State of Connecticut - Special Tax

Issuer: State of Connecticut		
Assigned	**Rating**	**Outlook**
Special Tax Obligation Bonds, Transportation Infrastructure Purposes, 2025 Series A	AAA	Stable
Affirmed	**Rating**	**Outlook**
Special Tax Obligation Bonds, Transportation Infrastructure Purposes	AAA	Stable

Methodology:

U.S. Special Tax Revenue Bond Rating Methodology

ESG Global Rating Methodology

Analytical Contacts:

Peter Scherer, Senior Director
+1 (646) 731-2325
peter.scherer@kbra.com

Douglas Kilcommons, Managing Director
+1 (646) 731-3341
douglas.kilcommons@kbra.com

Rating Summary: The long-term ratings for the Special Tax Obligation Bonds – Transportation Infrastructure Purposes reflect the ample coverage and stable nature of most revenues pledged to repayment, descending debt service requirements, and a robust legal framework that includes a covenant for the State to provide pledged revenues in each fiscal year sufficient to provide at least 2.0x annual debt service coverage. If debt service coverage does not meet the 2.0x requirement, the covenant requires that the State must pass legislation within one year adjusting pledged revenues to satisfy the coverage requirement. Such a covenant is a relative rarity in the broader category of special tax financings.

Bond proceeds will be used to fund transportation projects within the State, refund certain outstanding bonds for present value savings, and to pay the cost of issuance. The Bonds are payable from a diverse basket of state revenues derived largely from transportation-related activity. The pledged revenues consist of certain sales taxes, oil companies tax, motor fuels tax, highway use tax, and various transportation-related fees and charges. Pledged revenues declined 2.1% in the fiscal year ending June 30, 2025 to $2.36 billion. Unaudited debt service coverage in FY 2025 was strong at 2.75x.

The currently offered bonds (Bonds) are the second to be issued under an Amended and Restated Indenture of Trust (2024 Indenture). As permitted under the 2024 Indenture, the Bonds will not feature a debt service reserve requirement and advance debt service set-asides are not required, though the State has so far elected to structure bonds under the 2024 Indenture, including the presently offered series, as "Monthly Payment Bonds" with the same 1/6 interest and 1/12 principal monthly set-asides as prior bonds. The 2024 Indenture includes a number of changes that will become effective upon obtaining the consent of the holders of at least 60% in aggregate principal outstanding including the ability to issue variable rate debt, as well as make provisions for swaps, credit facilities, liquidity facilities and balloon payment indebtedness as parity obligations, in addition to other comparatively minor changes. Based on the certain assumptions, the State expects to reach the 60% threshold as early as calendar year 2028.

The Connecticut Constitution designates the Special Transportation Fund (STF) into which all pledged revenues are deposited and used first to pay debt service as a perpetual fund. It requires that all monies contained in the STF be used solely for transportation purposes, including payment of debt service on debt incurred for state transportation purposes. It additionally requires that so long as these sources of funds are authorized to be collected, they must be deposited into the STF.

The State has directed substantial new funding sources to the STF in recent years. Between FY 2016 and FY 2023 the state phased in the dedication of the proceeds of a 0.5% component of the State's 6.35% general sales and use tax as well as the proceeds of all motor vehicle sales and use taxes. The Legislature has additionally implemented a Highway User Fee that assesses a per-mile tax on commercial trucks that scales from 2.5 cents to 17.5 cents per mile based on vehicle weight class. The tax, all proceeds of which are deposited to the STF, became effective January 1, 2023 (mid-year FY 2024) and raised an unaudited $59.9 million in FY 2025.

The State uses STF revenues both to pay debt service and fund transportation programs and capital outlays on a pay-go basis. The future transportation capital needs of the State are significant, and the State plans to fund much of these capital plans with additional parity bonds as well as continuing pay-go contributions. The State's projections call for annual parity new money borrowing of $1.3 billion in FY 2026, $1.2 billion in FY 2027, and $1.1 billion annually thereafter through FY 2030.

Seasonally adjusted unemployment in August 2025 was 3.8%, a level lower than the U.S. average at 4.3%. Wealth levels remain very high, with per capita personal income of $93,235 at 129% of the national average in 2024. The economic growth trend in the State have been sluggish with real gross state product (GSP) growth of just 10.2% between 2010 and 2024, significantly lower than the New England regional growth of 26.8% and National growth of 38.8%.

The Stable Outlook reflects KBRA's expectation that debt service coverage on the STO Bonds will remain at comfortable levels based upon the stability and resilience of the pledged revenues and the State's demonstrated history of actively managing the basket of pledged revenues and transportation funding levels.

Key Credit Considerations

The rating actions reflect the following key credit considerations:

Credit Positives

- Diverse pledged revenue sources provide a stable source of payment and solid coverage of debt service requirements.
- Legal protections are favorable including a covenant to maintain at least 2.0x annual debt service coverage.

Credit Challenges

- The State's rate of economic growth has been slower than that of the U.S. and New England region for more than a decade although wealth levels are favorable.
- Transportation needs are substantial and place pressure upon the State's ability to fund them over the longer term.

Rating Sensitivities

▪ Not applicable at AAA rating level.	+
▪ An economic downturn that leads to a sustained decline in coverage and budgetary pressure on the State.	-

Highlights
FYE June 30 (dollars in millions)

	2023	2024	2025 Unaudited
Pledged Revenues and Coverage			
Sales and Use Tax	$ 838	$ 844	$ 878
Oil Companies Tax*	384	359	298
Motor Fuels Tax**	262	505	514
Motor Vehicle Receipts	255	279	275
Licenses, Permits, Fees	126	142	140
Sales Tax - DMV	117	115	114
Highway User Fee	29	60	60
Other, Net	58	107	(57)
Adjustments to Rev. For Coverage Purposes***	-	-	140
Total Net Revenues for Coverage Purposes	2,070	2,411	2,361
Combined Sen. and Sub. Lien DS	811	863	859
Debt Service Coverage Ratio	**2.55x**	**2.79x**	**2.75x**
Economic Data			
Per Capita Personal Income (2024)		$93,235	
as a % of U.S.		129%	
Population (2024)		3,675,069	
Δ 2010 to 2024		2.6%	
Real GSP, Δ 2010 to 2024			
Connecticut		10.2%	
New England		26.8%	
U.S.		38.8%	

Summary Legal Provisions	
Coverage Covenant	Pledged revenues must provide 2.00x annual debt service coverage.
Additional Bonds Test	Historical and projected annual receipts equivalent to 2.00x pro forma MADS, subject to adjustment for changes to pledged revenue sources. The historical coverage portion of the test will be eliminated upon achievement of 60% bondholder consent under the 2024 Indenture.
DSRF Requirement	2024 and Later Bonds: No DSRF requirement. Pre-2024 Bonds: MADS.

*Oil Companies Tax receipts declined 16.9% in FY 2025 unaudited due to lower pretroleum-related gross earnings attributable primarily to lower fuel prices.

**The State Legislature implemented an exememption from the 25 cent per gallon tax rate from April 1, 2022 through December 31, 2022. Beginning January 1, 2023, the tax rate on gasoline and gasohol was phased-in by 5 cent increments until reaching the original 25 cents per gallon on May 1, 2023. The estimated revenue loss as a result of such change was $90 million in FY 2022 and $240 million in FY 2023.

***Pursuant to section 44 of Public Act 25-168 the STF will delay recognition of $140 million in receipts in FY 2025 with $17 million instead recognized in FY 2026 and $123 million recognized in FY 2027. Coverage is calculated on a cash basis so this Adjustment of Revenue for Coverage Purposes line item is utilized to reverse this change for the purpose of coverage calculation.

Rating Determinants (RD)	
1. Legal Framework	AAA
2. Nature of Special Tax Revenues	AAA
3. Economic Base and Demographics	AA-
4. Revenue Analysis	AA
5. Coverage and Bond Structure	AAA

A discussion of each rating determinant, ESG Management, and the Bankruptcy Risk Assessment can be found in prior reports, the most recent of which is dated November 13, 2024.