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Research Update:

Minneapolis Series 2025 GO Bonds Assigned 'AAA' Rating; Outlook Is Stable

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Overview

- S&P Global Ratings assigned its 'AAA' rating to the City of Minneapolis' $140.97 million series 2025 general obligation (GO) bonds.
- At the same time, S&P Global Ratings affirmed its 'AAA' rating on the city's GO debt outstanding.
- The outlook is stable.

Rationale

Security

The bonds are secured by the full faith and credit of the city; a portion of the bonds' intended repayment source will be special assessments and net revenue of the water, sanitary sewer, and storm water systems. The bonds will be used for improvements to the city's water, storm, and sanitary sewer systems; various assessable public projects; and capital projects.

Credit highlights

The 'AAA' rating reflects Minneapolis' highly productive economy and robust tax base, the historical willingness and ability to increase property taxes to match expenditures, and a management team that consistently has built reserves to a high level by responding to unexpected budgetary changes and forward planning. Although not a current rating pressure, the city's plan to use reserves to plug near-term budget gaps, if not addressed, could be exacerbated by what we see as challenges including the lagging downtown economy and projected national slowdown, which could weaken performance of economically sensitive revenue that the city relies upon for operations.

The fiscal 2024 breakeven results were materially better than the $44 million deficit budgeted, largely due to unfilled vacancies and expenditures rolled over to the fiscal 2025 budget. Property tax collections were lower than budgeted, and the collection rate decreased to 96.6% from

99.3% in 2020, as the amount held in the appeal process increased. The city expects this will be collected in the subsequent year, but with the post-pandemic commercial real estate decline, the property tax burden is slowly shifting toward residential properties. Although the current shift is somewhat nominal, if it were to widen, we believe that the collection rate could worsen, pressuring operations.

The 2025 (yearend Dec. 31) general fund $25 million deficit budget (5% of revenue) includes an 6.8% levy, driven largely by rising public safety costs. Officials report that year to date budget performance is similar to the previous year, although the yearend results will likely be worse than in the prior year. The downtown assets fund (funded by a special sales tax) has performed well despite the city's lagging downtown economic recovery and has resumed post-pandemic-level transfers, with $41.9 million scheduled for 2025. While the five-year forecast calls for a 10.8% levy increase in 2026, management indicates that will likely be materially lower, as the city wants to lessen the residential tax burden, resulting in a deficit higher than the $6.2 million in the forecast. Management indicates that the fiscal 2026 budget will likely include 5% cuts across all departments, removal of positions that would likely remain vacant, and potential sunset of programs. In addition, if the downtown assets fund continues to perform well, the transfer to the general fund could be increased to ease budgetary pressure. With the expected drawdown in general fund reserves, management forecasts that fund balance will remain within its policy and use of fund balance will be spent on nonrecurring expenditures.

Key factors supporting the 'AAA' rating include the following:

- Tax base growth and new development continue, with other key economic measures also recovering. We are monitoring commercial office vacancies, as Minneapolis' are elevated compared with those of many other cities, but management expects the amount of taxes shifted to residential properties will remain nominal in the near term. In addition, the city has strong residential development and is working with developers to convert some spaces into residential property.
- Five-year projection details reveal easing budgetary pressure while preserving reserves in alignment with policy, but we note a variety of variables that could have a material impact, such as slowing job growth, shifting federal trade and immigration policy, and increased property tax appeals as the residential burden grows.
- We consider the management team sophisticated with long-term planning that can identify future challenges while preserving a healthy fiscal position.. Practices include multiyear financial and capital planning, periodic budget monitoring, a 17% fund balance policy, and robust planning around cyber security and environmental risk.
- Debt ratios are favorable compared with those of other large and growing U.S. cities. Pension and other postemployment benefit exposure is moderate although the funding levels improved due to higher funding and investment performance, but with little medium-term likelihood of meaningful cost acceleration.
- For more information on our institutional framework assessment for Minnesota municipalities, see "Institutional Framework Assessment: Minnesota Local Governments," Sept. 10, 2024.

Environmental, social, and governance

Although the U.S. Justice Department dismissed the federal consent decree, Minneapolis is still in a consent decree with the Minnesota Department of Human Rights regarding the practice of conduct in violation of state law and the mayor has publicly pledged to follow the dismissed decree. The city is budgeting and saving for these costs; however, should these amounts be insufficient and result in budgetary stress from the public safety staffing challenges or compliance with the consent decree, we could view risk management issues as an underpinning weakness in our credit analysis. We view social and environmental factors as neutral in our credit rating analysis.

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Rating above the sovereign

Minneapolis' 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," Nov. 19, 2013), U.S. local governments have moderate sensitivity to country risk. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy and independent treasury management with no history of federal government intervention, and we believe Minneapolis's financial flexibility is sufficiently demonstrated by its very strong budgetary reserves and liquidity.

Outlook

The stable outlook reflects our view of the city’s continued economic strengths and management’s forward-looking planning that we believe will be sufficient to address the emerging budgetary pressures, with reserves remaining above the fund balance policy.

Downside scenario

We could lower the rating if the city draws down its general fund reserves more rapidly than planned, which we believe could signify unanticipated budgetary pressure and would leave less room for fiscal maneuvering in outyear budgets.

Minneapolis, Minnesota--credit summary

Institutional framework (IF)	**1**
Individual credit profile (ICP)	1.55
Economy	1.0
Financial performance	2
Reserves and liquidity	1
Management	1.00
Debt and liabilities	2.75

Minneapolis, Minnesota--key credit metrics

	Most recent	**2024**	**2023**	**2022**
Economy				
Real GCP per capita % of U.S.	181	--	181	183
County PCPI % of U.S.	137	--	137	138
Market value ($000s)	69,507,600	69,980,226	69,629,877	65,938,298
Market value per capita ($)	161,692	162,791	161,976	154,019
Top 10 taxpayers % of taxable value	3.4	4.5	4.8	5.6
County unemployment rate (%)	2.9	2.8	2.5	2.4

Minneapolis, Minnesota--key credit metrics

	Most recent	2024	2023	2022
Local median household EBI % of U.S.	100	--	100	99
Local per capita EBI % of U.S.	116	--	116	116
Local population	429,877	--	429,877	428,119
Financial performance				
Operating fund revenues ($000s)	--	569,362	582,100	510,040
Operating fund expenditures ($000s)	--	640,104	574,799	509,748
Net transfers and other adjustments ($000s)	--	69,547	29,352	30,597
Operating result ($000s)	--	(1,195)	36,653	30,889
Operating result % of revenues	--	(0.2)	6.3	6.1
Operating result three-year average %	--	4.0	2.4	2.9
Reserves and liquidity				
Available reserves % of operating revenues	--	34.1	32.9	34.1
Available reserves ($000s)	--	194,150	191,370	173,717
Debt and liabilities				
Debt service cost % of revenues	--	8.2	9.0	9.9
Net direct debt per capita ($)	2,352	2,040	1,991	1,954
Net direct debt ($000s)	1,010,921	876,978	855,897	836,487
Direct debt 10-year amortization (%)	67	69	39	--
Pension and OPEB cost % of revenues	--	6.0	7.0	7.0
NPLs per capita ($)	--	894	1,172	2,038
Combined NPLs ($000s)	--	384,405	503,909	872,687

Financial data may reflect analytical adjustments and are sourced from issuer audit reports or other annual disclosures. Economic data is generally sourced from S&P Global Market Intelligence, the Bureau of Labor Statistics, Claritas, and issuer audits and other disclosures. Local population is sourced from Claritas. Claritas estimates are point in time and not meant to show year-over-year trends. GCP--Gross county product. PCPI--Per capita personal income. EBI--Effective buying income. OPEB--Other postemployment benefits. NPLs--Net pension liabilities.

Ratings List	
New Issue Ratings	
US$140.965 mil GO bnds ser 2025 due 12/01/2044	
Long Term Rating	AAA/Stable
Ratings Affirmed	
Local Government	
Minneapolis MN Unlimited Tax General Obligation and TIF Revenue - Condos on Blaisdell HIA	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation and Downtown East Project Parking Revenues	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation and Special Assessments	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation and Summit House Revenues	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation and Wellington Condos Tax Increment Revenues	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation with Special Assessments and Water Sewer and Storm Water System Revenues	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation, Water, Sewer, and Parking System, and Special Assessments	AAA/Stable
Minneapolis, MN Unlimited Tax General Obligation, and Sales, Hotel, and Downtown Liquor Taxes	AAA/Stable

The ratings appearing below the new issues represent an aggregation of debt issues (ASID) associated with related maturities. The maturities similarly reflect our opinion about the creditworthiness of the U.S. Public Finance obligor's legal pledge for payment of the financial obligation. Nevertheless, these maturities may have different credit ratings than the rating presented next to the ASID depending on whether or not additional legal pledge(s) support the specific maturity's payment obligation, such as credit enhancement, as a result of defeasance, or other factors.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, havespecific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at https://disclosure.spglobal.com/ratings/en/regulatory/ratings-criteria for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings referenced herein can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.