S&P Global Ratings

RatingsDirect®

Indiana
Indiana Bond Bank
Indiana Finance Authority; Appropriations; General Obligation; Moral Obligation

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Long Term Rating	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB		
Long Term Rating	AA/Stable	Affirmed
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Unenhanced Rating	AA(SPUR)/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'AAA' issuer credit rating (ICR) on Indiana, based on the application of its "Methodology for Rating U.S. Governments," published Sept. 9, 2024, on RatingsDirect.
- At the same time, we affirmed our 'AA+' rating on the state's appropriation debt and our 'AA' rating on the Indiana Bond Bank's moral obligation debt.
- We also affirmed our 'AA' long-term ratings on the Indiana Finance Authority (IFA)'s Railroad and Rehabilitation and Improvement Financing (RRIF) program loans (supporting the Double Track [DT] and West Lake Corridor commuter Rail Project [WLC Project]).
- The outlook on all ratings is stable.

Security

We rate Indiana's appropriation debt one notch lower than the state's general creditworthiness to reflect the appropriation risk associated with the annual payment. Our rating on the state's moral obligation debt is two notches lower than the state's general creditworthiness, reflecting our view of the preponderance of factors associated with the state's moral obligation.

The RRIF loans are secured and payable solely from a pledge of the trustee of the trust estate, in accordance with each of the trust indentures between the IFA and its trustee (Bank of New York Mellon [BNY]). The trust estates include revenues on deposit in the IFA Regional Development Authority (Northwest Indiana RDA) in respective accounts for each project, established pursuant to a revenue trust agreement among the IFA, the RDA, the Northern Indiana Commuter Transportation District (NICTD), and BNY (as deposit trustee and bond trustee under the indentures).

Revenues in the IFA RDA's respective accounts are derived from annual member dues (statutorily defined) from five entities ($3.5 million each).

WLC is further secured by a pledge of local income taxes from 16 local units of government (statutorily authorized) owed to RDA. Member dues and local income tax contributions are collected by the state treasurer and state comptroller, respectively, and will be subsequently remitted to the deposit trustee before being released into the IFA RDA's respective accounts under the trust fund agreement, based on rental payments owed by the RDA to the IFA (pursuant to separate master leases). Funds are subsequently transferred to the debt service fund under the indentures to satisfy debt service when due. Income tax contributions from the local units of government are, by statute, withheld according to a prescribed schedule before being released to the entity. In the event a member's dues are not paid in full, the state treasurer is authorized to intercept any revenue, excluding local property taxes, payable to the entity as prescribed in statute.

We rate the agreements under our "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" criteria (published Nov. 20, 2019). While we link the obligation to the State of Indiana (AAA/Stable), it has not pledged, committed, or appropriated state resources to the RRIF loan agreements. We rate these bonds two notches below the state's rating, reflective of the state's moderate involvement in the projects being financed, strong coverage over the last two years, our expectation that it will remain at least adequate in the near term, and no timing and administrative risks given the collection cycle of pledged revenues and the state's ability to intercept certain revenues.

Credit overview

In our view, Indiana has maintained robust financial management and oversight through cycles, and has preserved solid reserves. A key credit consideration for the state has been the trajectory of its manufacturing sector, which is a large contributor to the state's economic activity and comprises a notable portion of its employment base, but the state's economy has followed the steady U.S. economic expansion in recent years. Finally, the state's comparatively lower overall debt burden, with manageable pension liabilities, is another factor supporting its credit profile.

The state finished fiscal 2024 better than expected when compared with its December 2023 forecast, when it announced it could miss its Medicaid expenditure forecast. (For more information, please see our article on the state, published on April 16, 2024, on RatingsDirect.) Despite this forecast finding last year, the state finished fiscal 2024 with a 2% surplus. While the Medicaid forecast update is still expected to affect fiscal 2025 expenditures, the state projects it will finish with another surplus and no usage of Medicaid reserves in the current fiscal year. We believe the state's management of this unbudgeted cost escalation displays its consistent oversight mechanisms, and that its focus on replenishing reserves in positive budgetary times has allowed it to have a stabilizing tool to navigate the pressure.

Indiana also has had a demonstrated track record of maintaining strong reserves over time, including this biennium. Upon 2024 fiscal year-end, the state's rainy day fund, state tuition, Medicaid reserves, and general fund ending balance are estimated to total 11.6% of revenues. The state estimates they will total 10.3% at the end of the biennium (fiscal 2025 year-end), with the lower amount primarily driven by an increase in forecast revenues. We view the state's buildup of reserves in strong budgetary periods as a strength, given the cushion it provides the state to navigate potential pressures, and expect the state will adhere to its historical maintenance of reserves moving forward.

Currently, S&P Global Ratings' economists are forecasting steady U.S. real GDP growth of 2.5% in 2024, and still expect the economy to transition to below-potential growth over the next couple of years. Following the robust job market figures in the first quarter, we anticipate July numbers will drive the Fed to begin reducing rates in September. We forecast the nation's real GDP growth to be 1.7% in 2025 and 1.8% in 2026. For more information, see "Economic Outlook U.S. Q3 2024: Milder Growth Ahead," published June 24, 2024, on RatingsDirect and "A Cooling U.S. Labor Market Sets Up A September Start for Rate Cuts," published Aug. 6, 2024. As reflected in S&P Global's August U.S. Manufacturing Purchasing Managers' Index (PMI), the eight-month low could signal that our expectation for below-potential growth may be beginning. We will continue to monitor, but expect Indiana will follow similar trends to those of the nation.

The rating reflects our opinion of the state's:

- Stable budgetary reserves, which we expect to be maintained at or near the state's informal target range of 10%-12% and resilient financial performance across economic cycles;
- Active budget management, with practices that have been consistently applied to maintain sound reserve levels, including the administration's willingness to use its power to align appropriations with conservative revenue estimates and implement a lower-cost structure;
- Historically modest economic growth across sectors, albeit at a slower pace than the nation as a whole, but benefiting in recent years from enhanced economic development investments;
- Low overall debt levels, but with significant contingent liabilities tied to infrastructure investment projects that could result in higher debt levels if toll revenues fall short of expectations;
- Significant additional contributions toward pensions in recent years, specifically to its Teachers Retirement Fund Pre-1996 plan, which we believe will lead to material improvement in state costs related to the plan in the medium term, and keeping actual costs at a level we view as manageable in future budgets; and
- An institutional framework that supports the predictability of the state's budgeting and operations, in our view, and demonstrated fiscal transparency through regular reporting of key financial information.

Indiana's ICR is eligible to be rated above the sovereign because we believe the state can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions" (published Nov. 19, 2013), U.S. states are considered to have moderate sensitivity to country risk. The institutional framework in the U.S. is predictable, with significant state autonomy and flexibility demonstrated by serial bond amortization, as well as independent treasury management.

Environmental, social, and governance

We consider the state's social factors to be credit neutral, although its aging population and historically limited population growth could weigh on its demographic profile in the longer term, absent an improvement. We view the state's governance and environmental factors as being neutral within our credit rating analysis. Indiana has historically maintained a strong management and policy framework to respond to developing risks.

Outlook

The stable outlook reflects our view that management will continue its historical trend of strong oversight and aligning revenues with expenditures to ensure balance. It also reflects our expectation that the state will continue to monitor any unexpected budgetary challenges should they arise, and will respond in a timely manner.

Downside scenario

Should the state experience sustained budgetary stress that results in management being unable to align revenues and expenditures, leading to material decreases in its reserves, we could lower the rating. While we expect the state's economic metrics will remain below national levels, should the gap materially widen, we could also lower the rating.

Credit Opinion

Institutional Framework

Indiana maintains a robust and predictable institutional framework, in our view, including constitutional provisions that support predictability of the state's budgeting and operations, and no history of voter initiatives significantly affecting the state's finances. In 2018, the state's electorate supported a constitutional amendment requiring a balanced biennial budget. A suspension of the requirement is only feasible with a supermajority (two-thirds) approval from both legislative chambers. Embedding this requirement into the state's constitution strengthens the state's institutional framework, in our view. Indiana is not a voter initiative state, which we believe provides some stability.

We view the state's proactive mechanisms in place, which provide it with the flexibility to adjust both revenues and expenditures if believed to be necessary, as a credit strength. For example, only a simple majority of the legislature is required to raise taxes, and there is no constitutional constraint on the amount of the increase. Additionally, state statute provides that the state budget director, with the approval of the governor, can withhold allotments of appropriations to agencies if revenues are less than anticipated to prevent revenue and appropriation misalignments. Indiana has historically used its allotment authority to avoid deficits when revenues are falling short of targets. The state provides a limited level of assistance to local governments, but fully funds local school general operations as a result of the property tax reform passed in 2008. In fiscal 2010, the administration used its allotment power and withheld funds from schools, displaying some flexibility within its expenditure authority. Lastly, the state operates within a framework that provides interim budget transparency and comparability through its timely, annual presentation of audited financial information, as well as numerous reports published on an annual budgetary basis.

Management

We consider Indiana's budget practices, long-term planning, and management policies to be comprehensive, well-defined in most areas, and sustainable.

In terms of revenue assumptions and forecasts, the state convenes every December with the Revenue Forecast

Technical Committee, consisting of members from the executive branch, House, and Senate, along with economists, to prepare the upcoming revenue forecast. The same group updates the revenue forecast in April of odd-numbered years and compares the budget with the April forecast. The forecast is presented every December and in April of odd-numbered years to the state budget committee. The state has a biennium budget process, and standard practice is to not amend the budget. However, the budget director has the power to forego allotting appropriations. While the state performs some longer-term forecasts internally, they are not produced on a consistent basis and no formal long-term forecasts are maintained. In terms of long-term capital planning, state agencies and universities provide formal long-term plans for five years and 10 years, respectively, and the IFA requires long-term capital plans for lease transactions.

The state maintains its own investment policy, requiring regular reporting. The state's debt management policies are comprehensive and include a well-defined swap management policy. In addition, the state has a policy that limits appropriation debt to 15% of the previous year's revenues. In terms of liquidity and reserves, the state has an informal goal of maintaining 10%-12% of annual operating revenues in the general fund, and a statutory cap of 12.5%. Once the budget is approved, the state monitors revenue and expenditure performance monthly. With the approval of the governor, the state budget director can withhold allotments of appropriations to agencies if revenues are less than anticipated, toward preventing a deficit. Budget adjustments have historically been implemented on a regular and timely basis, which we view favorably.

Economy

We believe that Indiana's relatively low cost of living and business-friendly legislation and regulatory practices continue to make it an attractive target for firms looking to expand or relocate to the state. A majority of the state's gross state product is driven by manufacturing, at roughly 16% more than the U.S., with every other sector more in alignment with the nation. However, the state's economic activity is not concentrated in industries that we consider volatile, which we believe contributes to its stability over time.

The Indiana Economic Development Corp. (IEDC) leads the state's job creation efforts by trying to attract increased investment in several key areas, including advanced manufacturing, agriculture, life sciences, and defense and national security. The 2023-25 biennium budget included a new $500 million deal closing fund, provided additional resources for large economic development deals over $5 billion, and created a new site acquisition fund for shovel-ready development projects, as well as investing an additional $500 million in the state's Regional Economic Acceleration and Development Initiative (READI) program. The state's enhanced investments into its economic development strategy have resulted in positive gains, with the first quarter of 2024 posting the state's largest committed capital investment in its history, driven by numerous companies locating or expanding in the state, and ultimately leading to new jobs. We expect recent investments will continue to support IEDC's efforts over the course of the biennium, likely leading to further economic development.

Financial Performance, Reserves and Liquidity

Indiana has demonstrated its commitment to enacting and maintaining balanced budgets, and consistently building up budgetary reserves for flexibility when pressure arises. The state enacted its 2023-25 biennial budget last year, which recognized a roughly 20% general fund expenditure increase from the previous biennium. Appropriations for public education (kindergarten-through-grade 12 and higher education) and Medicaid account for 71% of the biennium's general fund appropriations. The state's primary sources of general fund revenue are personal income tax and sales tax, at 36.5% and 49.5% of forecast general fund revenues, respectively, for the 2023-25 biennium.

In the 2023 legislative session, the state expedited its planned personal income tax cuts, with decreases from 3.15% in 2023 to 2.9% by 2029, subject to certain revenue triggers. The personal income tax rate will now reach 2.9% by 2027, and trigger mechanisms were removed. In addition, the state passed further tax relief, including military exemptions, earned income tax credit updates, and additional tax deductions for adoptive parents. While we believe revenue triggers are prudent measures to include in tax legislation to ensure strong revenue performance before tax cuts, we believe the state's cautious planning, specifically budgeting for larger-than-typical surpluses, is a helpful mechanism to adjust to the phased-in lower rates over the course of the biennium.

The state has a statutory reserve cap of 12.5% of revenues as a percentage of the following year's appropriation. Any amounts in excess of that cap are equally divided among payments to pension funds and to an automatic taxpayer refund, except in 2016, in which any balance in excess of 11.5% at the end of fiscal 2016 was used to fund transportation improvements. The reserves must exceed the cap by $50 million to trigger the transfer, which only occurs in budget years. In fiscal year 2021, given the state's strong budgetary performance, $545.3 million was allocated for taxpayer refunds and another $545.3 million to the state's pension funds. In fiscal 2022, the state distributed $2.5 billion toward the state's pensions, and several hundred million for taxpayer refunds was triggered as a result of the reserve cap. Based on estimated actuals, the state finished fiscal 2024 with a combined 11.6% of annual revenues between its general fund and reserve balances, and is budgeting to finish fiscal 2025 with 10.3% of annual revenues.

Debt and Liabilities

The state's debt and liability profile, in our opinion, is a credit strength. Indiana's constitution does not allow new debt, except to meet deficits in revenue, pay interest on state debt, or provide funds for public defense. As a result, the state has no general obligation (GO) or tax-supported debt, but does have appropriation-backed debt, which is required to be authorized by the legislature. The state's debt profile is supported by low debt levels on a per capita basis and as a percentage of revenues. We currently do not include bond bank debt that is secured by the state's moral obligation pledge. While Indiana has appropriated fee-replacement debt for the universities in the past, there is no appropriation pledge supporting the bonds and the state is not obligated to appropriate for it in the future. Therefore, we do not include the university fee-replacement debt in Indiana's debt calculation.

Pension and other postemployment benefits (OPEB)

Indiana maintains a variety of pension plans, of which the Teachers Retirement Fund (TRF Pre-1996) and the Public Employees Retirement Fund (PERF) represent the largest proportionate shares of the state's unfunded pension liability. The Indiana State Teachers' Retirement Fund consists of the closed pre-1996 account and the new 1996 account. In 1996, Indiana closed the plan and moved new hires to actuarially sound plans. The new plan, which is the responsibility of school districts, includes transferred teachers from the state plan.

Plans representing a significant portion of the state's net pension liability (NPL) include:

- TRF-Pre 1996: 62% funded with the state's NPL of $5.2 billion (as of June 30, 2023); and
- PERF: 81% funded with the state's NPL of $915 million (as of June 30, 2023).

The state funds the closed pre-1996 account on a pay-as-you-go basis, so appropriations fund actuarially determined contributions (ADCs) in their entirety when they equal the expected benefit payment. In order to address the significant unfunded liability in the TRF Pre-1996 plan, Indiana established a pension stabilization fund, which should limit the annual growth rate for the TRF Pre-1996 to less than historical revenue growth rates. The pension stabilization fund is a dedicated fund in the TRF Pre-1996 plan, designed to accumulate balance during a 12-year period. The fund is allowed to smooth out yearly general fund contribution growth to less than 3%; the original statute allowed use of the fund to start in 2007. In recent years, the state has made significant one-time contributions toward its pre-1996 plan, ultimately elevating its total current cost percentage of total government revenues. Given that these contributions are one-time for fiscal 2023 (as well as for fiscal years 2022 and 2021 on a smaller basis), our debt and liabilities assessment reflects our expectation that current costs associated with these payments should moderate significantly over the near term given the pay-go funding approach and the state currently being at peak appropriations.

PERF assumes a closed amortization schedule with 20-year amortization based on level dollar. The system ratio of active members to beneficiaries is 1 to 2 and has been on a declining trend in recent years. PERF incorporates experience trends and industry standards through experience studies produced every five years. The state's five-year average rate of return for the plan was 6.26%, slightly above the assumed rate of return of 6.25%.

The pension relief fund, a holding account administered by the Indiana Public Retirement System, was created to support local governments with their legacy police and firefighter retirement plans. These pay-as-you-go plans include the 1925 Police Pension Fund, 1937 Police Pension Fund, and 1953 Pension Fund. While the liabilities belong to the local entities, the state has assumed 100% of the cost. Funding is provided through general fund appropriations, lottery proceeds, cigarette taxes, alcohol taxes, and investment income. Benefits are paid on a pay-as-you-go basis.

The state's other postemployment benefits (OPEB) liabilities are funded on a pay-as-you-go basis and are manageable, in our view, at roughly $85 million as of June 30, 2023.

Table 1

Indiana--Credit summary	
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Table 1

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Table 2

Indiana--Key credit metrics				
	2024	**2023**	**2022**	**2021**
Economy				
State population ('000s)	--	6,867	6,835	6,815
GSP per capita ($)	--	58,461	57,937	56,357
GSP per capita % of U.S.	--	88	89	88
State PCPI ($)	--	59,916	58,305	56,925
State PCPI % of U.S.	--	88	89	88
State unemployment rate (%)	--	3.3	3.1	3.9
Financial performance--S&P Global Ratings adjusted				
Operating fund revenues (mil. $)	21,912	21,594	21,443	18,857
Operating fund expenditures (mil. $)	21,490	17,995	17,574	17,039
Operating result (mil. $)	421	3,600	3,869	1,819
Operating result % of revenues	1.9	16.7	18.0	9.6
Reserves and liquidity--S&P Global Ratings adjusted				
Available reserves (mil. $)*	2,551	2,926	6,125	3,923
Available reserves (% of operating revenues)*	11.6	13.6	28.6	20.8
Debt and liabilities				
Net direct debt cost (% of revenues)	--	0.3	0.6	0.2
Pension and OPEB cost (% of revenues)	--	8.7	3.7	4.1
Total current cost (% of total government revenues)	--	9.0	4.2	4.4
Net direct debt (mil. $)	--	1,276	1,294	2,058
Net direct debt per capita ($)	--	186	189	302
Direct debt 10-year amortization (%)	--	75	86	68
Combined net pension liabilities (mil. $)	--	6,509	10,075	9,751
Net pension liabilities per capita ($)	--	949	1,474	1,431
Combined pension plan funded ratio (%)	--	76.1	68.9	75.2

GSP--Gross state product. PCPI--Per capita personal income. OPEB--Other postemployment benefits. *Includes rainy day fund, Medicaid reserve, tuition reserve, and GF ending balance.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of September 13, 2024)		
Indiana Bond Bank, Indiana		
Indiana		
Indiana Bnd Bank (Indiana) MORALOB		
Long Term Rating	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB		
Long Term Rating	AA/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (AGM)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (AMBAC)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Indiana Bnd Bank (Indiana) MORALOB (MBIA) (National)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Indiana Finance Authority, Indiana		
Indiana		
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Unenhanced Rating	NR(SPUR)	
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Unenhanced Rating	NR(SPUR)	
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
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Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
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Long Term Rating	AA+/Stable	Affirmed
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Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed

Ratings Detail (As Of September 13, 2024) (cont.)		
Indiana Fin Auth (Indiana) APPROP		
Long Term Rating	AA+/Stable	Affirmed
Indiana Fin Auth (Indiana) (Double Track Proj)		
Long Term Rating	AA/Stable	Affirmed
Indiana Fin Auth (Indiana) (West Lake Proj)		
Long Term Rating	AA/Stable	Affirmed
Indiana State Office Building Commission, Indiana		
Indiana		
Indiana St Office Bldg Comm (Indiana) APPROP		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Indiana St Office Bldg Comm (Indiana) APPROP		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Indiana Transportation Finance Authority, Indiana		
Indiana		
Indiana Transp Fin Auth (Indiana) APPROP (wrap of insured) (FGIC & AGM) (SECMKT)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Indiana Transp Fin Auth (Indiana) APPROP (FGIC) (MBIA) (National)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.