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CREDIT OPINION
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**Contacts**

| | |
|---|---|
| **Benjamin J VanMetre** | +1.312.706.9951 |
| *Analyst* | |
| ben.vanmetre@moodys.com | |
| **Rachel Cortez** | +1.312.706.9956 |
| *Senior Vice President/Manager* | |
| rachel.cortez@moodys.com | |

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# Bloomington (City of) MN

Update to credit analysis

## Summary

The City of Bloomington (Aaa) benefits from a large tax base that plays an integral role in the Twin Cities regional economy, strong resident income indices, consistently well-managed finances supported by ample reserves and a modest debt burden. The city's credit attributes are balanced against challenges including tax base concentration and an elevated pension burden.

## Credit strengths

» Favorably situated in the Twin Cities metropolitan area with strong resident income levels

» Stable financial operations and healthy reserves

» Modest debt burden

## Credit challenges

» Concentrated tax base

» Elevated pension burden

## Rating outlook

Outlooks are typically not assigned to local government issuers with this amount of debt.

## Factors that could lead to an upgrade

» Not applicable

## Factors that could lead to a downgrade

» Weakening of tax base valuation or resident income indices

» Declines in fund balances or liquidity

» Increased leverage related to long-term debt or pension liabilities

## Key indicators

Exhibit 1

| Bloomington (City of) MN | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|
| Economy/Tax Base | | | | | |
| Total Full Value ($000) | $10,073,586 | $10,372,315 | $11,461,897 | $12,316,534 | $13,088,048 |
| Population | 84,451 | 85,136 | 85,826 | 85,080 | 85,080 |
| Full Value Per Capita | $119,283 | $121,832 | $133,548 | $144,764 | $153,832 |
| Median Family Income (% of US Median) | 121.6% | 123.8% | 122.9% | 124.1% | 124.1% |
| Finances | | | | | |
| Operating Revenue ($000) | $69,043 | $72,778 | $75,771 | $76,583 | $79,256 |
| Fund Balance ($000) | $43,418 | $41,479 | $46,126 | $47,274 | $52,644 |
| Cash Balance ($000) | $48,793 | $42,418 | $45,995 | $52,468 | $52,602 |
| Fund Balance as a % of Revenues | 62.9% | 57.0% | 60.9% | 61.7% | 66.4% |
| Cash Balance as a % of Revenues | 70.7% | 58.3% | 60.7% | 68.5% | 66.4% |
| Debt/Pensions | | | | | |
| Net Direct Debt ($000) | $73,160 | $62,415 | $66,450 | $72,400 | $69,245 |
| 3-Year Average of Moody's ANPL ($000) | $155,466 | $174,581 | $172,216 | $209,305 | $226,069 |
| Net Direct Debt / Operating Revenues (x) | 1.1x | 0.9x | 0.9x | 0.9x | 0.9x |
| Net Direct Debt / Full Value (%) | 0.7% | 0.6% | 0.6% | 0.6% | 0.5% |
| Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x) | 2.3x | 2.4x | 2.3x | 2.7x | 2.9x |
| Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%) | 1.5% | 1.7% | 1.5% | 1.7% | 1.7% |

*Sources: Moody's Investors Service, US Census Bureau, Bloomington's audited financial statement*

## Profile

Bloomington is the State of Minnesota's (Aa1 stable) fifth most populous city and third largest city when ranked on tax base size. The city is located in Hennepin County (Aaa stable) approximately ten miles south of Minneapolis (Aa1 negative), serves more than 85,000 residents and provides primary services including police, fire, public works and parks.

## Detailed credit considerations

### Economy and tax base: large tax base in Twin Cities area; taxpayer concentration in Mall of America

We expect Bloomington's large tax base to remain a credit strength due to its integral role in the Twin Cities (Minneapolis, Aa1 negative; St. Paul, Aa1 negative) regional economy. The city's sizeable $14 billion tax base grew by more than 34% in just the last five years. Retail and the hospitality industries are key components of Bloomington's economy. The city's tax base is concentrated with the Mall of America (MOA) representing 11% of the city's net tax capacity. The city works closely with the MOA and reviews valuations annually, mitigating the effects of any unexpected or significant tax appeals. In addition to the retail industry, approximately 10,000 people are employed by Bloomington's hospitality industry, a sector which includes several hotels and restaurants.

As of August 2018, the city's unemployment rate (2.6%) was on par with the state's rate (2.5%) and below the national rate (3.9%). The city's median family income is strong at 124% of the national figure.

### Financial operations and reserves: consistently well managed financial operations with strong reserve levels

We expect the city will maintain stable financial operations supported by healthy reserves and conservative management. Most recently, the city closed fiscal 2017 with an available fund balance of balance of $53 million, or a healthy 66% of revenue across the General Fund and Debt Service Fund. Year to date results for fiscal 2018 reflect a more than $600,000 surplus in the General Fund due to conservative budgeting and higher than anticipated revenues. The city is in the process of adopting it's fiscal 2019 budget.

The majority of the city's revenues are derived from property taxes which comprised 60% of operating revenue. The city's second and third largest operating revenues are lodging & admissions tax, and licenses & permits, respectively, which comprised a combined 18% of revenue. While these revenues are sensitive to economic cycles, the revenues have performed better than budgeted in recent years.

**LIQUIDITY**

The city closed fiscal 2017 with a net cash balance $53 million, or a healthy 66% of revenue across the General Fund and Debt Service Fund.

### Debt and pensions: modest debt burden; elevated pension burden

The city's leverage related to long-term debt is modest though the pension burden is elevated. The city's debt burden is equal to a low 0.5% of full value and 0.9x fiscal 2017 operating revenue. In 2019, the city plans to issue $1.5 million for improvements to an ice garden, an additional $6.5 million for routine capital projects and approximately $2 million for park improvements.

Moody's adjusted net pension liability (ANPL) for the city totaled $226 million in fiscal 2017, equal to 1.6% of full value and 2.9x operating revenue. In comparison, the city's reported net pension liability, based on the use of different discount rates, was $21 million. The city's total fixed costs, inclusive of debt service, pension contributions, and other post-employment benefit (OPEB) costs, are equal to 21% of fiscal 2017 operating revenue.

**DEBT STRUCTURE**

All of the city's debt is fixed rate and amortizes over the long term, with approximately 85% of outstanding principal retired within 10 years.

**DEBT-RELATED DERIVATIVES**

The city is not a party to any derivative agreements.

**PENSIONS AND OPEB**

The city participates in two multiple-employer cost-sharing plans, the General Employees Retirement Fund (GERF) and the Public Employees Police and Fire Fund (PEPFF). Minnesota statutes establish local government retirement contributions as a share of annual payroll. Employer contribution rates are currently set at 7.5% of payroll for GERF and at 16.2% of payroll for PEPFF. The city's total fiscal 2017 pension contribution was $5.7 million, or 7% of operating revenue.

Statutory contribution levels have not kept pace with growing unfunded liabilities in state-wide pension plans. Contributions to PEPFF from all participating governments in aggregate amounted to 90% of the plan's "tread water" indicator in 2017.[1] The state of Minnesota approved legislation in 2018 that will modify benefits and modestly increase contributions for some pension plans. Employer contributions from cities to the police and fire plan, for example, will modestly increase to 17.7% by 2020 from the current rate of 16.2%. Because employer contributions will not rise significantly, cities are unlikely to contend with material budget strain from the increases. However, pension leverage will likely remain elevated.

OPEB obligations do not represent a material cost for the city. The city does not offer explicit OPEB benefits, but allows retired employees to stay on its health care plan, creating an implicit rate subsidy. The city made a $300,000 pay-as-you-go contribution to its OPEB plan in 2017. The city's most recent unfunded actuarial accrued liability (UAAL) was $12 million.

### Management and governance: strong institutional framework with conservative budgeting practices

Minnesota cities have an Institutional Framework score of Aa, which is strong. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector has one or more major revenue sources that are not subject to any caps. Revenues tend to be predictable, as cities rely primarily on property taxes and 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 currently in place for cities. Across the sector, fixed and mandated costs are relatively high. Minnesota has public sector unions, which can limit the ability to cut expenditures. Expenditures mostly consist of personnel costs, which are highly predictable.

City management adheres to a fund balance policy of maintaining reserves between 35% and 40% of expenditures. The city also follows 10 to 15 year financial forecasts across the various operating funds and capital projects.

## Endnotes

1 Employer contributions that tread water equal the sum of current year service cost and interest on reported net pension liabilities at the start of the year, using reported assumptions. If plan assumptions are met exactly, contributions equal to the tread water indicator will prevent the reported net pension liabilities from growing

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## Contacts


**Benjamin J VanMetre** +1.312.706.9951
*Analyst*
ben.vanmetre@moodys.com

**Rachel Cortez** +1.312.706.9956
*Senior Vice President/ Manager*
rachel.cortez@moodys.com


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