

RatingsDirect®

Summary:

Norwich, Connecticut; General Obligation

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Summary:

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Credit Profile

US\$7.48 mil GO bnds iss of 2017, ser A due 08/01/2036

<i>Long Term Rating</i>	AA/Stable	New
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US\$1.0 mil GO bnds iss 2017 ser B due 08/01/2036

<i>Long Term Rating</i>	AA/Stable	New
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Norwich GO

<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed
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Rationale

S&P Global Ratings assigned its 'AA' long-term rating to Norwich, Conn.'s series 2017A and series 2017B general obligation (GO) bonds. At the same time, we affirmed our 'AA' long-term and underlying ratings on the city's outstanding GO debt. The outlook on all ratings is stable.

The bonds are secured by the city's full faith and credit pledge to levy ad valorem taxes on taxable property without limit on the rate or amount. We understand the series 2017A bond proceeds will be used to refund a portion of the city's outstanding series 2009A bonds as well as provide capital for purchase of various road and gas improvements, among other capital items. We understand the series 2017B bonds will be used to finance gas system improvements.

The rating reflects our view of the city's:

- Weak economy, with projected per capita effective buying income at 89.7% of the national level and market value per capita of \$63,956;
- Strong management, with "good" financial policies and practices under our Financial Management Assessment methodology;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2016, which closed with a slight operating surplus in the general fund and an operating surplus at the total governmental fund level;
- Strong budgetary flexibility, with an available fund balance in fiscal 2016 of 11.5% of operating expenditures;
- Very strong liquidity, with total government available cash at 30.6% of total governmental fund expenditures and 8.6x governmental debt service, and access to external liquidity that we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges at 3.6% of expenditures and net direct debt that is 28.7% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 68.9% of debt scheduled to be retired in 10 years, but significant medium-term debt plans and a large pension and other postemployment benefit (OPEB) obligation; and
- Very strong institutional framework score.

Weak economy

We consider Norwich's economy weak. The city, with an estimated population of 41,036, is located in New London County. The city has a projected per capita effective buying income of 89.7% of the national level and per capita market value of \$63,956. Overall, the city's market value grew by 0.6% over the past year to \$2.6 billion in 2017. The county unemployment rate was 5.8% in 2015.

Norwich, which has a history as an industrial shipping hub, maintains direct access to Interstate-395 and State Route 2. The city has experienced slow, but steady, growth in population and market value over the past three years. City officials note that regional development has supported commercial and residential activity within city limits. In particular, the city benefits from the nearby Mohegan Sun casino and expects an expanded federal contract for Electric Boat, located in Groton, to support job opportunities for residents.

The Norwich Community Development Corporation (NCDC) maintains relationships with regional partners, which allows city officials to work to support potential developments which may in turn support the regional economy and Norwich's tax and employment base. One such ongoing development is Preston Riverwalk, approximately 693 acres south of the city available for development. The city is anticipating at least \$200 million in development by the Mohegans for housing and entertainment purposes, which would provide additional employment opportunities for Norwich's residents, supporting the health of the local residential property market.

Strong management

We view the city's management as strong, with "good" financial policies and practices under our Financial Management Assessment methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

Management reports using three to five years of budget to actuals when drafting its budget, which we believe is conservative in nature given recent variance trend. City council reviews budget to actuals monthly and maintain the ability to adjust or amend, as necessary. The annual budget process includes a five-year long-term financial plan and long-term capital plan, the latter of which includes detail on sources and uses of funding.

The city maintains its own investment management policy that is compliant with state guidelines, with holdings reviewed at least annually. Norwich's debt management policy caps overall debt to 5% of the city's total assessed value as well as dictates net utility income paying self-supporting debt to be no less than 125% of debt service. The city council adopted a fund balance policy of 12% of expenditures in December 2014; the city reached 11.7% of expenditures in fiscal 2016.

Adequate budgetary performance

Norwich's budgetary performance is adequate in our opinion. The city had slight surplus operating results in the general fund of 1.2% of expenditures, and surplus results across all governmental funds of 2% in fiscal 2016. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2016 results in the near term.

For analytic consistency, we have adjusted revenues and expenditures for the use of bond proceeds on capital outlays, deferred pension costs, one-time revenues, and recurring transfers to revenues and expenditures.

In fiscal 2016, the city's positive results were partially buoyed by one-time revenue from a personal property audit of Computer Sciences Corp., though we have adjusted for this revenue in our calculation of the city's budgetary performance. Other areas of improvement include improved utility revenues, 10% of which are diverted to the city's general fund as stated in the city charter, as well as health care savings after the completion of a dependent verification audit, both of which we expect to recur. We note that the city continues to defer a portion of its pension contributions, which have been included in our assessment of expenditures, but that this deferred amount has decreased year-over-year. We also note that the operating surplus occurred despite a reduction in state aid for special education costs and capital spending during the fiscal year. Despite continued budgetary pressures at the state level, which may affect municipal support statewide, preliminary analysis of municipal aid in the governor's proposed budget suggests the city should be able to manage changes to state aid over the near term.

The city expects to operate at a surplus in fiscal 2017, but we note that it will continue to defer a portion of pension payments until 2019; as such, we expect performance to remain adequate. Norwich is currently in negotiations with its police union and recently settled its contracts with firefighters and city hall supervisors, with 2% wage increases partially offset by increases in employee contributions.

Strong budgetary flexibility

Norwich's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2016 of 11.5% of operating expenditures, or \$14.9 million.

The city's strong budgetary performance in fiscal 2016 has supported the continued growth of available reserves. The city has generated consistent surpluses in recent years, supporting its ability to reach its stated target of 12% in available reserves as a share of expenditures. Given recent performance and the lack of appropriated reserves in the fiscal 2017 budget, budgetary flexibility should remain strong.

Very strong liquidity

In our opinion, Norwich's liquidity is very strong, with total government available cash at 30.6% of total governmental fund expenditures and 8.6x governmental debt service in 2016. In our view, the city has strong access to external liquidity if necessary.

Norwich maintains strong access to external liquidity which is demonstrated by its issuance of GO bonds regularly in the past several years. We understand the city has not entered into any bank loans or direct-purchase debt. Norwich follows state investment guidelines, and we do not consider the city's investments aggressive because nearly all are in mutual funds. The city has consistently had very strong liquidity, and we do not expect this to change in the near term.

Very strong debt and contingent liability profile

In our view, Norwich's debt and contingent liability profile is very strong. Total governmental fund debt service is 3.6% of total governmental fund expenditures, and net direct debt is 28.7% of total governmental fund revenue. Overall net debt is low at 1.7% of market value, and approximately 68.9% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors. Negatively affecting our view of the city's debt profile is its significant medium-term debt plans. The city has about \$3.2 million in authorized but unissued debt and officials believe the city will issue up to \$5 million annually over the near term.

In our opinion, a credit weakness is Norwich's large pension and OPEB obligation. Norwich's combined required pension and actual OPEB contributions totaled 9.7% of total governmental fund expenditures in 2016. Of that amount, 6.3% represented required contributions to pension obligations, and 3.4% represented OPEB payments. The city made 78% of its annual required pension contribution in 2016. The funded ratio of the largest pension plan is 57.4%.

The city is the administrator of its Consolidated Pension Plan, a single-employer contributory defined-benefit public employee retirement system, and a Volunteer Firefighters Relief Plan. As of June 30, 2016, the plan fiduciary net positions as a percentage of the total pension liability were 57.4% and 37.4%, respectively. The city's teachers participate in a state-run retirement system-for which in the past, the city had no liability-however, we note that the governor's budget includes a proposal to require municipalities to pay one-third of annual pension contributions into the teacher's retirement system.

Starting in fiscal 2015, the city lowered the assumed rate of return and shortened amortization periods. As a result, the liabilities and actuarially determined employer contributions for these plans rose higher than they would have been under the previous sets of assumptions. While we believe the assumption changes were prudent, they increased the city's actuarially determined contribution (ADC) substantially and led to the underfunding of its annual payment for the year. However, we recognize the city council adopted a plan as part of the formal funding policies for pensions and OPEBs in December 2014. Under these policies, the city will increase its pension contribution by 15% each year until it returns to funding 100% of the ADC, which will likely be in fiscal 2019. Norwich also provides a retiree health care plan and has an unfunded actuarial accrued OPEB liability of \$43.8 million (July 1, 2015), and is 23.7% funded. It is also meeting 100% of its OPEB annual required contribution (ARC) each year.

Although we consider the combined pension and OPEB contributions elevated and likely to increase, we believe the city has a credible plan to address the liability since contributions were the result of plan assumption changes, and management has a plan in place to fully fund its ARCs. However, such contribution increases may pressure its ability to further raise its reserves.

Very strong institutional framework

The institutional framework score for Connecticut municipalities is very strong.

Outlook

The stable outlook reflects our view of the city's strong management practices and policies, supporting the maintenance of the city's strong budgetary flexibility and very strong liquidity. We do not expect to change the rating in our two-year outlook horizon.

Upside scenario

We could consider a positive rating action should economic metrics improve significantly to those in line with peers of a higher rating, in addition to maintaining the city's strong reserves.

Downside scenario

We could lower the rating should the city experience a period of weak performance, resulting in the reduction of reserves to those in line with peers of a lower rating. Additionally, material deterioration in the city's local economy,

resulting in weak income and wealth levels, could also put downward pressure on the rating.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

Ratings Detail (As Of February 13, 2017)		
Norwich GO bnds iss (Cap Proj Bnds)		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Norwich GO bnds iss (Taxable Bnds)		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Norwich GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Norwich GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Norwich GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Many issues are enhanced by bond insurance.

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