Cheshire, Connecticut

New Issue Report

Ratings

Long Term Issuer Default Rating	AAA

New Issue

$14,500,000 General Obligation Bonds, Series 2019	AAA

Outstanding Debt

General Obligation Bonds	AAA

Rating Outlook

Stable

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New Issue Summary

Sale Date: Feb. 20 via competitive sale

Series: $14,500,000 GO Bonds, Series 2019

Purpose: To fund various sewer, general purpose and school construction projects

Security: Cheshire's full faith and credit and unlimited taxing power

Analytical Conclusion

The 'AAA' IDR and GO bond ratings reflect the town's low long-term liability burden and solid financial operations, supported by high levels of revenue-raising authority and strong expenditure flexibility, which position it to withstand the challenges associated with a moderate economic downturn.

Economic Resource Base: Cheshire is a wealthy residential suburban community located 14 miles outside of New Haven and 25 miles southwest of Hartford. The town has an estimated census population of 29,330 which has been relatively flat since 2010.

Key Rating Drivers

Revenue Framework: 'aa'
Revenues are derived primarily from property taxes, for which there is no limit on the rate or levy. Fitch expects natural growth prospects for revenues (absent tax rate increases) to remain slow as new development and long-term changes in property values contribute moderately to tax base expansion. The bulk of state funding is received for education, which has been variable.

Expenditure Framework: 'aa'
The majority of the general fund budget pays for education. Future spending growth is expected to remain in line with revenue performance. Fixed carrying costs are at the low end of the moderate range and are expected to remain a manageable portion of the budget. Management maintains moderate control over wages and benefits in labor contracts, providing solid expenditure flexibility.

Long-Term Liability Burden: 'aaa'
Cheshire's combined burden of debt and Fitch-adjusted net pension liabilities (NPLs) are low at 7% of residents' estimated personal income. Fitch expects the burden to remain close to this level based on future debt plans, the rapid pace of principal amortization and moderate growth in future NPLs. The town administered pension plans' Fitch-adjusted NPLs account for roughly one-third of the long-term liability burden metric.

Operating Performance: 'aaa'
The town has strong gap-closing capacity relative to Fitch's expectations of revenue sensitivity during economic cycles. Cheshire's superior level of inherent budget flexibility reflects the high revenue raising authority and solid expenditure flexibility. Conservative budget management practices have contributed to consistent reserve levels maintained at amounts above what Fitch deems adequate for an 'aaa' reserve safety margin notwithstanding annual allocations for pay-as-you-go capital spending.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	2/15/19
AAA	Revised	Stable	4/30/10
AA+	Upgraded	Stable	6/11/09
AA	Affirmed	Positive	12/08/06
AA	Affirmed	Stable	4/16/04
AA	Assigned		10/22/01

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 town's long-term operating profile.

Credit Profile

Cheshire has evolved over several decades from a predominately rural farming community to a more residential community with an established industrial and commercial component. Despite this growth, the town retains its rural characteristics with thousands of acres of open space and an active agricultural industry. Top taxpayers include a mix of industrial, retail and manufacturing companies. The town's proximity to interstates 84, 691 and 91 linking to larger nearby employment centers contributes to economic activity. Cheshire is also home to two large state prison facilities.

Cheshire's economic prospects and indicators remain positive. Residents' wealth levels exceed national and the state's above-average levels and unemployment rates are low and have historically been below the state's rate. Building permit values for the past five years have ranged from 1% to 2% of taxable assessed values as management continues to support efforts for new commercial and industrial development within the town.

Revenue Framework

The town derives the bulk of its revenues from property taxes. Such taxes represented roughly 83% of fiscal 2018 budgeted general fund revenues with state aid at 14% of revenues. The town has an unlimited legal ability to levy property taxes.

Fitch expects natural revenue growth exclusive of policy actions to remain slow as a moderate level of new development is planned or in the works and housing values are slow to appreciate. Prior years' growth in revenues has been supported by moderate annual tax rate increases and Fitch expects such actions to continue to support similar expenditure growth.

The town underwent a statutorily required five-year property revaluation as of Oct. 1, 2018 and effective for the fiscal 2020 budget that resulted in a modest 1% increase in taxable assessed values. This follows revaluation results of a 6% decline based on the Oct. 1, 2013 valuation and a 13% increase for the Oct. 1 2008 valuation. Changes in between valuations only incorporate values from new development, additions or results of tax appeals. Currently planned economic development activities should support a moderate level of future tax base growth.

Expenditure Framework

The town's primary expenditure responsibility is for education, which accounts for roughly two-thirds of budgeted spending. Public safety accounted for only 6% of fiscal 2018 spending, reflective in part to the town's use of a volunteer fire department. Expenses associated with administration and finance account for roughly 12% of budgeted spending.

Fitch expects the natural pace of spending growth to match or marginally exceed revenue growth.

The town maintains a solid level of expenditure flexibility. Fixed carrying costs for debt service, required pension contributions and annual other post-employment benefit (OPEB) contributions were moderate at approximately 12% of total governmental spending in fiscal 2018. Fitch expects fixed costs to remain moderate based on expected growth in the town's spending for

Related Research

Fitch Rates Cheshire, CT's $14.5MM GO Bonds 'AAA'; Outlook Stable (February 2019)

Related Criteria

U.S. Public Finance Tax-Supported Rating Criteria (April 2018) debt service and pension contributions. Pension contributions exclude those associated with teachers, which are paid by the state.

The town underwent a large water treatment plant upgrade resulting in an annual increase in debt service beginning in fiscal 2018. Management has prudently built up debt reserve funds to support the first five years of the new debt service to help stabilize debt costs and remove spikes in the operating budget. The town has a debt policy limiting debt service to no greater than 10% of spending and pro forma projections of future debt service costs (net of debt reserve funds) show annual debt service ranging between the current 6% of budget to 9% over the next ten fiscal years inclusive of expected new issuances. The plant upgrade alleviates the need for significant new water and sewer debt.

The town has adequate control over staffing, wages, and benefits. Management has the ability to reduce staff at any time if necessary. Union contracts are subject to arbitration but a decision may be rejected by two-thirds vote by the town council. 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.

Long-Term Liability Burden

Long-term liabilities for debt and unfunded pensions represent around 7% of residents' estimated personal income. This metric includes the town's borrowing for the water treatment plant upgrade. The town has no overlapping debt. Amortization of debt is above average at approximately 66% of principal retired in 10 years. Fitch expects liability levels to remain low based on assumptions for future debt and changes in pension NPLs based on close-to-full funding of actuarially determined contributions and changes in investment performance. The town's fiscal 2019-2023 capital improvement plan assumes moderate borrowing plans of $43 million of GO bonds (42% of current outstanding debt level) for town and school improvements.

The town administers three single-employer pension plans, one each for its town, police and volunteer firefighters. The town and police plans were closed to new hires between 2006 and 2012 for the town plan and 2014 for the police plan. The town's aggregate funded ratio for all three pension plans was 67% as of June 30, 2018 based on the town's 7.5% discount rate or an estimated 57% funded using Fitch's more conservative 6% rate of return. The combined Fitch-estimated NPL for the three plans was $56 million, or a low 3% of personal income.

Annual employer contributions to the police plan have gradually increased the past few years and equaled 89% of the $1.6 million actuarially determined contribution (ADC) in fiscal 2018. Management will continue to phase in higher annual contribution amounts with an expectation to gradually meet the ADC for the police plan over the next couple of years. While such a practice is not common for a Fitch 'AAA' rated issuer, as such practice typically leads to increases in the overall liability, the magnitude of the dollar amount of the current liability is considered manageable by Fitch and recent changes have been made to police pension benefits that should control growth in the ADC and the NPL.

The Board of Education teachers participate in the State Teacher's Retirement System, a cost-sharing pension plan, for which the state carries the NPL and is solely responsible for all contributions.

Fitch considers Cheshire's OPEB liabilities to be manageable. The unfunded net liability at June 30, 2018 was $29 million, with over half representing an implicit rate subsidy incurred by the town for retired teachers' participation in its health plan.

Operating Performance

Fitch believes the town is well-positioned to manage the challenges associated with a moderate economic downturn based on its superior level of inherent budget flexibility. For details, see Scenario Analysis, page 5.

During the most recent downturn, management demonstrated its ability to reduce spending through cost controls, staff reductions and deferred hiring practices. Fund balance levels remained stable. Fitch expects management would take similar actions if needed to maintain its superior level of financial resilience in a future downturn.

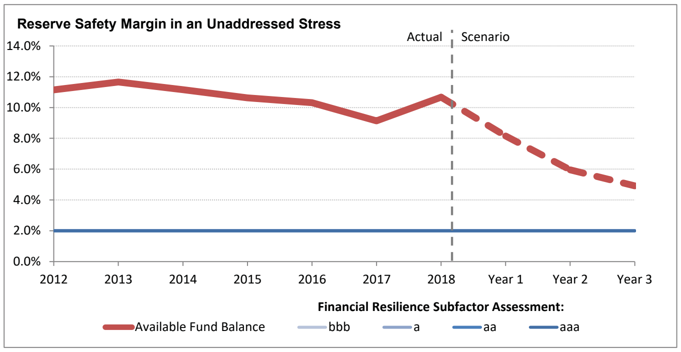
Fiscal 2018 operating results reflect a net operating surplus of $781,000 even though state aid came in under budget by approximately $1.2 million. Conservative tax collection assumptions, expenditure controls and a hold back on planned capital spending contributions of around $335,000 contributed to the results. The unrestricted general fund balance improved to $13 million or 11% of spending. Management uses conservative budget estimates and benefits from very strong tax collection rates averaging 99.8% providing for historically stable results.

The fiscal 2019 general fund budget of $111 million was up approximately 2% over the prior year's budget and includes a modest tax increase. State aid, primarily for education, is currently projected to exceed fiscal 2018 levels by approximately $1.1 million. Management projects operating results to show a moderate budgetary surplus similar to prior years.

The status of future levels of state aid remains uncertain as the state manages its financial challenges. Fitch believes that Cheshire will continue to manage its expenses to address any potential revenue declines, use its reserves prudently, and continue to comply with its operating and debt policies.

Cheshire (CT)

Scenario Analysis



Analyst Interpretation of Scenario Results:

Fitch believes the town is well-positioned to manage the challenges associated with a moderate economic downturn based on its superior level of inherent budget flexibility. The town's moderate fixed carrying costs, high revenue raising abilities, and solid control over expenditures afford the town substantial gap-closing capacity. Operating results (net of transfers out for capital paygo) have been stable and reserves for the last decade have remained at or above the town's 8%-9% fund balance policy level. The policy was revised in Jan. 2019 to maintain unassigned fund balance at a minimum of 9.25% of operating expenditures. Reserves outside of the general fund, particularly in the capital fund and afore-mentioned debt service fund, also buttress overall flexibility.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(1.0%)	2.3%	3.2%
Inherent Budget Flexibility		Superior	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2012	2013	2014	2015	2016	2017	2018	Year 1	Year 2	Year 3
Total Revenues	103,062	105,019	107,167	110,594	112,704	119,698	121,107	119,896	122,638	126,526
% Change in Revenues	-	1.9%	2.0%	3.2%	1.9%	6.2%	1.2%	(1.0%)	2.3%	3.2%
Total Expenditures	103,981	104,446	107,397	110,553	112,534	119,139	120,607	123,019	125,480	127,989
% Change in Expenditures	-	0.4%	2.8%	2.9%	1.8%	5.9%	1.2%	2.0%	2.0%	2.0%
Transfers In and Other Sources	6,779	1,061	11,037	6,113	7,189	755	1,063	1,052	1,076	1,110
Transfers Out and Other Uses	6,608	1,000	11,029	6,372	7,504	850	782	798	814	830
Net Transfers	171	61	8	(260)	(315)	(95)	281	255	263	281
Bond Proceeds and Other One-Time Uses	5,863	-	10,079	5,272	6,319	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	(748)	634	(222)	(219)	(144)	464	781	(2,868)	(2,579)	(1,183)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	(0.7%)	0.6%	(0.2%)	(0.2%)	(0.1%)	0.4%	0.6%	(2.3%)	(2.0%)	(0.9%)
Unrestricted/Unreserved Fund Balance (General Fund)	11,674	12,295	12,087	11,867	11,729	10,959	12,960	10,092	7,513	6,330
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	11,674	12,295	12,087	11,867	11,729	10,959	12,960	10,092	7,513	6,330
Combined Available Fund Bal. (% of Expend. and Transfers Out)	11.1%	11.7%	11.2%	10.6%	10.3%	9.1%	10.7%	8.2%	5.9%	4.9%

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.