Fitch Affirms Indianapolis Local PIB Bond Bank, IN GOs at 'AAA'; Outlook Stable

Fitch Ratings - New York - 28 January 2020:

Fitch Ratings has affirmed the following ratings of the Indianapolis Local Public Improvement Bond Bank, Indiana bonds:

--$111 million ad valorem special benefits tax bonds at 'AAA';

--$32 million unlimited tax general obligation (ULTGO) bonds at 'AAA';

--$300 million downtown tax increment financing (TIF) revenue bonds, series 2014A, 2014B, 2013F, 2009B, and 1999E at 'AA';

--$8 million Fall Creek TIF bonds, 2014C at 'AA-'.

Fitch also affirms the City of Indianapolis Issuer Default Rating (IDR) at 'AAA'.

The Rating Outlook is Stable.

SECURITY

The Indianapolis Local Public Improvement Bond Bank (the bond bank) ULTGO bonds are limited obligations of the bond bank, which under Indiana law is empowered to buy and sell securities of qualified entities including the City of Indianapolis (the city), Marion County, all special taxing districts in the city, and all entities with tax levies reviewed by the city-county council of Indianapolis and Marion County (the city-county council). The bond bank itself has no taxing power.

The ad valorem property tax bonds are payable from a special ad valorem tax levied by the city-county council on all taxable property in four special taxing districts (the districts) that are coterminous with the city of Indianapolis.

The TIF revenue bonds are limited obligations of the bond bank. The bonds are payable solely from the tax increment revenues and funds pledged under the indenture. The bonds are additionally supported by a standard cash funded debt service reserve fund (DSRF), which the city has pledged its moral obligation to replenish; this moral obligation serves as the basis for the ratings.

ANALYTICAL CONCLUSION

The city's 'AAA' IDR and the bond bank's 'AAA' ULTGO and ad valorem tax bond ratings reflect the city's substantial independent revenue-raising ability, solid expenditure flexibility, low long-term liability burden, and very strong financial resilience.

The TIF revenue bond ratings consider the strength of the city's commitment and strong mechanism for timely payment of debt service through the moral obligation pledge. Fitch considers various factors to determine the number of notches the ratings will be below the city's IDR. The 'AA' rating on the series 2014A, 2014B and 2013F bonds (downtown TIF) reflects Fitch's view that the downtown TIF bonds provide the strongest moral obligation pledge, resulting in a two-notch distinction from the city's IDR. The downtown projects are essential to the city and serves the broad economic interest related to essential governmental operations. The 'AA-' rating on the series 2014C bonds (Fall Creek TIF) is based on a three-notch distinction from the IDR due to the limited size and purpose of the Fall Creek TIF district, which benefits a narrow area within the city's tax base.

According to the ordinance governing the city's moral obligation, if revenues are projected to produce a shortfall in debt service requirements and cause a draw on the reserve fund, the chairman of the bond bank will certify the deficiency to the city-county council within 90 days of such projection, or prior to Dec. 1 of the fiscal year when the deficit is expected to occur, whichever is earlier, and well in advance of the Feb. 1 debt service payment. The bond bank covenants that it will take all actions required or permitted to certify any deficiency to the city-county council within 90 days, regardless of whether the deficiency was anticipated in the annual budget. The council could then choose to appropriate the funds necessary to replenish any deficiencies in the bonds' DSRF.

Economic Resource Base

Indianapolis is the largest city in the state of Indiana, with a diverse economy bolstered by its role as the state capital. The estimated 2018 population of 867,125 reflects a 5.7% increase since the 2010 census. The city is home to numerous industries including pharmaceuticals, health services, logistics, manufacturing and other professional services. Major taxpayers include Eli Lilly and Company, Citizens Energy Group, Federal Express, and Indianapolis Power and Light Company. The largest employers, Health Services Indiana University Health, St. Vincent Hospital, and Eli Lilly Company employ approximately 23,187, 17,398, and 10,005, respectively.

KEY RATING DRIVERS

Revenue Framework:: 'aaa'

Revenue growth is expected to remain above the rate of inflation, as it has historically, based on ongoing expansion in the local economy. The city has significant ability to increase local option income taxes to ensure ongoing fiscal stability.

Expenditure Framework:: 'aa'

Fitch believes that the city's natural rate of expenditure growth will be above revenue growth. The city has solid capacity to cut spending if necessary, due to moderate carrying costs for debt service and pension obligations and a labor environment that provides flexibility to management.

Long-Term Liability Burden:: 'aaa'

The city's long-term liability burden including net pension liabilities and overall debt is low relative to personal income.

Operating Performance:: 'aaa'

The city has exceptionally strong gap-closing capacity and solid general fund reserves to manage through a moderate economic downturn. Fitch expects the city to maintain financial resilience through downturns.

RATING SENSITIVITIES

Strong Operating Performance: The 'AAA' rating is sensitive to the city's strong willingness to maintain financial flexibility. While not anticipated, sharp declines in reserves could potentially pressure the current rating.

City Moral Obligation Commitment: The ratings on the downtown and Fall Creek TIF districts bonds are sensitive to changes in the city's IDR, to which the moral obligation pledge is linked. While no city support is pledged on behalf of bondholders, moral obligation support from the highly-rated city is critical to the TIF revenue bond ratings.

Funding of DSRF: The moral obligation credit enhancement for both series of bonds assumes that the DSRF will continue to be cash funded. Replacement by a surety policy could negatively affect the rating if, in Fitch's assessment, the mechanism for timely payment of debt service through the moral obligation is no longer considered adequate.

CREDIT PROFILE

The city's taxable assessed valuation has steadily improved over the past several years, after limited growth from 2008 through 2014. There has been ongoing improvement in taxable assessed values (TAV) due in large part to residential and commercial development. The average annual growth in TAV since 2012 has been 2.5% and 2020 indicates an estimated 5.0% increase over 2019. The city reports ongoing mixed use developments in the downtown area, which is expected to benefit from redevelopment projects that will convert the former Coca Cola bottling plant and the historic AT&T Building to mixed use developments.

The city's unemployment rate has been trending below the U.S. rate since 2015, and job growth is likely to continue given the expansion of the technology sector within the local economy. In 2018, Infosys Tech Hub (an IT company) announced plans for a $245 million dollar expansion at the site of the former Indianapolis International Airport, which is anticipated to create 3,000 new jobs in the next three years. Other technology developments include 16 Tech, an applied research institute to spur entrepreneurship and EHealth which is expected to result in 500 new jobs by 2023. Additionally, Fed Ex is in the midst of a $1.5 billion expansion to the Indianapolis International airport that will add 20 new commercial gates by 2023.

Revenue Framework

The majority of the city's general fund revenues are derived from local sources including property and income taxes, which combined accounted for approximately 61% of total general fund revenue in 2018. Intergovernmental revenue accounted for approximately 19% of general fund revenues, followed by charges for services at almost 12%.

Fitch believes that natural revenue growth will continue to perform above the rate of inflation, as it has historically. The city has seen growth in the property tax levy resulting from increases in TAVs in recent years after limited growth in TAV due to recessionary pressures, coupled with the implementation of a state tax cap. The 'circuit breaker' tax cap limits property tax rates to a percentage of gross assessed value depending on the property classification. The rates for homestead properties are capped at 1%, the rates for residential properties that are not homesteads, agricultural property or nursing homes are capped at 2% and commercial, industrial, and personal property rates are capped at 3%. All residential properties account for 44% of 2017 total TAV and commercial, industrial and personal properties account for 54% of TAV.

Ongoing income tax revenue growth reflects economic growth attributable to the uptick in employment and personal income. Estimated growth for 2019 reflects a 6% increase and Fitch anticipates natural tax revenue growth to continue to exceed the rate of inflation based on the trend of steady population growth and ongoing economic development. The 2020 budget assumes 5% growth in income tax collections.

Fitch considers the city to have a significant ability to independently increase revenue. The city-county council has the option to increase local option income tax rates to a maximum rate of 2.75% from the current 2.02%. Local option income tax increases can be imposed by County Income Tax Council (CITC), on which the city-county council has over 90% of the voting representation.

Expenditure Framework

The largest portion of the city' general fund expenditures are dedicated to public safety, including criminal justice, police and fire service. The remaining expenditures are for public works, culture and recreation and capex.

Fitch expects the natural pace of expenditure growth to exceed revenue growth absent policy action. The city's growth in expenditures is largely driven by employee salary and benefit costs, which account for approximately 60% of general fund expenditures. The average increase in employee salaries and benefits has grown at a pace above inflation, which Fitch expects to continue.

Flexibility of main expenditure items is solid given the city's ability to control expenditure growth under the current labor environment. Management continues to curtail spending pressures by managing the size of the workforce, mainly through employee attrition and by carefully managing service contracts. Union agreements are not subject to binding arbitration and management has strong control over staffing levels. By state statute, the City Controller has the flexibility to reduce an agency budget if revenues are less than budgeted expenditures; the controller rarely needs to use this power.

Carrying costs for debt service, annual pension costs, excluding state reimbursements for pre-1977 pension plans and other post-employment benefits (OPEB) contributions accounted for 16% of governmental expenditures in 2018. Since 2009, the state has reimbursed the city for the annual pension payments for the pre-1977 police and fire pension plans. Capital projects funded within the general fund provide additional expenditure flexibility, because the city can delay projects for budgetary relief (as was done during the last recession). In 2018, the city spent $66.4 million or 9% of general fund expenditures on capital projects.

Long-Term Liability Burden

The city's long-term liabilities are low with the combined net pension liability and overall debt at about 7% of personal income. The majority of the long-term liability burden is direct debt. The city's future borrowing plans include $50 million in revenue bonds for road projects, which is the last installment to complete the $120 million capital transportation plan that was phased in through 2022. The transportation bonds are payable from county motor vehicle excise surtaxes and county wheel taxes. Other planned borrowings include $45 million for tax increment revenue bonds for economic development near the Indianapolis International Airport. Fitch expects the long term liability burden to remain relatively low compared to the city's economic resource base given the city's growing economy.

The city participates in four separate pension plans: two pre-1997 Police and Firefighter pension plans, the 1997 Police and Firefighters Statutory plan (Statutory) for employees hired after April 1977 and the Indiana Public Employees Retirement Fund (PERF) which covers all other employees. As of Jan. 1, 2017, the city changed the PERF plan from a defined benefit plan to a defined contribution plan for all new civilian employees, to minimize future growth in the long-term net pension liability over time.

Beginning in 2009, the state began reimbursing the city's annual pension contributions for its pre-1977 plan to help offset the future liability. Despite this reimbursement, the pre-1977 pension plans' net pension liabilities are reported on the city's statement of net assets and included in Fitch's long-term liability burden assessment. The total net assets to accrued actuarial liabilities ratio for all four plans combined was approximately 55% as of June 30, 2018 at an adjusted 6% rate of return.

The net OPEB liability as of Dec. 31, 2018 was $221 million or 0.5% of personal income. The city primarily funds OPEB on a pay-as-you-go basis.

Operating Performance

The city's financial resilience is strong, given ample available general fund reserves, solid ability to independently increase revenues and solid expenditure flexibility. In June 2016, the city passed an ordinance to maintain the unrestricted general fund balance at 17% of general fund expenditures, which Fitch believes is consistent with the current rating level. General fund reserves have historically exceeded the 17% target despite the regular use of reserves for capex. Fitch anticipates that the city would continue to maintain reserve levels above the 'aaa' reserve safety margin in a moderate stress scenario.

The city has strong financial policies and has made consistent efforts to maintain healthy financial operations. For example, management increased local income taxes to offset property tax losses in the city's operating funds following the Great Recession. Additionally, the city actively manages expenditure pressures through a variety of measures that include outsourcing services, renegotiating existing service contracts and eliminating positions through attrition. The unrestricted general fund balance was $188 million in 2018, 26% of general fund expenditures, well above the 17% available fund balance policy target.

Fiscal 2018 ended with a $9 million use of general fund reserves, in part to fund one-time capex. General fund revenues performed better than budgeted assumptions primarily driven by increased income tax collections. The 2019 YE estimates assume that local tax revenue growth will increase by 6% on a budgetary basis due to improved economic conditions. The city's estimated YE results are positive and include plans to increase the fiscal stability fund balance by approximately $1.6 million.

The 2020 budget is balanced without the use of general fund reserves to fund operations. Fitch expects the city's financial operations to remain strong given the city's strong inherent budgetary flexibility, ample available reserves and formalized fund balance policy.

Fall Creek TIF Revenue Bond

The Fall Creek TIF revenue bonds were issued to fund economic development within two separate allocation areas, previously established in the city's Fall Creek/Citizens Consolidated Redevelopment Area (which is located within the redevelopment district). The TIF area is small and mature, with a relatively weak economic profile and limited governmental purpose. The Fall Creek bond indenture requires a cash-funded DSRF funded at the maximum annual debt service (MADS).

Downtown TIF Revenue Bonds

The downtown TIF revenue bonds were issued to finance the costs of the Massachusetts Avenue Project, the Market Square Arena Project and the Pulliam/Millikan Project, and to fund a DSRF. The downtown TIF bonds were issued as subordinate debt; however, there are no senior bonds outstanding and the district has covenanted not to issue additional senior bonds. The bond bank maintains reserves in excess of the level required by the indenture, which requires a cash-funded debt service reserve funded at MADS.

The downtown TIF district area includes residential and office buildings, hotels, and retail, wholesale and manufacturing interests. The area is highly concentrated; the top 10 taxpayers account for approximately 50% of TAV, including personal property and real property. The district benefits from ongoing economic development, including development of affordable housing units for senior citizens.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

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Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR
Indianapolis (IN) [General Government]	LT IDR AAA Affirmed		AAA
Indianapolis (IN) /Limited Ad Valorem Tax Revenues/1 LT	LT AAA Affirmed		AAA
Indianapolis (IN) /Moral Obligation - Downtown Tax Increment Revenues/1 LT	LT AA Affirmed		AA
Indianapolis (IN) /Moral Obligation - Fall Creek Tax Increment Revenues/1 LT	LT AA- Affirmed		AA-

Additional information is available on www.fitchratings.com

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (pub. 10 Jan 2020)

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Endorsement Policy

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