MANAGEMENT AND BUDGET

Office Memorandum

Date: December 2, 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 November 2016 debt capacity forecast.

Attachment

cc:

Senator Thomas M. Bakk
Senator David W. Hann
Senator Richard Cohen
Senator LeRoy A. Stumpf
Senator Paul Gazelka
Senator Julie Rosen
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Representative Kurt Daudt
Representative Paul Thissen
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Representative Paul Torkelson
Representative Melissa Hortman
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Minnesota Management and Budget
Debt Capacity Forecast
November 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 November 30, 2016, the state of Minnesota has outstanding principal totaling $8,064,385,000, which includes $6,454,955,000 in outstanding principal for general obligation bonds (both various purpose and trunk highway bonds) and $1,609,430,000 in outstanding principal for other tax-supported obligations. 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 2017 legislative session and then $800 million in the subsequent even-numbered legislative sessions and $230 million in the subsequent 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 and do not assume any additional bond authorizations. 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 <u>not</u> 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 November 2016 Budget and Economic Forecast.

Actual Annual Debt Service Costs

($ in Thousands)

	General Obligation Bonds				
Fiscal Year	**Various Purpose**	**Trunk Highway Fund**	**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 actual	$609,285	$180,725	$790,010	$148,484	$938,494
2017 forecast	$529,215	$193,539	$722,754	$150,838	$873,592
2018 forecast	$562,015	$213,190	$775,205	$150,292	$925,498
2019 forecast	$580,601	$223,328	$803,929	$148,931	$952,860
2020 forecast	$578,119	$222,789	$800,908	$139,659	$940,567
2021 forecast	$614,500	$213,817	$828,317	$139,404	$967,721
2022 forecast	$604,417	$204,341	$808,758	$139,317	$948,074
2023 forecast	$620,872	$199,709	$820,581	$137,866	$958,447

**Totals may not add due to rounding.*

Debt Authorized and Unissued

As of November 30, 2016, the state has authorized but not yet issued (sold) general obligation bonds for various purposes and trunk highway purposes totaling $643,511,600. In addition to the general obligation bonds, the state has authorized appropriation bonds that have not been sold. The 2015 Legislature authorized the sale of $10 million of state appropriation bonds to finance the Housing Finance Agency Housing Infrastructure bonding program, of which $2.710 million remains unissued as of November 2016. The 2015 Legislature also authorized $19 million of state appropriation bonds for the Lewis and Clark Regional Water System project, of which $7.210 million remains unissued as of November 2016. The 2012 legislature authorized $10 million in state appropriation bonds to finance the pay for performance bond program, which bonds remain unissued. The total amount of authorized and unissued tax-supported obligations is $663,431,600. All other currently authorized tax-supported obligations have been issued.

Managing State Debt Capacity

MMB adopted Capital Investment Guidelines in December 2009, 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 pay off our general obligation debt.

The following analysis is based on forecast assumptions[2] including that $800 million of bond authorization is approved in the 2017 legislative session and then $800 million of bond authorization is approved in subsequent even-year sessions and $230 million of bond authorization is approved in subsequent 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

[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.

period of years to make the funds available for the projects when needed, and not sooner. For example, if $800 million were authorized in 2017, we assume we would sell $120 million of bonds in 2017, an additional $280 million in 2018, 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	$8.064 billion
FY 2017 state personal income estimate – IHS forecast	$291.980 billion
As a percent of state personal income, not to exceed 3.25%	2.76%
Estimate of maximum amount of tax-supported debt that could be sold today before exceeding Guideline #1*	$1.425 billion*

*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 authorized state debt to personal income. This guideline differs from the first guideline in that it includes all authorized state debt, 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	$10.368 billion
FY 2017 state personal income estimate – IHS forecast	$291.980 billion
As a percent of state personal income, not to exceed 6.0%	3.55%
Estimated maximum amount of additional tax-supported debt that could be authorized before exceeding Guideline #2	$7.151 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, 2016, 40.3 percent were scheduled to mature within five years and 71.2 percent were scheduled to mature with ten years. Furthermore, of the state's general obligation bonds expected to be outstanding on June 30, 2017, 41.3 percent are scheduled to mature within five years and 72.2 percent are scheduled to mature with ten years. The state is currently within Guideline #3.

Maximum Debt Capacity under Current Guidelines

The maximum debt capacity refers to the amount of additional debt that could be authorized each legislative session without exceeding our debt guidelines. This information can be used to answer the question of how big a bonding bill *could* be, but does not suggest how big a bonding bill *should* be. The table below shows the maximum annual new debt authorizations until the limit in either Guideline #1 or Guideline #2 is reached. Our calculations assume that the maximum amount of state debt would be authorized and would impact our forecast assumptions into the future, including the assumed 10-year rolling average. The table also shows the additional general fund debt service costs resulting from the maximum authorization.

Dollars in millions	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**	**FY 2022**
Bonding Bill Assumed in Nov '16 Forecast	$800	$800	$230	$800	$230	$800
Maximum New Debt Authorizations Within Debt Guidelines	$3,450	$1,750	$687	$1,969	$959	$1,716
Impact on Guideline #1	2.70%	2.89%	3.13%	3.25%	3.23%	3.25%
Impact on Guideline #2	4.31%	4.48%	4.29%	4.45%	4.30%	4.34%
Additional Debt Service Required	$0	$40	$151	$270	$361	$415

It is IMPORTANT to note that:

1. The amounts listed in the "Maximum New Debt Authorizations" line could be allocated among any of the following types of debt: various purpose general obligation bonds, trunk highway general obligation bonds, state general fund appropriation bonds, certificates of participation and real estate and equipment capital leases.
2. The assumptions for personal income are based on the November 2016 Forecast information provided by IHS. Changes to personal income in subsequent forecasts will change the estimated capacity of both Guidelines #1 and #2.

Capital Investment Guidelines
Summary of Outstanding Principal as of 11/30/2016
As of November 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	$ 4,453,400,000	$ 292,688,500	$ 4,746,088,500
Trunk Highway Fund General Obligation Debt	2,001,555,000	350,823,100	2,352,378,100
Certificates of Participation (SWIFT/Integrated Tax)	24,420,000	0	24,420,000
BCA Bemidji Lease Revenue Bonds	3,420,000	0	3,420,000
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	26,015,000	0	26,015,000
MHFA Housing Infrastructure 2012	26,470,000	0	26,470,000
MHFA Housing Infrastructure 2014	73,210,000	0	73,210,000
MHFA Housing Infrastructure 2015	7,290,000	2,710,000	10,000,000
U of M:			
TCF Bank Stadium	85,490,000	0	85,490,000
Biosciences Facilities	177,170,000	0	177,170,000
State General Fund Appropriation Refunding Bonds	555,345,000	0	555,345,000
Professional Football Stadium Appropriation Bonds	445,330,000	0	445,330,000
Certificates of Participation - Legislative Office Facility	78,600,000	0	78,600,000
Lewis and Clark Regional Water System Bonds	11,790,000	7,210,000	19,000,000
Pay for Performance Appropriation Bonds	0	10,000,000	10,000,000
TOTAL - Tax-Supported Debt	$ 8,064,385,000	$ 663,431,600	$ 8,727,816,600

Other Obligations (Guideline #2)		
Tax-Supported Debt (issued and authorized but unissued)		$ 8,727,816,600
MHFA Moral Obligation Debt [(1)]		1,131,975,000
MOHE Moral Obligation Debt		467,970,000
Equipment Leases		30,880,629
Guaranteed Energy Savings Program (GESP) Equipment Leases		9,234,539
TOTAL - All Obligations		$ 10,367,876,768
FY 2017 State Personal Income Estimate - IHS Forecast:	291,980,000,000	
State Tax-Supported Debt as a Percent of Personal Income:	2.76%	
Estimated maximum additional principal capacity for all tax-supported debt @ 3.25%	$ 1,424,965,000	
All Obligations as a Percent of Personal Income:	3.55%	
Estimated maximum additional principal capacity for all obligations @ 6.0%	$ 7,150,923,232	

[(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 Home Ownership Mortgage-backed Exempt Securities and Homeownership Finance Bonds.