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Ratings

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Summary:

Hamden, Connecticut; General Obligation

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Summary:

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Credit Profile		
US$20.88 mil GO Bnds ser 2021 due 08/15/2031		
Long Term Rating	BBB+/Stable	New
Hamden Twn GO		
Long Term Rating	BBB+/Stable	Affirmed

Rating Action

S&P Global Ratings revised its rating outlook on Hamden, Conn.'s general obligation (GO) debt to stable from negative. At the same time, S&P Global Ratings assigned its 'BBB+' rating and stable outlook to the town's series 2021 A GO bonds and affirmed the BBB+ rating on its outstanding GO debt.

The outlook revision is due to the improving fund balance and liquidity, in part due to Hamden's 2020 debt restructuring which lowered debt service costs for fiscal years 2021 and 2022. Hamden did this to provide itself budgetary relief and grow reserves, while also giving it time to improve budgetary performance and ameliorate its structural imbalance. The town's revenues performed reasonably well during the pandemic, which aided management's ability to meet is financial goals highlighted in its deficit mitigation plan.

The 2020 debt restructuring was the first of two; management plans the second debt restructuring for 2022. With these restructurings, the town plans to improve fund balance to $20 million by 2023, which is a notable improvement from its current position. As part of the plan, the town is controlling costs and increasing the tax levy. The town is also budgeting an increase of debt service by approximately $2 million per year until the amount reaches $30 million, which is the debt service payable for fiscal 2025. At that point, the town is projecting structural balance in its budget without the need for additional restructurings.

Hamden's full-faith-and-credit pledge of ad valorem taxes levied on the taxable property within its borders secures the 2021 GO bonds.

Officials plan to use $6.04 million of the bonds toward capital projects and the remainder will refund 2011A bonds for interest rate savings. The city estimates it will generate a net present value savings of 6.65% on the refinancing.

Credit overview

The rating reflects our view of the town's weak financial position and structural imbalance. It also factors in high pension and other postemployment benefit (OPEB) liabilities, largely due to years of underfunding pension liabilities, including in fiscal 2020. The town's deficit mitigation plan requires the town adopt a fiscal 2021 budget with a 3-mill tax increase to aid in budgetary alignment with another similar tax increase planned in 2022. Currently, the town is estimating a surplus of $6.6 million and an estimated ending fund balance of $4.3 million at the close of fiscal 2021. Providing additional support to its finances is the receipt of American Rescue Plan funds ($12 million), which the town anticipates using toward eligible capital projects.

Additional rating factors incorporated into the rating include:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Weak management environment, despite standard financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Weak budgetary performance, with operating deficits in the general fund and at the total governmental fund level in fiscal 2020, although we anticipate improvement in 2021;
- Very weak budgetary flexibility, with a low nominal available fund balance (negative $2.2 million) that we expect will improve as a percent of expenditures in the near term from its fiscal 2020 level of negative 1.2%. The assessment also considers the town's limited capacity to reduce expenditures;
- Adequate liquidity, with total government available cash at 3.8% of total governmental fund expenditures and 58.1% of governmental debt service, but access to external liquidity we consider strong;
- Very weak debt and contingent liability profile, with debt service carrying charges at 6.5% of expenditures and net direct debt that is 115.1% of total governmental fund revenue, as well as a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Environmental, social, and governance factors

We analyzed the town's ESG risks relative to its economy, management, financial measures, and debt and liability profile. We consider the town's social risks in line with that of the sector, but we believe Hamden's high property tax rate poses some affordability challenges relative to its socioeconomic metrics if management needs to increase the tax levy beyond current estimates to remedy its structural imbalances. We also analyzed governance risks and believe that due to Hamden's growing fixed costs, this poses as a greater risk relative to sector peers. Environmental risks align with sector peers.

Stable Outlook

Downside scenario

We could lower the rating if the town were to deviate from its deficit mitigation plan and experience budgetary pressure beyond current projections, resulting in a reversal of reserves. We believe, despite its progress in replenishing its fund balance, the budgetary environment will remain challenging over the long-term particularly if its tax-base growth stagnates hampering the town's ability to raise taxes necessary to achieve structural balance.

Upside scenario

While not likely over the outlook time horizon, we could raise the rating should financial performance and reserves improve to levels necessary for Hamden to provide the financial flexibility to mitigate the budgetary effects of its high liabilities and growing debt service costs. This would require the town to align the budget without requiring one-time budget measures, including pension deferrals.

Credit Opinion

Strong economy

We consider Hamden's economy strong. The town, with an estimated population of 60,967, is in New Haven County in the New Haven-Milford, CT MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 111% of the national level and per capita market value of $97,831. Overall, the town's market value grew by 7.2% over the past year to $6.0 billion in 2022.

State Route 15 (The Wilbur Cross Parkway) and Interstate 91 traverse the town, connecting residents to regional employment opportunities in the New Haven-Milford MSA. In addition to public sector employment, Hamden's local economic and employment base centers on higher education, health care and assisted-living services, commercial retail, and manufacturing. Its municipal government and board of education (1,337 employees) is the community's leading employer, followed by Quinnipiac University (851), Genesis Health Care and Rehabilitation (350), Whitney Center (290), and the American Automobile Association (265).

Due to its predominantly residential property mix, Hamden historically experienced modest year-over-year gains in its net taxable grand list. Officials report that due to recent efforts to attract new economic growth, Hamden has identified several prospective new development and redevelopment projects that could provide some uplift to the net taxable grand list. Management also expects a proposed redevelopment of a former middle school and another residential complex to generate new tax revenue annually. Officials report several commercial retailers are in various stages of development and that several industrial employers have relocated to Hamden.

The county unemployment rate was 8% in 2020 increasing because of the stay at home orders during the pandemic. Unemployment remains above its average, but we note it has come down over the past few months as the economic recovery has taken hold. Strengthening of the macroeconomic environment is likely to also support continued growth in the tax base. For more information on S&P Global Ratings' economic view, see "Economic Outlook U.S. Q3 2021: Sun, Sun, Sun, Here It Comes," published June 24, 2021, on RatingsDirect.

Weak management environment

We view the town's structural imbalance requiring further debt restructurings as a sign of budgetary distress and limited financial flexibility, which we reflect in our management assessment. Further challenging the management team are the financial effects of and related uncertainty stemming from the ongoing pandemic as well as the town's growing and high fixed costs relative to peers.

While we consider the management environment challenging, we consider the town's management practices adequate, with standard financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

In our view, management historically developed optimistic revenue and expenditure assumptions, which contributed to structural deterioration and a significant decline in its available reserves in the years following the Great Recession. Over the past several fiscal years, we understand that management has implemented a more comprehensive approach in developing revenue and expenditure projections, including more realistic local revenue projections and conservative state revenue projections. However, in our assessment of the town's budget assumptions, we believe Hamden has faced pressures related to an uncertain state funding environment and satisfying its pension funding requirements, which limit our confidence that budget assumptions and financial projections are well-tested and sustainable from either a long-term or recent trend perspective.

During each fiscal year, management monitors Hamden's budget performance on a regular basis, with the ability to amend the budget if necessary. The town has a rolling six-year capital improvement plan (CIP), which identifies project costs for municipal and school projects. It reviews the CIP annually and incorporates it into the budgeting process. Hamden has also developed a six-year financial forecast, which it enacted in accordance with state statutes under the pension deficit-funding plan.

Hamden's investment policy restricts investment vehicles to certificates of deposits, repurchase agreements, and state investment funds. Under its debt policy, carrying charges for capital investment cannot exceed 10% of the current fiscal year's budgeted expenditures, unless it certified via binding referendum; noncapital-related borrowing cannot exceed 4% of the current fiscal year's budget. Although Hamden does not have a formal reserve policy, management hopes to restore available reserves to 5% of general fund expenditures.

Weak budgetary performance

Our forward-looking view of this assessment incorporates the town's recent financial performance, but also reflects the structural imbalance between recurring revenues and expenditures. The town's budgetary results will improve by $6.6 million (roughly 2% of expenditures) in fiscal 2021 in-line with its deficit mitigation plan.

For fiscal 2020, the town had operating deficits of 3.2% of expenditures in the general fund and 3.7% across all governmental funds, and its general fund closed with a negative balance. In our calculations of performance, we made analytical adjustments to account for the town's pension deferrals. Management reports that during the 2020 fiscal year, some of its revenue assumptions were optimistic, which was the primary reason for the projected $5.9 million general fund deficit.

The main source of downward budgetary pressure has been the town's persistent underfunding of pension and OPEB liabilities. Although the audited financial statement was showing break-even operating results over the past several fiscal years, the town deferred annual pension costs--including approximately $4.0 million in fiscal 2020--that, in our view, inflated budgetary performance. Hamden issued pension deficit funding bonds in fiscal 2015, and the state imposed statutory requirements on the town to increase its actuarially determined contribution (ADC) incrementally within six years (fiscal 2021). Although the town budgeted to fund the full ADC in fiscal 2019 and in 2020, it did not achieve its target. The town did achieve full funding of its ADC in 2021 and is budgeting full funding in the 2022 budget.

The council-approved 2022 budget totals $262.4 million, an increase of 6.05%, which is similar to the increase in fiscal 2021. The budget does appropriate the full amount of debt service prior to the debt restructuring, as well as a 3-mill tax levy increase, which should aid fund balance replenishment over the next few years. This assumes the town maintains cost controls and that it raises revenues as needed. The town anticipates producing a $7.2 million operating surplus for fiscal 2022, provided there are no midyear changes to the budget, and the revenue environment remains stable.

Hamden maintains a high millage rate relative to other municipalities in the state. Favorably, however, property tax collections have remained strong, in our view, between 98% and 99% over the past five fiscal years and even through the pandemic. Should there be a run-up of costs, or state funding gaps in future years, we believe the town will likely need to generate additional revenue from locally derived revenue sources to maintain balanced operations and address rising expenditures. This could prove difficult given Hamden's already high mill rate and limited grand list growth in recent years, which could place a substantial burden on its existing tax base.

Very weak budgetary flexibility

Hamden's budgetary flexibility is very weak, in our view, with an available fund balance that we expect to improve in fiscal 2021 from its fiscal 2020 level of negative 1.2% of operating expenditures. The town's fund balance will improve to $4.3 million, or 1.7% of budgetary expenditures. We note this level remains low on a nominal basis, which we consider vulnerably low and a negative credit factor. In addition, limiting our view of budgetary flexibility, remains the town's limited capacity to reduce expenditures given its high debt and contingent liabilities.

Over several years, financial reserves have been under pressure in part due to the cumulative effect of state aid reductions that had a material effect on the town's revenue and pressure from rising local expenditures. Reserves decreased from $3.04 million in fiscal 2015 to $1.19 million in fiscal 2017 before increasing in 2019. As noted above, management intends to achieve upwards of $20 million of fund balance over the next several years. Hamden may also receive additional funds through the potential sale of town-owned assets that could accelerate its replenishment plans.

Adequate liquidity

In our opinion, Hamden's liquidity is adequate, with total government available cash at 3.8% of total governmental fund expenditures and 58.1% of governmental debt service in 2020.

The town has strong access to external liquidity if necessary, which has aided its ability to meet its cash flow requirements despite its low reserves. In the past the town issued $20 million in tax anticipation notes which it paid in October 2020, which was when it received its first allotment of state funds, and when the COVID-19 tax deferral program ended. Over time, we expect liquidity will improve if the town successfully executes its deficit mitigation plan.

We note that Hamden does not have any contingent liquidity risk from financial instruments with payment provisions that change on the occurrence of certain events.

Very weak debt and contingent liability profile

In our view, Hamden's debt and contingent liability profile is very weak. Total governmental fund debt service is 5.8% of total governmental fund expenditures, and net direct debt is 127.8% of total governmental fund revenue.

Currently, the town's total direct debt totals $310 million. Hamden plans to prioritize and limit annual debt issuances over the next several years to roughly $10 million annually to provide funds for capital construction. As a part of its overall deficit mitigation strategy, it will also likely issue another debt restructuring in 2022 to lower debt service costs. We note that it could also engage in future restructurings; however, management indicates that the timing and magnitude are dependent on economic and fiscal conditions, and an assessment that the debt service payments are sustainable over the life of the bonds.

Pension and other postemployment benefits

- Annual costs represent a large portion of expenditures and our expectation is that costs will increase, presenting a budgetary burden for the town.
- Statutory funding policy below the actuarial recommendation, as well as weak assumptions and methodologies increase the risk of unexpected contribution escalation and volatility.
- OPEB liabilities are paid on a pay-as-you-go basis, which, given claims volatility as well as medical cost and demographic trends, is likely to lead to escalating costs. The town established an irrevocable OPEB trust fund; however, it had a negative asset position at the close of fiscal 2020.

The town participates in the following retirement plans:

- Public employees Retirement System (PERS): 36% funded, $298.3 million net pension liability (NPL)
- Municipal Employees' Retirement System (MERS): 74% funded, $31.3 million NPL
- Single-employer health care plan (OPEBs): negative 0.45% funded, $627 million net OPEB liability

In our opinion, a credit weakness is Hamden's large pension and OPEB obligation, without a plan in place that we think will sufficiently address it. Its combined required pension and actual OPEB contributions totaled 15.4% of total governmental fund expenditures in 2020. Of that amount, 9.4% represented required contributions to pension obligations, and 6.0% represented OPEB payments.

PERS is a single-employer system administered solely for town employees. In 2014, Hamden issued a pension obligation bond, which raised the system's funded ratio to 36% in 2015 from 11% in 2014. It is in the process of phasing in full annual payment of the ADC, which it has not met in the past 10 years. In fiscal 2019 and 2020, it paid 70.5%, and 82.6% of the ADC respectively, which we view as weak funding discipline. The plan fell short of both our static and minimum funding progress metrics in 2020, meaning it is not making progress in funding the NPL. We understand the town contributed 100% of the ADC in 2021 and in 2022. Its fiscal 2022 ADC totals about $23.7 million, or about $7 million more than it contributed in fiscal 2020. The 25-year closed amortization schedule is long, which defers costs. Additionally, we believe the static mortality table could not only be understating liability but is likely to lead to volatility in funded levels due to periodic updates to the assumptions. The 7% discount rate could lead to contribution volatility if market returns fall short of expectations. The plan was closed to new participants in 2007 and is primarily populated by pensioners, which limits Hamden's ability to share risk with employees and therefore puts contribution volatility squarely on the town.

All new hires participate in MERS, a cost-sharing multiple-employer plan administered by the state. It is 73.6% funded due to a change in the discount rate to 7% from 8%. While we believe this is likely to limit cost volatility relative to the higher rate, we expect costs will correspondingly increase alongside the change in the calculated NPL.

The town's OPEB liability is sizeable at $627 million. We do not expect Hamden to make material progress in addressing this liability in the near term..

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

Ratings Detail (As Of July 27, 2021)		
Hamden Twn GO (MBIA) (National)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO		
Long Term Rating	BBB+/Stable	Affirmed
Hamden Twn GO		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (AGM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (AGM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM)		
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Hamden Twn GO (BAM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM) (SECMKT)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (BAM) (SECMKT)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed
Hamden Twn GO (SYNCORA GTY)		
Unenhanced Rating	BBB+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.