MINNESOTA Management & Budget

# Office Memorandum

**Date:** February 26, 2016

**To:** Legislative Reference Library

**From:** Myron Frans, Commissioner

**Subject:** Report to the Legislature - Debt Capacity Forecast

Minnesota Statute 16A.105 requires the Commissioner of Management and Budget in February and November of each year to prepare a debt capacity forecast to be delivered to the governor and legislature.

Attached is the February 2016 debt capacity forecast.

Attachment

cc: Senator Thomas M. Bakk
Senator David W. Hann
Senator Richard Cohen
Senator LeRoy A. Stumpf
Representative Kurt Daudt
Representative Paul Thissen
Representative Jim Knoblach
Representative Paul Torkelson

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# Minnesota Management and Budget
# Debt Capacity Forecast
# February 2016

## Introduction

Minnesota Statute 16A.105 requires the Commissioner of Management and Budget ("MMB") to prepare a debt capacity forecast to be delivered to the governor and legislature in February and November of each year.

## Statement of Indebtedness

The statement of indebtedness describes the amount of debt we are currently obligated to repay. As of February 26, 2016, the state of Minnesota owed $6,545,780,000 in principal for general obligation bonds (this includes both various purpose and trunk highway bonds), as well as $1,639,690,000 in principal for other tax-supported obligations, for a total of $8,185,470,000. Please see the attached exhibit for more detail about these obligations.

The state has no general obligation short-term notes outstanding.

## Debt Service Costs

The details of the actual and forecasted debt service costs for all of the state's tax-supported debt are provided in the following table. For the purpose of this forecast, the assumption for future capital budgets for various purpose general obligation bonds is $800 million in the even numbered legislative sessions and $230 million in the odd numbered years. For trunk highway bonds, the forecast amounts for existing bond authorizations have been prepared based upon information provided by the Department of Transportation. The column entitled "Other Tax-Supported Bonds" reflects the actual debt service obligations in each fiscal year for the debt identified in the exhibit; it does not reflect the total amount appropriated in each fiscal year for such obligations. The estimate for interest rates used for future bond issues is derived from the IHS Economics ("IHS") data used to develop the February 2016 Budget and Economic Forecast.

## Actual Annual Debt Service Costs
**($ in Thousands)**

| Fiscal Year | General Obligation Bonds: Various Purpose | General Obligation Bonds: Trunk Highway Fund | General Obligation Bonds: Subtotal | Other Tax Supported Bonds | Total |
|---|---|---|---|---|---|
| 2006 actual | $353,728 | $36,347 | $390,075 | $10,629 | $400,705 |
| 2007 actual | $400,146 | $53,752 | $453,898 | $14,695 | $468,593 |
| 2008 actual | $409,426 | $52,170 | $461,596 | $17,999 | $479,595 |
| 2009 actual | $452,978 | $59,542 | $512,520 | $24,259 | $536,779 |
| 2010 actual | $429,123 | $70,542 | $499,665 | $27,640 | $527,305 |
| 2011 actual | $398,799 | $45,225 | $444,024 | $30,393 | $474,417 |
| 2012 actual | $190,799 | $72,601 | $263,400 | $38,194 | $301,594 |
| 2013 actual | $222,584 | $120,305 | $342,889 | $49,236 | $392,125 |
| 2014 actual | $619,935 | $136,488 | $756,423 | $97,492 | $853,915 |
| 2015 actual | $623,060 | $154,593 | $777,653 | $147,149 | $924,802 |
| 2016 forecast | $609,285 | $180,725 | $790,010 | $148,484 | $938,494 |
| 2017 forecast | $630,295 | $205,685 | $835,980 | $149,295 | $985,275 |
| 2018 forecast | $589,248 | $222,886 | $812,134 | $148,387 | $960,521 |
| 2019 forecast | $617,419 | $226,310 | $843,729 | $147,018 | $990,747 |
| 2020 forecast | $589,799 | $221,772 | $811,571 | $137,753 | $949,324 |
| 2021 forecast | $617,934 | $214,560 | $832,494 | $137,502 | $969,996 |
| 2022 forecast | $610,819 | $205,036 | $815,855 | $137,409 | $953,264 |

**Totals may not add due to rounding.*

## Debt Authorized and Unissued

As of February 26, 2016, the state has authorized but not yet issued (sold) general obligation bonds for various purposes and trunk highway purposes totaling $1,196,011,800. In addition to the general obligation bonds, the state has authorized appropriation bonds that have not been sold. The 2014 Legislature authorized the sale of $80 million of state appropriation bonds to finance the Housing Finance Agency Housing Infrastructure bonding program, of which $11.335 million remains unissued as of February 2016. The 2015 Legislature authorized an additional $10 million in state appropriation bonds to finance the Housing Finance Agency Housing Infrastructure bonding program and $19 million for the Lewis and Clark Regional Water System and the 2012 legislature authorized $10 million in state appropriation bonds to finance the pay for performance bond program. None of the debt for these programs has been issued. The total amount of authorized and unissued tax-supported obligations is $1,246,346,800. All other currently authorized tax supported bond projects and/or programs have been issued.

## Managing State Debt Capacity

MMB adopted Capital Investment Guidelines to measure and track the debt of the state. Debt or capital investment guidelines are used to assist in decision making, communicate policy goals, provide recommendations for the structure of debt issues, and demonstrate a commitment to long-term capital and financial planning. MMB's Guidelines are intended to:

- Be consistent with measures used by the credit rating agencies and foster direct comparisons with the debt burdens of other states;
- Be comprehensive to ensure all kinds of tax-supported debt obligations are recognized; and
- Continue Minnesota's conservative financial management practices.

Adherence to a debt management policy signals to rating agencies and the capital markets that a government is well managed and therefore is likely to meet its debt obligations in a timely manner. The capital investment guidelines are:

1. Total tax-supported principal outstanding shall be 3.25% or less of total state personal income.
2. Total amount of principal (both issued, and authorized but unissued) for state general obligations, state moral obligations, equipment capital leases, and real estate capital leases are not to exceed 6% of state personal income.
3. 40% of general obligation debt shall be due within five years and 70% within ten years, if consistent with the useful life of the financed assets and/or market conditions.

The first two guidelines help to determine our capacity for additional debt. Both guidelines compare the state's debt[1] to the state's personal income. The first comparison is what the state owes, based on the amount of debt we have sold. The second comparison is what the state would owe if all the debt that has been authorized were sold. The third guideline helps determine how well we manage how quickly we payoff our general obligation debt.

This analysis is based on forecast assumptions[2] including that $800 million of bond authorization is approved in the even-year sessions, starting with the 2016 session, and $230 million of bond authorization is approved in odd-year sessions.

### Debt Capacity Guideline #1

Guideline #1 compares the total amount of debt the state has sold and currently owes to the state's personal income. Each bonding bill authorizes MMB to sell bonds and use the proceeds for the projects identified in the bill. For any given bond authorization, we typically sell bonds over a period of years to make the funds available for the projects when needed, and not sooner. For

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[1] "State debt" refers to tax supported debt and includes state general obligation debt, both various purpose and trunk highway, certificates of participation and lease revenue bonds, state issued appropriation bonds, and other issuer bonds supported by a state appropriation.

[2] These estimates are based on a ten-year rolling average of bond authorizations.

example, if $800 million were authorized in 2016, we assume we would sell $120 million of bonds in 2016, an additional $280 million in 2017, and the remainder in the following years. It may be five years or more before the total amount authorized in each bonding bill is actually sold.

Our threshold for Guideline #1 is that the amount of debt sold and currently owed does not exceed 3.25% of personal income. The state is currently within Guideline #1.

| | |
|---|---|
| Tax-supported principal sold | $8.185 billion |
| FY 2016 state personal income estimate – IHS forecast | $281.653 billion |
| As a percent of state personal income, not to exceed 3.25% | 2.91% |
| Estimate of maximum amount of tax-supported debt that could be sold today before exceeding Guideline #1* | $968 million* |

*Bonds authorized are typically not sold all at once; they are sold over several years.

**Debt Capacity Guideline #2**

Guideline #2 compares the total amount of debt authorized, or approved in law to personal income. This guideline differs from the first guideline in that it includes all of state debt authorized, whether it has been sold or not, compared to the first guideline, which only includes the amount of bonds sold.

Our measure for guideline #2 is that total debt authorized does not exceed 6% of personal income. The state is currently within Guideline #2.

| | |
|---|---|
| Total principal sold plus authorized and not yet sold | $11.118 billion |
| FY 2016 state personal income estimate – IHS forecast | $281.653 billion |
| As a percent of state personal income, not to exceed 6.0% | 3.95% |
| Estimated maximum amount of tax-supported debt that could be authorized before exceeding Guideline #2 | $5.781 billion |

**Debt Capacity Guideline #3**

Guideline #3 evaluates how quickly we pay off our general obligation bonds. Our goal is that no less than 40% of our general obligation debt is paid within five years and no less than 70% within ten years. MMB structures general obligation debt to comply with this guideline.

Of the State's general obligation bonds outstanding on June 30, 2015, 40.3 percent were scheduled to mature within five years and 71.0 percent were scheduled to mature with ten years. Furthermore, of the State's general obligation bonds expected to be outstanding on June 30, 2016, 40.3 percent are scheduled to mature within five years and 71.2 percent are scheduled to mature with ten years.

**Total Debt Capacity**

Our total debt capacity refers to the amount of debt that could be authorized each legislative session without exceeding our debt guidelines. In other words, how big could the bonding bill be? Our calculations assume that the maximum amount of state debt would be authorized and would impact our forecast assumptions into the future. The table below identifies the authorization amounts currently assumed in our forecast, the maximum amount that could be authorized each year, the corresponding impact on each guideline, and the general fund debt service costs resulting from the maximum authorization.

| ***Dollars in millions*** | **FY 2016** | **FY 2017** | **FY 2018** | **FY 2019** | **FY 2020** | **FY 2021** |
|---|---|---|---|---|---|---|
| **Bonding Bill Assumed in Feb '16 Forecast** | $800 | $230 | $800 | $230 | $800 | $230 |
| **Maximum Bonding Bill Within Debt Guidelines** | $3,229 | $230 | $1,256 | $1,313 | $1,325 | $980 |
| **Impact on Guideline #1** | 3.04% | 3.13% | 3.25% | 3.23% | 3.25% | 3.18% |
| **Impact on Guideline #2** | 4.70% | 4.35% | 4.34% | 4.30% | 4.27% | 4.13% |
| **Additional Debt Service Required** | $0 | $38 | $108 | $194 | $224 | $322 |

It is IMPORTANT to note that:

1. The numbers assume all tax supported debt or state debt as defined earlier in the document: new authorizations for a bonding bill, new authorizations for GO Trunk Highway Bonds, and any other new appropriation debt.
2. The assumptions for personal income are based on the February 2016 Forecast information provided by IHS. Changes in subsequent forecasts will change the estimated capacity of both Guidelines #1 and #2.
3. If the enacted bonding bill is higher (or lower) than the assumed 10-year rolling average, the 10 year rolling average assumption in the debt capacity forecast will change accordingly, thus changing the debt capacity for Guidelines #1 and #2.

## Capital Investment Guidelines
## Summary of Outstanding Principal as of 2/26/2016
## As of February 2016 Budget and Economic Forecast

| ***Tax-Supported Debt (Guideline #1)*** | **Principal Outstanding** | **Authorized, Unissued** | **Total** |
|---|---|---|---|
| All State General Obligation Debt | | | |
| General Fund State General Obligation Debt | $ 4,641,045,000 | $ 630,188,700 | $ 5,271,233,700 |
| Trunk Highway Fund General Obligation Debt | $ 1,904,735,000 | $ 565,823,100 | $ 2,470,558,100 |
| Certificates of Participation (SWIFT/Integrated Tax) | 31,830,000 | 0 | 31,830,000 |
| BCA Bemidji Lease Revenue Bonds | 3,385,000 | 0 | 3,385,000 |
| Other Real Estate Capital Leases: | | | |
| Ag/Health Buildings | 43,190,000 | 0 | 43,190,000 |
| DHS Building | 51,690,000 | 0 | 51,690,000 |
| MHFA Supportive Housing 2008 | 27,270,000 | 0 | 27,270,000 |
| MHFA Housing Infrastructure 2012 | 27,430,000 | 0 | 27,430,000 |
| MHFA Housing Infrastructure 2014 | 63,665,000 | 11,335,000 | 75,000,000 |
| MHFA Housing Infrastructure 2015 | | 10,000,000 | 10,000,000 |
| U of M: | | | |
| TCF Bank Stadium | 90,075,000 | 0 | 90,075,000 |
| Biosciences Facilities | 182,420,000 | 0 | 182,420,000 |
| State General Fund Appropriation Refunding Bonds | 584,865,000 | 0 | 584,865,000 |
| Professional Football Stadium Appropriation Bonds | 453,770,000 | 0 | 453,770,000 |
| Certificates of Participation - Legislative Office Facility | 80,100,000 | 0 | 80,100,000 |
| Lewis and Clark Regional Water System Bonds | 0 | 19,000,000 | 19,000,000 |
| Pay for Performance Appropriation Bonds | 0 | 10,000,000 | 10,000,000 |
| TOTAL - Tax-Supported Debt | $ 8,185,470,000 | $ 1,246,346,800 | $ 9,431,816,800 |

***Other Obligations (Guideline #2)***

| | |
|---|---|
| Tax-Supported Debt (issued and authorized but unissued) | $ 9,431,816,800 |
| MHFA Moral Obligation Debt [(1)] | 1,189,570,000 |
| MOHE Moral Obligation Debt | 471,015,000 |
| Equipment Leases | 25,965,108 |
| TOTAL - All Obligations | $ 11,118,366,908 |

| | |
|---|---|
| FY 2016 State Personal Income Estimate - IHS Forecast: | 281,653,000,000 |
| State Tax-Supported Debt as a Percent of Personal Income: | 2.91% |
| Estimated maximum additional principal capacity for all tax-supported debt @ 3.25% | $ 968,252,500 |
| All Obligations as a Percent of Personal Income: | 3.95% |
| Estimated maximum additional principal capacity for all obligations @ 6.0% | $ 5,780,813,092 |

[(1)] MHFA has a $5 billion statutory debt limit. However, several of the MHFA bonding programs are not issued as Moral Obligation debt. The bond programs that are not included because they are not secured by a debt service reserve fund subject to replenishment from Legislative appropriation are the conduit multifamily revenue bonds and bonds issued under
4. Home Ownership Mortgage-backed Exempt Securities and Homeownership Finance Bonds.