FitchRatings

Public Finance

Tax-Supported / U.S.A.

Milwaukee Public Schools, Wisconsin

New Issue Report

Ratings

Long-Term Issuer Default Rating	A+

New Issue

$31,000,000 Redevelopment Lease Revenue Bonds, Series 2017 (Milwaukee Public Schools)	A

Outstanding Debt

Redevelopment Lease Revenue Bonds, Series 2016A (Milwaukee Public Schools)	A
Redevelopment Lease Revenue Bonds, Series 2016B (Milwaukee Public Schools – Qualified Energy Conservation Bonds – Direct Payment Subsidy)	A
Redevelopment Lease Revenue Bonds, Series 2016C (Milwaukee Public Schools – Qualified Zone Academy Bonds)	A
Federally Taxable Redevelopment Lease Revenue Bonds, Series 2015A (Milwaukee Public Schools – Qualified School Construction Bonds – Direct Payment Subsidy)	A

Rating Outlook

Stable

Analysts

Matthew Wong
+1 212 908-0548
matthew.wong@fitchratings.com

Shannon McCue
+1 212 908-0593
shannon.mccue@fitchratings.com

New Issue Summary

Sale Date: June 6.

Series: Redevelopment Lease Revenue Bonds, Series 2017 (Milwaukee Public Schools).

Purpose: Finance the costs of certain energy savings improvements to certain public schools in the city of Milwaukee.

Security: Limited obligations of the Redevelopment Authority of the City of Milwaukee (the authority), payable from rental payments by Milwaukee Public Schools (MPS, or the district) under a lease between the authority and MPS.

Analytical Conclusion

The 'A+' Issuer Default Rating (IDR) reflects MPS's narrow but stable operating margins and moderate long-term liability profile. Gap-closing ability is adequate, given moderate expected revenue volatility and strong expenditure flexibility. Fitch Ratings believes the city's management of MPS funds and provision of liquidity are a positive credit factor. The 'A' lease obligation rating is one notch below the IDR, reflecting the slightly higher optionality of the lease payment.

Key Rating Drivers

Economic Resource Base: MPS provides pre-K-12 education to approximately 75,000 students. Its taxing jurisdiction is coterminous with the city of Milwaukee (IDR of 'AA'/Stable). The city serves as the economic engine for the surrounding region and has a fairly diverse economic and employment base, but residents exhibit below-average wealth, and a relatively large proportion are below the poverty level. The local economy maintains a reduced but still above-average reliance on manufacturing that in the past has created vulnerabilities to recessionary employment shifts. MPS derives approximately 60% of its revenues from the state of Wisconsin (IDR of 'AA'/Stable). The state's economic growth during much of the current expansion has been slow and uneven, although more recently gains have accelerated.

Revenue Framework: 'bbb' factor assessment. Stagnant growth prospects for revenues are heavily influenced by the state's revenue growth prospects, which Fitch believes will influence future allowed increases in the statutory per pupil revenue limit, and a declining enrollment trend. The district has little independent legal ability to raise revenues.

Expenditure Framework: 'a' factor assessment. MPS has demonstrated a solid ability to control expenditures and operates within a fairly flexible labor environment. Carrying costs are moderate, but Fitch expects the natural pace of expenditure growth to exceed that of revenues, necessitating ongoing expenditure management.

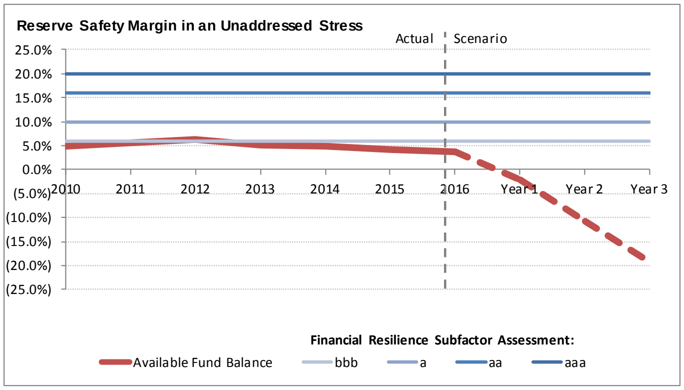
Long-Term Liability Burden: 'aa' factor assessment. The long-term liability burden is moderate relative to the resource base. The district participates in a well-funded pension plan, bolstered by prior issuance of pension obligation bonds.

Operating Performance: 'a' factor assessment. Financial operations are characterized by careful expenditure control in response to strict revenue limits. Reserves, although nominally narrow, should provide an adequate safety margin in a downturn given expected decreased levels of revenue volatility and adequate budgetary flexibility and control.

Milwaukee Public Schools (WI)

Scenario Analysis

v. 2.0 2017/03/24



Analyst Interpretation of Scenario Results:

Unrestricted general fund balance is narrow, averaging about 4%-5% of spending throughout and since the recent recession. Future revenue volatility is likely to be materially lower than historical data suggest. Fitch's FAST model suggests that the district's revenues might be vulnerable to a 4% decline in a moderate economic downturn. The FAST data are heavily influenced by the fiscal 2012 revenue limit cut which was associated with the implementation of Act 10 spending controls. Fitch believes that such a marked decline is unlikely to be repeated but that the district remains vulnerable to revenue limit cuts in an economic downturn. Enrollment declines could also lead to revenue declines, but the formula uses a three year rolling average, affording management ample time to adjust spending. Fitch expects the district will use its solid expenditure flexibility to maintain reserves throughout economic cycles. The reliability and stability of the revenue stream, the strength of budgetary oversight by the city and the moderate level of budgetary flexibility lead Fitch to expect that MPS will continue to maintain reserve levels at or above the level consistent with a 'bbb' financial resilience assessment.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(4.0%)	(1.0%)	1.9%
Inherent Budget Flexibility	Midrange		

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2010	2011	2012	2013	2014	2015	2016	Year 1	Year 2	Year 3
Total Revenues	1,177,403	1,187,336	1,099,163	1,084,584	1,085,178	1,086,304	1,092,362	1,048,701	1,037,846	1,057,856
% Change in Revenues	-	0.8%	(7.4%)	(1.3%)	0.1%	0.1%	0.6%	(4.0%)	(1.0%)	1.9%
Total Expenditures	1,174,032	1,167,599	1,073,451	1,080,750	1,061,655	1,057,952	1,066,659	1,087,992	1,109,752	1,131,947
% Change in Expenditures	-	(0.5%)	(8.1%)	0.7%	(1.8%)	(0.3%)	0.8%	2.0%	2.0%	2.0%
Transfers In and Other Sources	11,504	18	-	64	4	844	205	196	194	198
Transfers Out and Other Uses	19,506	20,169	20,963	21,287	23,695	28,351	25,246	25,751	26,266	26,791
Net Transfers	(8,002)	(20,151)	(20,963)	(21,224)	(23,690)	(27,507)	(25,041)	(25,554)	(26,071)	(26,593)
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	(4,631)	(414)	4,749	(17,390)	(168)	844	662	(64,846)	(97,977)	(100,684)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	(0.4%)	(0.0%)	0.4%	(1.6%)	(0.0%)	0.1%	0.1%	(5.8%)	(8.6%)	(8.7%)
Unrestricted/Unreserved Fund Balance (General Fund)	56,933	65,947	68,854	56,429	52,292	44,524	41,542	(23,304)	(121,280)	(221,964)
Other Available Funds (Analyst Input)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Analyst Input)	56,933	65,947	68,854	56,429	52,292	44,524	41,542	(23,304)	(121,280)	(221,964)
Combined Available Fund Bal. (% of Expend. and Transfers Out)	4.8%	5.6%	6.3%	5.1%	4.8%	4.1%	3.8%	(2.1%)	(10.7%)	(19.2%)

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	64.0%	32.0%	20.0%	12.0%	8.0%
Reserve Safety Margin (aa)	48.0%	24.0%	16.0%	10.0%	6.0%
Reserve Safety Margin (a)	32.0%	16.0%	10.0%	6.0%	4.0%
Reserve Safety Margin (bbb)	12.0%	8.0%	6.0%	4.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
A+	Affirmed	Stable	5/25/17
A+	Assigned	Stable	6/18/15

Rating Sensitivities

Revenue Volatility: The 'A+' IDR reflects a low level of revenue volatility. Increased volatility could change Fitch's assessment of the adequacy of reserves and lead to a rating downgrade.

Reserve Levels: The ratings assume maintenance of reserves sufficient to maintain financial flexibility throughout the economic cycle. Material declines in reserves beyond Fitch's expectations could put negative pressure on the ratings, while substantial increases to reserves would strengthen credit quality.

Credit Profile

Milwaukee is the largest city in the state of Wisconsin, encompassing a 97-square-mile area adjacent to Lake Michigan, 90 miles north of Chicago. The city's population of nearly 600,000 has shown stability or marginal growth since the 2000 census, reversing a multi-decade trend of decline.

MPS relies on the state of Wisconsin for a significant amount of support. The state benefits from a diverse economy, although there is some concentration in manufacturing. A key feature of the state's manufacturing sector is its diversity, with relatively little exposure to automotive compared to most Midwestern states. Personal income is average, with the state in the middle of the pack relative to the nation. Growth has trailed the U.S.'s in most years.

Revenue Framework

The district remains dependent on state shared revenue for approximately 59% of its general fund revenues, making its finances somewhat vulnerable to the state's fiscal condition (Wisconsin GOs rated 'AA'/Outlook Stable). The second largest source of revenue (26%) is its property tax.

The historical revenue growth trend has been marginally positive on a nominal basis, but has not kept pace with inflation. The district's revenue limit (property taxes plus equalization aid) is annually determined by state statute, which in recent years has allowed zero net growth on a per pupil basis. Fitch's expectation for stagnant revenue growth reflects both the revenue growth prospects for the state of Wisconsin, which provides the majority of operating revenues and which controls increases in the overall revenue limit, as well as the district's declining enrollment trend.

Like many U.S. school districts, MPS has little to no independent ability to raise revenues without voter or state approval.

Expenditure Framework

As is typical of school districts, instruction is the district's largest expense at 58% of general fund spending, followed by business services at 15% and pupil and staff services at 11%.

The pace of spending growth absent policy actions is likely to be well above the limited increases in revenues, necessitating careful expenditure control.

MPS's fixed cost burden is moderate, with carrying costs for debt, pensions and OPEB equaling 11% of fiscal 2016 governmental expenditures. The 2011 Wisconsin Act 10 enhances the district's ability to control spending by restricting collective bargaining rights of public employees and granting public employers significant flexibility over labor costs. The district routinely makes pre-funding contributions toward its OPEB liability.

Related Research

Fitch Rates Milwaukee Public Schools, WI's $31MM Lease Rev Bonds 'A'; Outlook Stable (May 2017)

Related Criteria

U.S. Public Finance Tax-Supported Rating Criteria (May 2017)

Long-Term Liability Burden

The long-term liability burden is moderate, with overall debt and net pension liability approximating 12% of personal income. The district has little direct debt as the city issues debt to address most school capital needs either directly or via the redevelopment authority. The bulk of the long-term liability relates to overlapping debt, including debt issued by the city and redevelopment authority for school purposes. Amortization of direct and city debt is rapid. The district has $35 million of remaining authority to issue qualified school construction bond debt but has no timetable for using it.

MPS's pension plan is almost fully funded, in part due to the redevelopment authority's issuance of pension obligation bonds in the early 2000s. The annual pension payment consistently meets actuarially-determined requirements. The net OPEB liability is notable at about 5% of personal income.

Operating Performance

Unrestricted general fund balance is narrow, averaging about 4%–5% of spending throughout and since the recent recession. For details, see Scenario Analysis, page 2.

Budgetary oversight and control by the city is strong, with little to no deferrals of required spending or non-recurring support of operations. The district expects fiscal 2017 financial operations to be balanced and has a balanced fiscal 2018 budget despite projected revenue declines that resulted in the elimination of 194 full-time equivalent positions.

Lease Provisions

The 'A' lease rating is one notch below MPS's 'A+' IDR, as is standard for U.S. local government tax-supported ratings. MPS, the city and the authority have entered into a cooperation agreement to provide for the redevelopment of real property and improvements which include 30-plus sites. The city and MPS lease the real property to the authority under a ground lease. The city currently holds title to the properties on behalf of MPS. The authority leases the real property and improvements to MPS. Rental payments are made by MPS under the lease in amounts sufficient to pay debt service on the bonds including required sinking funds. The authority has assigned its rights to receive the rent payments and other rights under the lease to a trustee. The lease is net lease to MPS with no right of set-off and at the end of the lease MPS may purchase the properties and improvements for $100.

The rental payments under the lease are general expenses of MPS. The lease does not include an MPS covenant to appropriate the lease payment, as it would constitute a debt for which MPS has no authority. MPS must notify the authority and the trustee if the lease payment is not included in its annual budget. MPS historically has included the lease payments in its budgets and adopted its budgets in a timely fashion.

Under the lease, the only allowable condition for MPS non-payment is in the event that MPS loses quiet enjoyment and experiences material disturbance at all 30-plus properties and improvements. In that event, there are no rights to evict MPS or retake the properties and improvements. Lease payments are paid in arrears such that MPS has already enjoyed use of the properties and improvements and therefore has no right for non-payment. The intention is to maintain MPS's quiet enjoyment of the properties and improvements so that there is never a condition for MPS non-payment. In the event there is loss of quiet enjoyment and material disturbance to all of the properties and improvements, the authority can retake the properties and improvements and release or sell. In the event of non-payment by MPS for any other reason, the authority and/or trustee could seek legal recourse in court to receive payment for rent on properties and improvements that MPS has already used. If MPS received the beneficial use of the properties and improvements, rental payments are owed.

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