FitchRatings

FITCH AFFIRMS NORWICH, CT'S IDR AT 'AA'; OUTLOOK STABLE

Fitch Ratings-New York-19 October 2016: Fitch Ratings has affirmed the following City of Norwich, CT (the city) bonds:

--$5.4 million general obligation (GO) bonds at 'AA'.

In addition, Fitch has affirmed the city's Issuer Default Rating (IDR) at 'AA'.

The Rating Outlook is Stable.

SECURITY
The bonds are a general obligation of the city backed by its full faith, credit, and unlimited taxing authority.

KEY RATING DRIVERS

The 'AA' rating on the IDR and GO rating reflects the city's healthy financial performance, largely supported by stable revenue growth prospects coupled with management's unlimited legal ability to raise taxes. The rating also considers the city's sound budget management practices and moderate long-term liability burden. These strengths are balanced against practical limitations on the city's expenditure flexibility, which somewhat inhibits budgetary flexibility.

Economic Resource Base
The city of Norwich is located adjacent to interstate 395 on the head of the Thames River, 40 miles southeast of the city of Hartford. The city's population has increased roughly 12% since the 2000 census, though growth has slowed over the past several years. The city's last property valuation, which was performed in October 2013, resulted in a 26% decline in taxable value--nearly equaling the percent increase from the assessment five years prior.

Revenue Framework: 'aa' factor assessment
Fitch expects future general fund revenue performance to slow given sporadic growth in the city's two primary revenue streams, property taxes and state aid, though the city receives notable revenue from the city-owned public utility system. Management has the independent legal ability to raise taxes.

Expenditure Framework: 'a' factor assessment
Fitch expects the natural pace of spending growth to remain above revenue growth. Moderate carrying costs and adequate control over labor-related costs afford the city some expenditure flexibility, though education and rising pension costs will continue to pressure spending.

Long-Term Liability Burden: 'aa' factor assessment
Norwich's debt burden is moderate relative to its resource base. Future debt needs are limited and the pace of amortization is rapid. More conservative pension plan assumptions were adopted, increasing the city's unfunded liability. The city is phasing in full ADEC funding, which it expects to reach by fiscal 2019.

Operating Performance: 'aaa' factor assessment

Norwich has incurred several minor deficits after transfers, but prudent financial management and the city's unlimited ability to raise revenues are expected to enhance the city's operating performance in the event of a mild economic downturn.

RATING SENSITIVITIES

Management Practices: Fitch expects the ratings to remain stable in the absence of a shift in management practices and/or policy and resultant weakening of the city's operating performance.

CREDIT PROFILE

The city's employment base, while diverse, is somewhat limited by healthcare and governmental centers of employment and the city is distant from municipalities with larger employment bases. The unemployment rate has been trending positively, declining 8% year-over-year (July 2016), though it still remains above county, state and national levels at 6.6%. Wealth levels are considerably below state levels, but more closely approximate the U.S. average.

Revenue Framework

Property taxes are the city's primary revenue stream, representing approximately 64% of budgeted fiscal 2017 revenues. State aid, which has been subject to recent cuts, accounts for another 36%. The city-owned utility system lends further operational support and revenue diversity to the general fund.

Historical general fund revenue growth remained below U.S. GDP but above inflation; however, this is partly reflective of tax rate increases. The city's first assessment since the recession, performed Oct. 1, 2013 and effective fiscal 2015, resulted in a 26% decline in taxable value. Housing values rose 3.2% over the past year but are expected to rise shy of inflation (1.8%) over the coming year, according to the Zillow Group. Housing value appreciation and modest economic development will continue to support positive tax base performance, though the city's reliance on state aid likely constrains revenue growth. In fiscal 2015 the education cost sharing and special education grants came in under budget, together contributing to over half a million dollar revenue shortfall.

The city has unlimited legal taxing authority over residential and commercial property.

In fiscal 2017 state legislation will cap the motor vehicle tax rate at 37 mills, and at 32 mills every year after. The Municipal Revenue Sharing Grant incorporates an additional amount to mitigate revenue loss stemming from the cap, though the city's share of the grant may be reduced due to state budget cuts.

The city-owned Norwich Public Utilities (NPU) operates gas, electric, water and wastewater systems. City charter mandates an annual transfer to the city, set at 10% of NPU's last fiscal year's gross revenues (excluding sewer revenues). NPU payments to the general fund have historically remained stable. The utility rates, which remain largely competitive, are independently established by the city's Public Utility Commissioners without regulatory approval.

Expenditure Framework

The city's general fund expenditures are primarily driven by educational costs, which represented over half of fiscal 2015 expenditures, though rising retiree benefits costs will also drive spending in the near term.

Fitch expects expenditures to outpace sluggish revenue growth in the absence of policy action.

Fixed carrying costs for retiree benefits and debt are moderate at roughly 13%. Management expects to take on additional debt service for capital projects in the out-years. Fitch anticipates that the city's increased debt burden will still yield carrying costs consistent with the 'a' category given the rapid amortization of existing debt.

Management is able to reduce some expenses tied to its programs, although educational expenses provide fewer opportunities for spending flexibility. There are also limitations in the ability to reduce certain public safety costs, give that firefighters are currently staffed at the minimum level required per labor contracts. Norwich has adequate control over staffing, wages and benefits. Union contracts are subject to arbitration, but a decision may be rejected by a two-thirds vote by the city's legislative body. A new arbitration panel would then be appointed by the state and their subsequent decisions are required to take into consideration the financial capability of the employer.

City charter includes a voter-approved provision requiring a restricted appropriation to capital spending at 2% of the prior year's general fund budget, further limiting the city's ability to cut expenditures.

State legislation passed last year will limit annual spending increases to 2.5% or the rate of inflation, whichever is greater, beginning in fiscal 2018. The cap excludes expenditures for debt service, special education, court orders, arbitration and national disasters given a declared state of emergency. Municipalities that increase their general fund budget above the cap will receive a reduced municipal revenue sharing grant, lowered to 50 cents for every dollar spent above the cap. Norwich is projected to receive $223 thousand from the grant in fiscal 2017.

Long-Term Liability Burden
The city's long-term liability burden is moderate relative to its economic resource base, with unfunded pension liabilities and direct debt totaling roughly 10% of personal income. The city has approximately $7.9 million of remaining unissued debt authorization. Management expects to issue $5 million early fiscal 2017 for gas line extensions, infrastructure improvements and technology, though approximately half of the issuance will be supported by payments from NPU. Fitch does not expect the additional issuance to pressure the 'aa' assessment.

Most of the city's non-certified employees are members of the city's single-employer defined benefit plan, while Board of Education employees participate in the state's multiple employer plan, for which the state is responsible. The ratio of assets to liabilities as of June 30, 2015 was 65.2%, which falls to a Fitch-estimated 60.3% using a more conservative 7% return assumption, resulting in a net pension liability of $106.2 million. The city adopted more conservative actuarial assumptions as of the July 1, 2013 valuation, increasing the city's ADEC significantly. The city will increase its contributions by 15% annually until contributions are funded in full, as mandated by a newly adopted city charter policy. The city should reach full funding by fiscal 2019.

The city has historically fully funded other post-employment benefits (OPEB) actuarially determined contributions. OPEB unfunded liabilities total $43.8 million, representing 2.8% of personal income and 1.7% of market value.

Operating Performance
Fitch assesses Norwich's inherent budget flexibility as high, largely due to its unlimited revenue raising ability. The scenario analysis indicates that the city could fall below its reserve safety margin shortly after a mild economic downturn, but Fitch believes the city would continue to utilize its budgetary flexibility in order to support financial stability. Norwich maintained satisfactory reserves throughout the most recent economic downturn by increasing the millage rate. Unaudited estimates for fiscal 2016 indicate a sizable general fund operating surplus that would increase reserves.

Norwich has demonstrated a strong commitment to enhancing its financial flexibility. Overall the city has maintained balanced operations despite several minor deficits after transfers out for charter mandated capital pay-as-you go transfers to its capital projects fund in recent years. The deficit of $582 thousand in fiscal 2015 was due to shortfalls in state aid, and management adopted more conservative revenue assumptions in the fiscal 2017 budget in order to mitigate for future fluctuations. In fiscal 2015 management also enacted a formal fund balance policy, targeting reserves between 12% and 17% of spending, in order to further support financial stability.

Unaudited fiscal 2016 results indicate a sizable general fund surplus of $4.2 million, or 11.5% of spending. The surplus was primarily due a personal property audit resulting in a $2 million gain as well as a mild winter resulting in lower heating and snow removal costs and savings from vacant positions created by early retirement incentives. The 2017 budget is balanced without the use of reserves and projects breakeven results. The city's five-year general fund projection expects continued increases in the city's tax rate in order to fulfill expenditure needs.

Contact:

Primary Analyst
Rachel Grossman
Analyst
+1-646-582-4967
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
George Stimola
Associate Director
+1-212-908-0770

Committee Chairperson
Barbara Ruth Rosenberg
Senior Director
+1-212-908-0731

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

In addition to the sources of information identified in the applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS. IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.
Copyright © 2016 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing

and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third- party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001