S&P Global Ratings

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Summary:

New London, Connecticut; General Obligation; Note

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Credit Profile		
US$35.83 mil GO BANs ser 2022 due 03/16/2023		
Short Term Rating	SP-1+	New
US$13.8 mil GO bnds ser 2022 due 03/15/2042		
Long Term Rating	AA-/Stable	New
New London GO		
Long Term Rating	AA-/Stable	Upgraded
New London GO bnds rfdg iss of 2020 ser C due 03/15/2034		
Long Term Rating	AA-/Stable	Upgraded
New London GO bnds ser 2015 C dtd 12/15/2015 due 10/01/2026		
Long Term Rating	AA-/Stable	Upgraded
New London GO (NPFGC)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded

Rating Action

S&P Global Ratings raised its rating on the City of New London, Conn.'s general obligation (GO) debt outstanding to 'AA-' from 'A+'. The outlook on the city's debt outstanding is stable.

At the same time, S&P Global Ratings assigned its 'AA-' long-term rating, with a stable outlook, to New London's issue of 2022 GO bonds ($13.8 million). We also assigned our 'SP-1+' short-term rating to the city's GO bond anticipation notes (BANs), due March 16, 2023 ($35.8 million).

The one-notch upgrade reflects a demonstrated trend of improved financial performance, supported by bolstered financial policies and practices and solid expansion of the city's tax base, including average annual grand list growth of 3.8% over the last five years.

New London's unlimited-tax-GO pledge to levy ad valorem taxes, without limit as to rate or amount, on all taxable property within its borders secures the bonds and notes.

The short-term note rating reflects our criteria for evaluating and rating BANs. In our view, New London maintains a very strong capacity to pay principal and interest when the notes come due. The city has what we view as a low market risk profile because it has strong legal authority to issue long-term debt to take out the notes and is a frequent issuer that regularly provides ongoing disclosure to market participants.

Management intends to use bond proceeds to retire outstanding notes issued to finance capital projects undertaken by the city. The notes are being issued to finance various capital projects, including renovations and upgrades to city school facilities, in addition to a community center project and equipment improvement.

Credit overview

New London's economy remains rooted in the defense sector but is increasingly diversifying into health care and service-related industries. Management continues to look for ways to diversify and expand the tax base. Through conservative financial management and enhanced financial policies, the city's financial performance has improved in recent years, with New London increasing available reserves to levels we consider very strong, while fully funding the actuarially determined employer contribution (ADEC) for its pension expenses. Specifically, the city has increased reserves each year for the past nine years, with available reserves reaching $15.6 million at the end of fiscal 2021, equal to a very strong 15.6% of operating expenses and net transfers. This has been a deliberate multiyear approach by management to strengthen its financial position, with management planning to increase the fund balance at least 1% annually, until it reaches an available fund balance equal to 16.67% of operating expenses. In addition, the city has managed well throughout the COVID-19 pandemic. We believe the city is well positioned in the near term due in part to continued conservative budgeting in addition to receiving $26.2 million in American Rescue Plan Act (ARPA) funds. We understand ARPA funds will be used for a variety of one-time purposes, including helping small businesses and enhancing the city's already good economic momentum, as illustrated by building permits reaching a decade-high level in dollar value in 2021 due primarily to strong commercial/industrial growth.

The long-term rating reflects our view of the following factors for New London:

- A diversifying tax base, historically rooted in the defense and health care sectors, which continues to see good growth;
- Bolstered financial policies and practices that have aided the city in improving its overall financial position;
- Improved financial performance, including nine consecutive years of surpluses, resulting in significant increases to available reserves to levels we consider very strong; and
- Manageable debt and pension costs despite ongoing capital needs.

Environmental, social, and governance

We evaluated New London's environmental, social, and governance (ESG) factors relative to the city's economy, financial measures, management, and debt and long-term liability profile. We consider New London's social risks and governance risks to be in line with those of the sector. We view environmental risks and their potential effect on taxable properties as somewhat higher relative to that of peers, given the city's location on the Atlantic Ocean and Thames River. However, we understand the majority of the property exposed to sea-level rise is largely park land, and management is working to mitigate potential future stormwater and rising sea-level pressures.

Stable Outlook

Upside scenario

Should New London's economic indicators strengthen, particularly in the form of increased income levels, coupled with a meaningful reduction in its retirement liabilities, all else being equal, we could raise the rating.

Downside scenario

We could take a negative rating action if operating performance becomes imbalanced, leading to a draw on reserves, or if the city fails to comply with its improved financial policies and practices.

Credit Opinion

Diversifying tax base, historically rooted in the defense and health care sectors, which continue to see good growth

New London, with a population of 26,111, is located in New London County. The city's economy has long been based on defense-related activities, particularly submarine construction. The largest employer is the defense contractor General Dynamics Electric Boat Corp. (Electric Boat; 3,500 employees). The U.S. Coast Guard (900 military and civilian employees) also maintains a sizable presence. We note that Electric Boat is the primary contractor for a new class of submarine and we expect continued investment in its New London facility. We do not believe there is material risk in contraction or relocation of either private or government-related defense activities in New London, and Electric Boat's growth is likely to help strengthen the local economy. In addition, while we do not believe the number of students is materially suppressing economic metrics, we note that the city is also home to the U.S. Coast Guard Academy and Connecticut College, which could provide some stability to the local economy.

Recent developments and acquisitions have helped diversify the local tax base, particularly following Yale New Haven Health System's purchase of the Lawrence & Memorial Hospital (2,500 employees). The Coast Guard Museum is expected to be built near downtown, which itself has seen investments in quality-of-life- and tourism-related infrastructure, particularly in city parks. The port is home to ferry service to Fishers and Long islands, N.Y., as well as to Block Island, R.I. We understand that the city expects to benefit from a new payment in lieu of taxes (PILOT) due to private activity in the offshore wind sector on the tax-exempt state pier, in its deep-water port on the Thames River. Beyond direct revenue, currently expected to generate $2.2 million in additional revenue for fiscal 2022, this could also generate additional housing demand in New London.

The city's last full revaluation led to a 9.5% increase in assessed value for fiscal 2020, due to both appreciation and new development, followed by a 2.9% increase for fiscal 2021. Of the total real property, residential accounts for 54% of taxable real property, while commercial and industrial properties accounting for 45%. Also included in the net grand list are motor vehicles and other personal property. We believe that the economy will continue to rely on its established industries, but that new development will keep adding to the city's tax base.

Bolstered financial policies and practices have aided the city in improving its financial position

We believe that management is continuing to work to improve its financial management policies, practices, and controls. Notably, the city is now conducting formal, long-term financial planning, including projections of both revenues and expenditures through 2031, which the city is in the process of updating for the current year. The plan incorporates expected changes through revaluations and includes constant growth factors for both revenues and expenditures. Management expects to continue refining this tool and tweaking assumptions as it integrates it into its budget development process.

The annual budget process includes a review of the previous year's actual results and monthly budget updates, with quarterly reports distributed to elected officials. New London maintains a 10-year capital improvement plan (CIP) that identifies funding sources, which is incorporated into the long-term budget process. We anticipate that the city will continue to use its CIP to identify and develop a plan to address outstanding deferred capital needs.

The adopted fund balance policy requires a minimum of 8.3% of budgeted general fund appropriations to be held in unassigned reserves, to be used for unforeseeable expenditures or unanticipated increases in service delivery costs. The policy also mandates a phase-in period through which the city will increase fund balance at least 1.00% annually, until it reaches a total fund balance of 16.67%, or about two months of budgeted expenditures, which the city is now just slightly below. We expect New London to be in compliance with this policy within the year or two. The city also established a new capital reserve fund as of fiscal 2021 year-end, which had an ending balance of $866,000. The investment policy sets limits on the types of investments, as well as outlining internal reporting and controls. There is no formal debt management policy.

Improved financial performance in recent years, resulting in significant increases to available reserves

We adjusted performance to account for one-time revenues and expenditures, recurring transfers, and deferred pension contributions for analytical consistency. With regard to New London's liquidity, we included general fund investments in our calculation of the city's available cash, but excluded certain grant, special revenue, and bond proceeds cash.

Over the past several years, management has shown a willingness and ability to adjust the budget to address potential pressures. We believe management has made significant budgetary improvements over the past few years, including fully funding the ADEC related to its annual pension contribution.

For fiscal 2021, although revenues came in slightly below budget by about $160,000, city management adjusted expenses accordingly and some savings were realized from reduced expenses associated with the pandemic, resulting in a $1.6 million positive expense variance. As a result, New London generated a slight surplus of $425,922 at fiscal 2021 year-end due primarily to conservative budgeting and to expense savings. Property taxes are the city's predominant general fund revenue source, providing about 57% of revenues, followed by intergovernmental (38%) and charges for services (4%), a revenue mix that we expect to remain relatively stable.

For fiscal 2022, the city budgeted $95.6 million in general fund revenues. We understand management indicates revenues and expenses have tracked well relative to budget and that New London is expecting at least balanced operations for the year and likely a surplus. Specifically, through the first six months of the year, management indicates operating expenditures were $3.2 million, or 8.3%, under budget, while revenues have tracked well relative to budget. Management indicates the city has collected 95.5% of real property taxes for the year, compared to 93% at the time last year and that it expects additional PILOT payments of as much as $2.2 million. Therefore, we understand New London should maintain available reserves above $15 million, or above 15% of expenditures, a level we consider very strong.

The city has also received substantial pandemic-related funding, which should provide additional financial flexibility over the next couple of fiscal years. In total, New London has received more than $27 million in pandemic-related funding, consisting primarily of ARPA funds ($26.2 million). We understand ARPA funds will be used for a range of one-time projects and expenses.

Manageable debt pension costs despite ongoing capital needs

We do not expect the city's debt profile to materially change over the next few years. Following this issuance, the city will have approximately $123.2 million in outstanding debt, of which we consider about $7.5 million self-supporting enterprise debt. We understand the city has about $85.3 million in authorized but unissued debt. Nevertheless, given the amortization of existing debt, and the anticipation of receiving state grants for a portion of capital expenditures, we do not believe the layering on of additional debt over the next five years is expected to materially change the city's debt profile.

Pension and other postemployment benefits

- We do not view New London's retirement obligations as a significant budgetary pressure.
- The city began fully funding its required pension contribution in fiscal 2020, although we note some of the city's assumptions may lead to contribution volatility.

As of June 30, 2020, New London participated in the following pension plans:

- Municipal Employees Retirement System (MERS): 71.2% funded, $32.8 million net pension liability (NPL).
- A contributory plan: 84.3% funded, $5.3 million NPL.
- A noncontributory plan: 0.0% funded, $6.9 million NPL.
- The city also provides other postemployment benefits (OPEBs). It has a net OPEB liability of $25.7 million. The OPEB trust has a funded ratio of 4.9%.

The city achieved 100% of its annual required pension contribution in 2020 and 2021 and we understand it continues to fully fund the ADEC for the MERS and contributory plans for fiscal 2022. The locally administered contributory plan has a blended discount rate and a crossover date; however, we believe the plan has sufficient liquid assets to meet liabilities at this time and, in conjunction with the improved funding discipline, do not believe it is likely to present a budgetary pressure. We note that New London closed the noncontributory plan in 1971 and has funded costs on a pay-as-you-go basis. This plan has no assets and the NPL is equal to the total liability. We note that pay-as-you-go contributions for the noncontributory plan have fallen since 2014, along with a decline in the NPL.

MERS recently lowered its discount rate to 7.0%, which significantly reduced the funded status of the plan. We view this discount rate as slightly higher than the 6.5% benchmark. The plan's closed, 21-year amortization is positive, along with a level-dollar basis and generational mortality assumptions. While MERS costs have nearly doubled since 2015, we believe current assumptions are less likely to result in significant cost volatility.

Strong institutional framework

The institutional framework score for Connecticut municipalities is strong.

New London, Conn.--Key Credit Metrics				
	Most recent	**Historical information**		
		2021	**2020**	**2019**
Weak economy				
Projected per capita EBI % of U.S.	65			
Market value per capita ($)		81,632		
Population (no.)			26,111	26,111
County unemployment rate(%)			9.6	
Market value ($000)		2,131,490	2,072,370	1,893,403
Ten largest taxpayers % of taxable value	16.0			
Strong budgetary performance				
Operating fund result % of expenditures		0.4	1.3	2.0
Total governmental fund result % of expenditures		3.3	2.6	2.4
Very strong budgetary flexibility				
Available reserves % of operating expenditures		15.6	15.4	15.1
Total available reserves ($000)		15,564	15,776	15,080
Very strong liquidity				
Total government cash % of governmental fund expenditures		16	18	26
Total government cash % of governmental fund debt service		310	314	503
Strong management				
Financial Management Assessment	Good			
Adequate debt & long-term liabilities				
Debt service % of governmental fund expenditures		5.1	5.7	5.1
Net direct debt % of governmental fund revenue	67			
Overall net debt % of market value	5.1			
Direct debt 10-year amortization (%)	52			
Required pension contribution % of governmental fund expenditures		3.3		
OPEB actual contribution % of governmental fund expenditures		0.6		
Strong institutional framework				

EBI--Effective buying income. OPEB--Other postemployment benefits. Data points and ratios may reflect analytical adjustments.

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 February 28, 2022)		
New London GO bnds		
Long Term Rating	AA-/Stable	Upgraded
New London GO BANs ser 2021 due 03/18/2021		
Short Term Rating	SP-1+	Current

Ratings Detail (As Of February 28, 2022) (cont.)		
New London GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (AGM) (SEC MKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (BAM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (BAM)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (BAM) (SECMKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded
New London GO (BAM) (SECMKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Upgraded

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.