S&P Global
Ratings

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Summary:

Minneapolis; General Obligation

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Credit Profile		
US$120.0 mil GO imp and various purp bnds ser 2016 due 12/01/2026		
Long Term Rating	AAA/Stable	New
Minneapolis GO		
Long Term Rating	AAA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' rating to Minneapolis' series 2016 general obligation (GO) improvement and various purpose bonds. At the same time, we affirmed our 'AAA' ratings on the city's existing GO debt. The outlook is stable.

The bonds are secured by the city's GO pledge and are payable from ad valorem tax against all taxable property within the city without limit as to rate or amount. The bonds are additionally secured by special assessments, parking revenues, and net revenues of the city's water and sanitary sewer systems. Though secured by multiple revenue streams, we rate the bonds to the city's GO pledge, and we similarly rate several of its existing GO bonds that are additionally secured by other revenues to its GO pledge. City officials will use bond proceeds to finance various capital projects and to refund existing debt for interest cost savings.

The city's GO bonds are eligible to be rated above the sovereign because we believe the city can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above the Sovereign--Corporate and Government Ratings: Methodology and Assumptions" (published Nov. 19, 2013, on RatingsDirect), U.S. local governments are considered to have moderate sensitivity to country risk. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, and no history of government intervention, and we believe Minneapolis's financial flexibility is sufficiently demonstrated by its very strong budgetary reserves and liquidity.

The 'AAA' rating reflects our view of the city's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our financial management assessment (FMA) methodology;
- Strong budgetary performance, with a slight operating surplus in the general fund and break-even operating results at the total governmental fund level in fiscal 2015;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2015 at 23% of operating expenditures;
- Very strong liquidity, with total government available cash at 72.4% of total governmental fund expenditures and 5.4x governmental debt service, as well as access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 13.3% of expenditures, net direct debt at 66.5% of total governmental fund revenue, and low overall net debt at less than 3% of market value and

rapid amortization, with 85.7% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Very strong economy

We consider Minneapolis' economy very strong. The city, with an estimated population of 404,168, is in Hennepin County in the Minneapolis-St. Paul-Bloomington MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 111% of the national level and per capita market value of $107,068. Overall, market value grew by 10.3% over the past year to $43.3 billion in 2016. The county unemployment rate was 3.3% in 2015.

With the post-recessionary lull in key measures of economic strength now a few years past, Minneapolis' economy is growing at a solid pace, as signaled most obviously by its multiyear run of very healthy tax base growth. Buoyed in large part by gains in residential and apartment valuations, along with some commercial and industrial growth, the city's net tax capacity saw back-to-back years of essentially double-digit increases in 2014 (for taxes payable 2015) and 2015, growing by 9.7% and 10.7%, respectively, in those years. Estimates for 2017 show tax capacity increasing an additional 8.4% from 2016 levels to $493 million. Economic market value, totaling $43.3 billion in 2016, has grown along similar lines over the same period. We understand the city is experiencing its fifth consecutive year of $1 billion or more in permitted construction, which, most recently, has reflected several large, high-profile developments, such as the new Minnesota Vikings Stadium and the nearby Wells Fargo office towers, along with numerous smaller scale multi-residential developments, office developments, and hotels throughout the downtown area. While we believe it will be difficult for the city to sustain nearly double-digit growth in tax capacity and market value indefinitely and believe that growth will likely begin to moderate, the amount of new construction and number and scope of projects in various stages of development suggest that the near- to medium-term growth prospects should remain strong.

With steady job gains, low unemployment, and a generally strong private sector anchored by a number of well-known Fortune 500 companies, the city's employment base remains strong and diverse. As of 2015, its largest industries by share of total jobs included health care and social assistance (18.1% of total employment base), professional and technical services (11.5%), educational services (9.7%), finance and insurance (8.8%), and accommodation and food services (8.6%). Countywide unemployment in Hennepin County peaked at 7.3% during the Great Recession in 2009 and has since declined to only 3.3% in 2015, well under the nationwide rate of 5.3%. Among leading employers, we understand that Target had a large round of layoffs in 2015 following a major downsizing at its corporate headquarters, though this did not have a pronounced or prolonged effect on the city's overall employment levels, and we understand that no further job cuts have been announced. Management reports that other major employers are stable, with several expanding.

The broader Minneapolis-St. Paul-Bloomington MSA is home to nearly two-thirds of the state's population and is the central hub of the state's economy, accounting for about three-quarters of statewide gross domestic product. S&P Global's most recent "State and Local Government Credit Conditions Forecast" (published July 27, 2016) has the multistate West North Central regional economy growing at a slightly faster pace than the national baseline scenario through 2018, and the region boasts the lowest projected unemployment rate of any region in the country.

Very strong management

We view the city's management as very strong, with "strong" financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Highlights to the FMA include:

- Strong, well-grounded revenue and expenditure assumptions consistently embedded in the city's annual budget, which, for example, includes reference to historical trends and detailed analyses explaining expected variance from these trends and which places current-year revenue and expenditure forecasts in the context of a multiyear financial plan;
- Quarterly budget-to-actual reporting to the city council to identify potential sources of budget variance and the ability to amend the budget as needed;
- An annually-updated, multiyear financial plan that identifies and discusses upcoming issues or variances and possible solutions;
- An annually-updated, five-year capital improvement plan (CIP) that includes detailed descriptions of specific projects, along with cost estimates and funding sources;
- A council-approved investment management policy and quarterly reporting to the council of investment holdings and earnings;
- A basic debt management policy that, while lacking detailed quantitative restrictions or limits, includes substantive, qualitative guidelines; and
- A formal reserve policy to which the city has historically adhered requiring the city to maintain a minimum unrestricted general fund balance equal to 17% of the subsequent-year budgeted expenditures to facilitate cash flow and meet unanticipated contingencies.

Strong budgetary performance

Minneapolis' budgetary performance is strong, in our opinion. The city had slight surplus operating results in the general fund at 0.8% of expenditures, and balanced results across all governmental funds at 0.2% in fiscal 2015.

The city reports its finances on the basis of a fiscal year ending Dec. 31 and on a modified accrual basis of accounting. We have adjusted general fund revenues and expenditures to account for routine transfers and total governmental fund revenues and expenditures to account for routine transfers (to and from non-governmental funds) and the spending of bond proceeds.

The city's general fund budget has seen surpluses for the past five audited fiscal years, resulting in the addition of $33.6 million to its total fund balance over the same period. With reserves at the highest level in recent memory at the end of fiscal 2015 and in excess of the 17% minimum required by the city's fund balance policy, the fiscal 2016 budget was structured with a $28 million use of reserves, which we understand was part of an effort to more closely align reserves with the city's policy. At midyear, the city was projecting revenues coming in slightly under budget and expenditures approximately $5 million under budget, mainly due to $4 million budgeted for contingencies that will not likely be spent, resulting in a projected ending fund balance of approximately $83 million, or 17% of expenditures. Management reports that actual results will likely be better than the midyear projections suggest, largely due to about $10 million in budgeted expenditures for a bridge project that will be deferred due to a lack of state funding.

The mayor's recommended budget for fiscal 2017 includes a 3.9% increase in general fund spending (excluding transfers) from 2016, overall revenues remaining flat (though with a 10% increase in the general fund property tax levy, offset by decreases elsewhere), and $5.5 million use of reserves, assuming that the city spends all of the $4 million budgeted for contingencies. We note that the mayor's budget is preliminary, and the city council typically votes on and adopts a final budget closer to the end of the year.

While we expect the city to spend some reserves in fiscal 2016 and perhaps in 2017, we recognize that this is planned and believe that the city's structural budgetary performance will remain strong, as it has been historically, supported by comprehensive and well-embedded long-term planning practices and a solid, rapidly growing economic base. Should the city continue to rely on reserves, however, on an ongoing basis to balance the budget in subsequent years and in particular, should it fall materially out of compliance with its 17% fund balance policy as the result of unexpectedly large draws, we could revise our view of its budgetary performance.

Most of the city's operating revenues are locally derived, so they are tied in some fashion to local economic activity. Fiscal 2015 (audited) general fund revenue sources comprised mostly taxes (59% of revenues), intergovernmental aid (18%), charges for services and sales (10%), and licenses and permits (10%).

Very strong budgetary flexibility

Minneapolis' budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2015 at 23% of operating expenditures, or $104.7 million.

As discussed above, the city's total and available (assigned and unassigned) fund balances were at recent highs at the end of fiscal 2015, and we expect the fund balance to fall closer to its 17% policy level within the next few years. As such, while we expect reserves to decline, we still expect them to remain at levels we consider very strong.

Very strong liquidity

In our opinion, Minneapolis' liquidity is very strong, with total government available cash at 72.4% of total governmental fund expenditures and 5.4x governmental debt service in 2015. In our view, the city has strong access to external liquidity if necessary.

We have adjusted cash and cash equivalents for primary government to exclude unspent bond proceeds and amounts that carry restrictions. We expect overall cash levels to remain stable and very strong for at least the next several years. The city is a frequent debt issuer and has a history of accessing the market to issue GO debt, which supports our view that it has strong access to external liquidity if needed. Most of its investments are in obligations guaranteed by the U.S. government, so we do not believe the city is exposed to liquidity risk stemming from an aggressive investment portfolio.

The city has six variable-rate bank notes outstanding that were issued in 2015, with $102 million drawn to date and $166 million authorized. Each of the bank agreements includes events of default that allow the banks to accelerate unpaid principal and interest, but each specifies that bank must allow 180 days to cure a default. Pursuant to our criteria governing contingent liquidity risk, we believe that the 180-day cure period is sufficient time to allow the city to cure a default or refinance any note in default, and so we do not consider the notes a source of liquidity risk. We also understand that the city intends to refinance the bank note debt with fixed-rate GO debt within the next year or two.

Strong debt and contingent liability profile

In our view, Minneapolis' debt and contingent liability profile is strong. Total governmental fund debt service is 13.3% of total governmental fund expenditures, and net direct debt is 66.5% of total governmental fund revenue. Overall net debt is low at 2.4% of market value, and approximately 85.7% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

Our direct debt calculation excludes a share of the city's direct debt secured solely by enterprise revenues and GO debt that we consider eligible for self-support credit. The city's current five-year CIP includes about $900 million in projects, roughly one-quarter of which will be cash-funded and a little over half of which will be financed through new-money debt, with the rest funded through other revenue sources. Though the city currently intends to issue more than $200 million in debt as part of its CIP in 2017 and 2018, more principal than this is scheduled to roll off over the same period, so we anticipate no material weakening in the overall debt profile from new-money issuance. We note, as well, that the city's current GO debt burden (totaling about $656 million) is less than half of what it was a decade ago and has declined each year since then.

Minneapolis' combined required pension and actual other postemployment benefit (OPEB) contributions totaled 8.7% of total governmental fund expenditures in 2015. The city made its full annual required pension contribution in 2015.

The city contributes to two multiemployer, cost-sharing defined-benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). These include the General Employees Retirement Fund (GERF), the Public Employees Police and Fire Fund (PEPFF). The city's closed, single-employer plans were fully merged with the PERA plans starting in fiscal 2015. The city also contributes to the Teacher Retirement Association Fund (TRA) of Minnesota, pursuant to 2006 legislation that consolidated the Minneapolis Teachers Retirement Fund Association with TRA and required the city to annually pay a fixed contribution to TRA through 2037. As of the most recent actuarial valuation, on 30 June 2015, Minneapolis' proportionate share of the net pension liability was $354.8 million for GERF (78.2% plan fiduciary net position of the total pension liability), $220.7 million for PEPFF (86.6%), and $36.6 million for TRA (76.8%).

The GERF and PEPFF liabilities are calculated using a 7.9% discount rate and the TRA liability an 8% rate, and for each plan, contribution rates, benefit provisions, and actuarial standards are governed by state statute. While estimates show pension costs remaining more or less flat through fiscal 2017 and we see no immediate source of budgetary strain arising from the city's pension liabilities, we believe that pensions could be a source of pressure over the longer term, particularly if the plan actuarial assumptions (especially the discount rates) prove optimistic, understating the long-term liability.

The city also provides a single-employer defined-benefit health care plan that it funds on a pay-as-you-go basis and under which it provides an implicit rate subsidy to retirees. As of the most recent valuation (Jan. 1 2015), the plan had no assets and an unfunded actuarial accrued liability of $35.7 million.

Strong institutional framework

The institutional framework score for Minnesota cities with a population greater than 2,500 is strong.

Outlook

The stable outlook reflects our expectation that the Minneapolis economy should continue to see strong growth through at least the two-year outlook horizon, with the city's very strong economic base supporting ongoing revenue growth and overall budget stability. We also believe that debt levels should remain relatively low for a city with such an extensive capital program, and its pension costs manageable. Downside pressure would most likely come via weakening across multiple factors, such as a slowdown in the economy leading to weaker economic metrics, resulting in weaker revenue performance, and perhaps accompanied by rising pension costs. Given that we do not expect such a scenario in the next few years, we do not anticipate lowering the rating within the two-year outlook horizon.

Related Research

- U.S. State And Local Government Credit Conditions Forecast, July 27, 2016
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- 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 September 23, 2016)		
Minneapolis taxable GO bnds (downtown/E project) ser 2014 due 03/01/2044		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis taxable GO hsg imp area bnds		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis taxable GO various purp pk bnds		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO convention ctr rfdg bnds ser 2011A dtd 11/22/2011 due 12/01/2018		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO imp bnds ser 2014 due 12/01/2034		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO library referdum rfdg bnds		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO tax increment rfdg bnds (Heritage Park) ser 2012 dtd 10/04/2012 due 03/01/2013-2026		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO various purp bnds ser 2014 due 12/01/2019		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO var purp bnds ser 2012 dtd 10/30/2012 due 12/01/2013-2024		
Long Term Rating	AAA/Stable	Affirmed

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.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.