

Research

Summary:

West Hartford, Connecticut; General Obligation

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Credit Profile

US\$324.4 mil GO bnds ser 2021B due 07/01/2046

Long Term Rating

AAA/Stable

New

West Hartford Twn GO

Long Term Rating

AAA/Stable

Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to West Hartford, Conn.'s \$324 million series 2021B general obligation (GO) taxable bonds. At the same time, S&P Global Ratings affirmed its 'AAA' rating on the town's GO debt outstanding. The outlook is stable.

West Hartford's full faith and credit pledge, payable from the levy of an unlimited ad valorem tax on all taxable property in the town, secures the bonds and GO debt outstanding.

Proceeds from the series 2021 bonds will fully fund the town's unfunded actuarially accrued liability of its pension system. The town estimates that fully funding the actuarial accrued liability reduces cumulative pension contributions by over \$140 million on a present-value basis over the next 30 years. Initially, while the debt burden increases, the town's pension costs will substantially decrease, resulting in little to no budgetary effect in the beginning. Management is reducing the discount rate of the pension plan from the current 6.99% level to a more conservative 6.25%, along with establishing a pension bond reserve fund. In terms of credit, we understand these actions likely limit the budgetary effects of future cost volatility to operations in the event of adverse investment returns.

Credit overview

West Hartford has a very strong set of financial policies and controls that are institutionalized and embedded into its overall financial management, which, in our view, is a key factor contributing to its ability to sustain budgetary balance, even through a period of economic uncertainty due to the pandemic. Moreover, the town will likely maintain a steady pace of modest economic growth as construction-related development has been largely unaffected by the pandemic, and the level of economic deterioration in the county is less severe than the national base-case forecasts.

The rating also factors the town's steady operations and proactive management team that has been able to navigate the challenges related to the pandemic and address long-term challenges in a proactive manner. We anticipate management will continue and make budgetary adjustments to preserve its current strong reserve position as it has demonstrated through various economic and business cycles.

West Hartford's GO debt is eligible to be rated above the sovereign because we believe the town can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), West

Hartford has a predominantly locally derived revenue source, with approximately 84% of general fund revenue coming from property taxes. The town also has independent taxing authority and treasury management from the federal government.

The rating further reflects our opinion of the following factors for West Hartford, specifically its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with slight operating surpluses in the general fund and at the total governmental fund level in fiscal 2020;
- Strong budgetary flexibility, with an available fund balance in fiscal 2020 of 13.8% of operating expenditures;
- Very strong liquidity, with total government available cash at 18.0% of total governmental fund expenditures and 3.1x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability profile, with debt service carrying charges projected to increase to 12.2%, from 5.8% of expenditures in 2019, following this issuance, as well as net direct debt that is also increasing, to 129.6% of total governmental fund revenue; and
- Strong institutional framework score.

Environmental, social, and governance factors

We evaluated the town's environmental, social, and governance (ESG) factors relative to its economy, financial measures, management, and debt and long-term liability profile, and consider each in line with the sector standard. We note its favorable demographics are a social advantage supporting its historically strong financial operations through consistently strong economic activity and revenue collections. We acknowledge the town's proactive posture in managing its pension and other postemployment benefits (OPEB) exposure as positive governance factors.

Stable Outlook

Downside scenario

Should the town's budgetary performance unexpectedly deteriorate as a result of pressure from rising operating expenditures, shortfalls in key revenue sources, or otherwise, leading to a significant weakening of reserves or liquidity to levels we no longer view as commensurate with those of similarly rated peers, we could lower the rating.

Additionally, while we believe this issuance addresses the town's retirement liabilities, over the long term, we could lower the rating should growth in fixed costs associated with debt, pension, and OPEB crowd out other general fund expenditures or outpace revenue, leading to a deterioration in budgetary performance and weakened reserves.

Credit Opinion

Very strong economy

We consider West Hartford's economy very strong. The town, with a population of 63,360, is a largely developed and suburban residential community, bordering Hartford in Hartford County. It is in the Hartford-West Hartford-East Hartford MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 160% of the national level and per capita market value of \$144,616. Overall, market value was stable over the past year, at \$9.1 billion in 2021.

Interstate 84 traverses the town, connecting residents with a diverse regional employment base. Although the tax base is primarily residential, West Hartford hosts a substantial local commercial base and is a regional retail and restaurant destination. The local economy also features employers in government, health care, higher education, and manufacturing.

Prior to the pandemic, West Hartford experienced diversified residential and commercial development activity, contributing to a steady increase in building permit revenue and tax base growth. Due to the desirability of the community's service base, the town's real estate environment has been robust, with steady appreciation in values.

The regional economy in Hartford County is well-diversified and has been slowly growing over the past few years, but the pandemic has stymied its momentum. The county unemployment rate was 3.9% in 2019, although it increased significantly because of the stay-at-home orders, peaking at 10.7% in July 2020. Unemployment has since come down to 8.6% as of March 2021. IHS Markit forecasts Hartford County's real gross county product (GCP) fell by 2.7% in calendar 2020, which we note is better than the state's decline. The forecast suggests that economic activity will return to pre-pandemic levels in late 2021, increasing 4.8% in 2021 and 2.2% in 2022. This is in line with S&P Global Economics' U.S. base-case forecasts. (For more information on S&P Global Ratings' economic outlook, please see "Economic Outlook U.S. Q2 2021: Let The Good Times Roll," published March 24, 2021.)

Very strong management

We view the town's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well-embedded, and likely sustainable.

Demonstrating the town's key budgeting practices is management's use of three to five years of historical data to forecast annual revenue and expenditure assumptions. In preparing its annual budget, management conducts a line-item review of each department's annual operation request; prioritizes operating expenditures, including future debt service and long-term liability costs; and incorporates changes in contractual obligations. Due to the uncertainty of state aid in recent years, finance officials conservatively estimate revenue from this source, and management solicits department input on local fees and charges for services.

During each fiscal year, management monitors the budget regularly, reporting budget-to-actual results to the town council monthly. Furthermore, West Hartford adheres to its formal investment policy and reports earnings and holdings monthly to the town council. The town also has a comprehensive five-year financial forecast in its budget development process, which features analysis of key revenue and expenditure assumptions and tests budget performance under various conditions; this allows it to manage decisions and changes related to future operations, capital projects, and debt service.

West Hartford also maintains a strong focus on capital planning, as evidenced by its 12-year comprehensive capital improvement program (CIP) that identifies capital and nonrecurring capital expenditures. The town updates its CIP annually and details pay-as-you-go funding requirements, intergovernmental grants and reimbursements, and debt financing of all capital projects. Furthermore, management has historically met and sustained reserves in accordance with its fund balance policy. The formal policy calls for unassigned fund balance to stay between 7.5% and 15% of general fund expenditures to manage financial resources and maintain current service levels in the event of unexpected revenue shortfalls or unpredicted one-time expenditures. In accordance with the policy, should funds fall below 7.5%, the town will take necessary steps to restore unassigned fund balance to, or above, the minimum target level.

West Hartford also sustains a formal debt management policy which stipulates the use of certain debt instruments and reporting requirements. The policy formalizes measurable debt benchmarks and metrics, including annual debt service that will be no more than 10% of general fund expenditures and that debt amortization will not be less than 65% of principal being retired over 10 years. The town has historically monitored and sustained debt management practices in accordance with this policy and does acknowledge the policy will require some revisions following the issuance of the pension obligation bonds (POB).

Strong budgetary performance

The town had slight operating surpluses of 0.9% of expenditures in the general fund and 1.1% across all governmental funds in fiscal 2020. General fund operating results of the town have been stable over the last three years, with results of 0.3% in 2020 and 0.2% in 2018. Despite steady operating performance, we continue to factor in the potential downside risks stemming from the COVID-19 pandemic and its effects on economically sensitive revenues. Ultimately, in our view, the general fund performance should remain steady and in line with the budget, in large part due to the town's proactive budget monitoring and generally conservative budgeting practices.

The pandemic and state-mandated stay-at-home measures dampened fiscal 2020 revenues, primarily economically sensitive local receipts. However, a conservative budget and immediate expenditure-monitoring measures, implemented following the onset of the pandemic, allowed the town to post a general fund surplus.

West Hartford has a comprehensive budgeting development and monitoring framework, as well as forward-looking expenditure and fixed-cost planning, which has allowed it to navigate the financial effects of COVID-19 without significant deterioration. Changes in the tax rate have been consistent and timely to match West Hartford's expenditure needs. The town benefits from an overall stable and strong property tax base, which generated approximately 81% of general fund revenue in fiscal 2020. Tax collections have remained strong, exceeding 99%. Notably, there was no significant disruption in tax collections in fiscal year 2020, and for 2021, current collections are in line with previous years.

Direct pandemic-related costs are reimbursable through Federal Emergency Management Agency (FEMA) and Coronavirus Aid, Relief, and Economic Security (CARES) Act funding, further limiting negative pressure on the budget. For the fiscal 2021 budget, the town cut both revenues and certain expenditures to reflect any potential downside risks from COVID-19. The 2021 budget initially included an appropriation of reserves; however, given better-than-anticipated revenue performance, management is stating overall balances will remain level, if not

improved from 2020 results. Moreover, the town is eligible to receive upward of \$37 million in direct American Rescue Plan (ARP) funds, and the school district is also benefiting from Elementary and Secondary School Emergency Relief (ESSER) stimulus funds, which we believe will support steady operating performance across all its major departments. The fiscal 2022 budget totals \$308.4 million, an increase of 2.7% over the previous year.

Strong budgetary flexibility

West Hartford's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2020 of 13.8% of operating expenditures, or \$44.9 million. The available fund balance includes \$29.8 million (9.2% of expenditures) in the general fund and \$15.1 million (4.6%) that is outside the general fund in the town internal service funds but legally available for operations. Operating activity in the internal service funds have been stable, and reserve balances have seen steady improvements.

While not included in our reserve ratios, the town has also traditionally committed recent surpluses as stabilization reserves to its capital nonrecurring expenditure fund (approximately \$5.1 million balance) and the debt service fund (about \$1.3 million). While these are designated for debt and capital, we generally view them as part of the town's overall reserve capacity, which indirectly alleviates reliance on available general fund balance.

West Hartford will likely continue to budget for balanced operations annually, and it will make expenditure and revenue adjustments to try and outperform the budget at year-end. Based on the town's projections to finish fiscal 2021, we believe West Hartford will sustain reserves at strong levels over the next two years. As noted above, further enhancing our view of the stability of West Hartford's fund balance is its formal reserve policy, which sets a minimum reserve level at 7.5% of expenditures, which are levels management is intent on maintaining.

Very strong liquidity

In our opinion, West Hartford's liquidity is very strong, with total government available cash at 18.0% of total governmental fund expenditures and 3.1x governmental debt service in 2020. In our view, the town has strong access to external liquidity, if necessary.

West Hartford is a regular market participant that has issued debt periodically over the past 20 years, including GO bonds. Furthermore, with the majority of cash invested in liquid money market funds, certificates of deposit, and the state investment pool, which maintain maturities of less than one year, we believe its investments are not aggressive.

We understand West Hartford has not entered into bank loans, direct-purchase debt, or contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. Given its strong overall cash position and historically stable budgetary environment, we believe West Hartford's liquidity profile should remain very strong.

Weak debt and contingent liability profile

Following this bond issuance, total governmental fund debt service is projected to increase to an estimated 12% of total governmental fund expenditures, and net direct debt is 129.6% of total governmental fund revenue. West Hartford has approximately \$456 million of total direct debt outstanding, inclusive of the POB. Our assessment of the town's overall net debt includes its proportionate share of overlapping debt--totaling \$183 million--related to the Metropolitan District Commission, a special district in Hartford County providing water and sanitary sewer services to

eight member towns. As outlined in West Hartford's 12-year CIP, it expects to issue approximately \$20 million in bonds annually over the next several years for capital-related purposes.

Pension and other postemployment benefits:

- We no longer believe West Hartford's pension and OPEB obligation is a credit weakness, given how management has proactively managed these accounts and the projected funded status pension plan. As noted, management is reducing the discount rate of the pension plan to a more conservative 6.25%, from the current 6.99% level, and establishing a pension bond reserve fund to manage market volatility.
- The town is making progress in addressing its OPEB liability, and we note costs remain low. We recognize that costs will likely continue and increase, given the size of the unfunded liability. We view this a long-term challenge, but continually recognize management's efforts in funding the plan as well as reviewing underlying assumptions and making prudent changes to mitigate the town's exposure to unforeseen risks.

The town participates in the West Hartford Contributory Retirement System. The town also provides medical benefits to eligible retirees and covered dependents. As of June 30, 2020, its net OPEB liability totaled \$213 million and was 4% funded. We believe West Hartford continues to actively manage its pension and OPEB liabilities through comprehensive long-term planning, full funding of the ADC on an actuarial basis, and through its working relationship with collective-bargaining units.

West Hartford contributes the full normal cost for current employees hired since 2003, in addition to prefunding its OPEB liabilities in an OPEB trust fund; the total net position of the trust fund was \$9.6 million as of June 30, 2020. It also maintains a retiree health reserve that had a balance of \$13.4 million as of June 30, 2020. The annual OPEB cost to amortize the liability over 30 years was \$14.8 million in fiscal 2020, of which the town contributed \$16.0 million, or 108% of the required contribution.

Strong institutional framework

The institutional framework score for Connecticut municipalities is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

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