

CREDIT OPINION

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Hartford County Metropolitan District, CT

Update to credit analysis

Summary

The credit profile of the Hartford County Metropolitan District (Aa2 GO and revenue rating) reflects the MDC's large and stable service area that is comprised of seven member municipalities with generally strong credit profiles including healthy resident wealth, stable economies and solid financial performance. The ratings of this group range between Aa1 (West Hartford) and Aa3 (East Hartford) and are in contrast to the comparatively weak credit profile of the City of Hartford (Ba2 positive), which is the 8th and largest member municipality and constitutes approximately 26% of the MDC ad valorem property tax revenues. However, the City of Hartford's financial profile has trended favorably over the last several years including stronger reserves and liquidity through fiscal 2022.

MDC's solid financial operations include reflected in healthy days cash on hand in the water and sewer system and strong financial performance of the clean water project fund evidenced by 2.4 times debt service coverage and 449 days cash on hand. The district also has a very strong capital planning program that is done in collaboration with Department of Energy and Environmental Protection (DEEP). The detailed and constantly monitored plan reduces the likelihood that the MDC will suffer any prohibitively negative financial or operational impacts from the administration of its very large \$2 billion capital plan. The size of this plan will also result the district continuing to have a well above average leverage position.

The MDC's credit quality is also boosted by provisions of Public Act 17-1, which stipulates that in the event of non-payment by a member entity, the district can establish an emergency budget increasing the levy on other members to cover the short-fall. Public Act 17-1 also allows the state to redirect a member municipality's PILOT payments to the MDC if the city fails to pay its ad valorem taxes.

On July 18, we upgraded the district's general obligation bond rating to Aa2 from Aa3 and affirmed the Aa2 rating on the district's revenue bonds. The outlook is stable.

Credit strengths

- » Large service area customer base
- » Solid resident income
- » Ample water supply and treatment capacity
- » Healthy financial operations
- » Provisions of Public Act 17-1

Credit challenges

- » Sizable debt burden
- » Substantial capital plan
- » Weak credit quality of City of Hartford, the largest member municipality

Rating outlook

The stable outlook reflects our expectation that there will be no material credit deterioration among the member cities, water and sewer operating performance will remain consistent and the clean water project fund will continue to produce strong coverage of the revenue bonds.

Factors that could lead to an upgrade

- » Improved credit quality of member cities
- » Service area expansion and growth including strengthened wealth indicators
- » Further improvement in sewer and water funds' financial position, including increased liquidity and unrestricted reserves
- » Substantially decreased debt burden

Factors that could lead to a downgrade

- » Ineffective implementation of capital improvement plans
- » Significant deterioration of member city credit quality
- » Weakening of the service area, including income and wealth metrics
- » Material reduction of MDC's cash reserves and financial flexibility
- » Weakened liquidity resulting in need for cash flow borrowing

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 1

Hartford County Metropolitan District, CT

Hartford Metropolitan Water District	2018	2019	2020	2021	2022
Economy/Tax Base					
Total Full Value (\$000)	\$35,539,971	\$36,006,951	\$36,508,899	\$37,076,934	\$37,580,942
Population	362,767	362,877	361,856	365,727	365,727
Full Value Per Capita	\$97,969	\$99,226	\$100,893	\$101,379	\$102,757
Median Family Income (% of US Median)	112.0%	112.0%	112.0%	112.0%	112.0%
Finances					
Operating Revenue (\$000)	\$68,897	\$75,656	\$83,424	\$82,280	\$91,102
Fund Balance (\$000)	\$23,227	\$24,700	\$81,870	\$25,590	\$29,069
Cash Balance (\$000)	\$16,213	\$21,965	\$28,835	\$26,945	\$29,214
Fund Balance as a % of Revenues	33.7%	32.6%	98.1%	31.1%	31.9%
Cash Balance as a % of Revenues	23.5%	29.0%	34.6%	32.7%	32.1%
Debt/Pensions					
Net Direct Debt (\$000)	\$559,330	\$527,219	\$476,391	\$435,416	\$433,151
3-Year Average of Moody's ANPL (\$000)	\$0	\$0	\$201,281	\$216,106	\$204,158
Net Direct Debt / Full Value (%)	1.6%	1.5%	1.3%	1.2%	1.2%
Net Direct Debt / Operating Revenues (x)	8.1x	7.0x	5.7x	5.3x	4.8x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.0%	0.0%	0.6%	0.6%	0.5%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.0x	0.0x	2.4x	2.6x	2.2x

General Fund

Source: US Census Bureau, Hartford County Metropolitan District, CT's financial statements and Moody's Investors Service

Profile

The district provides water supply, sewer collection, treatment and disposal services to its eight member communities including Bloomfield, East Hartford, Hartford, Newington, Rocky Hill, West Hartford, Wethersfield, and Windsor. The district also has special agreements for water supply and sewage disposal facilities with non-member towns and various state facilities.

Detailed credit considerations

Economy and Service Area: Large and stable economy and water system

The MDC's large service territory and population is anchored by the greater Hartford metro area, in which the City of Hartford (Ba2) is the largest member. In addition to being the state capitol, the City of Hartford has long been a hub of insurance and financial services and supports a broad public sector. However, the city's resident wealth and income measures are the weakest of the member cities and in sharp contrast to the other, wealthy cities that predominate the MDC membership and counterbalance the weakness of Hartford's wealth profile. We anticipate that these dynamics will persist and that the district will continue to have a stable economy characterized by comparatively weak core ringed by fairly strong suburban wealth and income.

The district is authorized to levy unlimited ad valorem taxes on its member municipalities in proportion to their participation in the MDC and the revenue they provide to support debt service on the GO bonds. Current assessment proportions are: Town of Bloomfield (Aa2) 7%; Town of East Hartford (Aa3) 12%; City of Hartford 26%; Town of Newington 9%; Town of Rocky Hill 6%; Town of West Hartford (Aa1 stable) 23%; Town of Wethersfield (Aa2) 8%; and Town of Windsor 9%. In aggregate, the member communities' tax bases (equalized net grand lists or ENGLs) is quite substantial at approximately \$48 billion for 2023.

The weighted average median family income is approximately 112% of the US median, as the concentration of wealth in the suburban areas is balanced by the City of Hartford's well-below average resident incomes.

System Characteristics

The district draws water from the Barkhamsted Reservoir, which at 30.3 billion gallons, is the single largest water source in Connecticut. MDC also has access to the Nepaug Reservoir, which holds 9.5 billion gallons. These sources provides the MDC with ample supply to meet its average daily use of approximately 37 mgd, which is a mark that has held fairly steady over the last several years. Though the pandemic drove significant declines in commercial, industrial and public water customers this was offset by increased residential water customers, which constitute 95% of ratepayers. Nonetheless, fiscal 2023 average daily consumption was 37 mgd, which is inline with usage over the last five years.

Sewer service is provided through the operation of four water pollution and treatment facilities that have a total design flow capacity of 105 mgd and a treatment capacity of 200 mgd. This compares favorably to the MDC average daily sewer flow of 80 mgd.

Financial Operations: Solid operating performance for sewer, water, and clean water project fund

The MDC financial operations are solid and are characterized by healthy liquidity, reserves and coverage among the sewer, water and clean water project funds. Each of these areas have been bolstered by sound rate management and consistent cost oversight resulting in stable operating performance for the last several years. We anticipate a continuation of this profile and only minimal change among the key financial ratios.

The MDC's ad valorem taxes primarily support the system's sewer (general fund) operations. After a modest deficit in fiscal 2021, the district's fiscal 2022 audit (most recent available) show a \$4 million surplus. This was driven by increased revenues resulting from higher property tax receipts and sewer user fee revenue. The fiscal 2023 budget is balanced though the district is on track to have a modest \$2.9 million surplus. The sewer fund's 37% fund balance is healthy and in line with MDC historical average.

The water system produced a strong \$33.5 million surplus in fiscal 2022 and has budgeted for balanced operations in fiscal 2023 though we anticipate another operating surplus of approximately \$2.6 million. Audited results for fiscal 2022 show that the clean water project fund generated a \$30.5 million surplus prior to transfers, which resulted in a \$5.8 million reduction to reserves. Nonetheless, the clean water project fund has a \$65 million ending balance that is 79% of fiscal 2022 revenues. Clean water project revenues will rise in fiscal 2023 in part because of a \$0.15 increase to the clean water project charge. This is the first of four successive projected rate increases through 2026.

Fiscal 2023 debt service coverage of the revenue bonds is projected to be 2.4x, including the clean water fund loan and general obligation bonds (GO bonds that were issued to support water projects). The district projects revenue bond coverage to be between 2.5 and 3 times for the next three years.

Liquidity

The water and sewer system have a combined days cash on hand of approximately 294 days, which is a figure we expect to remain consistent for the foreseeable future. Liquidity within the clean water project fund is an even more solid 449 days and likely to remain consistent.

Debt, Pensions and OPEB

The district is highly leveraged with debt totaling approximately 5% of the tax bases of the towns it services. The district entered into a consent order and a consent decree with the State Department of Environmental Protection, Department of Justice and US Environmental Protection Agency to address sanitary sewer overflow, nitrogen reduction and combined sewer overflow issues. The project is estimated to cost approximately \$2.1 billion. Moving forward, the district plans to fund the remaining CWP costs through SRF loans, state and federal grants and, to a lesser extent, revenue bonds.

Legal security

The GO bonds are payable from general property tax revenues collected from the City of Hartford and the Towns of Bloomfield, East Hartford, Newington, Rocky Hill, West Hartford, Wethersfield and Windsor, Connecticut. The district is authorized to levy unlimited taxes upon the Member Municipalities comprising the district proportionately.

The revenue bonds are secured by a gross revenue pledge of the district's dedicated Clean Water Project Charge revenue, including transfers from the rate stabilization fund. The charge is billed directly to system customers, not the member municipalities. The MDC has unlimited ability to increase the charge.

Debt structure

All outstanding debt is fixed-rate.

The revenue bonds have adequate legal protections including a rate covenant and additional bonds test of 1.2 times, as well as a closed loop flow of funds. The flow of funds mandates that the Clean Water Project Charge may only be used for debt service on CWP debt and the revenue bonds have a senior claim on clean water charges. After debt service on the revenue bonds is paid, residual charge revenues are deposited in the RSF, where they are legally available to pay debt service on any debt issued to fund the CWP as well as capital expenses for the CWP. During any period, the district can make transfers from the RSF to the revenue fund to an overall maximum of 35% of debt service on the bonds; these transfers can be included as revenue for coverage calculations to meet the rate covenant. There is no limitation on the amount of the RSF that can be used for debt service.

Debt-related derivatives

The MDC is not party to any interest rate swaps or other derivative agreements.

Pensions and OPEB

MDC maintains the Metropolitan District Employees' Retirement System ("MDERS"), which is a defined benefit, single employer retirement system. The MDERS provides retirement, disability and death benefits to plan members and beneficiaries.

The district's pension costs are manageable and only about 4% of water and sewer system revenue. In addition, the district's pensions contribution was 173% of the "tread water" indicator or the amount necessary to prevent the liability from rising over time. The district actuarially determined contribution for its OPEB expense fell to \$12 million in fiscal 2022 to \$7.8 million in fiscal 2023. This allowed the district's actual contribution to match its ADC for the first time in the last four years.

ESG considerations**Environmental**

MDC is an area with low exposure to heat and water stress and medium risk for hurricanes and extreme rain. Because of its inland location, the MDC has no exposure to sea level rise. As such, environmental risks are not a material credit weakness for the district

Social

Social factors do not represent a new material credit risk and are incorporated into the rating. Though the economy and resident income levels of the City of Hartford are weaker than the remaining portions of the district, this has not resulted in a significant change to the customer base and is somewhat offset by economic quality of the other participating municipalities.

Governance

The MDC benefits from solid governance functions that include effective rate management, detailed and sophisticated capital plans, a history of stable operating performance.

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