Debt Capacity Forecast

Report to the Minnesota State Legislature | February 29, 2024

Office Memorandum

Date: February 29, 2024

To: Legislative Reference Library

From: Erin Campbell, Commissioner EC

Subject: Report to the Legislature - Debt Capacity Forecast

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

Attached is the February 2024 debt capacity forecast. The state remains in compliance with its Capital Investment Guidelines with $7.8 billion in outstanding debt.

Attachment

cc:

Senator Erin Murphy
Senator Mark Johnson
Senator John Marty
Senator Sandy Pappas

Representative Melissa Hortman
Representative Lisa Demuth
Representative Liz Olson
Representative Fue Lee

Minnesota Management and Budget
Debt Capacity Forecast | February 2024

Introduction

Minnesota Statutes, Section 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 29, 2024, the state of Minnesota has outstanding principal totaling $7,837,405,000 which includes $6,250,980,000 in outstanding principal for general obligation bonds (both various purpose and trunk highway bonds) and $1,586,425,000 in outstanding principal for other tax-supported obligations. Please see the attached Exhibit 1 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 this forecast, the assumption for future capital budgets for various purpose general obligation bonds is $980 million in the 2024 legislative session and then $1.010 billion in subsequent even-numbered years and $165 million in 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 non-general obligation debt identified in Exhibit 1; 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 S&P Global Market Intelligence, IHS Global Inc. ("SPGMI") data used to develop the February 2024 Budget and Economic Forecast.

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*
2018	actual	$563,123	$211,009	$774,133	$150,439	$924,572
2019	actual	$549,785	$214,903	$764,688	$150,675	$915,363
2020	actual	$540,081	$209,821	$749,902	$144,487	$894,389
2021	actual	$515,544	$177,571	$693,115	$145,383	$838,498
2022	actual	$592,426	$213,138	$805,564	$148,572	$954,137
2023	actual	$547,759	$247,908	$795,667	$538,938	$1,334,605
2024	forecast	$507,577	$229,906	$737,483	$149,110	$886,593
2025	forecast	$629,228	$271,390	$900,618	$177,660	$1,078,278
2026	forecast	$645,460	$290,395	$935,856	$165,596	$1,101,452
2027	forecast	$704,524	$314,583	$1,019,107	$166,185	$1,185,292
2028	forecast	$710,045	$330,798	$1,040,843	$166,647	$1,207,490
2029	forecast	$721,973	$340,102	$1,062,074	$167,185	$1,229,259
2030	forecast	$729,647	$360,531	$1,090,177	$156,929	$1,247,106

**Totals may not add due to rounding.*

Debt Authorized and Unissued

As of February 29, 2024, the state has authorized but not yet issued (sold) general obligation bonds for various purposes and trunk highway purposes totaling $3,768,026,480. In addition to the general obligation bonds, the state has authorized appropriation bonds that have not been sold as of February 29, 2024. The 2021 Legislature authorized the sale of $100 million of state appropriation bonds by the Housing Finance Agency to finance a housing infrastructure bonding program, of which $12,960,000 million remains unissued. The total amount of authorized and unissued tax-supported obligations is $3,780,986,480. 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
- Continue Minnesota's responsible 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. Minnesota's three Capital Investment Guidelines are:

1. Total tax-supported principal outstanding is 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 is 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 measures how well we manage how quickly we pay off our general obligation debt.

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 only when needed, and not sooner. For example, if $980 million were authorized in 2024, we assume we would sell $147 million of bonds in fiscal year 2025, an additional $343 million in fiscal year 2026, 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.

[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.

Our measure 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. See Exhibit 2 for the State's compliance with Guideline #1 for the past 10 years.

Tax-supported principal sold	$7.837 billion
FY 2024 state personal income estimate – SPGMI forecast	$418.722 billion
As a percent of state personal income, not to exceed 3.25%	1.87%
Estimate of maximum amount of tax-supported debt that could be sold today before exceeding Guideline #1*	$5.771 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, including state moral obligations and equipment capital leases, 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, and it also captures state moral obligations and equipment capital leases.

Our measure for Guideline #2 is that total debt authorized does not exceed 6% of personal income. The state is currently within Guideline #2. See Exhibit 2 for the State's compliance with Guideline #2 for the past 10 years.

Total principal sold plus authorized and not yet sold	$15.578 billion
FY 2024 state personal income estimate – SPGMI forecast	$418.722 billion
As a percent of state personal income, not to exceed 6.0%	3.72%
Estimated maximum amount of additional tax-supported debt that could be authorized before exceeding Guideline #2	$9.545 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, 2023, 42.7% were scheduled to mature within five years and 74.8% were scheduled to mature with ten years. Furthermore, of the state's general obligation bonds expected to be outstanding on June 30, 2024, 43.4% are scheduled to mature within five years and 75.6% 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.

Rating agencies view the state's adherence to debt guidelines as a positive factor in the state's overall credit rating.

The following tables highlight the maximum debt limits under the debt guidelines. Because the guidelines measure debt differently, there can be different maximums under each guideline.

Maximum Limits Under Guidelines #1 and #2: Personal Income

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. This table shows that the maximum limit under Guideline #1 would be reached first in FY 2030. The table also shows the additional general fund debt service costs resulting from the maximum authorizations.

Maximum Debt Capacity:
Personal Income (Guidelines #1 and #2)

Dollars in millions	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
Bonding Bills Assumed in Feb '24 Forecast	$980	$165	$1,010	$165	$1,010	$165
Maximum New Debt Authorizations Within Debt Guidelines #1 and #2	$3,100	$2,200	$2,700	$2,200	$2,700	$2,200
	FY 2025	**FY 2026**	**FY 2027**	**FY 2028**	**FY 2029**	**FY 2030**
Impact on Guideline #1	2.17%	2.40%	2.76%	2.97%	3.18%	3.25%
Impact on Guideline #2	4.15%	4.29%	4.53%	4.66%	4.90%	4.96%
Additional Debt Service Required	$35	$145	$349	$478	$651	$753

* Impacts to Guidelines #1 and #2 from a bonding bill passed during regular legislative session are first reported in a November debt capacity forecast and therefore shown in the following fiscal year

Notes about the table above:

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 February 29, 2024 Forecast information provided by SPGMI. Changes to personal income in subsequent forecasts will change the estimated capacity of both Guidelines #1 and #2.
3. Impacts to Guideline #3 are not reflected in this table.

Maximum Limit Under Guideline #3: Scheduled Debt Retirement

The purpose of Guideline #3 is to preserve additional borrowing capacity for future legislatures by paying off general obligation debt quickly. MMB structures general obligation debt with level principal in each maturity as a means of rapidly repaying the obligations, which has helped the state maintain compliance with Guideline #3. New bond authorizations at the maximum Guideline #1 and #2 amounts shown in the table above would result in a repayment schedule that drops below the 40 percent and 70 percent thresholds under a level principal payment structure. If faced with that situation, MMB would need to seek alternative repayment schedules to stay in compliance with Guideline #3. Those alternative repayment schedules would add additional general fund debt service costs in the near-term to preserve long-term capacity.

The table below shows the maximum amount of general obligation debt that can be authorized in the next 6 years while allowing the state to remain in compliance with Guideline #3. These amounts would also allow the state to continue the practice of using level principal payments consistent with the current forecast. The maximum amounts shown are in addition to the existing $3,768,026,480 billion in authorized but unissued general obligation debt the state is already authorized to sell. The percentages below have been calculated based on assumed bond sale sizes over the coming years.

Maximum Debt Capacity:
Scheduled Debt Retirement (Guideline #3)

	Bonding Bills Assumed in the Feb. 2024 Forecast (*millions*)	Maximum New Debt Within Guideline #3 (*millions*)	% Retired in 5 Years as of 6/30 (Maximum Scenario)	% Retired in 10 Years as of 6/30 (Maximum Scenario)
FY 2024	$980	$980	43.4%	75.6%
FY 2025	$165	$170	40.6%	71.0%
FY 2026	$1,010	$1,180	40.2%	70.0%
FY 2027	$165	$260	40.2%	70.0%
FY 2028	$1,010	$1,390	40.2%	70.1%
FY 2029	$165	$270	40.0%	70.1%

Notes about the table above:

The following factors might change the anticipated schedule of debt retirements over time:

1. Changes to the cash flow needs of authorized projects, resulting in either acceleration or delay of assumed future bond sales.
2. Changed market conditions, such as higher interest rates resulting in lower premiums and higher par amount of bonds sold.
3. Refinancing opportunities that reduce total outstanding debt.

Summary of Outstanding Principal as of 02/29/2024
February 2024 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	$ 3,933,345,000	$ 2,211,409,586	$ 6,144,754,586
Trunk Highway Fund General Obligation Debt	2,317,635,000	1,556,616,894	3,874,251,894
Other Real Estate Capital Leases:			
Ag/Health Buildings	6,205,000	0	6,205000
DHS Building	6,975,000	0	6,975,000
MHFA Supportive Housing 2008	15,910,000	0	15,910,000
MHFA Housing Infrastructure 2012	18,835,000	0	18,835,000
MHFA Housing Infrastructure 2014	66,405,000	0	66,405,000
MHFA Housing Infrastructure 2015	9,390,000	0	9,390,000
MHFA Housing Infrastructure 2017	28,610,000	0	28,610,000
MHFA Housing Infrastructure 2018	71,960,000	0	71,960,000
MHFA Housing Infrastructure 2019	56,470,000	0	56,470,000
MHFA Housing Infrastructure 2020	95,705,000	0	95,705,000
MHFA Housing Infrastructure 2021	85,495,000	12,960,000	98,455,000
U of M TCF Bank Stadium	46,685,000	0	46,685,000
U of M Biosciences Facilities	110,720,000	0	110,720,000
State General Fund Appropriation Refunding Bonds	300,185,000	0	300,185,000
Certificates of Participation - Legislative Office Facility	62,745,000	0	62,745,000
Certificates of Participation - State Office Building	454,175,000	0	454,175,000
Lewis and Clark Regional Water System Bonds	13,575,000	0	13,575,000
Duluth Regional Exchange Appropriation Bonds	95,875,000	0	95,875,000
Public Television Equipment Appropriation Bonds	11,565,000	0	11,565,000
Electric Vehicle Infrastructure Appropriation Bonds	1,545,000	0	1,545,000
Response to Releases Appropriation Bonds	27,395,000	0	27,395,000
TOTAL - Tax-Supported Debt	$ 7,837,405,000	$ 3,780,986,480	$ 11,618,391,480

Other Obligations (Guideline #2)	
Tax-Supported Debt (issued and authorized but unissued)	$ 11,618,391,480
MHFA Moral Obligation Debt[1]	3,565,115,000
MOHE Moral Obligation Debt	311,010,000
Equipment Leases	58,253,976
Guaranteed Energy Savings Program (GESP) Equipment Leases	25,462,972
TOTAL - All Obligations	$ 15,578,233,428

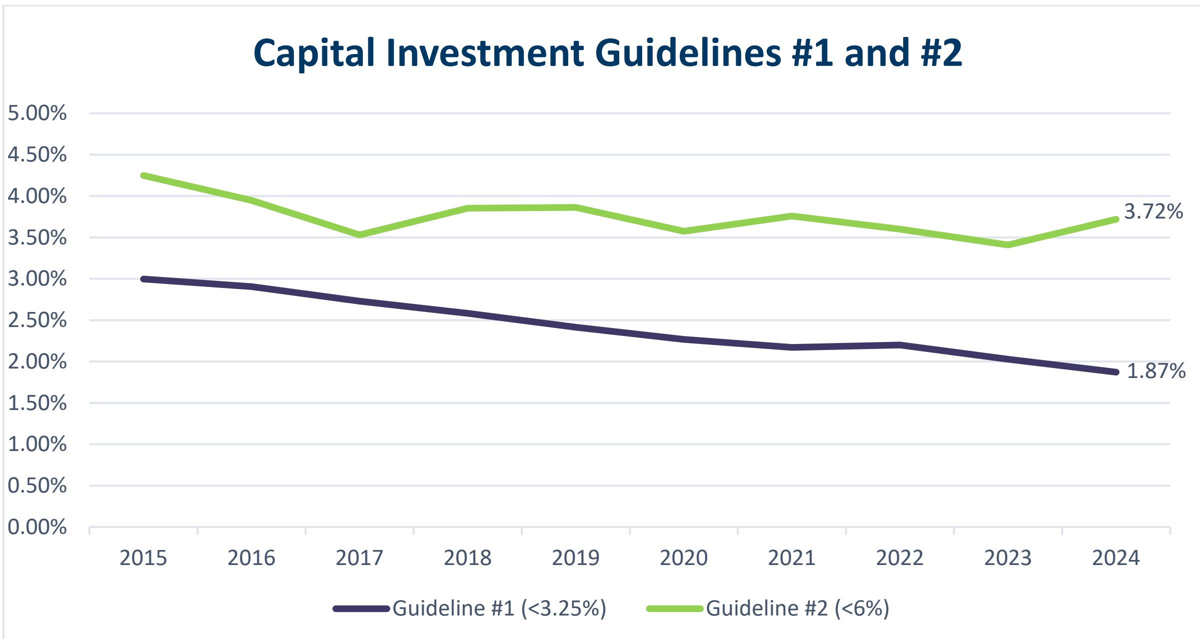
FY 2024 State Personal Income Estimate – SPGMI Forecast:	$ 418,722,000,000
State Tax-Supported Debt as a Percent of Personal Income:	1.87%
Estimated maximum additional principal capacity for all tax-supported debt @ 3.25%	$ 5,771,060,000
All Obligations as a Percent of Personal Income:	3.72%
Estimated maximum additional principal capacity for all obligations @ 6.0%	$ 9,545,086,572

[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.

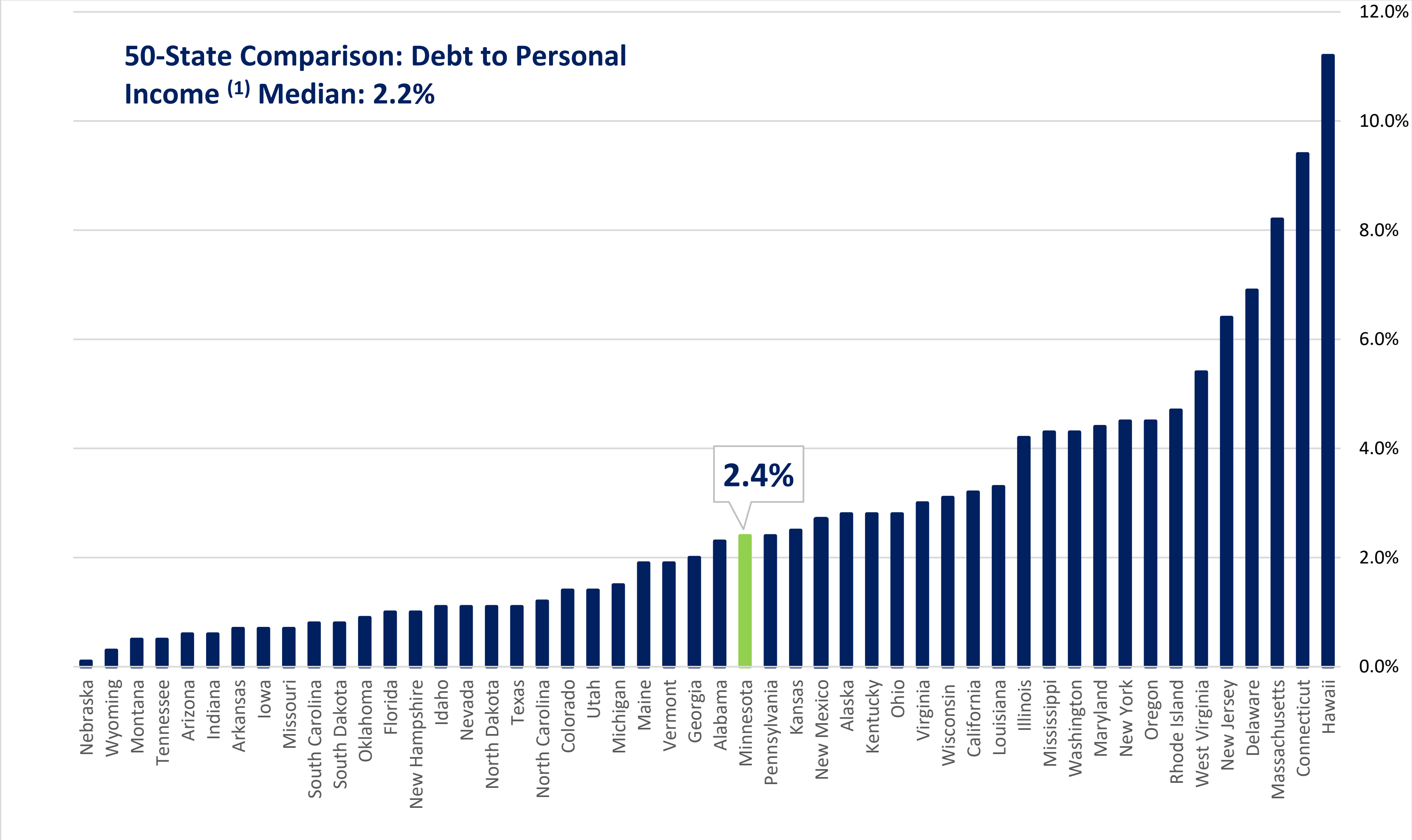
Historic and Comparative Debt Metrics

This Exhibit provides additional information regarding the State's debt capacity. It includes a graph showing historic compliance with Guideline #1 and Guideline #2 under the State's Capital Investment Guidelines, as well as graphs showing direct comparisons to the debt of other states.

The following graph shows the amount of outstanding debt owed compared to state personal income (Guideline #1) and the total amount of authorized debt compared to state personal income (Guideline #2) for each of the last 10 fiscal years.



The following two graphs show how all 50 states compare on two commonly used debt capacity ratios – Debt to Personal Income and Debt Service to Revenues – highlighting how Minnesota ranks relative to the other states.



Source: Moody's State Debt Medians 2023, September 26, 2023.

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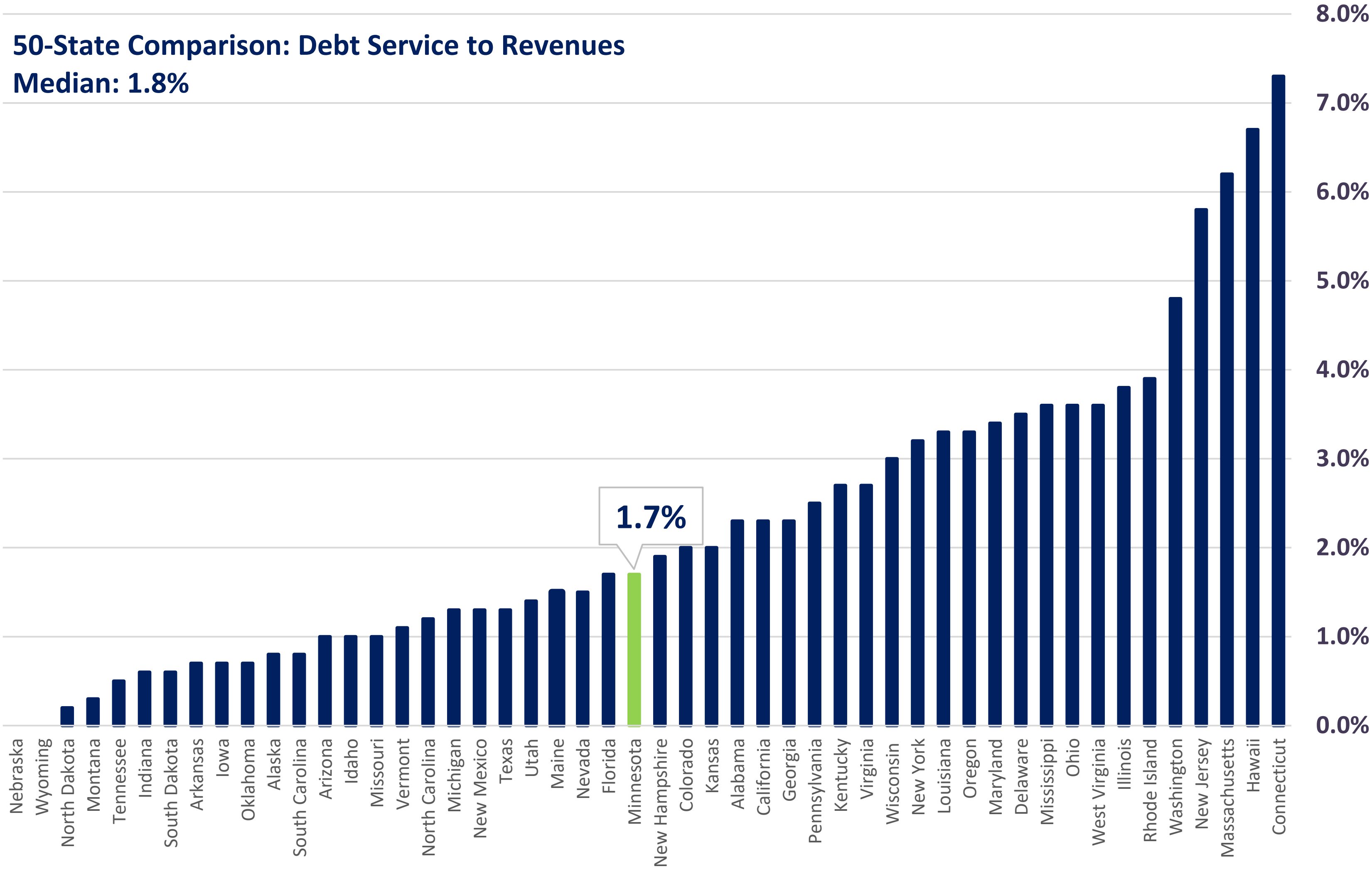
(1) Moody's compared 2021 personal income to 2022 net tax supported debt, while MMB's calculations throughout this report use current personal income estimates from SPGMI and current outstanding net tax supported debt. These factors account for the difference in the ratio reported by Moody's in this chart from MMB's Guideline #1 calculation.



Source: Moody's State Debt Medians 2023, September 26, 2023.