

CREDIT OPINION

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Hartford County Metropolitan District, CT

Update to credit analysis

Summary

The credit quality of the Metropolitan District of Hartford County (MDC, Aa2) reflects the district's strong and sizable property tax base resultant of the combined values of the district's eight member municipalities. None of the member municipalities has ever failed to pay their property taxes to the district on time and in full. 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.

In addition, the member municipalities have generally solid overall credit profiles that includes healthy resident income and overall stability. MDC's credit position is also driven by its solid fiscal profile, including healthy reserves and a very large but well managed capital program and our expectation of continued managerial effectiveness.

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

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 resident income above approximately 125%

- » 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 resident income below 100%
- » Material reduction of MDC's cash reserves and financial flexibility
- » Weakened liquidity resulting in need for cash flow borrowing

Key indicators

Exhibit 1

Hartford MDC	2019	2020	2021	2022	2023
Economy/Tax Base					
Total Full Value (\$000)	\$36,006,951	\$36,508,899	\$37,076,934	\$37,580,942	\$40,779,779
Population	362,877	361,856	365,727	365,727	365,727
Full Value Per Capita	\$99,226	\$100,893	\$101,379	\$102,757	\$111,503
Median Family Income (% of US Median)	112.0%	112.0%	112.0%	112.0%	114.0%
Finances					
Operating Revenue (\$000)	\$139,020	\$142,978	\$139,947	\$150,438	\$157,037
Fund Balance (\$000)	\$27,445	\$34,615	\$30,790	\$31,817	\$38,438
Cash Balance (\$000)	\$24,710	\$31,580	\$32,146	\$31,962	\$39,024
Fund Balance as a % of Revenues	19.7%	24.2%	22.0%	21.1%	24.5%
Cash Balance as a % of Revenues	17.8%	22.1%	23.0%	21.2%	24.9%
Debt/Pensions					
Net Direct Debt (\$000)	\$1,310,834	\$1,320,077	\$1,383,676	\$1,399,466	\$1,414,999
3-Year Average of Moody's ANPL (\$000)	\$0	\$201,281	\$216,106	\$204,158	\$174,834
Net Direct Debt / Full Value (%)	3.6%	3.6%	3.7%	3.7%	3.5%
Net Direct Debt / Operating Revenues (x)	9.4x	9.2x	9.9x	9.3x	9.0x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.0%	0.6%	0.6%	0.5%	0.4%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.0x	1.4x	1.5x	1.4x	1.1x

Source: Hartford MDC audited financial statements and Moody's Ratings

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 10 non-member towns and various state facilities.

Detailed credit considerations

Economy and Service Area: Large and generally stable economy and service area

MDC's economy is anchored by the City of Hartford (Baa3), which as the state capitol, is also the area's economic focal point and a hub for financial services, insurance and a broad public sector. Hartford is the largest of the MDC's eight member municipalities and contributes the largest portion of ad valorem property taxes at 26.1%. However, the city's resident wealth and income measures are the weakest of the member cities and in sharp contrast to the other, wealthier cities that predominate the MDC membership.

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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) 7.3%; Town of East Hartford (Aa3) 11.6%; Town of Newington 9%; Town of Rocky Hill 6.3%; Town of West Hartford (Aa1 stable) 22.7%; Town of Wethersfield (Aa2) 8.1%; and Town of Windsor 9%. In aggregate, the member communities' tax bases (equalized net grand lists or ENGLs) is quite substantial and more than \$40 billion.

The weighted average median family income is approximately 114% 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

Sewer service is provided through the operation of four water pollution and treatment facilities that have a total design flow capacity of 115 mgd and a treatment capacity of 225 mgd. This compares favorably to the MDC average daily sewer flow of 80 mgd.

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.

Residential water customers are approximately 95% of water sales, though wet weather drove consumption modestly below budgeted expectations in fiscal 2023.

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. However, the district has maintained a collaborative relationship with the regulators and we expect that the district will meet the requirements of the decree without material compromise to credit quality.

The district also has exposure to a pending litigation related to construction of the South Hartford Conveyance and Storage Tunnel. The project was funded by the district and the State, who are in mediation with the contractor. The district has set aside money to fund any potential liability in the event of an adverse ruling. In addition, the state is responsible for 42% of any judgement.

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

The MDC's ad valorem taxes primarily support the system's sewer (general fund) operations. The district's fiscal 2023 audit (most recent available) show a \$10 million surplus net of debt service payments. This result was a function of the district continuing its pattern of managing expenses well below budgeted expectation and benefitting from revenues that were \$7 million higher than the conservatively set budget. The revenue variance was largely produced by strong interest income and developer fees. MDC expects additional surplus in fiscal 2024.

The water fund, with a primary revenue source from water sales, also generated solid fiscal 2023 results from interest income that was \$6.3 million above budget and comfortably offset a \$1.6 million shortfall in water sales due to wet weather. Water fund operating expenses were \$4.8 million below budget primarily because of savings from vacant positions and reduced consulting costs.

Fiscal 2024 debt service coverage of the revenue bonds is projected to be 2.9x, 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 no lower than 2.6x for the next three years.

Debt, Pensions and OPEB

The district is highly leveraged with debt totaling approximately 5% of the tax bases of the towns it services. Given the size and scope of the district's capital plan, we anticipate that leverage will remain elevated through at least 2028. 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 including a \$40 million issuance anticipated in August 2024.

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 MDC's 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 contribution was 100% of the Moody's "tread water" indicator or the amount necessary to prevent the liability from rising over time. The district actuarially determined contribution for its OPEB expense was \$7.4 million in fiscal 2023 compared to actual contributions of \$7.8 million. 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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