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ISSUER IN-DEPTH
31 AUGUST 2015

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RATINGS

Indianapolis (City of) IN

General Obligation	Aaa Negative

KEY METRICS:

KEY INDICATORS

	2012	2013	2014
Assessed Value ($ Billions)	$39.1	$39.2	$41.6
Net Direct Debt as a % of Assessed Value	3.3%	2.9%	2.7%
Available Fund Balance as % of Revenue	55.3%	43.1%	33.9%

	2011	2012	2013
Adjusted Net Pension Liability ($ Millions)	$296.4	$567.3	$423
Adjusted Net Pension Liability/ Operating Revenues	0.30x	0.84x	0.60x
Adjusted Net Pension Liability as a % Assessed Value	0.75%	1.45%	1.08%

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Indianapolis, IN

Job Growth Bolsters Economy as Operating and Capital Costs Weigh on Credit Profile

Indianapolis, IN's (Aaa negative) strong credit profile is supported by a fundamentally healthy economy, as evidenced by job growth that has outpaced other Midwest regional hubs. However, escalating operating costs under a somewhat restrictive revenue-raising environment have weighed on the city's finances. The region's strong economy and a recent influx of cash from the sale of the city's water and sewer utility will buoy credit quality in the short term, but continued operating budget pressures and elevated leverage pose hurdles in the long term.

» **Diverse and growing economy spurred by private-sector activity.** Indianapolis' growing economy has experienced a relatively rapid pace of private-sector job creation. The city is benefiting from a swelling e-commerce industry, while its established transportation network supports the expansion of the regional pharmaceutical sector. The two-year job growth rate of 5.4% exceeds many peer Midwest regional hubs.

» **Economic stability provided by government, higher education and health care institutions.** As the state capital and home to large medical facilities, the city benefits from substantial economic anchors. At 4.5%, the Indianapolis area's unemployment rate is below the national average, albeit slightly, and nearly down to pre-recession levels.

» **Operating and capital budgetary pressures persist, temporarily offset by sale of water and sewer utilities.** Indianapolis received $260 million for the 2011 sale of its water and sewer utilities to Citizens Energy Group (A2 stable). The influx of cash immediately increased the city's General Fund balance by 16% of General Fund revenues to $372 million. Since then, operating costs and planned capital projects have sharply reduced reserves. For fiscal 2015, city officials project a 12% decline in the General Fund balance (as a percentage of General Fund revenues) to $171 million, which would be a drop for a fourth straight year.

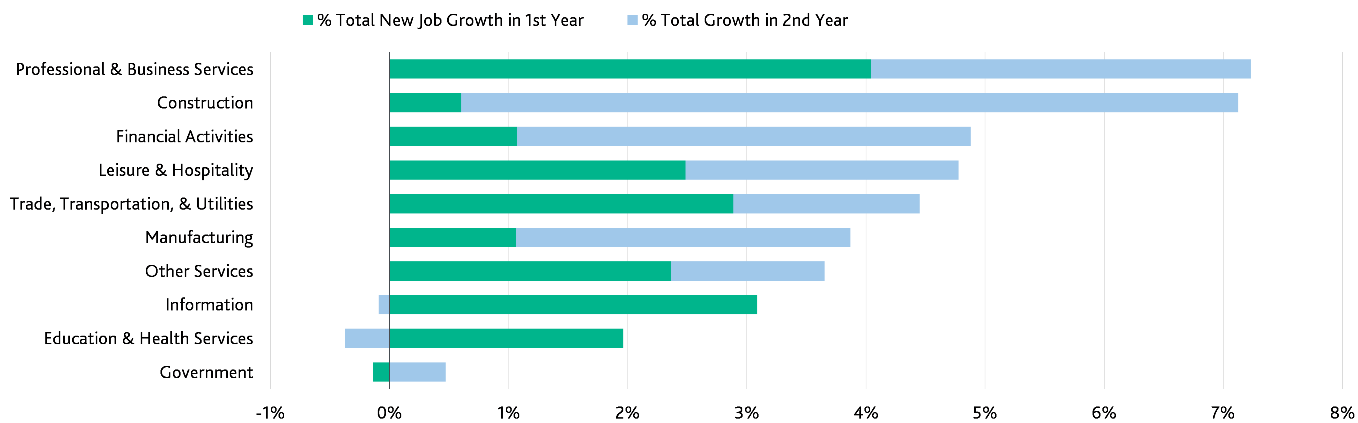
» **Indianapolis' exposure to pension liabilities is moderate, though debt levels remain elevated.** State action to reimburse cities and towns to cover costs for pre-1977 pensions plans has reduced Indianapolis' pension liability. The city also consistently funds its total pension obligations at or near annual required contribution (ARC) levels. Pension liabilities will remain moderate. Direct debt, however, is a high 2.7% of full value.

Private sector spurs job growth

Despite budget challenges, Indianapolis' rating is high and expected to remain so due largely to its vibrant economy. Historically known for its heavy industrial and manufacturing sector and its status as the state capital of Indiana (Aaa stable), Indianapolis' economy has diversified in recent decades. Alongside redevelopment and a growing population, private-sector activity has served as the impetus behind recent job growth. In the 2015 second quarter, the professional and business services sector showed rapid hiring in computer systems, scientific and other technical services. For instance, Emarsys, an Austrian digital marketing technology company, announced plans to locate its North American headquarters in downtown Indianapolis, with projections of 167 new jobs to be created by 2020. In the past two years alone, Indianapolis' private-sector employment growth outpaced gains in government, higher education, health care, and other traditional mainstays of the regional economy (see Exhibit 1).

Exhibit 1

Private Sector Growth Outpaces Indianapolis Region's Traditional Sectors



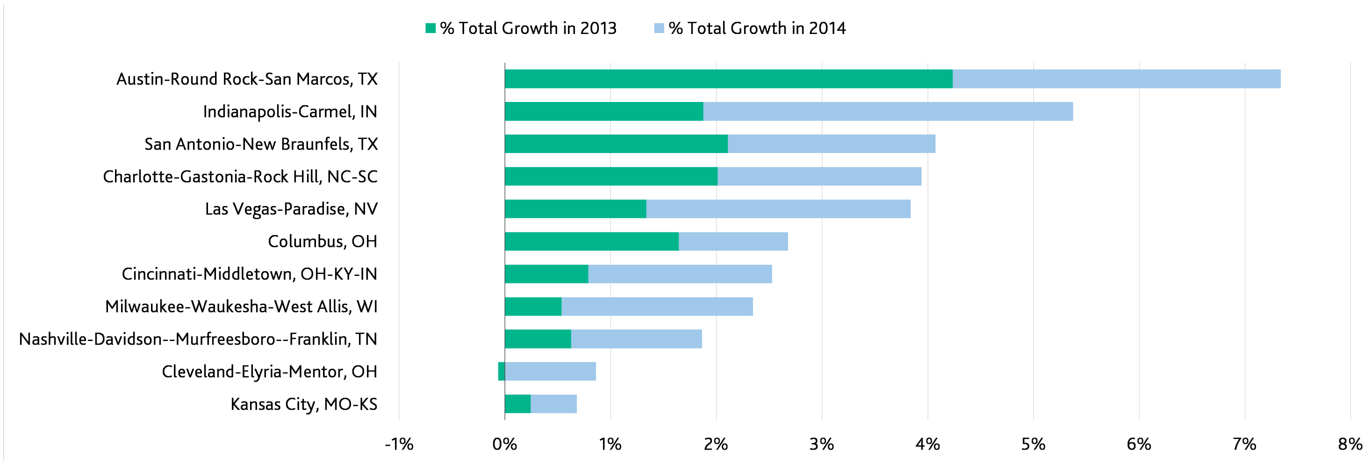
Source: US Department of Labor, Bureau of Labor Statistics

The increase in professional and business services employment reflects the city's role as home to prominent operations for several large expanding companies. Lowe's (A3 stable), the home improvement retailer, completed the construction of a customer support center in Indianapolis, with plans to create up to 1,000 new jobs by 2016. Additionally, Amazon (Baa1 negative), the online retailer, recently announced plans to hire 1,400 new employees at its existing fulfillment centers in Indianapolis, Plainfield, IN (unrated) and Whitestown, IN (unrated) by 2017. Eli Lilly (A2 stable), one of the top employers in the metropolitan statistical area (MSA) with approximately 10,500 employees, is expanding its regional footprint, recently entering into a joint venture with Indiana University School of Medicine (Indiana University, Aaa stable) to research and create a cheaper and more efficient model for drug development.

Logistics, transportation, distribution and related businesses are other bright spots in the economy. Indianapolis has one of the world's busiest airports in terms of cargo traffic and is home to the second-largest Federal Express (Baa1 negative) hub, which specializes in cold-chain transport with temperature-controlled air freight service. Pharmaceutical and life science companies depend on airline transport to satisfy time constraints on the delivery of temperature-controlled drug products. Between 2008 and 2014, the State of Indiana's exports of pharmaceuticals and medicine has more than doubled in nominal value.

New job growth in Indianapolis has outpaced Midwestern and national peers, as evidenced by the relatively rapid rate of growth over fiscal years 2013 and 2014 in the city's MSA (see Exhibit 2). Indianapolis' two-year job growth totaled 5.4%, falling below Austin, TX (Aaa stable) but surpassing other similarly sized MSAs over the same time period.

Exhibit 2
Indianapolis Region's Job Growth Ranks High Among Other Peer Regions



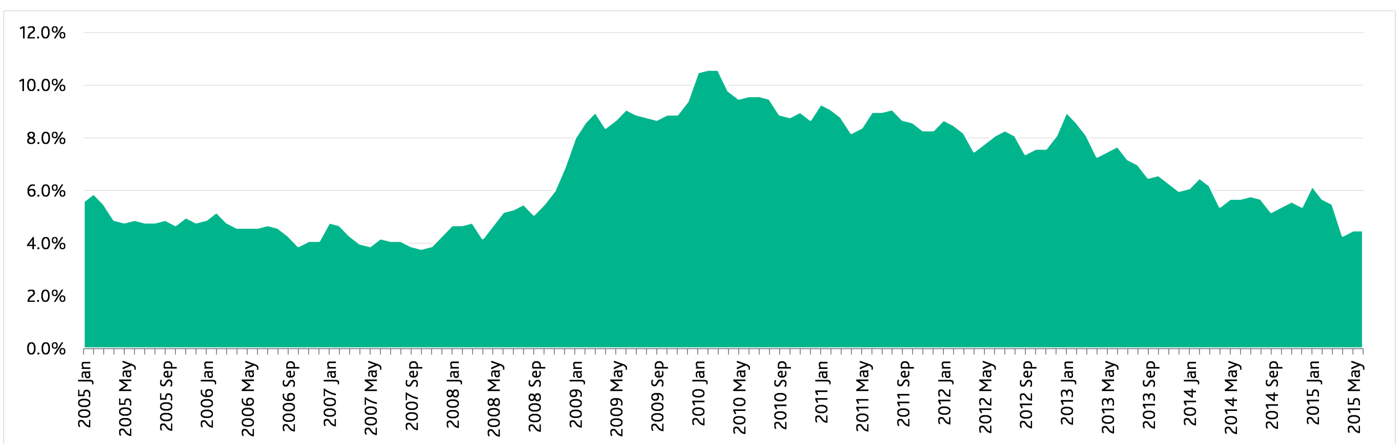
Source: US Department of Labor, Bureau of Labor Statistics

State government, education and health care provide economic stability

Complementing private-sector activity, several long-standing institutions underpin the strength of the Indianapolis economy. As the state capital, government employment at multiple levels represents approximately 13% of the MSA workforce.The regional economy also benefits from the stability of large health care and higher education institutions. The MSA's top two employers are St. Vincent Hospitals & Health Services (unrated) and Indiana University Health (Aa3 stable), which employ approximately 17,000 and 12,000, respectively. *U.S. News & World Report* recently included Indiana University Purdue University Indianapolis' (IUPUI) graduate nursing program in its top-20 ranking and cited IUPUI as one of the top-10 up-and-coming national universities. Indiana University School of Medicine, with more than 2,000 students in 2015, is the second-largest medical school in the US.

Unemployment in the Indianapolis MSA area has declined in recent years to near pre-recession levels (see Exhibit 3). At 4.5% in May, the unemployment rate exceeded the state level of 4.8% but was well below the national level of 5.3%. The median family income is relatively low at 81.4% of the nation.

Exhibit 3
Indianapolis Region Unemployment Rate Drops to Near Pre-Recession Level



Source: US Department of Labor, Bureau of Labor Statistics

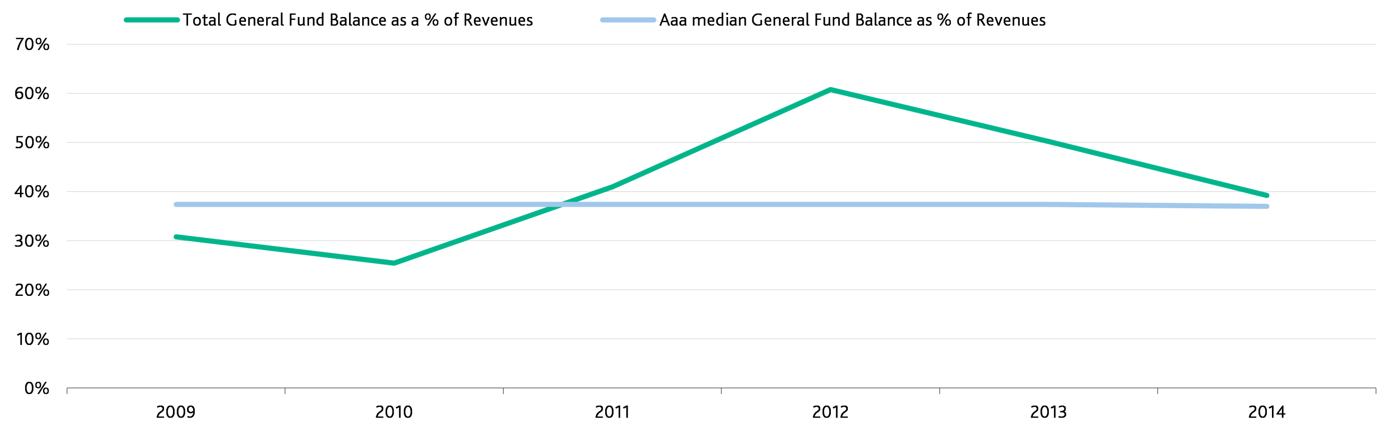
Asset sale gives city cash infusion, though budget pressures continue

The city's liquidity position is healthy, but continued operating and capital budget pressures pose a threat to the credit profile. Indianapolis received an influx of cash from the sale of its water and sewer utilities to Citizens Energy Group. The sale and other transactions, including the privatization of the city's parking meters, generated over $280 million in fiscal years 2010 and 2011 to bolster General Fund reserves (see Exhibit 4). The proceeds from the utility sale were used to establish the Rebuild Indy Fund for planned capital projects and the Fiscal Stability Fund to bolster reserves. Both funds are accounted for in the General Fund in the city's audited financial statements.

Although the city's sound reserve levels are rooted in a non-recurring revenue source, the city's financial position became markedly stronger following the asset sale. In fiscal years 2012 and 2013, Indianapolis' General Fund reserves as a percentage of revenue exceeded the median for Aaa-rated US local government cities. However, in fiscal 2014, General Fund reserves continued to decline and fell near the median for Aaa-rated US local government cities.

Exhibit 4

After Cash Infusion from Utility Sale in 2011, General Fund Reserves Have Declined Steadily



Source: City of Indianapolis' Audited Financial Statements

Audited fiscal 2014 results indicate a General Fund balance decline of approximately $56 million. Approximately $21 million is attributable to operating expenditures related to higher-than-anticipated snow removal costs and road repairs. The remaining $35 million is related to cash financing of capital projects from Rebuild Indy reserves. The fund balance declined despite an estimated increase in property tax and income tax revenue. Still, the resulting General Fund balance of $225 million equals 39% of General Fund revenue, a level that approximates Aaa medians.

In fiscal 2015, city officials expect the total General Fund balance to further decline by approximately $26 million on a budgetary basis, which includes using the remaining Rebuild Indy reserves for various infrastructure projects. Although continued growth in property tax and income tax revenue is anticipated for fiscal 2015, city officials project that expenses will exceed revenue in fiscal 2015. If these projections are realized, it will mark four consecutive years in which the General Fund balance declined. The continued decline in reserves reflects management's decision to use reserves to supplement revenue streams to fund ongoing operations and capital improvements. City officials plan to maintain a minimum of $80 million in the General Fund balance for the foreseeable future. Depletion of cash reserves beyond current projections would further pressure the city's credit quality.

State circuit breaker legislation constrains the city's ability to raise revenue in excess of property tax caps. The city estimated the revenue loss due to circuit breaker legislation was $27 million in fiscal 2015, down from $34 million in fiscal 2014. The decline in 2015 was the result of the city's effort to prevent property owners from declaring multiple homestead deductions. State law allows for one homestead deduction per property owner, capped at 1% of gross assessed valuation, even if the property owner has several single-family properties.

In addition to a reduced circuit breaker loss for 2015, the city's efforts led to an increase in assessed value by approximately $2 billion and one-time property tax revenue increase of $18 million. While the circuit breaker will continue to limit the city's ability to increase property tax revenue, officials cite efforts to address exemption errors as a way to curb some losses going forward.

Moderate pension exposure, debt levels remain elevated

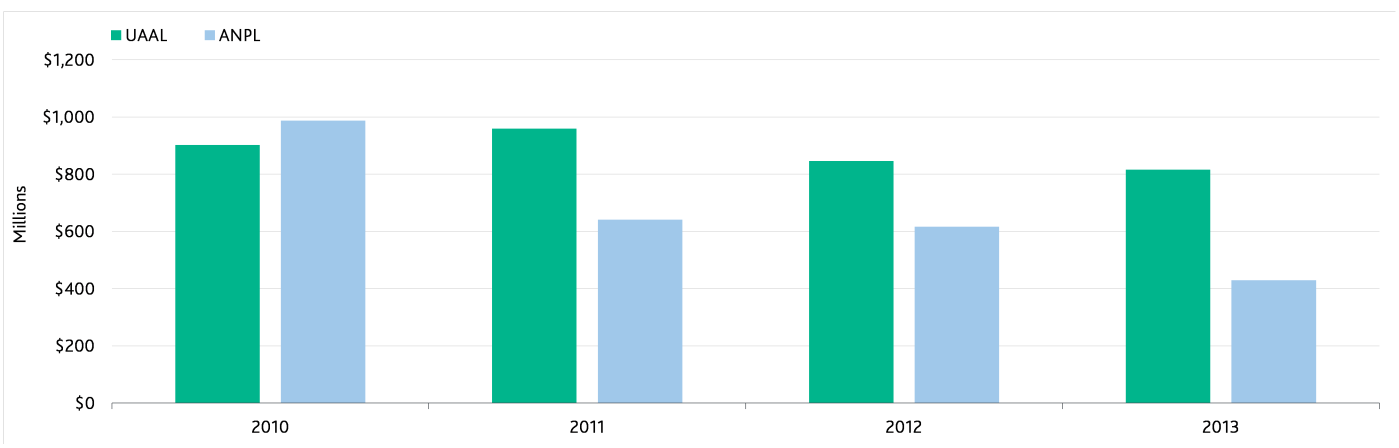
Indianapolis' debt burden poses a continued credit challenge, though pension exposure will likely remain moderate. The city's debt profile will remain elevated but manageable over the near term. As of June 2015, Indianapolis' direct debt burden was 2.7% of full value. A large majority (over 60%) of the debt is secured by the city's moral obligation (MO) pledge and paid for with alternate revenues, including tax increment district revenues. The city's overlapping debt burden is slightly above average at 3.8% of full value. Principal amortization is slow with 57.4% of debt to be repaid in 10 years. Favorably, 90.3% of debt is expected to be repaid in 20 years. While elevated, debt levels are unlikely to rise significantly given the city's use of Rebuild Indy funds to cash finance most of the city's long-range capital needs.

Indianapolis' exposure to multiple pension plans is likely to remain moderate. The city participates in four separate plans: The Statutory Plan, two Pre-1977 Plans, and the All Other City Employees' Plan. As reported in fiscal year 2014, the combined ARC for the four plans was an estimated $102 million, or 14% of 2014 operating revenues (which includes the General Fund and Debt Service Fund). The city's pension contributions are consistently funded at or near the ARC, a cost that has risen moderately in recent years. The combined percentage of ARC currently funded is approximately 93% for all four funds.

Beginning in 2009, the state agreed to pay the entire annual cost of future pension payments to the pre-1977 police and firefighters plans. The cost shift is reflected in a low three-year average adjusted net pension liability (ANPL) and combined reported unfunded actuarial accrued liability (UAAL) (see Exhibit 5).

The Moody's ANPL of $423 million was 0.6 times the city's operating fund revenue and equal to 1.08% of the full value in fiscal 2014. This represents a significant reduction from the $987 million ANPL in fiscal 2009, reflecting the lowered pension burden due to the state paying the entire annual cost of pension benefits for the pre-1977 police and firefighters plans. The city's pension liability figures include reimbursements made by the state, but exclude pay-as-you-go financing for retirement health care (Other Post-Employment Benefits or OPEB) liabilities.

Exhibit 5
Indianapolis' UAAL and ANPL Are Declining



Source: City of Indianapolis' audited financial statements

The city's other OPEB annual pay-go equaled 0.43% of General Fund revenues in fiscal 2014. The city's combined pension and OPEB burden is average compared to peers. Given management's commitment to continually address pension obligations, the city's pension obligations should not materially affect the city's credit quality.

Moody's Related Research

New Issuer Report:

» Moody's affirms Aaa on Indianapolis, IN's; outlook revised to negative, June 2015 (902616604)

Rating Update Report:

» Moody's affirms A2 Rating on Indianapolis Citizens Energy Group Gas Distribution Revenue Bonds; Outlook Stable, April 2015 (902427354)

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