Fitch Affirms Indianapolis Local Public Improvement Bond Bank, IN Bonds at 'AAA'; Outlook Stable

Fitch Ratings-Chicago-29 January 2015: Fitch Ratings affirms the 'AAA' rating on the following Indianapolis Local Public Improvement Bond Bank, Indiana (the bond bank) bonds:

--$61.3 million series 2013B taxable refunding bonds;
--$12 million series 2013C multipurpose refunding bonds;
--$55.1 million series 2008A ad valorem bonds;
--$55 million series 2007D multipurpose refunding bonds.

The Rating Outlook is Stable.

SECURITY

The bonds are limited obligations of the bond bank, which under Indiana law is empowered to buy and sell securities of qualified entities such as the city, all special taxing districts in the city, and all entities with tax levies reviewed by the city council. The bond bank has no taxing power.

The series 2013B are supported by the general obligation and unlimited ad valorem property tax pledge of the city of Indianapolis.

The series 2013C and series 2007D bonds are supported by the requirement of the city, acting through its Board of Public Works, Board of Parks and Recreation, and Board of Transportation, to levy a special ad valorem property tax on the property of the respective districts (which are coterminous with the city) to pay principal and interest on the respective obligations of the bond bank.

The series 2008A bonds are supported by the requirement of the city to levy an ad valorem tax, if needed, on all property in the Indianapolis Redevelopment District, which is coterminous with the city, to pay debt service to the extent not paid from revenues of the Metropolitan Development Commission. The bonds are additionally supported by a cash funded debt service reserve fund and the city's moral obligation pledge to replenish any draw on the reserve.

KEY RATING DRIVERS

MAJOR ECONOMIC HUB: The city anchors a deep and diverse employment base that should serve to promote long-term stability and continued commercial development. Employment metrics are strong and income levels are comparable to state averages and slightly below those of the U.S.

STRONG FINANCIAL FUNDAMENTALS: The city's strong management team has prudently overseen the reduction in tax revenues as a result of state wide circuit breaker legislation and despite planned drawdowns, has maintained healthy reserve levels.

MANAGEABLE LONG-TERM LIABILITIES: Debt ratios are moderate and should remain stable given no significant borrowing plans and average amortization. Carrying costs are high at almost 25% of general fund spending. Well-funded pension plans and the state's subsidization of a portion of pension liabilities help balance the debt profile.

RATING SENSITIVITIES

MAINTENANCE OF SOUND OPERATIONS: The rating is sensitive to shifts in fundamental credit qualities including sound financial operations. The Stable Outlook reflects Fitch's expectation that such shifts are unlikely.

CREDIT PROFILE

In 1970, the governments of the city of Indianapolis and Marion County were combined to form the state's only consolidated government. By the consolidating act, the boundaries of the city were extended to the county line, although the small municipalities of Beech Grove, Lawrence, Speedway and Southport were excluded.

Indianapolis serves as the capital and economic center of the state. The city's population has grown 2.8% since 2010 and currently totals about 852,866, making it the largest city in the state and 12th largest by population in the nation.

DIVERSE AND GROWING ECONOMY

The city's economy is well diversified and includes pharmaceutical production, health services, life and sciences companies, manufacturing and other business and professional service companies. Major employers include Indiana University Health (20,292 employees), St. Vincent Hospitals and Health Services (11,075), Eli Lilly and Company (10,500) and Wal-Mart (9,000).

Employment and labor force growth have been strong with increases of 3.6% and 2.6% respectively from November 2013 to November 2014, higher than both the state and U.S. levels. The November 2014 unemployment rate of 5.9%, while down from the November 2013 rate of 6.9%, remains slightly above the MSA (5.4%), state (5.8%) and nation (5.5%). Per capita income levels in the city are comparable to the state average but below the U.S.

Taxable assessed value (TAV) has been fairly stable over the last few years, totaling $34.4 billion for 2014. An 8.2% increase from 2013 to 2014 was primarily related to an audit that revealed several fraudulent homestead exemptions which were added back to assessed value in 2014. The top 10 taxpayers are diverse and comprise a moderate 7.4% of 2013 TAV. Property tax collections, although generating fewer dollars because of the circuit breaker tax credits, continue to be fairly strong, with total collections averaging over 98% for the past three years.

PRUDENT FINANCIAL MANAGEMENT IN FACE OF REVENUE CHALLENGES

On a combined basis, property and local income taxes total approximately 38% and 21%, respectively of general fund revenues. State circuit breaker tax cap legislation was enacted in 2008. The legislation limits property taxes to a percentage of gross assessed value, depending upon the class of property. As a result of the tax cap, the city's property tax revenue decreased by $22.7 million in 2012 followed by a $29 million decrease in 2013. Since enactment of the legislation, management has responded prudently to lower property tax revenues by implementing spending freezes, budget reductions and increasing some local income tax rates. Given past history, Fitch expects the city to face this on-going revenue challenge through continued strong fiscal management practices.

UTILITY SALE ENHANCES FINANCIAL POSITION

The sale of the city's water utility and wastewater collection and treatment facilities (the utility) to Citizens Energy Group (CEG) in August of 2011 provided the city with the opportunity to fund some capital needs on a pay-go basis. Approximately $216 million from the sale was set aside to 'RebuildIndy'. After spending down a portion of the proceeds in 2012, the city spent down $64 million (from committed general fund balance)in 2013 on infrastructure projects such as rebuilding bridges, repaving roads, upgrading sidewalks and curbs and other projects. Of the $45 million left in the 'RebuildIndy' fund at the end of 2014, $35 million has been contracted out and it is projected that all of the remaining funds will be used in 2015.

Additionally, $80 million of the proceeds of the utility sale were used by the city council to establish a fiscal stability fund. The fund is reported as part of the city's unassigned general fund and has been set aside to support the credit ratings of the city. The ordinance establishing the fund provides that any draw-down requires city council approval and does not provide for requirements for any further additions. Fitch would view unfavorably the city's use of these funds for ongoing spending without a plan for replenishment.

AMPLE RESERVES DESPITE PLANNED GENERAL FUND DRAWDOWNS

For the year-end Dec. 31, 2013 (last available audit), the general fund balance declined to $280.7 million from $348.7 million the prior year. This $68 million decrease is primarily a result of $63.8 million in planned spend down of the 'RebuildIndy' funds. The unrestricted general fund balance remained strong at 44.7% of general fund spending.

Management is still compiling results for 2014; preliminary numbers are not available. Fitch expects the general fund balance to be lower as the city continued to use funds for infrastructure projects during 2014. In addition to the planned spend down, management reports that expenses were higher due to emergency road repairs as a result of the harsh winter. Positively, property tax collections were higher than anticipated.

At the end of December 2014, the fiscal stability fund totaled $65.2 million (10.5% of 2013 GF spending) compared to $80 million (12.9% of 2013 GF spending) at the end of 2013. During 2014, the city used $6.8 million to fund a police class and borrowed $8 million under a short-term loan for needed emergency road repairs due to a harsh winter. The $8 million loan repayment is required to be paid back by June 30, 2015 and is included in the 2015 budget. The $6.8 million is not required to be repaid because it was used for public safety purposes, but the city intends to also repay it. There are no appropriations in the 2015 budget to use fiscal stability funds.

For 2015, the city has budgeted for general fund revenues and expenditures of $516.4 million and $542.7 million, respectively. Revenue projections are conservative - they do not include $16 million expected to be generated from an increase in the public safety income tax rate that went into effect on Jan. 1, 2015. The budget does include a $26 million appropriation of fund balance.

Fitch expects the city will continue to maintain healthy operating margins and ample reserve levels to support the current high rating given management's past commitment to prudent fiscal stewardship. Additionally, Fitch believes the city will continue to exceed its informal goal of maintaining an unassigned balance of over 10% of general fund expenditures. The balance has consistently exceeded the target totaling 13.2%, 14% and 14.7%, in 2011, 2012 and 2013, respectively.

MANAGEABLE DEBT PROFILE

Overall debt ratios are moderate at $1,929 per capita and 4.8% full value but should remain stable as the city does not foresee any significant new debt issuance in the next few years and amortization is slightly above average.

In connection with the utility sale, in return for receiving the capital assets, CEG assumed $1.4 billion in utility debt and also agreed to fund the future principal and interest payments on general obligation (GO) bonds related to the facilities. At Dec. 31, 2013, the outstanding balance of that GO debt was $35.4 million with maturities that extend through Jan. 1, 2018.

The city participates in the State's Public Employees' Retirement Fund (PERF) for its police and fire fighters hired after April 1977 and in another plan administered by PERF for all other city employees. On a combined basis, the plans are well funded at approximately 89% as of June 30, 2013 with the pension system assuming a 7% rate of return. In 2013, city contributions totaled $35.6 million or a modest 4% of 2013 government fund spending. The state's reimbursement of the city's annual pension contributions for its pre-1977 plan, commencing in 2009, helps offset this growing fixed cost and future liability. The city is making pay-as-you-go payments on its other post-employment (OPEB) obligations and paid $1.6 million in 2013. The unfunded liability was $161.3 million, or a modest 0.5% of taxable market value as of Dec. 31, 2013.

Carrying costs inclusive of debt service, pension and OPEB consume a high 24.8% of governmental fund spending.

Contact:

Primary Analyst
Karen Wagner
Director
+1-212-908-0230
Fitch Ratings, Inc.

33 Whitehall Street
New York, NY 10004

Secondary Analyst
Brendan Scher
Analyst
+1-212-908-0686

Committee Chairperson
Amy Laskey
Managing Director
+1-212-908-0568

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, and National Association of Realtors.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria (http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015)
U.S. Local Government Tax-Supported Rating Criteria (http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314)

Additional Disclosure
Solicitation Status (http://www.fitchratings.com/gws/en/disclosure/solicitation?pr_id=978836)