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Ratings

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Summary:

Minneapolis, Minnesota; General Obligation

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Table Of Contents

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Credit Profile		
US$40.0 mil taxable GO sales tax rfdg bnds ser 2017 due 12/01/2035		
Long Term Rating	AAA/Stable	New
US$40.0 mil GO imp & various purp bnds ser 2017 due 12/01/2027		
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, Minn.'s series 2017 general obligation (GO) improvement and various purpose bonds, and to its taxable GO sales tax refunding bonds. At the same time, we affirmed our 'AAA' ratings on the city's existing GO debt. The outlook is stable.

The GO improvement and various purpose 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 assessment revenue, though we rate the bonds to the city's GO pledge. Officials will use bonds proceeds for various capital improvement projects and to refund a portion of its outstanding series 2015A GO note. The taxable GO sales tax refunding bonds are secured by sales tax revenues and by the city's GO pledge, though we rate to the GO pledge. Officials will use proceeds to refund a portion of the city's outstanding series 2016 taxable GO sales tax revenue note.

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, titled "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, 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.

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

- 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 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 of 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, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 13.3% of expenditures and net direct debt that is 66.8% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 74.7% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Strong economy

We consider Minneapolis' economy strong. The city, with an estimated population of 404,168, is located in Hennepin County in the Minneapolis-St. Paul-Bloomington MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 109.1% of the national level and per capita market value of $107,068. Overall, the city's 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 slump in several 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 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 (payable 2016), growing by 9.7% and 10.7%, respectively, followed by an additional 8.5% increase in 2016 to $493.5 million. Economic market value, totaling $43.3 billion, has grown along similar lines over the same period. We understand that in 2016 the city experienced 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 the third quarter of 2016, its largest industries by share of total jobs included health care and social assistance (18.3% of total employment base), professional and technical services (11.5%), finance and insurance (9.7%), educational services (9.4%), and accommodation and food services (8.7%). 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 Ratings' most recent "State and Local Government Credit Conditions Forecast" (published April 18, 2017) has the multistate West North Central regional economy growing at a slightly slower pace than the national baseline scenario through 2018, largely reflecting low agricultural commodity prices.

Very strong management

We view the city's management as very strong, with "strong" financial policies and practices under our Financial Management Assessment 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 to requiring the city to maintain a minimum unrestricted general fund balance equal to 17% of the subsequent-year's 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 of 0.8% of expenditures, and balanced results across all governmental funds of 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. Management's estimated year-end results, however, reflect a $1.5 million increase in the general fund balance, which we understand was the result of $15.5 million that had been earmarked for spending on one-time projects that did not materialize during the year and that has been assigned for spending in 2017, along with revenues outperforming the budget by more than $12 million.

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The fiscal 2017 general fund budget is structured for break-even operating results and reflects a 5.5% increase in the city's property tax levy, flat local government aid, lower fees and permits, and sales tax and hospitality-related revenues up. On the expenditure side, the 2017 budget shows an increase in public safety spending due to personnel increases. While we believe the city could spend reserves in 2017 (or beyond) on one-time projects, 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 and are therefore 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 of 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 increased slightly in 2016. We believe the fund balance could fall closer to its 17% policy level within the next few years, with expenditures related to one-time projects. 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 currently has six variable-rate bank notes outstanding that were issued in 2015 and 2016. 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. With the current issuance, the city is refinancing portions of two of the bank notes into fixed rate debt, and we understand that the city intends to do the same with the remaining bank debt in the near future.

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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 66.8% of total governmental fund revenue. Overall net debt is low at 2.5% of market value, and approximately 74.7% 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 $927 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 $688 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 benefits (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 GASB valuations, dated 30 June 2016, the GERF plan had a 68.9% plan fiduciary net position as a percentage of the total pension liability (assuming a 7.5% discount rate), and the PEPFF plan had a 63.9% plan fiduciary net position (assuming a 5.6% discount rate).

For each of the city's plans, 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 long 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 city 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, 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 April 27, 2017)		
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 and various purp bnds ser 2016 due 12/01/2026		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Minneapolis GO imp bnds ser 2012 dtd 12/04/2012 due 12/01/2013-2019 2022 2025 2028 2032		
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 parking assessment rfdg bnds ser 2012 dtd 10/30/2012 due 12/01/2013-2026		
Long Term Rating	AAA/Stable	Affirmed

Ratings Detail (As Of April 27, 2017) (cont.)		
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
Minneapolis GO imp bnds ser 2011 dtd 11/22/2011 due 12/01/2031		
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.

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