully funded, at 18% of general fund appropriations through the biennium, or \$4.5 billion at fiscal 2027 year-end which could be used to help fund potential deficits if revenues fall significantly below estimates. The budget includes modest tax relief, including increasing property tax credits, eliminating certain occupational license and renewal fees, and accelerating the elimination of the capital base tax. The tax relief proposals are expected to reduce revenue by \$121 million in fiscal 2026 and \$132 million in fiscal 2027.

Based on S&P Global Ratings Economics' most recent report, "Economic Outlook U.S. Q2 2025: Losing Steam Amid Shifting Policies, March 25, 2025, March 25, 2025," (published March 25, 2025, on RatingsDirect), the shifting policy mix is altering the U.S. economic outlook, with our assumptions reflected in a likely downshift in GDP growth in 2025. We now forecast the U.S. real GDP growth rate will slow to 1.9% in 2025 and 2026, representing a sizable deceleration from the 3.2% and 2.5% expansion seen in 2023 and 2024, respectively. The forecast also incorporates assumptions on tariffs, some of which have been implemented and others that are likely forthcoming. The risk of a sharper slowdown has increased amid persistent policy uncertainty, which could lead to precautionary spending and retrenchment by households and businesses. That said, S&P Global Ratings Economics does not see a recession as the most likely outcome yet, penciling in a 25% probability of a recession starting within the next 12 months (see "U.S. Business Cycle Barometer: Increasing Likelihood Of A Slowdown, March 13, 2025," published March 13, 2025). However, we acknowledge that the risk of a downturn will rise if current conditions weighing on growth and sentiment intensify. Notably, trade comprises a smaller proportion of Connecticut's gross product (11%) compared with the U.S. (20%), which could help mitigate potential negative effects from imposed and potential tariffs. Connecticut's economic fundamentals, specifically income and gross state product (GSP) growth, are projected to increase at a rate that is below the U.S. each year from 2024-2028. However, per capita metrics will remain generally stable and well above U.S. averages. Connecticut's broad and diverse industry composition--including the substantial presence of education and health services, financial services, insurance, and defense manufacturing--will continue to support the state's high per capita productivity and personal income levels well above the national average.

The state's ongoing efforts to fund its very high debt and significantly underfunded pension and OPEB will remain key credit considerations, although we expect funding progress and lowering very high fixed costs in the budget will be gradual. Supplemental SERS and TRS payments from budget surpluses and revenue volatility cap transfers from 2020-2024 have reduced unfunded pension liabilities across these plans by approximately \$8.6 billion, and additional contributions of \$1.4 billion are projected to be available from excess fiscal 2025 revenue which could continue to generate budget savings and chip away at Connecticut's substantial liability burden. The Office of Policy and Management (OPM) estimates that these additional pension paydowns have resulted in around \$731 million in annual budget savings.

Despite recent funding progress, combined debt service, pension, and OPEB costs comprise a comparatively high 30% of Connecticut's fiscal 2024 appropriations. When factoring in the state's high proportionate state-only share of entitlement programs (like Medicaid and other social assistance), all-in fixed costs comprise more than 50% of the state's appropriations, which we believe poses a significant potential barrier to closing budgetary gaps during future economic downturns. If excess pension contributions are sustained and we believe the overall size and growth trajectory of the state's long-term liabilities is meaningfully reduced, we could view these additional pension contributions as a credit strength.

The 'AA-' rating reflects our view of Connecticut's:

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- High income and GSP per capita metrics that rank among the highest in the U.S., fueled by a broad and diverse economic base across the financial services, education and health services, defense manufacturing, and professional and business services sectors.
- Recent financial predictability embedded within its institutional framework, albeit with some restricted flexibility to adjust spending due to a high fixed-cost burden.
- Active management, with regular monitoring of revenues and expenditures, including monthly reporting and consensus revenue forecasting three times annually, and authority of the executive branch to make mid-biennium adjustments to the budget.
- Budget reserves at historical highs, with expectations that balances in the BRF will be maintained at approximately 18% of net general fund appropriations through the fiscal 2026-2027 biennium.
- Very high debt and significantly underfunded pension and OPEB liabilities, which could pose a substantial impediment to solving future structural budget gaps during recessions.

### Environmental, social, and governance

Environmental, social, and governance factors do not materially influence our credit analysis for Connecticut. We consider the state's social capital risks to have an overall neutral influence on our credit analysis, as recent in-migration trends and agency-level planning, which anticipates future service needs, help mitigate potential demographic pressures. We view risk management, culture, and oversight risks as having a neutral influence on our credit analysis for Connecticut, although future changes could affect the state's high-to-very high fixed costs and potentially constrain expenditure flexibility and financial performance if left unmitigated. We view implemented reforms to the state's pension and OPEB plans and a strong policy framework, including forecasting fixed costs and statutory allowances to prefund its liabilities, as demonstrating the state's ability to manage fixed costs and helping to offset other long-term developing risks.

## Outlook

The outlook incorporates our expectation that the state will continue its commitment to recently extended statutory financial and debt controls, and our view that Connecticut's recent financial momentum and buildup of high reserves during a period of economic and revenue growth will help to address future budget uncertainties. We also believe the state will demonstrate a commitment to curbing future fixed-cost growth by transferring excess revenues and budget surpluses to pay down its high pension and OPEB liabilities, while also moderating GO debt issuance.

### Downside scenario

We could lower the rating if the state cannot reach consensus on recurring budget solutions that prioritize structural stability in future biennial budgets, or if it demonstrates a weakened commitment to financial controls or sustaining its reserve and liquidity position at currently high levels. We could also lower the rating if the debt and liability burden rises to a level that we view as less sustainable.

## Upside scenario

Although unlikely over the outlook period, we could raise the rating if the state demonstrates timely and consistent structural adjustments to balance future budgets and makes sustainable progress in reducing its overall debt, pension, and OPEB liability burden from its currently very high level.

## Credit Opinion

### Institutional Framework

In our view, Connecticut's institutional framework supports predictability, revenue and expenditure management, and transparency. Under its constitution, the state requires adoption of a balanced budget, but we view its flexibility to reduce spending as limited, given its historically comparatively high fixed cost and entitlement (Medicaid and other social services) structure.

Connecticut is not a voter-initiative state, and the framework governing both state-derived and federal revenue has generally historically been predictable, with no significant changes to revenue structure or operations in recent years. Appropriations are limited to 98.75% of annual projected revenues helping support budgetary balance. The state also adheres to a revenue volatility cap, that requires it to transfer business pass-through entity tax, and certain annual income tax revenue receipts above a set threshold to the BRF. Any excess money above the BRF's 18% statutory reserve cap is used to make additional payments toward the state's unfunded pension liabilities. The revenue volatility cap was designed to capture expected one-time windfalls from personal income tax and pass-through entity tax revenues to bolster reserves and address long-term liabilities, while also shielding Connecticut from historically cyclical income tax fluctuations. The legislature and executive branch have agreed to extend the volatility cap and appropriation limits through July 1, 2033, with an opportunity to revisit these provisions in 2028.

### Management

We consider Connecticut's management robust, reflecting our view that policies and practices are well embedded and likely sustainable.

Our assessment incorporates management's evolving practices and planning over the past three fiscal biennia as Connecticut demonstrated a firm commitment to the statutory provisions put into its bond covenants. We view these fiscal guardrails favorably, as they have resulted in more disciplined financial practices in the areas of debt, budget, and reserve management and more forward-looking planning that informs the executive branch and legislature's financial decision-making.

Key practices and policies of the state include:

- Consensus revenue estimates by the OPM and the legislature's Office of Fiscal Analysis as required by statute, on or by Nov. 10, Jan. 15, and April 30 of each year, that must cover a five-year period. The state's long-term financial planning includes a three-year forecast in addition to the biennial budget.

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- Statutorily required monthly revenue and expenditure forecasts measured against the budget, conducted by both OPM and Office of the State Comptroller. These two offices generate monthly reports projecting year-end surpluses or deficits.
- Well-embedded intra-year budget monitoring practices, and if the comptroller reports a projected general fund deficit of greater than 1%, the governor is required to file a deficit-mitigation plan. Although the governor might reduce appropriations, this is limited to 5% of total appropriations and 3% of any fund, with any additional reductions requiring legislative approval. The state is allowed to end the year in a deficit position, although statutory provisions provide that any new budget deficit after fiscal 2013 must be funded in the budget of the year following the next fiscal year.
- A comprehensive five-year capital improvement plan as part of the state's annual November update, which includes funding sources.
- Statutes prescribing the investment of state funds and debt management policies that guide amortization and issuance. Dedicated staff monitors investments and generates monthly reports. Connecticut also holds at least quarterly meetings with the investment advisory commission.
- Statutorily authorized BRF at a maximum of 18% of general fund appropriations, beginning July 1, 2024, an increase from the previous statutory maximum to 15%. State statutes prescribe that all unappropriated general fund surpluses must be transferred into the state's BRF, and that the fund can be drawn on only to fund operating deficits.

## Economy

Connecticut's GSP growth trailed the U.S. for much of the past decade, including each year from 2021-2024 and we forecast state GSP growth of 4.87% between 2025-2028 compared with 7.16% national growth. However, we recognize the state's highly skilled workforce and broad and diverse industry composition--including the substantial presence of education and health services, financial services, insurance, and defense manufacturing--anchor the state's high per capita productivity and personal income levels well above the national average.

The two largest contributing industries to state GSP are finance and insurance (27%), and professional and business services (14%). We view both industries as generally stable, but recognize occasional revenue volatility stemming from income tax collections that are partially derived from employee bonus pools that are highly dependent on corporate profits. However, the state's prudent implementation of and commitment to its revenue volatility cap helps mitigate this risk. The state does not have any elevated exposure to industries that we consider volatile, in fact, every industry we classify as volatile comprises a lower proportion of Connecticut's GSP than the national average.

Employment improved to above pre-pandemic levels by June 2023 and has continued to improve with about 17,000 jobs gained in the past 12-month period, but the state's employment growth rate of 0.84% in 2024 trailed the U.S.' 1.44%. Finance industry employment remains below pre-pandemic levels, with about 4,000 less employed in the industry, and we project it could take decades to recover, if at all. However, hiring in the sector will continue slowly along with growth in education and health services, leisure and hospitality, and other services.

The state's population increased each year from 2021-2024, reporting approximately 70,000 new residents, but we anticipate slower growth and that the population will remain relatively flat through 2028. An important credit consideration for Connecticut will be the track of its

population growth and aging of its prime working-age labor force as it faces increasing demographic challenges that weigh on economic growth. The state also has an aging population, consistent with that of the rest of New England, that will likely contribute to slower economic growth and create higher service-level demands that affect finances. Favorably, the state's highly educated workforce, with more than 40% of its population over the age of 45 holding a bachelor's degree or higher, is likely to ensure continued innovation and growth in business expansion and support

## Budgetary Performance And Reserves

During good economic periods, Connecticut has generally reported general fund operating surpluses, which have helped it increase reserve balances to manage potential economic and financial downturns. Our assessment, however, reflects the state's previous use of gap-closing solutions during downturns that relied on significant nonrecurring measures and substantial use of reserves. Nevertheless, based on current revenue expectations and the extension of fiscal guardrails that support budget predictability, we generally view the state's budget projections as supporting structural balance in the fiscal 2026-2027 biennium.

The OPM's most recent consensus revenue estimate projects total general fund revenue increasing 4.2% in 2025, 1.1% in 2026 and 2.8% in 2027, which would exceed expenditure growth and generate small operating surplus results. In April 2025, the state will update these projections and we will closely monitor the cost trajectory of debt and long-term liabilities as well as other spending drivers such as Medicaid and other social services for any potential medium-term pressures. As economic conditions evolve and effects on the state's finances materialize, we will monitor whether revenues continue to keep pace with outyear spending. Connecticut's commitment to statutory provisions that reduce budget volatility and managing the budget proactively to sustain structural balance beyond the current biennium, particularly as extraordinary federal funds diminish and some program costs shift back to the state, will remain important to the state's long-term credit quality.

The BRF is projected to remain fully funded, at 18% of general fund appropriations through the biennium, or \$4.5 billion at fiscal 2027 year-end. We view these strong reserves as an important tool for the state to navigate cyclical revenue declines during economic downturns and a potentially slower financial recovery compared with other states. We believe there are robust mechanisms in place--through the state's revenue volatility cap--to replenish potential draws and build balances should they be drawn on.

## Debt And Liabilities

### Debt

We view the state's tax-supported debt to be very high by nearly all measures and the elevated debt burden has historically been a constraining factor on the state rating. Net direct debt totaled approximately \$25 billion (including GO, transportation, and capital lease debt) as of June 30, 2024. Although several of the state's debt metrics fell slightly in fiscal 2023 from fiscal 2022, Connecticut's debt remains the highest of all states at \$6,829 per capita, but we also recognize that the state amortizes its debt comparatively rapidly with nearly 80% expected to be retired within 10 years.

We expect most of Connecticut's debt metrics will remain elevated for the foreseeable future, with modest reductions to the debt burden over the long term. The governor's budget proposal

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would authorize about \$2.5 billion in new general bond issuances in fiscal years 2026 and 2027, which marks a modest reduction from the \$2.6 billion authorized in fiscal 2024 and \$2.8 billion in fiscal 2025. However, we expect that annual debt issuance will remain well below authorized levels over the near-term.

### Pension and OPEB liabilities

The state's net pension liability (NPL) is very high compared with that of peers. Its unfunded pension liability across all plans remains approximately \$34.97 billion for fiscal 2024, although funding progress has improved following \$8.6 billion in supplemental pension payments to the state's two largest plans between fiscal years 2020 and 2024, with expectations of a year-end supplemental contribution of \$1.4 billion for fiscal 2025.

Connecticut's pension funded ratios as of June 30, 2024, for plans representing a significant portion of the state's NPL are:

- SERS: 56% funded with the state's applicable NPL of \$19.2 billion
- TRS: 62% funded with the state's applicable NPL of \$15.9 billion

In our opinion, lowering the assumed rate of return to 6.9%, using a closed-layered amortization method, and converting to a level-dollar funding plan should improve plan liquidity in the long term and stabilize future costs. Although changes in assumptions more closely align with our evaluation of pension risk, the state's large unfunded liability presents a persistent credit pressure.

The state's OPEB liability also remains a source of credit pressure because the liability is high compared with that of peers, but recent actions to reduce the liability and pre-fund an OPEB trust reduced the unfunded liability. Based on the Governmental Accounting Standards Board Statement Nos. 74 and 75 actuarial valuation results for June 30, 2024, the state's applicable net OPEB liability for the state employee OPEB plan was \$15.6 billion, or about \$4,310 per capita, which is elevated compared with other state OPEB plans. The OPEB trust had a current market value of \$2.96 billion as of July 31, 2024, reflecting a funded level of 19%. Connecticut is also statutorily required to fund one-third of teacher pension OPEB costs, plus the shortfall left after employer and employee contributions. The teachers' net OPEB liability was \$3.2 billion, and 7.4% funded.

### Connecticut--Credit summary

Institutional framework (IF)	2
Individual credit profile (ICP)	2.20
Economy	1.0
Financial performance	2
Reserves and liquidity	1
Management	1.00
Debt and liabilities	6.00

### Connecticut--Key credit metrics

	2024a	2023a	2022a
<b>Economy</b>			
State population ('000s)	3,647	3,621	3,607



**Connecticut--Key credit metrics**

	2024a	2023a	2022a
<b>Economy</b>			
Real GSP per capita (\$)		78,592	77,043
Real GSP per capita % of U.S.	118	118	116
State PCPI (\$)		89,208	84,704
State PCPI % of U.S.	129	128	127
State unemployment rate (%)	3.7	4.1	6.4
<b>Financial performance - S&amp;P Global Ratings adjusted</b>			
Operating fund revenues (mil. \$)	22,716	22,823	21,991
Operating fund expenditures (mil. \$)	22,315	22,267	20,731
Operating result (mil. \$)	401	556	1,260
Operating result % of revenues	1.8	2.4	5.7
<b>Reserves and liquidity - S&amp;P Global Ratings adjusted</b>			
Available reserves (mil. \$)	4,105	3,316	3,313
Available reserves % of operating revenues	18.1	14.5	15.1
<b>Debt and liabilities</b>			
Net direct debt cost % of revenues	9.5	8.8	8.0
Pension and OPEB cost % of revenues	14.3	14.7	12.8
Total current cost % of total government revenues	21.6	23.5	20.8
Net direct debt (mil. \$)	25,112	25,416	25,739
Net direct debt per capita (\$)	6,829	6,969	7,108
Direct debt 10-year amortization (%)	75	75	75
Combined NPLs (mil. \$)	34,974	38,010	40,591
NPLs per capita (\$)	9,511	10,422	11,210
Combined pension plan funded ratio (%)	59.2	54.4	49.9

Financial data might reflect analytical adjustments and are sourced from issuer audit reports or other annual disclosures. Economic data is generally sourced from S&P Global Market Intelligence, the Bureau of Labor Statistics, Claritas, and issuer audits and other disclosures. GCP--Gross county product. PCPI--Per capita personal income. EBI--Effective buying income. OPEB--Other postemployment benefits. NPLs--Net pension liabilities.

**Ratings List**

**New Issue Ratings**

US\$500,000,000 State of Connecticut, General Obligation Bonds, Series 2025A, dated: Date of Delivery, due: March 15, 2044

Long Term Rating AA-/Stable

US\$1,151,000,000 State of Connecticut, General Obligation Refunding Bonds, Series 2025B, dated: Date of Delivery, due: December 1, 2034

Long Term Rating AA-/Stable

US\$300,000,000 State of Connecticut, Taxable General Obligation Bonds, Series 2025A, dated: Date of Delivery, due: March 15, 2034

Long Term Rating AA-/Stable

**Ratings Affirmed**

**Pooled**

Connecticut, CT General Obligation Equivalent and Connecticut St Univ Sys, CT Unlimited Student Fees AA-/Stable

Connecticut, CT General Obligation Equivalent and University of Connecticut, CT Unlimited Student Fees AA-/Stable

**States**

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### Ratings List

Connecticut Housing Finance Authority CT, General Obligation Equivalent	AA-/Stable
Connecticut, CT Appropriation Contract	A+/Stable
Connecticut, CT General Obligation	AA-/Stable
Connecticut, CT General Obligation Equivalent	AA-/Stable
Connecticut, CT General Obligation Equivalent State Supported Green Bonds	AA-/Stable
Connecticut, CT General Obligation Equivalent State Supported Parking and Energy Fee Rev Bnds	AA-/Stable
Connecticut, CT Lease Appropriation	A+/Stable
Connecticut, CT Moral Obligation	A-/Stable

The ratings appearing below the new issues represent an aggregation of debt issues (ASID) associated with related maturities. The maturities similarly reflect our opinion about the creditworthiness of the U.S. Public Finance obligor's legal pledge for payment of the financial obligation. Nevertheless, these maturities may have different credit ratings than the rating presented next to the ASID depending on whether or not additional legal pledge(s) support the specific maturity's payment obligation, such as credit enhancement, as a result of defeasance, or other factors.

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