State of Connecticut

Issuer: State of Connecticut		
Assigned	**Rating**	**Outlook**
General Obligation Bonds (2021 Series B) (Social Bonds)	AA	Stable
General Obligation Refunding Bonds (2021 Series C)	AA	Stable
General Obligation Refunding Bonds (2021 Series D) (Forward Delivery) (Social Bonds)	AA	Stable
Taxable General Obligation Bonds (2021 Series A)	AA	Stable
Upgrade	**Rating**	**Outlook**
General Obligation Bonds	AA *(from AA-)*	Stable
Issuer: Connecticut Innovations, Incorporated		
Upgrade	**Rating**	**Outlook**
State of Connecticut General Fund Obligation Bonds 2014 Series A	AA *(from AA-)*	Stable

Methodology:
U.S. State General Obligation Rating Methodology

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Rating Summary: The rating upgrade from AA- to AA reflects the significant progress the State has made in improving its financial position in the last three years, building the balance of its Budget Reserve Fund (BRF or rainy day fund) from just 1.3% of General Fund expenditures at FYE 2017 to 15.3% at FYE 2020. Statute requires that the BRF balance be limited to 15% of the subsequent year budget with excess amounts applied to long-term liabilities. Accordingly, the State applied $62 million from the FYE 2020 BRF balance in the early months of FY 2021 to unfunded pension liabilities of SERS, a contribution supplementing the ordinary actuarial contribution. The Connecticut Office of Policy and Management (OPM) revenue estimates for FY 2021 have improved through the second half of the fiscal year as the pandemic's impact and social distancing measures have eased. Based on OPM's latest April 30 revenue estimates and expenditure projections included in the Governor's February 2021 Proposed FY 2022 – FY 2023 Biennium Budget, the BRF balance is projected to increase to $4.0 billion at FYE 2021. In order to comply with the 15% statutory BRF cap, OPM projects transferring $890 million to the state's pension systems.

The State received a $1.4 billion allocation of from the Coronavirus Aid, Relief, and Economic Security (CARES) Act which was passed March 27, 2020 as part of the $150 billion state-focused Coronavirus Relief Fund (CRF). Substantially all of this has been spent or allocated. The State expects to receive $2.6 billion from the American Recovery Plan enacted by Congress on March 11, 2021.

The stay-at-home orders from the pandemic implemented in March caused a significant falloff in economic activity in Connecticut as it did nationwide. The unemployment rate increased peaked to 11.6% in May 2020 from 4.0% in February 2020, but this was less than the increases seen in the New England region and the U.S. The unemployment rate is now at 8.3%, which is somewhat higher than the region and U.S. averages. The State expects to lift business restrictions imposed during the pandemic on May 19, 2021.

Furthermore, the State seems to be benefitting from pandemic-induced in-migration, primarily from New York. According to the US Postal Service change of address submissions, 16,501 people moved to Connecticut through October 2020 compared to -7,523 that moved from the state through the same period in 2019. Whether or not these trends prove to be longer lasting remains to be seen.

Wealth levels remain very high, with per capita income of $79,771 at 134% of the national average in 2020. The longer-term, pre-pandemic economic growth trend in the state was sluggish. Real gross state product (GSP) contracted in six of the last thirteen years. The depth and duration of the current downturn and ultimate pace of the recovery as the economy eventually reboots is unclear.

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 21.7% of general government expenditures in FY 2020, which KBRA views as high. Debt amortization is favorable with 71% of general obligation debt retired in 10 years.

The Stable Outlook reflects the diversity and high wealth levels of the economic base and strong reserve position which provides a good framework for future operations.

Key Credit Considerations

KBRA continues to monitor the direct and indirect impacts of the COVID-19 virus. Click here to access KBRA's ongoing research on the topic.

The rating actions reflect the following key credit considerations:

Credit Positives

- Budget Reserve Fund balance has increased in recent years and is now 15% of general fund expenditures.
- Strong financial management framework for tracking revenues, monitoring budget performance and a history of making required adjustments.
- Strong wealth levels with State per capita income the highest in the nation.

Credit Challenges

- Lower relative growth in the important economic indicators of population, employment and gross state product, although there are very recent signs of growth in population.
- Unfunded pension liabilities and tax-supported debt burden are high relative to personal income, each exceeding 3.0x the respective U.S. averages. However, the State borrows for many local purposes and the comparison on a combined state and local basis is more moderate.

Rating Sensitivities

▪ Stronger economic growth trends than what have been experienced since the Great Recession. ▪ Significant improvement in the funded ratios for the State's pension systems.	+
▪ Structural operating deficits in the General Fund. ▪ Weakening in the State's employment base and economic activity.	-

Key Ratios

Rating Highlights	
Per Capita Personal Income (2020) (in dollars)	$79,771
as a % of U.S.	*134%*
Population (2020)	3,605,944
Growth 2010 to 2020	*0.9%*
Real GDP, % Change 2010 to 2020	
Connecticut	-2.8%
New England	8.9%
United States	18.1%
Budget Reserve Fund Balance ($ in millions)	
FYE 2017	$213
FYE 2018	$1,185
FYE 2019	$2,506
FYE 2020	$3,075
FYE 2021 Proj.[1]	$3,968
Pro Forma Direct Debt ($ in millions)	$26,957
Net Pension Liability[2] ($ in millions)	$42,808
Fixed Costs as a % of Governmental Expenditures (FY 2020)	21.7%

[1] Statute limits the BRF balance to 15% of the subsequent year's budget. To comply with this requirement, the State anticipates applying $890 million of this projected balance toward the State's pension liabilities as a supplemental contribution in addition to the ADEC.

[2] Reflects 6/30/2020 measurement date for SERS and TRS and 6/30/2019 for JRS.

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

RD 1: Management Structure, Budgeting Practices and Policies

KBRA views Connecticut's management structure and policies as providing a very strong framework for managing its financial operations and debt issuance compared with other states. This framework is established by the State Constitution, Statutes, and administrative practices. Within this framework, favorable financial results have been achieved in recent years.

Constitutional Provisions

Under Connecticut's Constitution, the State is divided into three distinct branches: The Legislative, Executive, and Judicial. The executive power of the State is vested in the Governor. Governor Ned Lamont was elected in November of 2018 for a term beginning in January 2019. Treasurer Shawn Wooden was also elected November 2018. The Treasurer is primarily responsible for receiving and disbursing monies of the State and is the sole fiduciary of the State's retirement funds. The Treasurer also has the responsibility for carrying out the issuance of debt. The Comptroller is required to issue monthly budgetary reports on the State's financial condition, in conjunction with the Office of Policy and Management (OPM). OPM is directly responsible to the Governor for policy development in the areas of budget and financial management and prepares the State budget.

The State's Constitution provides that the General Assembly may not authorize general budget expenditures in excess of estimated revenues. The Constitution also includes a spending cap on annual growth in expenditures which limits the increase in expenditures to the greater of the five-year average growth in personal income or inflation over the previous year. The cap excludes debt service for general obligation debt, annual funding of unfunded pension liabilities, and spending supported by federal funding. The cap may be exceeded if the Governor declares a fiscal emergency, and both houses of the legislature support such action by a three-fifths vote.

Under the State Constitution, the Governor has the power to veto any line item of any itemized appropriation bill, while at the same time approving the remainder of the bill. The General Assembly may override the Governor's veto by two thirds vote of each legislative house.

Statutory Provisions

State law requires that total net appropriations for each fund shall not exceed a percentage of estimated revenues for each respective fund. Under State statute, the State is required to monitor its financial performance monthly and the Governor is empowered to take action, under statutory limitations, to maintain budget balance. State statutes require consensus revenue forecast to be developed on a regular basis three times a year. The State's statutes allow for broad revenue raising ability.

Financial Management Policies

The State operates under a strong and comprehensive framework of financial management policies, most of which are codified in statute. The State's framework for financial management includes the following planning and reporting components:

- <u>Monthly Reports on Financial Performance</u>— By statute, OPM is required to provide the State Comptroller with a letter with monthly updates to revenue and expenditure projections for the General Fund in the current fiscal year, along with projections for end of fiscal year surplus or deficits. Based on the OPM letter, the Comptroller prepares a monthly letter on financial performance. Both the OPM and the State Comptroller's monthly letter is available on the state's website. KBRA views the Comptroller's and OPM's monthly monitoring and projection of the year-end financial position as an extremely valuable tool in managing the State's finances.
- <u>Annual Report to Legislature</u>— By statute, each November, OPM and the Office of Fiscal Analysis (OFA) is required to submit a Fiscal Accountability report to the Legislature which projects revenues for the current biennium and the next three fiscal years.
- <u>Three Year Out Report</u>— As part of the budget process, the Governor must annually submit a separate report to the Legislature which sets forth the estimated revenues and expenditures for the current biennium and the next three fiscal years.
- <u>Consensus Revenue Estimates</u>— OPM and the OFA are required by statute to issue consensus revenue estimates each year by November 10, January 15, and April 30 that cover the current biennium and the next three fiscal years. The development of consensus revenue forecasts utilizes both in house analytic staff and external economic forecasting services. Economic trends are monitored and factored into monthly updates on revenue projections.

The Treasurer has investment responsibility for all funds of the State and functions as the trustee of all State pension, retirement, and trust funds. The Treasurer is required to report annually on investment activities by December 31 to the Governor and the State's Investment Advisory Council.

State Budget Process

The State's fiscal year begins on July 1 and ends on June 30. The Governor is required to transmit a budget document to the General Assembly in February of odd numbered years setting forth a separate budget for each of the biennium years. Under State Statute, the Governor has the ability to run the State under Executive Order to maintain essential services in the absence of a budget.

In each even numbered year, the Governor must prepare a report (Mid Term Budget Report) on the status of the budget enacted in the previous year with any recommendations on adjustment and revisions for the coming year. All budget recommendations incorporate the consensus revenue estimate process. If a budget surplus or deficit is projected, the Governor will recommend how the deficit will be mitigated or how the surplus will be used.

Ability to Adjust Expenditures and Deficit Mitigation

Under State statute, the Governor is empowered during the fiscal year to reduce the budget allotment, or expenditure request, by up to 5.0% of any specific appropriation to an agency, except for aid to municipalities, up to 3% of the total appropriations of any fund under certain circumstances without Legislative approval in order to maintain balanced financial operations. Such budget allotments are subject to further modification by the Governor throughout the fiscal year if necessary. Beyond these limits, the General Assembly must act to reduce expenditures.

Budget Reserve Fund

State statutes dictate that unappropriated surpluses left in the General Fund (GF) shall be transferred to the Budget Reserve Fund (BRF) until the Fund reaches 15% of the net GF appropriations. The Revenue Volatility Cap requires that beginning in FY 2018 estimated and final payments of the personal income tax and the pass-through entity tax in excess of a threshold, the Revenue Volatility Cap, are deposited into the BRF. The threshold for deposits adjusts under a statutory formula pegged to a base of $3.15 billion for FY 2017, adjusted each year by the compound annual growth rate of personal income in the state over the prior five years, as calculated annually by the State Comptroller. After the BRF reaches 15% of net GF appropriations, revenues in excess of the 15% threshold are to be applied to long term liabilities, initially pension liabilities.

Briefly, uses of the BRF include:

- To fund a deficit in the preceding fiscal year
- By transfer of the General Assembly if the consensus revenue forecast projects a GF revenue decline of more than 1%

State Debt Limit

State statutes impose a ceiling on the amount of GF supported debt which may be authorized by the Legislature. The limit is 1.6x net GF tax receipts as projected by the Finance, Revenue and Bonding Committee of the General Assembly. Certain types of debt are excluded from this cap, including cash flow borrowings and emergency financings. Per the November 2020 Fiscal Accountability Report, the estimated debt incurring margin for FY 2020 is $4.5 billion.

General obligation debt is issued under State debt statutes and specific bond authorizations. Statutes provide that the bonds will be general obligations of the State and that the full faith and credit of the State is pledged for repayment. As per the State's contract with bondholders, appropriations for principal and interest do not need legislative approval. There are no express statutory provisions establishing any priorities in favor of general obligation bondholders over other claims against the State. Connecticut is not a voter initiative state.

Municipal Accountability Review Board (MARB)

Statutes passed by the General Assembly as part of the FY 2018-FY 2019 budget process established a Municipal Accountability Review Board (MARB) to provide oversight and assistance to municipalities experiencing fiscal distress. The State has assumed the annual debt service obligations of the City of Hartford under this program. KBRA has added Hartford's outstanding debt to the State's aggregate outstanding debt. The State is also providing support to the City of West Haven under MARB which is expected to be short-term.

ESG Management

Environmental Factors

The State has established the Governor's Council on Climate Change (GC3) which expects to present recommendations to the Governor regarding funding sources for investment in resilience and adaptation. The Governor has also set a goal for the executive branch of State government to achieve 45% reduction in greenhouse gas emissions below 2001 levels by 2030, a 25% reduction in waste disposal from 2020 levels by 2030, and a 10% reduction in water consumption from 2020 to 2030.

Bankruptcy

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.

RD 2: Debt and Additional Continuing Obligations

State Tax-Supported Debt

Connecticut's pro forma tax-supported debt burden is $27.0 billion including $19.3 billion in general obligation bonds, $7.0 billion in special tax debt secured by a pledge of transportation related taxes and fees, and $244 million in various other obligations. Also included in this figure is $453 million in City of Hartford debt. The State has assumed Hartford's debt service payments on this debt under a Contract for Financial Assistance executed in April 2018 as part of a plan to stabilize the financially distressed city.

In comparison with other states, Connecticut's state tax-supported debt burden is high. These high debt levels result in part from the State's practice of issuing general obligation debt for certain university projects and for purposes that municipal entities and counties fund in other states, including local school construction. Connecticut has not had a county form of government since October 1960.

Figure 1

Pro Forma Direct Tax-Supported Debt Principal Amount Outstanding
(dollars in millions)

	2/1/2017	2/15/2018	2/1/2019	5/1/2020	2/1/2021[1,2]
General Obligation Bonds	$14,091	$14,038	$15,008	$14,005	$15,229
General Obligation Bond Anticipation Notes	-	400	-	-	0
Pension Obligation Bonds (GO)[3]	2,351	2,370	2,368	2,394	2,411
UConn 2000 Bonds (GO)	1,533	1,421	1,635	1,569	1,661
Total General Obligation Debt	17,975	18,228	19,011	17,968	19,301
Special Tax Obligation Bonds	5,042	5,540	5,958	5,575	6,959
Other[4]	327	302	257	216	244
State Guaranteed City of Hartford Debt	-	-	516	488	453
Total Direct Tax-Supported Debt	**23,343**	**24,071**	**25,741**	**24,246**	**26,957**

Source: POS and historic GO Official Statements.

[1]General Obligation Bond balance adjusted to include $600 million in currently offered new money bonds. Does not reflect impact of simultaneously offered $400 million refunding bonds.

[2]Special Tax Obligation Bond balance adjusted to reflect April 23, 2021 issuance.

[3]Includes accreted value of Capital Appreciation bonds.

[4]ncludes lease financing, tax increment financings, CHFA Supportive Housing Bonds and CHFA Emergency Mortgage Assistance

Connecticut's state tax-supported debt burden is high relative to population, personal income and GSP, ranking among the very highest in the Country by all three metrics. The State's debt burden compares more favorably however when analyzed on the basis of aggregate state and local borrowings. By this more inclusive measure, the State's debt burden falls to the top 25% of states compared to personal income and to GSP.

Figure 2

Debt Ratios[1] (in dollars)	Connecticut	Average of U.S. States	Connecticut Rank Among the 50 States
Tax-Supported Debt:			
Per Capita	$7,561	$1,654	Highest 5%
as a % of Personal Income	9.6%	2.9%	Highest 5%
as a % of GSP	9.4%	2.6%	Highest 5%
Aggregate State and Local Debt:			
Per Capita	$14,460	$9,586	Highest 5%
as a % of Personal Income	19.3%	17.6%	Highest 25%
as a % of GSP	18.5%	15.2%	Highest 10%

Source: U.S. Census Bureau, U.S. Bureau of Economic Activity, Credit Scope, and Annual Disclosures.

[1]Includes currently offered bonds.

Connecticut has a relatively small level of exposure to variable rate debt or derivative financings; hence these types of transactions do not pose a significant risk to the State's liquidity position. As of February 1, 2021 the State has $912 million in variable rate general obligation bonds, which represents approximately 4.8% of pro forma long-term GO debt. The State is not party to any interest rate derivatives with respect to its outstanding GO debt.

Debt Amortization

Connecticut's debt amortization parameters are conservative, with GO debt generally required to be amortized over 20 years on a level principal basis, which generates a declining debt service schedule. Speed of amortization of direct general obligation debt, is above average with 71% of principal retired over the next 10 years. In FY 2020, GO bond debt service represented 9.7% of total governmental expenditures (on a GAAP basis).

Capital Improvement Plan

The State's general obligation bond allocations for capital projects declined from $2.7 billion in calendar year (CY) 2016 to $1.4 billion in CY 2020. The Governor's Proposed budget calls FY 2022 issuance of $1.6 billion GO and $800 million in STO bonds as well as FY 2023 issuance of $1.6 billion GO and $925 million in STO bonds.

State of Connecticut Retirement Systems

Connecticut administers two major pension plans: the State Employees' Retirement System (SERS) and the State Teachers' Retirement System (TRS). It also administers the much smaller Judicial Retirement System (JRS). The State's level of funding for its pension plans remains among the lowest for US states. The actuarial funded ratio for SERS is 38.5% (June 30, 2020) and for TRS is 51.3% (June 30, 2020). The State has contributed to these funds at the full Actuarially Determined Employer Contribution (ADEC) in recent years, but funding progress has lagged as realized investment returns have not reached actuarial assumptions.

State Employees' Retirement System (SERS)

SERS is a single-employer defined benefit pension plan that provides retirement, disability, and death benefits to plan members and their beneficiaries. Employees also contribute. The assumed annual investment rate of return was reduced gradually from 8.5% in 2010 to 6.9% in 2016. This revised assumption is more realistic in KBRA's view and has contributed to a trend of significant growth in annual contribution requirements.

On July 31, 2017, the General Assembly approved an agreement between the State and State Employee Bargaining Agent Coalition (SEBAC) which made substantial changes to pension and healthcare benefits for employees and retirees, including a three-year wage freeze, increased employee pension contributions for existing SERS members, a reduced COLA formula and a change in timing for post-2022 retirees, revisions to the healthcare design plan, and cost sharing for current employees. The State also agreed to extend the expiration date of the existing agreement with SEBAC on pension and healthcare from 2022 to 2027.

Teacher's Retirement System (TRS)

TRS is a single-employer defined benefit pension plan administered by the Teachers' Retirement Board (TRB) for teachers, principals and other education supervisors employed in public school districts. Connecticut pays the entire ADEC on behalf of participating school districts and public universities. The teachers also contribute.

Figure 3

Pension Funded Status and Actuarially Determined Employer Contribution Requirements as of June 30, 2020 (dollars in millions)	SERS	TRS	Total
Market Value of Assets	$13,311	$18,286	$31,598
Actuarial Value of Assets	14,243	19,055	33,298
Actuarial Accrued Liability	36,971	37,128	74,099
Unfunded Actuarial Accrued Liability	22,728	18,073	**40,801**
Funded Ratio (based on the actuarial value of assets)	38.5%	51.3%	44.9%
Funded Ratio (based on the market value of assets)	36.0%	49.3%	42.6%
FY 2020 Actuarially Determined Employer Contribution (ADEC)	1,616	1,209	**2,825**
% of ADEC Contributed	100%	100%	
FY 2021 ADEC	1,807	1,250	**3,057**
FY 2022 ADEC	1,993	1,444	**3,437**
FY 2023 ADEC	2,157	1,578	**3,735**
FY 2024 ADEC	2,175	1,741	**3,915**

Source: State of Connecticut Annual Information Statement dated February 15, 2021.

Net Pension Liability

The State's net pension liability (NPL), based on GASB 67 reporting requirements, represents a combined liability for all of the State pension funds, SERS, TRS and JRS. The NPL begins with the total actuarial pension liability based upon the entry age normal actuarial method. From this amount, the market value of invested pension fund assets is deducted and the balance is the NPL.

The combined NPL is $42.8 billion as of June 30, 2020 based on the latest SERS and TRS valuations provided in the Information Statement with February 15, 2021 accompanying the POS and June 30, 2019 JRS valuation data from the FY 2020 CAFR. This NPL ranks among highest in the country when compared to population, personal income, and GSP. In FY 2020, the State's combined contribution toward pensions was $2.85 billion including $1.62 billion to SERS, $1.21 billion to TRS, and $27 million to JRS. This total contribution was equivalent to 9.1% of FY 2020 total governmental expenditures.

Figure 4

Net Pension Liability (NPL) Ratios (in dollars)	Connecticut	Average of U.S. States	Connecticut Rank Among the 50 States
Net Pension Liability:			
Per Capita	$12,007	$1,978	Highest 5%
as a % of Personal Income	15.2%	3.4%	Highest 5%
as a % of GSP	15.0%	3.1%	Highest 5%

Source: U.S. Census Bureau, U.S. Bureau of Economic Activity, Credit Scope, and Annual Disclosures.

The State has fully funded the ADEC for the SERS plan since 2012 and on the TRS plan since 2006, but the funded status of the two plans has eroded in part because actual investment returns have lagged assumptions. The revised return assumptions assume that investment returns will provide a smaller portion of the cashflows needed to maintain the plans, resulting in increased State contributions.

Other Post-Employment Benefits (OPEB)

Connecticut provides healthcare and life insurance benefits to eligible state employees. The State funds the benefit costs on a pay as you go basis, as do most states, through a transfer from the General Fund to its OPEB trust fund. Beginning in 2009, new hires had OPEB trust contribution requirements. The most recent SEBAC contract requires employee trust contributions of 3% of salary for 15 years for employees hired on or after July 1, 2017. In FY 2020, the State's contribution to retiree healthcare and life insurance costs was $896 million, which represents 2.9% of FY 2020 total governmental expenditures.

Total Fixed Costs

Total FY 2020 fixed costs, including debt service, pension contributions and pay-as-you-go OPEB costs, represented 21.7% of total governmental expenditures.

RD 3: Financial Performance and Liquidity Position

KBRA has revised the Financial Performance and Liquidity Position rating determinant to AA from AA- reflecting the State's improved revenue forecasting, recent trend of favorable operating results, and the replenishment of the Budget Reserve Fund (BRF or rainy day fund) to the statutory cap.

The State made significant progress in improving its financial position in the last three years, building the balance of its BRF from just 1.3% of General Fund expenditures at FYE 2017 to 15.3% at FYE 2020. Statute requires that the BRF balance be limited to 15% of the subsequent year budget with excess amounts applied to long-term liabilities. Accordingly, the State applied $62 million from the FYE 2020 BRF balance in the early months of FY 2021 to unfunded pension liabilities of SERS, a contribution supplementing the ordinary actuarial contribution. OPM revenue estimates for FY 2021 have improved through the second half of the fiscal year as the pandemic's impact and social distancing measures have eased. Based on OPM's latest April 30 revenue estimates and expenditure projections included in the Governor's February 2021 Proposed FY 2022 – FY 2023 Biennium Budget, the BRF balance is projected to increase to $4.0 billion at FYE 2021. In order to comply with the 15% statutory BRF cap, OPM projects transferring $890 million to the state's pension systems. KBRA views the fully funded BRF and the projected availability of surplus revenues for the extraordinary pay down of long-term liabilities as positioning the State soundly to navigate the ongoing pandemic related recovery.

Figure 5

General Fund Statement of Revenues, Expenditures, and Net Surplus
Budgetary Modified Cash Basis (FYE June 30) (dollars in millions)

	2016	2017	2018	2019	2020	2021 *4/30/2021 Est.*
Operating Revenues[1]	17,781	17,703	18,199	19,650	19,724	19,878
Operating Expenditures	17,921	17,763	18,611	19,249	19,189	19,628
Other Resources	(30)	37	(71)	(31)	34	-
Operating Surplus (Deficit)	**(170)**	**(23)**	**(483)**	**371**	**569**	**250**
Transfers from (to) Budget Reserve Fund	170	23	483	(371)	(530)	(311)
Reserve for Statutory Transfer	-	-	-	-	(39)	(62)
Unappropriated Surplus (Deficit)	**-**	**-**	**-**	**-**	**-**	**-**
Budget Reserve Fund[2]						
Beginning Budget Reserve Fund Balance	406	236	213	1,185	2,506	3,075
Transfers from (to) General Fund	(170)	(23)	(483)	371	39	188
Volatility Cap Deposit[3]	-	-	1,471	950	530	705
Ending Budget Reserve Fund Balance	**236**	**213**	**1,201**	**2,506**	**3,075**	**3,968**
as a % of Operating Expenditures[4]	*1.3%*	*1.2%*	*6.5%*	*13.0%*	*15.3%*	*19.3%*[5]

Source: Annual Financial Reports of the State Controller (Historic) and Office of Policy and Management (Estimated)

[1] FY 2019, FY 2020, and FY 2021 revenue is reported net of volatility deposits to the BRF.

[2] Held in special revenue fund.

[3] Volatility transfers became effective in FY 2018.

[4] As presented in POS, FY 2016 through FY 2019 BRF Balance is shown as a % of Operating Expenditures for said year, while FY 2020 BRF balance is calculated as a % of budgeted appropriations for FY 2021 of $20,086.3 million.

[5] State anticipates applying $890 million of this balance toward the State's pension liabilities as the BRF will exceeds its 15% limit. Calculated relative to Governor's Proposed FY 2022 expenditures of $20.519 billion.

FY 2020 Results

Realized revenues came in just $266 million (1.4%) below the budgeted amount in FY 2020 despite onset of the virus in the final few months of the year. Notable shortfalls include:

- PIT collections (withholding as well as estimate and finals) $275 million (2.9%) under budget.
- Sales and Use Tax collections $126 million (2.8%) under budget.
- CIT collections $165 million (15.0%) under budget.

A $180 million shortfall in the estimated and final portion of PIT collections was more than offset by a $392 million outperformance in pass-through entity tax collections. The combined collection of $3.82 billion from the two sources, which together are the basis of the aforementioned volatility cap mechanism, resulted in the substantial $530 million BRF deposit, exceeding the budgeted deposit by $212 million.

Several other items additionally contributed to favorable performance in FY 2020 including:

- Federal Coronavirus Relief Funds received in the amount of $1.38 billion were applied to offset virus related costs including testing ($230 million), PPE and Supplies ($100 million), State Operations for enhanced pandemic related services and cleaning ($198 million), education reopening ($165 million) and to support for non-profit providers ($120 million).

- Federal Medicaid reimbursements for hospital inpatient and outpatient payments totaling $368 million were received, which had not been anticipated to arrive until the following year.
- Medicaid Reimbursements per the Families First Coronavirus Relief Act were increased 17.7% resulting in an additional $271 million.

As the BRF now exceeds the statutorily specified ceiling of 15% of budgeted expenditures, the balance exceeding this amount (now estimated at $61.6 million) will be transferred in FY 2021, at the discretion of the State Treasurer, as an additional contribution to the State Employees Retirement Fund or to the Teacher's Retirement System.

FY 2021 Budget Projections

OPM's April 2021 estimates project that FY 2021 revenues will finish the year up 3.6% YoY despite the pandemic's impact driven by strong personal income and sales and use tax performance.

Figure 6

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

	2016	Δ YOY (%)	2017	Δ YOY (%)	2018	Δ YOY (%)	2019	Δ YOY (%)	2020	Δ YOY (%)	2021 Apr. Est.
Revenues											
Personal Income Tax	9,182	-2.1%	8,989	19.8%	10,770	-10.5%	9,640	-2.5%	9,398	3.3%	9,704
Federal Grants	1,302	1.8%	1,325	-13.7%	1,143	82.3%	2,084	-13.8%	1,797	-16.1%	1,507
Sales and Use Tax	4,182	0.2%	4,192	0.2%	4,202	3.2%	4,338	-0.5%	4,318	7.4%	4,637
Corporate Income Tax	880	17.8%	1,038	-11.3%	921	15.2%	1,061	-11.9%	934	5.9%	990
Pass-through Entity Tax	-	-	-	-	-	-	1,172	6.0%	1,242	18.5%	1,471
Excise Taxes (Alcohol and Cigarettes)	437	1.8%	445	-1.1%	440	-4.2%	421	-0.4%	419	1.4%	425
Indian Gaming Payments	266	1.5%	270	1.1%	273	-6.6%	255	-35.6%	164	41.5%	232
Statutory Transfers from Other Funds	178	-33.5%	118	-7.3%	110	0.0%	110	24.0%	136	-2.1%	133
Other	1,355	-2.1%	1,326	-74.4%	340	67.4%	569	38.0%	785	-0.9%	778
Total Revenues	**17,781**	-0.4%	**17,703**	2.8%	**18,199**	8.0%	**19,650**	-2.3%	**19,194**	3.6%	**19,878**
Expenditures											
General Government	627	-6.8%	585	10.7%	648	0.8%	653	-2.8%	635		n.a.
Public Safety	289	-4.9%	274	-5.3%	260	4.7%	272	3.2%	281		n.a.
Conservation and Development	195	-7.1%	181	0.0%	181	-6.2%	170	0.9%	172		n.a.
Health and Hospitals	1,766	-32.6%	1,190	-2.2%	1,163	2.6%	1,194	0.7%	1,203		n.a.
Human Services	3,102	16.9%	3,625	18.4%	4,292	0.5%	4,312	1.0%	4,357		n.a.
Education, Libraries and Museums	5,122	-2.3%	5,004	0.4%	5,025	3.7%	5,208	-1.0%	5,155		n.a.
Corrections and Judicial	2,061	-5.4%	1,949	-2.0%	1,911	3.0%	1,968	1.8%	2,004		n.a.
Debt Service	1,831	5.7%	1,935	1.1%	1,956	13.8%	2,225	-0.9%	2,205		n.a.
Other	2,929	3.1%	3,020	5.1%	3,175	2.3%	3,247	-2.1%	3,179		n.a.
Total Expenditures	**17,921**	-0.9%	**17,763**	4.8%	**18,611**	3.4%	**19,249**	-0.3%	**19,189**	2.3%	**19,628**

Source: Annual Financial Report of the State Controller (through FY 2020) and OPM Letter Dated April 30, 2021

The FY 2021 budget was revised downward significantly earlier in the year as the State braced for the uncertain trajectory of the pandemic and related public health measures which have weighed upon economically sensitive tax receipts. OPM's most recent April 2021 estimates indicate favorable variance relative to November 2020 estimates. Current revenue and expenditure projections however remain 1.9% and 2.3%, respectively, below amounts identified in the December 2019 biennium budget revision. Among strong performing revenues was personal income tax which is projected to exceed the revenue volatility cap by $705 million, which together with other surplus revenues is projected to support a deposit to the BRF of $955 million.

Figure 7

General Fund Estimated and Proposed Budget Operations and BRF Balance
FYE June 30 (dollars millions) (Budgetary Basis)

	FY 2021			FY 2022			FY 2023		
	12/2019 Budget Revision	11/2020 Estimate	4/2021 Estimated	Baseline Estimate	Governor's Proposed Budget	Adjusted for 4/30 Consensus Rev Est.	Baseline Estimate	Governor's Proposed Budget	Adjusted for 4/30 Consensus Rev Est.
General Fund									
Revenues[1]	20,253	19,194	19,878	19,165	20,730	21,323	19,629	21,403	21,737
Expenditures	20,086	19,845	19,628	20,915	20,519	20,519	21,756	21,131	21,131
Operating Surplus (Deficit)	166	(651)	250	(1,750)	211	804	(2,127)	272	606
Budget Reserve Fund									
Starting Balance			3,075		3,506 [1]			2,825	
as % of Current Year Budget			*15.3%*		*17.1%*			*13.4%*	
Revenue Transfers Cap			(62)		(428)			-	
Volatility Cap Deposit			705		312			339	
Deposit from Rev. Cap and Balanced Operations			250		211			272	
Transfer for Operations[1]			-		(775)			(975)	
Ending BRF Balance			3,968		2,825			2,461	
Ending Balance as a % of Ensuring Year Budget			19.3%		13.0%			N/A	

Source: State of Connecticut

[1]The $3.5 billion FY 2022 BRF starting balance assumed in Governor's Proposed Budget is based on January 2021 Concensus Revenue Estimates. This balance is lower than the $4.0 billion FY 2021 ending balance projected by OPM based on April 2021 estimates.

[2]Governor's Proposed Budget was completed in February 2021 at which time additional Federal stimulus was anticipated but not certain. Recognizing this uncertainty, it included revenues of $775 million for FY 2022 and $975 million for FY 2023 which would be derived from Federal stimulus if available and alternatively, the BRF. The American Recovery Act was passed March 11, 2021 provides substantial direct support to States so a draw on the BRF appears very unlikely at this time.

Proposed Biennium Budget

Governor Lamont released his Proposed Executive Budget for FY 2022 to FY 2023 on February 11, 2021. The proposed budget addresses baseline budgetary shortfalls of $1.8 billion in FY 2022 and $2.1 billion in FY 2023 through a variety of revenue and expenditures actions. Revenue actions considered at the time included the tentative use of $775 million from the BRF in FY 2022 and $975 million in FY 2023 as well as the delay of a planned municipal revenue sharing revenue diversion, among others. The proposal also reduces expenditures relative to baseline by $396 million (1.9%) in FY 2022 and $625 million (2.9%) in FY 2023.

Notably, the budget proposal was released prior to Congress's March 11, 2021 enactment of the American Recovery Plan (ARP), which includes $2.6 billion in direct State aid. The proposed budget accounted for the probable but uncertain receipt of additional state aid through the aforementioned allocation of the BRF balance. While it remains to be seen how the State chooses to allocate its $2.6 billion in ARP funds, KBRA notes that this amount exceeds the aggregate $1.75 billion in BRF draws identified in the budget. Given the ample federal support it is likely that the BRF will not be drawn below the 15% statutory cap during the biennium.

FY 2020 Audited GAAP Results

Audited results from the State's FY CAFR confirm stable performance in FY 2020 despite the impact of the pandemic in the final few months of the fiscal year. Of the $1.38 billion of CARES Act funds received by the State in FY 2020, $63.5 million was spent during the fiscal year with the remaining balance anticipated to be fully utilized by December 31, 2021. Revenues declined $714 million (3.4%) YoY due to pandemic related headwinds while expenditure increased $368 million (2.0%). Net other financing uses additionally declined by $285 million (19.6%) YoY reflecting reduced transfers in support of the University of Connecticut and other non-major governmental funds. In sum, General Fund balance increased $170 million (8.0%) YoY to $2.3 million including an assigning BRF balance of $3.0 billion balanced by a deficit unassigned fund balance of $1.0 billion.

Figure 8

General Fund Summary Statement of Income and Balance Sheet
FYE June 30 (Audited, GAAP Basis) (dollars in millions)

	2016	2017	2018	2019	2020
Statement of Income					
Revenues	18,215	18,502	20,663	20,776	20,062
Expenditures	17,444	17,138	18,077	18,358	18,726
Excess (Deficiency) of Rev. Over Exp.	771	1,364	2,586	2,418	1,336
Other Financing Sources (Uses)	(1,195)	(1,243)	(940)	(1,451)	(1,166)
Net Change in Fund Balance	**(424)**	**121**	**1,646**	**968**	**170**
Fund Balance (Deficit) - Beginning	(190)	(614)	(494)	1,151	2,121
Change in Reserve for Inventories	(0)	(1)	(0)	2	2
Fund Balance (Deficit) - Ending	**(614)**	**(494)**	**1,151**	**2,121**	**2,293**
Balance Sheet					
Assets					
Cash and Cash Equivalents	-	-	481	1,927	1,078
Taxes Receivable, Net	1,321	1,381	1,801	1,781	3,081
All Other	532	543	1,041	709	742
Total Assets	**1,853**	**1,924**	**3,323**	**4,417**	**4,901**
Liabilities					
Accounts Payable and Accrued Liabilities	**334**	**350**	**373**	**358**	**596**
Due to Other Funds	**432**	**356**	**84**	**75**	**84**
All Other	**1,123**	**1,062**	**1,030**	**1,049**	**1,151**
Total Liabilities	**1,889**	**1,768**	**1,487**	**1,482**	**1,831**
Deferred Inflows of Resources	578	650	685	814	777
Fund Balances					
Nonspendable	53	54	56	62	69
Committed for:	-	-	-	-	-
Continuing Appropriations	97	60	134	165	139
Budget Reserve Fund	**236**	**213**	**1,201**	**2,506**	**3,013**
Future Budget Years	-	-	-	-	-
Assigned to Surplus Transfer for 2020-2021	-	-	-	160	144
Unassigned	(999)	(821)	(241)	(771)	(1,072)
Fund Balance (Deficit) - Ending	(614)	(494)	1,151	2,121	2,293
Budget Reserve Fund as a % of Expenditures	*1.4%*	*1.2%*	*6.6%*	*13.6%*	*16.1%*
Unassigned Fund Balance as a % of Expenditures	*-5.7%*	*-4.8%*	*-1.3%*	*-4.2%*	*-5.7%*
Total Fund Balance as a % of Expenditures	*-3.5%*	*-2.9%*	*6.4%*	*11.6%*	*12.2%*

Source: State of Connecticut CAFRs FY 2016 to FY 2020

Liquidity Position

The common cash pool represents the State's operating cash and includes the Budget Reserve Fund. Available cash includes bond funds and other balances which can be made available to the common cash pool through temporary transfers under long established State practice. The State's level of cash in the common cash pool at a given point in the fiscal year reflects the seasonality of cash flow. The level of total available cash is impacted both by the rate of bond issuance and the rate of spending from those bond funds. The State has no plans to issue cash flow notes.

Figure 9

Available Cash Balance FYE June 30 (dollars in millions)						
	2016	**2017**	**2018**	**2019**	**2020**	**4/24/2021**
Common Cash Pool	$821	$1,101	$1,871	$3,558	$4,353	n.a.
Total Available Cash	$1,764	$2,657	$3,399	$4,827	$5,725	$6,942

Source: State of Connecticut Treasurer's Office | Treasurer's Cash and Debt Monthly Reports.

RD 4: State Resource Base

The State's economic base is highly developed but has experienced slow growth in recent years. Per capita personal income ranks first among the 50 States and high levels of educational attainment and low levels of poverty position the State well relative to peers in several areas. Population growth however has lagged New England and the U.S. over the last decade. Per capita personal income levels have also grown slowly in recent years and real gross state product (GSP) has been nearly flat since 2010.

The State however continues to benefit from a diverse and highly productive economic base. In 2020, 13 "Fortune 500" companies were headquartered in Connecticut, including United Technologies Corporation (UTC), Cigna, Charter Communications, Hartford Financial Services and Stanley Black & Decker. The defense industry is an important component of the State's economy and has demonstrated renewed strength since 2002, a trend that is expected to continue. Major defense companies include Sikorsky Aircraft (a division of Lockheed Martin), and General Dynamics Corporation's Electric Boat Division.

UTC, historically headquartered in Hartford, CT completed a merger with Raytheon Company in April 2020 to form Raytheon Technologies. The consolidated entity is headquartered in Waltham, MA but Governor Lamont has stated that nearly all of UTC's 19,000 employees will remain in Connecticut, with approximately 100 moving to the new headquarters.

Population

The U.S. Census Bureau had estimated a trend of modest population decline in Connecticut over the last decade, but recently released population counts from the decennial census indicate a trend of slight growth from 2010 to 2020. Connecticut's population increased 0.89% over the period compared to New England Growth of 2.39% and U.S. growth of 7.35%.

Figure 10

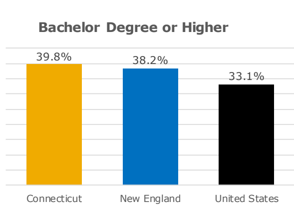
Population Change					
	2000	2010	2020	10-Yr CAGR	10-Yr Change
Connecticut	3,405,565	3,574,097	3,605,944	0.09%	0.89%
New England	7,573,420	7,897,236	8,086,288	0.24%	2.39%
United States	281,421,906	308,745,538	331,449,281	0.71%	7.35%

Source: U.S. Census Bureau Decennial Population Counts

Educational Attainment, Poverty, and Age Groups

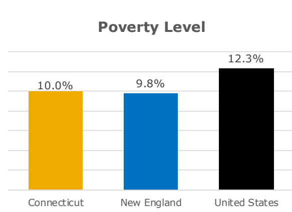
Educational attainment in Connecticut and the New England region is high relative to the U.S. Poverty in the State is well below the U.S. average. Connecticut's proportion of working age individuals is higher than the U.S.

Figure 11



As of 2019

Figure 12

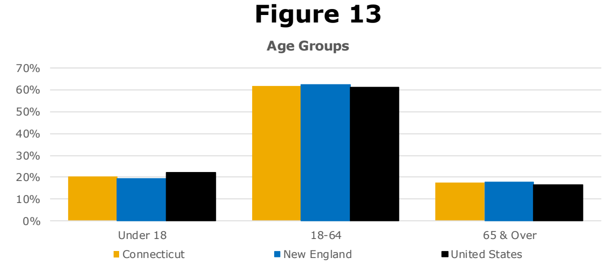


As of 2019

	Point Δ 2010 to 2019	Point Δ 2010 to 2019
Connecticut	4.3	-0.1
New England	5.2	-1.8
United States	4.9	-3.0

Source: U.S Census
Bachelor degree or higher defined as "% of population over 25 with Bachelor's degree or higher".
Poverty level defined as "portion of population living below the poverty line".

Figure 13



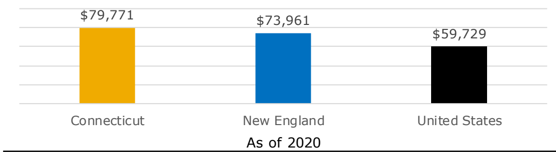
	Under 18	18-64	65 & Over	Age Dependecy Ratio
Connecticut	20%	62%	18%	61.4%
New England	20%	63%	18%	59.7%
United States	22%	61%	16%	63.1%

Per Capita Personal Income

Per capita personal income at $79,771 in 2020 is the highest in the country reflecting the concentration of the State's economy in high value-added industries. Per capita personal income growth however has lagged since 2010.

Figure 14

Personal Income Per Capita



	% Δ 2010 to 2020	Comparison
Connecticut	28.5%	-
New England	42.0%	108% of Region
United States	47.3%	134% of U.S.

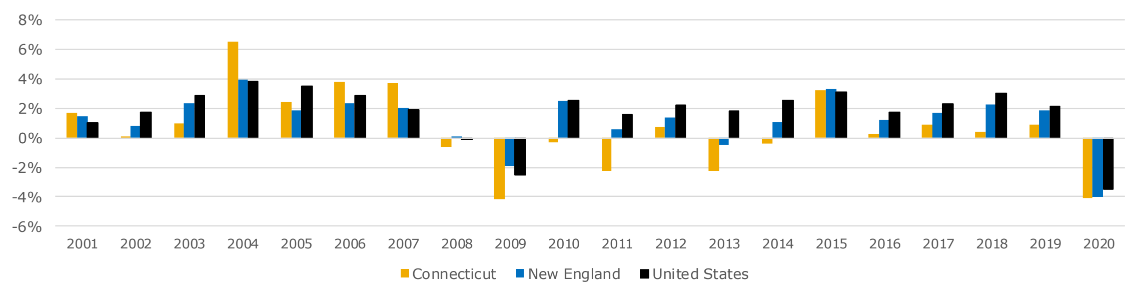
Source: U.S. Bureau of Economic Analysis

Real Gross State Product

Connecticut's real (inflation adjusted) GSP experienced a more pronounced decline and weaker recovery following the Great Recession than the region and U.S. overall, contracting in seven of the last thirteen years. In KBRA's view, the decline reflects poor performance in the State's pharmaceuticals and financial activities sectors, both of which were outsized contributors to growth in the decade preceding the Great Recession. The financial activities sector declined from 31.0% of GSP in 2009 to 27.7% in 2019. Pharmaceutical sector activity has additionally declined due to the reduction of activity in the State by Pfizer, Bayer, and Bristol Myers Squibb. This drag is evidenced by the decline in chemical manufacturing as a share of total GSP from 7.5% in 2006 to 1.7% in 2017.[1] Per onset of the pandemic, real GSP declined 4.1% in 2020, a decline somewhat larger than the New England region (down 4.0%) and U.S. (down 3.5%).

Figure 15

Real GSP Annual Change
(chained 2012 dollars)



($ in Millions)	2000	2010	2020	% Δ 2010 to 2020	10-Year CAGR (2020)
Connecticut	216,293,100	247,876,800	241,053,000	-2.8%	-0.3%
New England	749,152,700	872,608,700	950,674,000	8.9%	0.9%
United States	13,130,987,000	15,598,753,000	18,426,076,000	18.1%	1.7%

Source: U.S. Bureau of Economic Analysis

Note: Output for the "United States" represents GDP of the United States, not the sum of all 50 states.

Employment

State unemployment peaked to increased from an average of 3.6% in 2019 to a high of 11.5% in July 2021 following onset of the pandemic and implementation of public health measures. This peak was lower than the New England and U.S. highs of 13.8% and 14.4%, respectively, in April 2021. As of March 2021, Connecticut unemployment has recovered to 8.3%, which is somewhat higher than New England (6.4%) and the U.S. (6.2%).

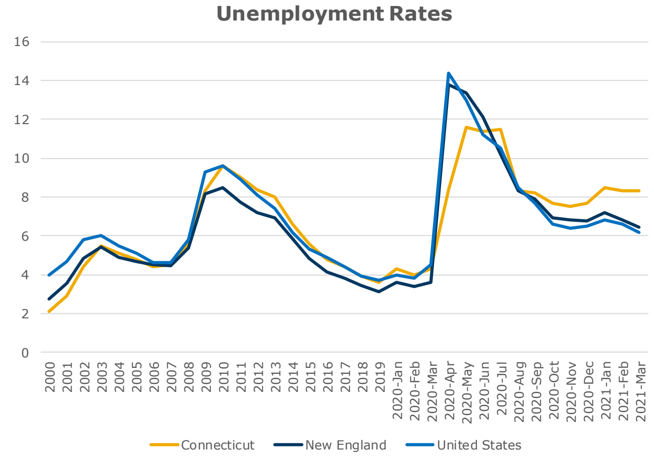
[1] Most recent GSP data for chemical manufacturing sector is 2017.

Figure 16

Total Employment (Not Seasonally Adjusted) (in thousands)	Connecticut	Δ(%)	New England	Δ(%)	United States	Δ(%)
2000	1,724		7,138		136,891	
2001	1,699	-1.5%	7,120	-0.3%	136,933	0.0%
2002	1,698	0.0%	7,125	0.1%	136,485	-0.3%
2003	1,688	-0.6%	7,100	-0.4%	137,736	0.9%
2004	1,687	-0.1%	7,118	0.2%	139,252	1.1%
2005	1,708	1.2%	7,164	0.6%	141,730	1.8%
2006	1,750	2.5%	7,260	1.3%	144,427	1.9%
2007	1,773	1.3%	7,311	0.7%	146,047	1.1%
2008	1,772	0.0%	7,297	-0.2%	145,362	-0.5%
2009	1,731	-2.3%	7,097	-2.7%	139,877	-3.8%
2010	1,728	-0.2%	7,102	0.1%	139,064	-0.6%
2011	1,742	0.8%	7,154	0.7%	139,869	0.6%
2012	1,730	-0.7%	7,192	0.5%	142,469	1.9%
2013	1,719	-0.6%	7,204	0.2%	143,929	1.0%
2014	1,764	2.6%	7,348	2.0%	146,305	1.7%
2015	1,786	1.2%	7,437	1.2%	148,834	1.7%
2016	1,801	0.9%	7,532	1.3%	151,436	1.7%
2017	1,819	1.0%	7,638	1.4%	153,337	1.3%
2018	1,831	0.6%	7,758	1.6%	155,761	1.6%
2019	1,848	1.0%	7,822	0.8%	157,538	1.1%
2020	1,725	-6.7%	7,749	-0.9%	156,994	-0.3%
Δ 2010 to 2020	-0.2%		9.1%		12.9%	
March 2021	1,582		7,202		150,493	
Δ 2019 Avg to March 2021	-14.4%		-7.9%		-4.5%	

Source: U.S. Bureau of Labor Statistics

Figure 17



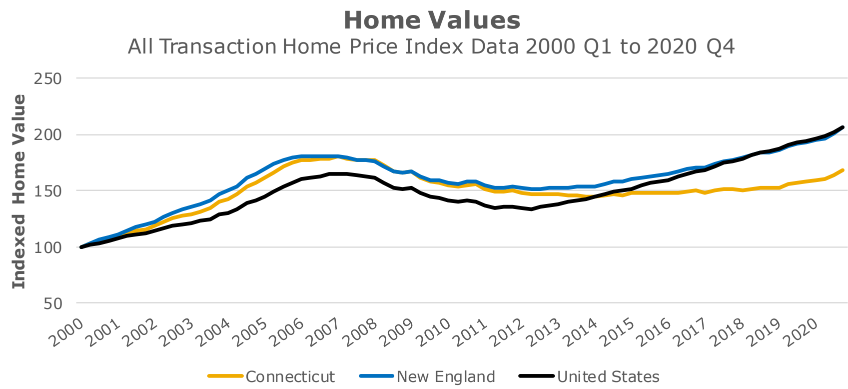
	Connecticut	New England	United States
March 2021	8.3	6.4	6.2
Great Recession Peak	9.6	8.5	9.6
Point Δ Since Great Recession Peak	-1.3	-2.0	-3.4

Source: U.S. Bureau of Labor Statistics

Home Values

Connecticut home value appreciation has lagged the region and the U.S. by a significant margin since the year 2000. As of Q4 2020, home values are 7% below the prior Q1 2007 peak compared to New England and U.S. home value 13.8% and 24.7%, respectively, in excess of prior highs. Home value have performed well through the pandemic and as of Q4 2020 are up 6.3% YoY versus New England values up 6.6% and U.S. values up 6.0%

Figure 18



Source: Federal Housing Finance Agency