

RatingsDirect®

Summary:

Windham, Connecticut; General Obligation; Note

Primary Credit Analyst:

John Kennedy, CFA, New York + 1 (212) 438 2128; john.kennedy@spglobal.com

Secondary Contact:

Victor M Medeiros, Boston (1) 617-530-8305; victor.medeiros@spglobal.com

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Credit Profile

US\$30.94 mil GO BANs dtd 10/01/2020 due 09/30/2021

<i>Short Term Rating</i>	SP-1+	New
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US\$27.265 mil GO bnds issue of 2020 due 08/15/2045

<i>Long Term Rating</i>	AA-/Stable	New
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US\$5.26 mil GO rfdg bnds 2010 ser B dtd 10/21/2010 due 06/01/2022

<i>Long Term Rating</i>	AA-/Stable	New
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Rating Action

S&P Global Ratings assigned its 'AA-' long-term rating to Windham, Conn.'s \$27.265 million series 2020 general obligation (GO) bonds. We also assigned our 'SP-1+' short-term rating to the town's \$30.940 million series 2020 GO bond anticipation notes (BANs). Additionally, we assigned our 'AA-' long-term rating to the town's series 2010b bonds. At the same time, we affirmed our 'AA-' rating on the town's existing rated long-term GO debt. The outlook, where applicable, is stable.

Windham's full faith and credit pledge secures the bonds and notes. The short-term rating on the notes reflects our criteria for evaluating and rating BANs. In our view, Windham maintains a very strong capacity to pay principal and interest when the notes come due. We view the town's market risk profile as low because it has strong legal authority to issue long-term debt to take out the notes and is a frequent debt issuer that regularly provides ongoing disclosure to market participants.

Proceeds from the bonds will finance a sewer and water plant upgrades, permanently finance a portion of outstanding BANs, and refund Clean Water Fund (CWF) loans. The series 2020 BANs will roll existing BANs, temporarily finance a parking garage project the town expects to be self-supporting, and provide temporary financing for various capital projects. We are rating the series 2010b bonds at the issuer's request; two maturities remain outstanding.

Credit overview

Windham's good management practices have historically allowed the town to maintain stability despite a weak, although growing, economy. After drawing on reserves for fiscal years 2016-2018, the town produced a positive operating result in fiscal 2019, and initial projections show another one for fiscal 2020.

As with most local governments, we believe challenges associated with the pandemic and a national recession could pressure Windham's budgets in the next one-to-two years. In line with our view of the ongoing economic contraction, we expect revenues to lag their historical performance. (For more information, see "The U.S. Faces A Longer And Slower Climb From The Bottom," published June 25, 2020, on RatingsDirect.) Windham serves more college students and university students than any other municipality in Connecticut, and we believe local economic activity based on those students may recover more slowly than other sectors given the effects of social distancing. However, we believe

the town's conservative budgeting should help it maintain its strong financial position. Therefore, we do not expect to change the rating in the near term. Our outlook is generally for two years, but we see some risks due to the COVID-19 pandemic and U.S. recession over the next six-to-12 months.

The long-term rating also reflects our view of Windham's:

- Weak economy, with projected per capita effective buying income (EBI) at 58.0% and market value per capita of \$54,972, that benefits from access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with a slight operating surplus in the general fund and break-even operating results at the total governmental fund level in fiscal 2019, but potential revenue pressure from COVID-19 and the national recession;
- Strong budgetary flexibility, with an available fund balance in fiscal 2019 of 9.0% of operating expenditures;
- Very strong liquidity, with total government available cash at 15.5% of total governmental fund expenditures and 6.3x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 2.5% of expenditures and net direct debt that is 78.7% of total governmental fund revenue; and
- Strong institutional framework score.

Environmental, social, and governance factors

We analyzed the town's environmental and governance risks relative to its economy, management, financial measures, and debt and liability profile and determined that they are in line with our view of the sector standard. The rating also incorporates our view regarding the health and safety risks posed by the COVID-19 pandemic. We believe the town's economic activity based on students may recover more slowly than other forms of economic activity given the effects of social distancing. However, we also believe its conservative budgeting helps mitigate these risks' effects on its finances. Absent the implications of COVID-19, we consider the town's social risks in line with those of the sector.

Stable Outlook

Downside scenario

We could lower the rating if the town were to experience a substantial weakening of budgetary performance, due to significant state aid reductions or otherwise, leading to a material decline of available reserves or constrained liquidity.

Upside scenario

If Windham improves financial reserves through sustained improvement in its financial performance, while growing and diversifying locally generated revenue to reduce its moderate reliance on state aid, and exhibiting improved wealth and income levels that are commensurate with those of higher-rated peers, we could raise the rating.

Credit Opinion

Weak economy

We consider Windham's economy weak. The town, with a population of 24,699, is in Windham County in the Worcester, Mass. MSA, which we consider to be broad and diverse. It has a projected per capita EBI of 58.0% of the national level and per capita market value of \$54,972. Overall, market value grew by 6.4% over the past year to \$1.4 billion in 2020.

After picking up in 2019 and early 2020, we understand Windham's economic growth likely continued through the pandemic. Windham completed a revaluation in 2018 and sent out the first tax bills reflecting the new valuation in July 2019. Commercial property valuations increased 14%. Officials attribute this growth to multiple unused or underused properties being redeveloped, commercial renters choosing to purchase properties, and out-of-state developers investing in properties in the town. Management notes that a large mixed-use housing and commercial development is under construction, and a tax-exempt building was converted into a taxable strip mall. The downtown area was also designated an opportunity zone under the federal Tax Cuts and Jobs Act, which incentivizes additional development in the area.

As noted, however, Windham's projected per capita EBI and market values are weak compared with those of its regional and state peers. Based on our forecasts, we anticipate the regional economy will remain steady, but with growth likely to remain modest. Residential real properties account for about 49% of Windham's tax base, while 27% is commercial and industrial. The top 10 taxpayers constitute a very diverse 14.2% of the grand list. The largest taxpayer is Connecticut Light and Power, accounting for 2.9% of the grand list. Income metrics may somewhat understate Windham's economic activity because more four-year college students live in the town than anywhere else in Connecticut. Management did not note seeing a large economic effect from students not returning. We note that students returned to the nearby Eastern Connecticut State University campus in late August, although we believe that the effects of social distancing may mute the economic activity that students typically generate.

The county unemployment rate was 4.0% in 2019. However, rapidly evolving economic conditions as a result of COVID-19 have affected the labor market. During the Great Recession, local unemployment peaked at 10.3%, although it held at 9.8% in July 2020, below the national and state averages. We will monitor the longer-term effects of the current downturn on the labor market and the economy overall.

Strong management

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

The board of finance is the budget-making authority responsible for financial and taxation matters. It presents annual operating budgets to the town meeting for its approval and tax rate establishment. In our view, Windham maintains some best practices we consider critical to supporting credit quality, and these are embedded in the town's daily operations and practices. The town maintains formal policies supporting some of these activities, adding to the likelihood that it will continue and transcend changes in the operating environment or personnel.

The town regularly monitors revenue and expenditures, ensuring timely budget adjustments, and makes realistic budget assumptions based on trends, with the goal of yielding positive operating results. For example, in preparation of the 2018 budget, the town used a zero-based budget approach amid the uncertainty related to the state budget and its effects on state revenues. This allowed it to produce a near-balanced budget.

Windham also maintains a comprehensive five- and 10-year capital plan that looks at both facilities and infrastructure improvements, and links funding sources for each project. In addition, the town maintains an informal 8% fund balance policy for its unassigned funds, a level to which it has historically adhered. According to the town's calculations, it is currently meeting the target. Windham's investment policies adhere to state guidelines and the town's board of finance committee reviews holdings and performance monthly.

Adequate budgetary performance

Windham's budgetary performance is adequate, in our opinion. The town had slight surplus operating results in the general fund of 0.8% of expenditures, and balanced results across all governmental funds of negative 0.3% in fiscal 2019. Our adequate assessment accounts for bond-financed capital expenditures, as well as potential revenue pressures related to a national recession and possible future state aid reductions.

Historically, Windham has maintained balanced operations, supported by its strong budget development and monitoring framework. The town's fiscal 2019 surplus reflected its conservative budgeting as well as its cost control, with general fund expenditures shrinking by 7.3% from the previous year. The year's performance also included strong pension asset performance as well as other postemployment benefit (OPEB) implicit subsidy cost decreases from lower insurance premiums and eligible retiree counts.

For fiscal 2020, Windham adopted a balanced \$75.1 million general fund budget. The adopted budget incorporated the town's receipt of 2.5% higher state aid and forecasts level statutory aid and a 0.43-mill decrease in the property tax mill rate. Although the town did not implement explicit cost-saving measures in response to COVID-19, it estimates that positive expenditure budget-to-actual variances more than offset the estimated 1% negative revenue budget-to-actual variance. The town conservatively estimates it produced a \$560,000 general fund surplus during fiscal 2020.

For fiscal 2021, the town adopted a \$74.8 million general fund budget that is balanced without the use of fund balance. The budget does not include changes in state funding assumptions, informed by the town's communications with state officials. The budget also includes a 0.81-mill property tax rate increase. Officials hope to hold back on discretionary spending and find additional cost-control opportunities during the year. Property taxes contributed 51.6% of general fund revenue in fiscal 2019, with intergovernmental contributing 44.5%. We expect that the town will likely continue its positive performance over the long term, although we recognize some short-term revenue pressures in the next one-to-two fiscal years.

Strong budgetary flexibility

Windham's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2019 of 9.0% of operating expenditures, or \$6.9 million.

While the town's fiscal 2019 audit showed a large portion of fund balance from interfund receivables, we understand that those were repaid in fiscal 2020 and management estimates the full general fund balance position will be backed

by cash. The town estimates that available fund balance at fiscal year-end 2020 totaled \$7.5 million, or 10.1% of operating expenditures.

At its peak, Windham maintained total general fund balance of \$13 million, which amounted to about 21% of general fund expenditures. We anticipate reserves will regrow slowly after bottoming out in fiscal 2018. While it does not have a formal reserve policy, the town does maintain an informal target of maintaining reserves at a level above 8% of expenditures, to which it has historically adhered. According to the town's calculations, it is currently meeting the target.

Very strong liquidity

In our opinion, Windham's liquidity is very strong, with total government available cash at 15.5% of total governmental fund expenditures and 6.3x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

We believe the town maintains strong access to external liquidity if needed. It has issued bonds frequently over the past several years, including GO bonds and short-term BANs. We include investments we consider to be highly liquid in our calculation of the town's cash position. The town does not have any investments we consider aggressive. In addition, it does not have any nonremote contingent liability risks. It privately placed a series 2015 GO bond with Webster Bank. It does not contain nonstandard events of default or acceleration clauses, and only \$525,000 remains outstanding.

Adequate debt and contingent liability profile

In our view, Windham's debt and contingent liability profile is adequate. Total governmental fund debt service is 2.5% of total governmental fund expenditures, and net direct debt is 78.7% of total governmental fund revenue.

We calculate that Windham will have approximately \$85 million in total direct debt following this issuance. Of this, we consider approximately \$3 million to be adequately supported by enterprise rates and charges according to a debt service coverage test. Windham intends to issue approximately \$9 million in debt to finance a high school construction project. However, we do not expect our view of the town's debt profile to change.

Pension and other postemployment benefits

- We do not view pension and OPEB liabilities as an immediate credit risk for Windham.
- Pension costs are low as a percentage of expenditures, and plans are generally well funded.
- OPEB liabilities are limited to an implicit subsidy from allowing retirees to buy into the employee health care plan.

The town is the administrator of three separate single-employer public-employee contributory pension plans for its municipal employees, police, and firefighters, and one separate single-employer defined-benefit noncontributory pension plan for all board of education employees (excluding teachers). These plans all have high funded ratios ranging between 84%-91%, which we view as a positive credit factor. The aggregate net pension liability of these plans totals \$8.3 million, which, in our view, is low. Contributions for the largest plan exceeded our static and minimum funding progress calculations, meaning we expect the net pension liability to shrink over time. In addition, Windham's OPEB costs are limited to an implicit subsidy from allowing retirees to buy into the employee health care plan.

Windham's pension contributions totaled 2.9% of total governmental fund expenditures in 2019. The town made its full annual required pension contribution in 2019.

Strong institutional framework

The institutional framework score for Connecticut municipalities is strong.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of September 9, 2020)		
Windham GO		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
Windham GO		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
Windham GO rfdg bnds		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
Windham GO BANs		
<i>Short Term Rating</i>	SP-1+	Affirmed

Many issues are enhanced by bond insurance.

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