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New Issue

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Minneapolis (City of), MN

New Issue - Moody's Assigns Aa1 to Minneapolis, MN's GO Bonds; Outlook Remains Stable

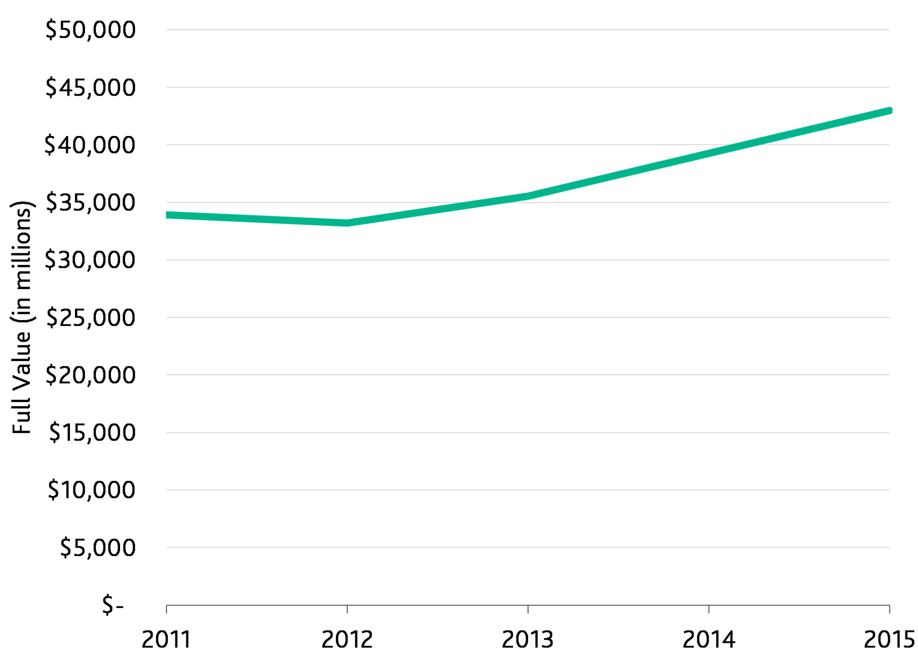
Summary Rating Rationale

Moody's Investors Service assigns a Aa1 rating to Minneapolis, MN's $120 million General Obligation (GO) Improvement and Various Purpose Bonds, Series 2016. Moody's also maintains the Aa1 rating on the city's outstanding GO bonds. Post-sale, the city will have $763.5 million of GO debt outstanding.

The Aa1 rating reflects the strong regional economy demonstrated by full valuation growth and a low unemployment rate, well-managed financial operations with healthy reserve levels, an above average debt burden and outsized Moody's adjusted net pension liability (ANPL).

Exhibit 1

After Significant Declines, Minneapolis' Full Valuation Has Grown For Three Consecutive Years



Source: Minnesota Department of Revenue

Credit Strengths

» Role as a regional economic center with a sizeable tax base that benefits from diverse employment opportunities and institutional stability

- Well-managed financial operations with comprehensive multi-year planning
- Strong valuation growth after years of declines through 2012

Credit Challenges

- Debt levels that exceed national medians with future borrowing plans
- Outsized Moody's adjusted net pension liability of 4.75 times fiscal 2015 operating revenues
- High fixed costs associated with debt and pensions as percentage of operating expenditures

Rating Outlook

The stable outlook reflects our expectation that the city's tax base will remain strong in the long term as the city continues its role as the economic engine of the state, and that financial operations will remain healthy given strong management policies and positive budget performance.

Factors that Could Lead to an Upgrade

- Moderation of fixed costs
- Reduction in outsized pension liability

Factors that Could Lead to a Downgrade

- Economic weakening that leads to increased unemployment or declines in tax base valuation
- Further growth in pension liabilities
- Budgetary pressures that lead to significant narrowing of reserves or liquidity

Key Indicators

Exhibit 2

Minneapolis (City of) MN	**2011**	**2012**	**2013**	**2014**	**2015**
Economy/Tax Base					
Total Full Value ($000)	$ 33,904,392	$ 33,199,913	$ 35,524,653	$ 39,248,772	$ 42,992,297
Full Value Per Capita	$ 88,794	$ 86,228	$ 91,297	$ 99,509	$ 104,620
Median Family Income (% of US Median)	100.0%	100.9%	101.8%	104.7%	104.7%
Finances					
Operating Revenue ($000)	$ 435,547	$ 426,475	$ 430,833	$ 515,965	$ 503,041
Fund Balance as a % of Revenues	24.5%	27.8%	30.1%	25.9%	21.7%
Cash Balance as a % of Revenues	25.3%	28.0%	31.2%	25.4%	27.7%
Debt/Pensions					
Net Direct Debt ($000)	$ 781,449	$ 672,895	$ 643,594	$ 648,783	$ 576,003
Net Direct Debt / Operating Revenues (x)	1.8x	1.6x	1.5x	1.3x	1.1x
Net Direct Debt / Full Value (%)	2.3%	2.0%	1.8%	1.7%	1.3%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	3.6x	3.6x	3.4x	3.6x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	4.6%	4.3%	4.4%	4.2%

The table above reflects data through the close of fiscal 2015.
Source: City's Audited Financial Statements, US Census Bureau, Moody's Investors Service.

Detailed Rating Considerations

Economy and Tax Base: Strong Economy With Improving Tax Base Valuations

We expect the city's economy to remain strong given ongoing investment in the tax base, a low unemployment rate and significant job opportunities available for residents. Minneapolis' large $43 billion tax base is recovering from the significant declines that occurred between 2006 and 2012. After increasing by 7% in 2013 and 10% in 2014, the city's economic market value grew by 9.5% in 2015. Management anticipates additional growth of up to 9% next year, with up to 2% of the growth driven by new construction and the remainder from appreciation. The city's ten largest taxpayers consist of mostly office and real estate properties, and comprised 10.7% of total net tax capacity.

Redevelopment and new development continues to occur in the city. The Central Corridor, a light rail that connects the downtowns of Minneapolis and St. Paul (Aa1 stable) opened in July 2014. The Southwest Light Rail Transit, which will connect downtown Minneapolis with suburbs including St. Louis Park and Eden Prairie (Aaa), is funded and expected to begin construction in 2017. The US Bank Stadium, home of the NFL Minnesota Vikings, opened earlier this year and is expected to spur ancillary commercial and retail development in the surrounding area. Over the longer term, the city plans to redevelop the Upper Harbor Terminal. The closure of the lock and dam due to the Asian carp infestation and low barge traffic has opened 50 acres of land available for redevelopment.

Despite a layoff of 2,500 employees by the city's fourth largest employer, Target Corporation (A2 stable), the city still had a net gain of more than 1,600 jobs in 2015. The city's largest employer is the University of Minnesota (Aa2 stable) with 14,400 employees, followed by Wells Fargo Bank, N.A. (Aa2 stable; 11,000 employees) and Fairview Health Service (A2 stable; 10,200 employees). Pointing to the strong economy, the city's unemployment rate in July 2016 was 3.4%, lower than both the state's rate of 3.7% and the national unemployment rate of 5.1% during the same month. The city's demographic profile is average with median family income estimated at 104.7% of the US median, according to the American Community Survey.

Financial Operations and Reserves: Healthy Reserves With Spend Down Expected

After budgetary challenges during the recent recession, Minneapolis' strong financial controls and multi-year financial planning practices have enabled the city to rebuild financial reserves. The city's available General Fund balance grew from $60 million (16.3% of revenues) in fiscal 2010 to $104.7 million (22.8% of revenues) in fiscal 2015. The city achieved these surpluses by increasing the property tax levy, conservatively budgeting expenditures, and including expense contingencies. Looking ahead, management plans to spend down reserves to invest in city infrastructure, development and technology, though expect to remain in compliance with its General Fund policy of holding a minimum of 17% of expenditures in reserve.

While the fiscal 2015 budget included the use of $10 million of General Fund reserves, actual results show fund balance growth of $3.6 million. Both revenues and expenditures had significant positive budget-to-actual variances with revenues coming in $10.3 million over budget and expenditures $10.9 million under budget. For 2016, management budgeted to use $28 million of General Fund reserves, though now anticipates a smaller $23.2 million draw due to strong sales tax collections following the opening of the US Bank Stadium. Despite the draw, management expects reserves to remain at or above its General Fund policy of a minimum of 17%.

The city's largest General Fund operating source is taxes (58.1%), including property taxes and local sales and hospitality taxes. State aid also provided 18.0% of the city's fiscal 2015 General Fund revenues. While the city's 2017 budget is not yet finalized, the Mayor's budget, which was presented to the City Council in August, includes a 5.5% property tax levy, with 1%, equivalent to $3 million, for the city's parks operations. The city anticipates Local Government Aid (LGA) to remain stable from the state in 2017.

In addition to the city's General Fund, its enterprise and internal service funds continue to remain healthy with positive operations. Additionally, the city's Convention Center Special Revenue Fund continues to remain healthy and had a fund balance of $67.2 million at the end of fiscal 2015. Management reports that the convention center has benefited from high occupancy and outperformed revenue expectations. The city has a fund balance policy for its Internal Service Funds which maintains a minimum balance ranging between 10% and 15% of annual operating expenditures in each respective fund. The enterprise funds' balance policy requires a minimum cash balance equal to approximately three months of operating expense, or 25% of the annual operating budget.

LIQUIDITY

The city's liquidity is strong with cash across the General Fund and Debt Service Fund totaling $139.9 million, or 27.7% of revenues in 2015. In addition, the city retains additional liquidity in its Internal Service Funds and Enterprise Funds. The city's six Internal Service

Funds had a combined unrestricted cash balance of $144.2 million at the end of 2015. The Internal Service Funds are partially funded with transfers from the General Fund which totaled $10.7 million in fiscal 2015. The Municipal Parking Fund had $14.0 million in unrestricted cash at the end of fiscal 2015. The city's Sanitary Sewer, Stormwater, Water, and Solid Waste funds had a combined $101 million unrestricted cash balance.

Debt and Pensions: High Fixed Costs and Outsized Pension Burden

At 1.8% of full valuation and 1.5 times operating revenues, the city's direct debt burden is above average yet manageable. Including borrowing by overlapping entities, the city's overall debt burden increases to 3.0%. We expect the city's debt profile to remain affordable given management's conservative use of debt instruments, above average pace of GO debt amortization, and recent growth in valuations. Debt service was the city's second largest operating expenditure (inclusive of the General Fund and Debt Service Funds) and accounted for 20.5% of operating expenditures in fiscal 2015. Total fixed costs, which include debt service, pension and OPEB contributions are high and totaled $153.6 million in fiscal 2015, or a high 30.5% of revenues. High fixed costs limit financial flexibility. Looking ahead, the city's five-year capital budget includes $473 million of bonds. In fiscal 2017, management expects to issue up to $133 million in new money debt for capital projects.

DEBT STRUCTURE

The city has some exposure to variable rate risk. The city has six series of variable rate bonds outstanding, with par amount totaling $83.6 million. Five of the series are through direct purchase loans with US Bank, NA (A1 stable) and the sixth is a direct purchase loan with Well Fargo. All six are secured by the city's general obligation pledge. The city's total variable rate debt currently comprises approximately 14% of its total GO debt. Two of the series, the 2015A and 2016 which total $34.4 million, are expected to be refunded with fixed rate GO debt in 2017. Per the term loan agreements, rates are reset the first of every week which is equal to the one week SIFMA or LIBOR index plus a spread based on the city's current GO rating. The city has budgeted conservatively with a 5% interest rate on all of its variable debt. In recent months, interest rates have remained favorable averaging less than 1%. All of Minneapolis' variable rate debt is uninsured, and the city is not a party to any interest rate swap agreements. Moody's believes that the city has sufficient liquidity to withstand unbudgeted increases in interest rates. City officials report no current plans to issue additional variable rate debt.

DEBT-RELATED DERIVATIVES

The city has no exposure to any debt-related derivatives.

PENSIONS AND OPEB

The city has a very high employee pension burden, based on the unfunded liabilities associated with its share of multi-employer statewide cost-sharing plans. Current city employees participate in either one of two state administered Public Employees Retirement Fund (PERA) pension program plans which include the General Employees Retirement Fund (GERF) and Public Employees Police and Fire Fund (PEPFF).

Most employees hired before 1980 are covered by one of three closed pension funds. The city's three closed funds were the Minneapolis Employees Retirement Fund (MERF), Minneapolis Police Relief Association (MPRA), and Minneapolis Fire Relief Association (MFRA). MERF merged into GERF and is now administered, as a separate account, by PERA as of June 30, 2010. The MPRA and MFRA funds merged into the larger statewide PEPFF plan on December 30, 2011. MPRA and MFRA were completely absorbed into the PEPFF and no longer exist as of December 31, 2011.

Moody's has allocated liabilities of statewide cost-sharing plans to the city in proportion to its contributions to each plan for analytic purposes and, beginning in 2015, used the cost-sharing plan allocations reported by the city under new GASB accounting standards. The city makes its full statutory contributions set by the state, to the multi-employer cost-sharing plans annually. In addition, as part of the merger, the city is required to make additional annual equal payments into the State's pension plans to improve the funded ratio. These obligations are included in the city budgets and the city is required to make these payments until 2031, or when full funding is achieved. In fiscal 2015, the city made contributions totaling $69.4 million towards pension payments.

Moody's adjusted net pension liability (ANPL) for the city as of fiscal 2015, under our methodology for adjusting reported pension data, is $2.2 billion, or a high 4.3 times operating revenues. The city's three-year Moody's ANPL is a more moderate $1.9 billion, or a still high 3.6 times operating revenues. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported contribution and liability information, or the reported liability information of the statewide cost-sharing plans, but to improve comparability with other rated entities. We note that the ANPL referenced above is net of all liabilities that we attribute to the utility enterprises that serve the city and surrounding area.

The city's Unfunded Actuarial Accrued Liability (UAAL) for Other Post Employment Benefit (OPEB) liabilities is manageable at $35.7 million. This liability represents the implicit cost of allowing retirees to remain on the City's health plans if they choose to pay the full cost of premiums and does not require any additional contribution from the City.

Management and Governance: Strong Institutional Framework With Multi-Year Financial Planning Practices

Minneapolis management is strong, engaging in multi-year financial planning practices and exhibiting strong financial controls.

Minnesota cities have an institutional framework score of “Aa,” or strong. Revenues are moderately predictable as cities rely primarily on property taxes. Some cities also rely on State Local Government Aid (LGA), which is distributed based on demographic and tax base factors. Revenue-raising flexibility is moderate as cities generally benefit from unlimited levying authority, except during years in which the state has imposed limits. Levy limits are not in place for the 2016-2017 biennium. Expenditures mostly consist of personnel costs, which are highly predictable. Cities typically maintain low fixed costs and have a moderate ability to reduce expenditures.

Legal Security

The bonds are secured by the county's full faith and credit general obligation pledge which benefits from a dedicated levy unlimited by rate or amount.

Use of Proceeds

Of the proceeds, $33.9 million will be used to refund for expected interest savings certain maturities of the city's outstanding GO Various Purpose Bonds, Series 2009 and GO Various Purpose Refunding Bonds, Series 2009B. The remaining proceeds will be used for capital improvements throughout the city.

Obligor Profile

The City of Minneapolis is located in Hennepin County (Aaa stable), in southeastern Minnesota (Aa1 stable). It is directly west of St. Paul, with the Mississippi River creating the border between the two cities. The city's population in 2015 was estimated at 410,939.

Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 3

Minneapolis (City of) MN

Issue	Rating
General Obligation (GO) Improvement and Various Purpose Bonds, Series 2016	Aa1
Rating Type	Underlying LT
Sale Amount	$120,000,000
Expected Sale Date	10/05/2016
Rating Description	General Obligation

Source: Moody's Investors Service

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