

# SECURITIES AND EXCHANGE COMMISSION

## FORM N-30D

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### FILER

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**PUTNAM MINNESOTA TAX EXEMPT INCOME FUND II**

CIK: **794612** | IRS No.: **046626128** | State of Incorporation: **MA** | Fiscal Year End: **0531**  
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Putnam  
Minnesota  
Tax Exempt  
Income Fund

ANNUAL REPORT

May 31, 1998

[LOGO: BOSTON \* LONDON \* TOKYO]

Fund highlights

\* "Despite Minnesota's rather limited supply of municipal securities, we have found significant income and value investment opportunities. Health care and long-term care have been particularly fruitful sectors for the fund, as have industrial revenue bonds."

-- Leslie J. Burke, manager  
Putnam Minnesota Tax Exempt Income Fund

\* "Surging tax revenues in most states helped bolster municipal credit bond ratings. Standard and Poor's says the number of ratings upgrades in this year's first quarter was more than nine times the number of downgrades."

-- The Wall Street Journal, April 8, 1998

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From the Chairman

[GRAPHIC OMITTED: PHOTO OF GEORGE PUTNAM]

[copyright] Karsh, Ottawa

Dear Shareholder:

Analyzing risk premiums, yield spreads, call dates, yield curves, credit ratings, supply-and-demand dynamics, taxable versus tax-exempt yield relationships, and a host of other factors is all in a day's work for Putnam's Tax-Exempt Bond Group. The result was another period of competitive performance for Putnam Minnesota Tax Exempt Income Fund's fiscal year that closed on May 31, 1998.

Using her knowledge of Minnesota's tax-exempt bond environment and backed by Putnam's extensive credit analysis capability, Fund Manager Leslie Burke made the strategic and tactical decisions that provided these positive results. In the following report, Leslie discusses the fund's performance during fiscal 1998 and then takes a look at prospects for the tax-exempt market, especially with regard to Minnesota, in the months ahead.

Respectfully yours,

/S/GEORGE PUTNAM  
George Putnam  
Chairman of the Trustees  
July 15, 1998

Report from the Fund Manager  
Leslie J. Burke

The 12 months ended May 31, 1998, marked another period of solid performance for Putnam Minnesota Tax Exempt Income Fund. While supply-and-demand dynamics and concerns over the situation in Asia did produce some price and yield fluctuations, the municipal bond market generally experienced little volatility over the course of the year. Within this quiet playing field, there were fewer opportunities for profit, but Putnam Minnesota Tax Exempt Income Fund continued to deliver what it promised shareholders: a reliable stream of income exempt from state and federal taxes along with relatively low share price volatility. For the 12 months ended May 31, 1998, the fund provided a

total return of 7.90% at net asset value (2.73% at public offering price) for class A shares. Results for class B and class M shares can be found on pages 9 and 10 of this report.

\* MUNICIPAL BOND MARKET BOASTS ATTRACTIVE PRICES, ROBUST SUPPLY AND DEMAND

Despite the relative calm that has fallen over the \$1.3 trillion municipal bond market, prices on these bonds have actually become especially attractive relative to the Treasury market -- a state of affairs that has not occurred since the flat-tax scare of 1996. By the end of May, municipal bonds (as represented by 30-year insured municipals) were offering almost 90% of the yield of long-term Treasury bonds. Since the typical level is 84%, the current percentage makes municipal prices remarkably low.

The bargain prices in this market have maintained investors' interest and enabled demand to keep pace with supply. Also noteworthy is the unusually flat tax-exempt yield curve. With the 30-year bond paying only a modest 30 to 40 basis points over a 10-year bond, investors are not compensated for taking on higher risk. For this reason, we often find the best value (attractive yield with minimal volatility) in the intermediate-plus range of the yield curve -- anywhere from 10 to 20 years.

Low interest rates also acted as a catalyst for municipal bond refundings and new issues in recent months. In fact, 1998 so far has been most notable for its huge supply, including the sale of the largest municipal bond issue in history -- \$3.4 billion by the Long Island Power Authority in May. Of course, in Minnesota, the situation is a bit different. The state's robust economy continues to limit the borrowing needs of many municipalities, although overall the municipal bond supply has increased over the period.

\* FUND MAINTAINS FLEXIBILITY, STAYS FULLY INVESTED

As the period drew to a close, a number of crosscurrents continued to drive the financial markets. The U.S. economy remained quite exuberant with strong employment and solid income growth fueling robust consumer spending. Indeed, the Federal Reserve Board remained on alert for indications that economic strength was producing any uptick in inflation or incipient inflationary pressures. Through the end of the period, however, Fed action was restrained by concerns that the Asian recessions might yet have additional negative consequences for the U.S. economy, since manufacturers in various industries had already reported declines in exports to Asia and tough competition from cheaper Asian imports.

Amid these competing forces, the future direction of interest rates remains unclear. Will the strong economy eventually convince the Fed to raise short-term rates or will the Asian financial crisis slow growth enough to prevent such a move? Given this uncertainty, we have positioned the fund flexibly with a neutral duration. Duration is a mathematical measure used to indicate how much the prices of portfolio holdings are likely to move up or down with each percentage-point shift in interest rates.

[GRAPHIC OMITTED: HORIZONTAL BAR CHART OF TOP INDUSTRY SECTORS]

TOP INDUSTRY SECTORS\*

|                 |       |
|-----------------|-------|
| Health care     | 26.9% |
| Housing         | 11.7% |
| Education       | 9.9%  |
| Utilities       | 9.7%  |
| Water and sewer | 7.0%  |

Footnote reads:

\* Based on net assets as of 5/31/98. Holdings will vary over time.

When we believe interest rates are more likely to move in one direction or another, we carefully adjust the fund's duration profile in order to manage its interest-rate risk more effectively. In the present environment, however, a fairly neutral duration appears to us to be the most prudent way to keep the fund ready for potential interest-rate changes while minimizing share price volatility and continuing to pursue a steady stream of current income.

Although the uncertain interest-rate climate has not prompted us to take a more emphatic stand on portfolio duration, the attractive prices of municipal securities are a compelling argument for staying fully invested in the market. Because this move could extend the fund's duration farther out than we deem prudent, we have balanced the fund's municipal investments by selling Treasury futures contracts, a strategy that has the effect of shortening duration.

The current supply-and-demand situation has also made it wise to keep the fund fully invested. While the supply of municipal securities has been quite high

for most of the year, there were signs that new issuance was tapering off toward mid May. Furthermore, by remaining fully invested, the fund was positioned to capitalize on gains resulting from any rise in prices during a potential surge in demand preceding the seasonal swell in coupon payments on June 1 and July 1.

#### \* PURSUING INCOME AND VALUE

In a municipal market boasting attractive prices and a flat yield curve, a focus on value rather than duration management has dominated the fund's investment strategy. Essentially this means emphasizing issues that offer the best relative value along with structural components that will enhance the fund's income stream while minimizing its share price volatility. For the most part, we have found these issues among the intermediate-plus bonds mentioned above.

[GRAPHIC OMITTED: PIE CHART OF CREDIT QUALITY OVERVIEW]

#### CREDIT QUALITY OVERVIEW\*

Baa -- 8.3%

A -- 14.1%

Aa -- 21.8%

Ba -- 7.8%

Aaa -- 48.0%

Footnote reads:

\* As a percentage of market value as of 5/31/98. A bond rated Baa or higher is considered investment grade. All ratings reflect Moody's descriptions unless noted otherwise; percentages may include unrated bonds considered by Putnam Management to be of comparable quality. Ratings will vary over time.

In terms of sectors, the health-care and long-term care industries provided the most productive opportunities for income and value over the period. In the health-care sector, we added several hospital holdings during the past six months including Big Lake Hospital, Children's Health, and Fairview Hospital. Among long-term care facilities, we added The Northfield Project and a group of nursing homes for the Board of Social Ministry. All of the new holdings are solid credits with strong coupons to enhance the fund's income stream. While these holdings, as well as others discussed in this report, were viewed favorably at the end of the period, all holdings are subject to review and adjustment in accordance with the fund's investment strategy and may well vary in the future.

To capitalize on Minnesota's favorable economic climate, we invested in industrial revenue bonds. Specifically we took a position in bonds issued to finance an expansion of the Minneapolis International Airport and added to the fund's position in projects issued for Boise Cascade, a long-term holding that continues to provide solid income for the fund. Paper companies fall into an industrial category known as late cyclicals, meaning that they typically begin to outperform similar commodities once an economic expansion is fully under way. Although the current growth cycle has already lasted longer than many economists and policymakers thought possible, we believe that Minnesota's economy is still strong enough for the fund to reap additional performance benefits from its Boise Cascade investment.

#### \* NONCALLABLE BONDS ENHANCE PERFORMANCE, PRICE STABILITY

In our pursuit of securities that provide strong income and solid relative value, we have continued to seek out noncallable bonds. Because callable bonds have the option of being called away by the issuer at a certain future date -- usually if interest rates are lower than when the bonds are first issued -- investing in noncallable bonds or bonds with distant call dates enables the fund to provide the most durable level of income. Unfortunately Minnesota's tight securities supply also limits the availability of noncallable securities. During the recent period, however, we did purchase some high-coupon noncallable bonds issued by the University of Minnesota.

#### \* OUTLOOK IS CAUTIOUSLY OPTIMISTIC

While the Asian crisis has been widely publicized as negative for economic growth around the world, it has produced some positive effects in the United States. Fears of the financial turmoil in Asia and other emerging markets have helped keep interest rates low. In turn, low interest rates have helped improve corporate balance sheets, contributed to low unemployment, and helped bring out additional municipal securities supply. Minnesota's economy has more than kept pace with the national trend, and it continues to provide a favorable credit backdrop for the state's municipal bond market.

Our outlook for the municipal market remains fairly positive. With municipal bond supply relatively high and demand on the upswing, securities valuations

are unlikely to remain so inexpensive relative to Treasuries. Municipal investors stand to benefit from any price appreciation that may occur as this supply-and-demand imbalance straightens out. Eventually, however, today's economic good times may give way to slightly higher inflation, and so we remain somewhat cautious. In our opinion, this is not a good time to expose the portfolio to bonds with longer maturities and higher interest-rate risk. Accordingly we believe the fund's neutral duration, and emphasis on low call risk and in-depth credit research will continue to produce the best returns in the months ahead.

The views expressed here are exclusively those of Putnam Management. They are not meant as investment advice. Although the described holdings were viewed favorably as of 5/31/98, there is no guarantee the fund will continue to hold these securities in the future.

Performance summary

This section provides information about your fund's performance, which should always be considered in light of its investment strategy. Putnam Minnesota Tax Exempt Income Fund is designed for investors seeking a high level of current income free from federal and state income tax consistent with preservation of capital.

TOTAL RETURN FOR PERIODS ENDED 5/31/98

| (inception date) | Class A<br>(10/23/89) |       | Class B<br>(7/15/93) |       | Class M<br>(4/3/95) |       |
|------------------|-----------------------|-------|----------------------|-------|---------------------|-------|
|                  | NAV                   | POP   | NAV                  | CDSC  | NAV                 | POP   |
| 1 year           | 7.90%                 | 2.73% | 7.20%                | 2.20% | 7.70%               | 4.20% |
| 5 years          | 32.39                 | 26.13 | 27.51                | 25.51 | 30.34               | 26.05 |
| Annual average   | 5.77                  | 4.75  | 4.98                 | 4.65  | 5.44                | 4.74  |
| Life of fund     | 78.55                 | 70.15 | 67.12                | 67.12 | 72.92               | 67.32 |
| Annual average   | 6.97                  | 6.38  | 6.15                 | 6.15  | 6.58                | 6.17  |

COMPARATIVE INDEX RETURNS FOR PERIODS ENDED 5/31/98

|                | Lehman Bros.<br>Municipal Bond Index | Consumer<br>Price Index |
|----------------|--------------------------------------|-------------------------|
| 1 year         | 9.39%                                | 1.69%                   |
| 5 years        | 38.53                                | 12.90                   |
| Annual average | 6.74                                 | 2.46                    |
| Life of fund   | 96.00                                | 29.62                   |
| Annual average | 8.16                                 | 3.07                    |

Past performance is not indicative of future results. Returns for class A and class M shares reflect the current maximum initial sales charges of 4.75% and 3.25%, respectively. Class B share returns for the 1-, 5-year (where available) and life-of-fund periods reflect the applicable contingent deferred sales charge (CDSC), which is 5% in the first year, declines to 1% in the sixth year, and is eliminated thereafter. Returns shown for class B and class M shares for periods prior to their inception are derived from the historical performance of class A shares, adjusted to reflect both the initial sales charge or CDSC, if any, currently applicable to each class and, in the case of class B and class M shares, the higher operating expenses applicable to such shares. All returns assume reinvestment of distributions at NAV. Investment return and principal value will fluctuate so that an investor's shares when redeemed may be worth more or less than their original cost. Returns shown for class A shares have not been adjusted to reflect payments under the class A distribution plan prior to its implementation.

PRICE AND DISTRIBUTION INFORMATION

12 months ended 5/31/98

|                            | Class A    |     | Class B    |     | Class M    |  |
|----------------------------|------------|-----|------------|-----|------------|--|
| Distribution (number)      | 12         |     | 12         |     | 12         |  |
| Income                     | \$0.453916 |     | \$0.392783 |     | \$0.426624 |  |
| Capital gains <sup>1</sup> | --         |     | --         |     | --         |  |
| Total                      | \$0.453916 |     | \$0.392783 |     | \$0.426624 |  |
| Share value:               | NAV        | POP | NAV        | NAV | POP        |  |

|                                       |        |        |        |        |        |
|---------------------------------------|--------|--------|--------|--------|--------|
| 5/31/97                               | \$8.95 | \$9.40 | \$8.92 | \$8.94 | \$9.24 |
| 5/31/98                               | 9.19   | 9.65   | 9.16   | 9.19   | 9.50   |
| Current return (end of period)        |        |        |        |        |        |
| Current dividend rate <sup>2</sup>    | 4.85%  | 4.62%  | 4.20%  | 4.55%  | 4.40%  |
| Taxable equivalent <sup>3</sup>       | 8.78   | 8.36   | 7.60   | 8.23   | 7.96   |
| Current 30-day SEC yield <sup>4</sup> | 4.71   | 4.49   | 4.06   | 4.41   | 4.27   |
| Taxable equivalent <sup>3</sup>       | 8.52   | 8.12   | 7.35   | 7.98   | 7.73   |

<sup>1</sup>Capital gains, if any, are taxable for federal and, in most cases, state tax purposes. For some investors, investment income may also be subject to the federal alternative minimum tax. Investment income may be subject to state and local taxes.

<sup>2</sup>Income portion of most recent distribution, annualized and divided by NAV or POP at end of period.

<sup>3</sup>Assumes maximum 44.73% combined federal and state tax rate. Results for investors subject to lower tax rates would not be as advantageous.

<sup>4</sup>Based only on investment income, calculated using SEC guidelines.

TOTAL RETURN FOR PERIODS ENDED 6/30/98  
(most recent calendar quarter)

| (inception date) | Class A<br>(10/23/89) |       | Class B<br>(7/15/93) |       | Class M<br>(4/3/95) |       |
|------------------|-----------------------|-------|----------------------|-------|---------------------|-------|
|                  | NAV                   | POP   | NAV                  | CDSC  | NAV                 | POP   |
| 1 year           | 7.23%                 | 2.13% | 6.54%                | 1.54% | 7.04%               | 3.59% |
| 5 years          | 31.01                 | 24.74 | 26.24                | 24.24 | 28.96               | 24.75 |
| Annual average   | 5.55                  | 4.52  | 4.77                 | 4.44  | 5.22                | 4.52  |
| Life of fund     | 79.48                 | 71.04 | 67.89                | 67.89 | 73.77               | 68.15 |
| Annual average   | 6.97                  | 6.38  | 6.15                 | 6.15  | 6.57                | 6.17  |

Performance data represent past results, do not reflect future performance, and will differ for each share class. Investment returns and principal value will fluctuate so that an investor's shares, when sold, may be worth more or less than their original cost. See first page of performance section for performance calculation method.

[GRAPHIC OMITTED: MOUNTAIN CHART OF GROWTH OF A \$10,000 INVESTMENT]

GROWTH OF A \$10,000 INVESTMENT

PLOT POINTS

Cumulative total return of  
a \$10,000 investment since  
10/23/89

| Date     | Fund's class A<br>shares at POP | Lehman Bros.<br>Municipal Bond Index | Consumer Price<br>Index |
|----------|---------------------------------|--------------------------------------|-------------------------|
| 10/23/89 | 9,525                           | 10,000                               | 10,000                  |
| 5/31/90  | 10,300                          | 10,453                               | 10,287                  |
| 5/31/91  | 11,353                          | 11,507                               | 10,796                  |
| 5/31/92  | 12,242                          | 12,637                               | 11,122                  |
| 5/31/93  | 13,665                          | 14,149                               | 11,480                  |
| 5/31/94  | 12,927                          | 14,499                               | 11,743                  |
| 5/31/95  | 15,048                          | 15,824                               | 12,118                  |
| 5/31/96  | 15,545                          | 16,547                               | 12,468                  |
| 5/31/97  | 16,725                          | 17,919                               | 12,746                  |
| 5/31/98  | 17,015                          | 19,600                               | 12,962                  |

Past performance is no assurance of future results. At the end of the same time period, a \$10,000 investment in the fund's class B shares would have been valued at \$16,712 and no contingent deferred sales charges would apply; a \$10,000 investment in the fund's class M shares would have been valued at \$17,292 at net asset value (\$16,732 at public offering price). See first page of performance section for performance calculation method.

TERMS AND DEFINITIONS

Total return shows how the value of the fund's shares changed over time, assuming you held the shares through the entire period and reinvested all distributions in the fund.

Class A shares are generally subject to an initial sales charge.

Class B shares may be subject to a sales charge upon redemption.

Class M shares have a lower initial sales charge and a higher 12b-1 fee than class A shares and no sales charge on redemption.

Net asset value (NAV) is the value of all your fund's assets, minus any liabilities, divided by the number of outstanding shares, not including any initial or contingent deferred sales charge.

Public offering price (POP) is the price of a mutual fund share plus the maximum sales charge levied at the time of purchase. POP performance figures shown here assume the maximum 4.75% sales charge for class A shares and 3.25% for class M shares.

Contingent deferred sales charge (CDSC) is a charge applied at the time of the redemption of class B shares and assumes redemption at the end of the period. Your fund's CDSC declines from a 5% maximum during the first year to 1% during the sixth year. After the sixth year, the CDSC no longer applies.

#### COMPARATIVE BENCHMARKS

Lehman Brothers Municipal Bond Index is an unmanaged list of long-term fixed-rate investment-grade tax-exempt bonds representative of the municipal bond market. The index does not take into account brokerage commissions or other costs, may include bonds different from those in the fund, and may pose different risks than the fund. It is not possible to invest directly in an index.

Consumer Price Index (CPI) is a commonly used measure of inflation; it does not represent an investment return.

#### Report of independent accountants

To the Trustees and Shareholders of  
Putnam Minnesota Tax Exempt Income Fund

In our opinion, the accompanying statement of assets and liabilities, including the portfolio of investments owned (except for bond ratings), and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of Putnam Minnesota Tax Exempt Income Fund (the "fund") at May 31, 1998, and the results of its operations, the changes in its net assets and the financial highlights for the periods indicated, in conformity with generally accepted accounting principles. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the fund's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of investments owned at May 31, 1998, by correspondence with the custodian and the application of alternative auditing procedures where investments purchased were not yet received by the custodian, provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP  
Boston, Massachusetts  
July 10, 1998

<TABLE>  
<CAPTION>

Portfolio of investments owned  
May 31, 1998

#### Key to Abbreviations

AMBAC -- AMBAC Indemnity Corporation  
COP -- Certificate of Participation  
FGIC -- Financial Guaranty Insurance Company

FNMA Coll. -- Federal National Mortgage Association Collateralized  
 FRB -- Floating Rate Bonds  
 FSA -- Financial Security Assurance  
 GNMA Coll. -- Government National Mortgage Association Collateralized  
 G.O. Bonds -- General Obligation Bonds  
 IFB -- Inverse Floating Rate Bonds  
 MBIA -- Municipal Bond Investors Assurance Corporation  
 VRDN -- Variable Rate Demand Notes

MUNICIPAL BONDS AND NOTES (98.4%) (a)

| PRINCIPAL AMOUNT  |   | RATING (RAT) | VALUE        |
|-------------------|---|--------------|--------------|
| <S>               | <C>   | <C>          | <C>          |
| Minnesota (95.9%) |   |              |              |
| \$ 1,200,000      | Bemidji, Hosp. Fac. Rev. Bonds<br>(First Mtge.-North Country Hlth. Svcs.),<br>5 5/8s, 9/1/21                          | A            | \$ 1,239,000 |
| 1,760,000         | (First Mtge.-North Country Hlth. Svcs.),<br>5 5/8s, 9/1/15  | A            | 1,826,000    |
| 500,000           | Centennial, Indpt. G.O. Bonds (School Dist. No. 12),<br>Ser. A, FSA, 7.15s, 2/1/12                                    | Aaa          | 525,625      |
| 1,930,000         | Chaska, Indl. Dev. Rev. Bonds<br>(Lifecore Biomedical, Inc.), 10 1/4s, 9/1/20   | BB/P         | 2,105,456    |
| 3,000,000         | Cloquet, Poll. Control Rev. Bonds (Potlatch Corp.),<br>5.9s, 10/1/26  | A            | 3,165,000    |
| 885,000           | Crystal, Coml. Dev. Rev. Bonds FRB<br>(Crystal Gallery Mall), 3.8s, 4/15/14   | Aa           | 885,000      |
| 1,000,000         | Duluth, Gross Rev. Bonds (Duluth Entertainment),<br>7.6s, 12/1/11   | Baa          | 1,138,750    |
| 1,000,000         | Duluth, Econ. Dev. Auth. Hlthcare Fac. Rev. Bonds<br>(Duluth Clinic), AMBAC, 6.3s, 11/1/22                            | Aaa          | 1,087,500    |
| 500,000           | Duluth, Econ. Dev. Auth. Hlthcare Fac. Rev. Bonds<br>(BSM Prop.), 5 7/8s, 12/1/28                                     | Ba           | 500,000      |
| 500,000           | Fergus Falls, Cmnty. Dev. Rev. Bonds<br>(Lincoln - St. Andrews Assn.), 8 3/4s, 11/1/06                                | BB/P         | 507,000      |
| 1,000,000         | Hutchinson, Indpt. G.O. Bonds (School Dist. No. 423),<br>Ser. A, 5 3/4s, 2/1/13                                       | Aa           | 1,076,250    |
| 1,565,000         | Intl. Falls, Env. Fac. Rev. Bonds (Boise Cascade Corp.),<br>7.2s, 10/1/24   | Baa          | 1,778,231    |
| 1,500,000         | Intl. Falls, Poll. Ctr. Rev Bonds (Boise Cascade Corp.),<br>5.65s, 12/1/22  | BBB          | 1,530,000    |
| 1,105,000         | Minneapolis, Cmnty. Dev. Agcy. Supported Dev.<br>Rev. Bonds (Grace-Lee Products Inc.),<br>Ser. 91-3, 8 1/4s, 12/1/11  | A            | 1,225,169    |
| 3,000,000         | Minneapolis, G.O. Bonds (Sports Arena)<br>5.2s, 10/1/24   | Aaa          | 3,045,000    |
| 1,500,000         | 5 1/8s, 10/1/20   | Aaa          | 1,518,750    |
| 1,675,000         | Minneapolis, Sales Tax G.O. Bonds, 6 1/4s, 4/1/12   | Aaa          | 1,819,469    |
| 2,000,000         | Minneapolis, Single Family Rev. Bonds (Phase V),<br>FNMA Coll. & GNMA Coll., 6 1/4s, 4/1/22                           | Aaa          | 2,147,500    |
| 3,050,000         | Minneapolis, Special G.O. Bonds (School Dist. No. 1),<br>5s, 2/1/12   | Aa           | 3,103,375    |
| 530,000           | Minneapolis-St. Paul, Hsg. Fin. Board Single Fam. Mtge.<br>Rev. Bonds (Phase VI), Ser. A, GNMA Coll.,<br>8.3s, 8/1/21 | AAA          | 541,358      |
| 4,000,000         | Minneapolis & St. Paul, Hsg. & Redev. Auth. Hlthcare<br>Syst. Rev. Bonds<br>(Group Hlth. Plan, Inc.), 6.9s, 12/1/22   | A            | 4,425,000    |
| 2,000,000         | (HlthOne Obligated Group), Ser. A, MBIA,<br>6 3/4s, 8/15/14   | Aaa          | 2,137,500    |
| 1,000,000         | (Children's Hlthcare), Ser. A, FSA, 5.7s, 8/15/16   | Aaa          | 1,055,000    |
| 2,715,000         | Minnetonka, Indpt. Rev. Bonds (School Dist. No. 276),<br>Ser. B, 5 3/4s, 2/1/22                                       | Aa           | 2,864,325    |
|                   | MN Agricultural & Econ. Dev. Board Rev. Bonds<br>(Small Bus. Dev. Loan Program)                                       |              |              |
| 575,000           | Ser. E-Lot 1, 8 1/2s, 8/1/10  | BB/P         | 588,139      |
| 400,000           | Ser. A-Lot 2, 8.2s, 8/1/09  | BB/P         | 409,144      |
| 750,000           | Ser. B-Lot 1, 7s, 8/1/16  | BB/P         | 797,813      |
| 3,000,000         | MN Agricultural & Econ. Dev. Board Rev. Bonds<br>(Fairview Hosp), Ser. A, MBIA, 5 1/2s, 11/15/17                      | Aaa          | 3,146,250    |
|                   | MN Pub. Fac. Auth. Wtr. Poll. Control Rev. Bonds  |              |              |
| 1,500,000         | Ser. A, 6.95s, 3/1/13   | Aaa          | 1,640,625    |
| 3,000,000         | Ser. A, 6 1/2s, 3/1/14  | Aaa          | 3,300,000    |
| 3,000,000         | Ser. B, 5s, 3/1/18  | Aaa          | 3,007,500    |
| 2,245,000         | Ser. B, 5s, 3/1/17  | Aaa          | 2,256,225    |
| 1,000,000         | MN State G.O. Bonds, 6s, 8/1/05   | Aaa          | 1,108,750    |
| 3,000,000         | MN State Duluth Arpt. Tax Increment G.O. Bonds,<br>Ser. 95A, 6 1/4s, 8/1/14   | Aa           | 3,247,500    |
|                   | MN State Higher Ed. Fac. Auth. Rev. Bonds   |              |              |
| 1,000,000         | (U. St. Thomas), Ser. 3-C, 7 1/8s, 9/1/14   | A            | 1,077,500    |
| 580,000           | (U. St. Thomas), Ser. 4-P, 5.4s, 4/1/23   | A            | 586,525      |
| 1,000,000         | (St. Johns U.), Ser. 4-L, 5.35s, 10/1/17  | A            | 1,011,250    |
|                   | MN State Hsg. Fin. Agcy. Single Fam. Mtge. Rev. Bonds   |              |              |
| 1,640,000         | Ser. B-1, 6 3/4s, 1/1/26  | Aa           | 1,750,700    |
| 975,000           | Ser. Q, 6.7s, 1/1/17  | Aa           | 1,059,094    |

|            |  |       |             |
|------------|--|-------|-------------|
| 5,000,000  | MN State Hsg. Fin. Agcy. Single Fam. Rev. Bonds,<br>Ser. E, 6.85s, 1/1/24  | Aa    | 5,368,750   |
| 1,500,000  | MN State Hsg. Fin. Agcy. Dev. Rev. Bonds, Ser. A,<br>6.95s, 2/1/14   | A     | 1,593,750   |
| 1,000,000  | Monticello, Big Lake Cmnty. Hosp. Dist. Rev. Bonds<br>(Hlthcare Fac.), Ser. A, 5 3/4s, 12/1/19                           | BBB/P | 997,500     |
| 250,000    | Morris Hosp. Fac. Rev. Bonds (Stevens Cmnty.,<br>Memorial Hosp.)<br>Ser. A, 8 1/4s, 5/1/10                               | AAA/P | 271,875     |
| 500,000    | Ser. B, 8 1/4s, 5/1/10   | AAA/P | 543,750     |
| 1,000,000  | North Branch, MN Indpt. G.O. Bonds (School Dist.<br>No. 138), Ser. A, FGIC, 5 1/2s, 2/1/12                               | Aaa   | 1,047,500   |
| 2,000,000  | North St. Paul, Maplewood Indpt. Sch. Dist. No. 622<br>G.O. Bonds, Ser. A, MBIA<br>7.1s, 2/1/19                          | Aaa   | 2,327,500   |
| 3,000,000  | 6 7/8s, 2/1/15   | Aaa   | 3,472,500   |
| 600,000    | North Suburban Hospital Dist. VRDN (Anoka &<br>Ramsey Cnty. Hosp., Hlth. Ctr.), 3.8s, 8/1/14                             | AA    | 600,000     |
| 2,000,000  | Northern MN Muni. Pwr. Agcy. Rev. Bonds<br>Ser. A, 7 1/4s, 1/1/16  | A     | 2,078,460   |
| 2,450,000  | FSA, 5 1/2s, 1/1/07  | Aaa   | 2,639,875   |
| 1,000,000  | Northfield, College Fac. Rev. Bonds<br>(St. Olaf College), 6.4s, 10/1/21   | A     | 1,066,250   |
| 1,230,000  | Northfield, Hlthcare Fac. Rev. Bonds<br>(Retirement Ctr.), Ser. A<br>6s, 5/1/28  | BB/P  | 1,236,150   |
| 690,000    | 5 3/4s, 5/1/16   | BB/P  | 693,450     |
| 1,160,000  | Ramsey Cnty., G.O. Bonds, Ser. A, 5 3/8s, 2/1/16   | Aaa   | 1,184,650   |
| 3,000,000  | Rochester Hlthcare Fac. IFB (Mayo Foundation)<br>Ser. E, 9.37s, 11/15/12   | AA    | 3,292,500   |
| 3,300,000  | Ser. H, 9.081s, 11/15/15 (SEG)   | AA    | 3,823,875   |
| 4,000,000  | Rochester, Hlthcare Fac. Rev. Bonds<br>(Olmsted Med. Group), 7 1/2s, 7/1/19  | BB/P  | 4,390,000   |
| 2,440,000  | Rochester, Indpt. Sch. G.O. Bonds (Dist. No. 535),<br>Ser. A, 5 1/4s, 2/1/15   | Aaa   | 2,507,100   |
| 2,500,000  | Sartell Poll. Control Rev. Bonds (Champion Intl.),<br>6.95s, 10/1/12   | Baa   | 2,731,250   |
| 2,500,000  | SCA Multi-Fam. Mtge. Rev. Bonds (Burnsville),<br>Ser. A-9, FSA, 7.1s, 1/1/30   | Aaa   | 2,796,875   |
| 1,240,000  | Southern MN Muni. Pwr. Agcy. Syst. Rev. Bonds<br>Ser. B, 5s, 1/1/13  | A     | 1,236,900   |
| 10,000,000 | MBIA, zero %, 1/1/20   | Aaa   | 3,350,000   |
| 1,760,000  | Spring Lake Park, Indpt. Rev. Bonds (School Dist.<br>No. 16), MBIA, 5 1/4s, 2/1/17                                       | Aaa   | 1,786,400   |
| 2,400,000  | St. Cloud, Hosp. Fac. Rev. Bonds, Ser. C, AMBAC,<br>6 3/4s, 7/1/11   | Aaa   | 2,634,000   |
| 3,500,000  | St. Paul, Hsg. & Hosp. Redev. Auth. Rev.<br>Bonds (Hltheast)<br>Ser. A, 6 5/8s, 11/1/17                                  | Baa   | 3,780,000   |
| 1,000,000  | Ser. B, 5.85s, 11/1/17   | Baa   | 1,023,750   |
| 500,000    | Ser. A, 5.7s, 11/1/15  | Baa   | 509,375     |
| 2,475,000  | St. Paul, Indpt. COP (School Dist. No. 625),<br>Ser. C, 5 1/4s, 2/1/16   | Aa    | 2,521,406   |
| 3,500,000  | Todd Morrison & Stearns Cntys., Indpt. (School Dist.<br>No. 2753) G.O. Bonds (School Dist. No. 625),<br>MBIA, 5s, 4/1/17 | Aaa   | 3,500,000   |
| 1,000,000  | U. of MN Rev. Bonds, Ser. A<br>5 3/4s, 7/1/18  | Aa    | 1,098,750   |
| 3,000,000  | 5 1/2s, 7/1/08   | Aa    | 3,255,000   |
| 4,310,000  | Western MN Muni. Pwr. Agcy. Rev. Bonds, Ser. A,<br>AMBAC, 6 1/4s, 1/1/06   | Aaa   | 4,832,587   |
|            |  |       | -----       |
|            |  |       | 140,425,001 |

Puerto Rico (2.5%)

|           |   |     |               |
|-----------|---|-----|---------------|
| 2,150,000 | Cmnwlth. of PR, G.O. Bonds, MBIA, 6 1/4s, 7/1/12                              | Aaa | 2,499,375     |
| 1,000,000 | Cmnwlth. of PR, Hwy. Trans. Auth. Rev. Bonds, Ser. Y,<br>MBIA, 6 1/4s, 7/1/13 | AAA | 1,161,250     |
|           |   |     | -----         |
|           |   |     | 3,660,625     |
|           |   |     | -----         |
|           | Total Investments (cost \$134,855,213) (b)                                    |     | \$144,085,626 |

(a) Percentages indicated are based on net assets of \$146,398,329.

(RAT) The Moody's or Standard & Poor's ratings indicated are believed to be the most recent ratings available at May 31, 1998 for the securities listed. Ratings are generally ascribed to securities at the time of issuance. While the agencies may from time to time revise such ratings, they undertake no obligation to do so, and the ratings do not necessarily represent what the agencies would ascribe to these securities at May 31, 1998. Securities rated by Putnam are indicated by "P" and are not publicly rated. Ratings are not covered by the Report of independent accountants.

(b) The aggregate identified cost on a tax basis is \$134,855,213, resulting in gross unrealized appreciation and depreciation of \$9,388,084 and \$157,671, respectively, or net unrealized appreciation of \$9,230,413.

(SEG) A portion of this security was pledged and segregated with the custodian to cover margin requirements for futures contracts at May 31, 1998.

The rates shown on Floating Rate Bonds (FRB) are the current interest rates at May 31, 1998 which are subject to change based on the terms of the security.

The rates shown on IFB, which are securities paying interest rates that vary inversely to changes in the market interest rates, and VRDN's are the current interest rates at May 31, 1998.

The fund had the following industry group concentrations greater than 10% at May 31, 1998 (as a percentage of net assets):

|             |       |
|-------------|-------|
| Health care | 26.9% |
| Housing     | 11.7  |

The fund had the following insurance concentration greater than 10% at May 31, 1998 (as a percentage of net assets):

|      |       |
|------|-------|
| MBIA | 16.0% |
|------|-------|

-----  
Futures Contracts Outstanding at May 31, 1998

|                             | Total Market Value | Aggregate Face Value | Expiration Date | Unrealized Appreciation/ (Depreciation) |
|-----------------------------|--------------------|----------------------|-----------------|---|
| Municipal Bond Index (long) | \$ 4,590,313       | \$ 4,502,000         | Jun-98          | \$ 88,313                               |
| U.S. Treasury Notes (short) | 12,293,594         | 12,152,656           | Jun-98          | (140,938)                               |
|                             |                    |                      |                 | \$ (52,625)                             |

-----

The accompanying notes are an integral part of these financial statements.

</TABLE>

<TABLE>  
<CAPTION>

Statement of assets and liabilities  
May 31, 1998

| <S>  | <C>                |
|--|--------------------|
| <b>Assets</b>  |                    |
| Investments in securities, at value (identified cost \$134,855,213) (Note 1) | \$144,085,626      |
| Cash   | 939,447            |
| Interest and other receivables   | 2,337,819          |
| Receivable for shares of the fund sold                                       | 456,260            |
| <b>Total assets</b>  | <b>147,819,152</b> |
| <b>Liabilities</b>   |                    |
| Payable for variation margin   | 18,313             |
| Distributions payable to shareholders  | 259,045            |
| Payable for securities purchased   | 500,000            |
| Payable for shares of the fund repurchased                                   | 271,718            |
| Payable for compensation of Manager (Note 2)                                 | 221,610            |
| Payable for investor servicing and custodian fees (Note 2)                   | 30,040             |
| Payable for compensation of Trustees (Note 2)                                | 7,517              |
| Payable for administrative services (Note 2)                                 | 1,017              |
| Payable for distribution fees (Note 2)                                       | 66,526             |
| Other accrued expenses   | 45,037             |
| <b>Total liabilities</b>   | <b>1,420,823</b>   |

-----

|   |               |
|---|---------------|
| Net assets  | \$146,398,329 |
| Represented by  |               |
| Paid-in capital (Notes 1 and 4)   | \$140,578,486 |
| Undistributed net investment income (Note 1)                              | 5,569         |
| Accumulated net realized loss on investments (Note 1)                     | (3,363,514)   |
| Net unrealized appreciation of investments                                | 9,177,788     |
| Total -- Representing net assets applicable to capital shares outstanding | \$146,398,329 |

Computation of net asset value and offering price

|  |        |
|--|--------|
| Net asset value and redemption price per class A share<br>(\$100,806,003 divided by 10,965,356 shares) | \$9.19 |
| Offering price per class A share (100/95.25 of \$9.19)*  | \$9.65 |
| Net asset value and offering price per class B share<br>(\$44,100,128 divided by 4,812,654 shares) +   | \$9.16 |
| Net asset value and redemption price per class M share<br>(\$1,492,198 divided by 162,409 shares)      | \$9.19 |
| Offering price per class M share (100/96.75 of \$9.19)**   | \$9.50 |

\* On single retail sales of less than \$25,000. On sales of \$25,000 or more and on group sales the offering price is reduced.

\*\* On single retail sales of less than \$50,000. On sales of \$50,000 or more and on group sales the offering price is reduced.

+ Redemption price per share is equal to net asset value less any applicable contingent deferred sales charge.

The accompanying notes are an integral part of these financial statements.

</TABLE>

<TABLE>  
<CAPTION>

Statement of operations  
Year ended May 31, 1998

|                             |              |
|-----------------------------|--------------|
| <S>                         | <C>          |
| Tax exempt interest income: | \$ 8,359,615 |

Expenses:

|  |           |
|--|-----------|
| Compensation of Manager (Note 2)               | 856,443   |
| Investor servicing and custodian fees (Note 2) | 202,234   |
| Compensation of Trustees (Note 2)              | 8,109     |
| Administrative services (Note 2)               | 6,180     |
| Distribution fees -- Class A (Note 2)          | 203,841   |
| Distribution fees -- Class B (Note 2)          | 336,512   |
| Distribution fees -- Class M (Note 2)          | 7,684     |
| Reports to shareholders                        | 17,812    |
| Registration fees                              | 1,374     |
| Auditing                                       | 28,495    |
| Legal  | 17,161    |
| Postage  | 12,012    |
| Other  | 7,635     |
| Total expenses                                 | 1,705,492 |

|  |              |
|--|--------------|
| Expense reduction (Note 2)   | (72,782)     |
| Net expenses   | 1,632,710    |
| Net investment income  | 6,726,905    |
| Net realized loss on investments (Notes 1 and 3)                                 | (237,680)    |
| Net realized loss on futures contracts (Note 1)                                  | (1,040,223)  |
| Net unrealized appreciation of investments and futures contracts during the year | 5,048,065    |
| Net gain on investments  | 3,770,162    |
| Net increase in net assets resulting from operations                             | \$10,497,067 |

The accompanying notes are an integral part of these financial statements.

</TABLE>

<TABLE>  
<CAPTION>

Statement of changes in net assets

|   | Year ended May 31 |               |
|---|-------------------|---------------|
|   | 1998              | 1997          |
|   | <C>               | <C>           |
| Increase in net assets  |                   |               |
| Operations:   |                   |               |
| Net investment income   | \$ 6,726,905      | \$ 6,770,788  |
| Net realized gain (loss) on investments   | (1,277,903)       | 460,729       |
| Net unrealized appreciation of investments  | 5,048,065         | 2,249,425     |
| Net increase in net assets resulting from operations  | 10,497,067        | 9,480,942     |
| Distributions to shareholders:  |                   |               |
| From net investment income  |                   |               |
| Class A   | (5,020,689)       | (5,182,778)   |
| Class B   | (1,688,604)       | (1,529,534)   |
| Class M   | (71,593)          | (49,476)      |
| Increase from capital share transactions (Note 4)   | 7,935,353         | 4,855,431     |
| Total increase in net assets  | 11,651,534        | 7,574,585     |
| Net assets  |                   |               |
| Beginning of year   | 134,746,795       | 127,172,210   |
| End of year (including undistributed net investment income of \$5,569 and \$59,550, respectively) | \$146,398,329     | \$134,746,795 |

The accompanying notes are an integral part of these financial statements.

</TABLE>

<TABLE>  
<CAPTION>

Financial highlights  
(For a share outstanding throughout the period)

CLASS A

Per-share  
operating performance

Year ended May 31

|  | 1998      | 1997     | 1996     | 1995     | 1994     |
|--|-----------|----------|----------|----------|----------|
| <S>  | <C>       | <C>      | <C>      | <C>      | <C>      |
| Net asset value, beginning of period                     | \$8.95    | \$8.76   | \$8.95   | \$8.79   | \$9.06   |
| Investment operations                                    |           |          |          |          |          |
| Net investment income                                    | .45       | .47      | .47      | .51      | .51      |
| Net realized and unrealized gain (loss) on investments   | .24       | .19      | (.19)    | .15      | (.27)    |
| Total from investment operations                         | .69       | .66      | .28      | .66      | .24      |
| Less distributions:                                      |           |          |          |          |          |
| From net investment income                               | (.45)     | (.47)    | (.47)    | (.50)    | (.51)    |
| Total distributions                                      | (.45)     | (.47)    | (.47)    | (.50)    | (.51)    |
| Net asset value, end of period                           | \$9.19    | \$8.95   | \$8.76   | \$8.95   | \$8.79   |
| Ratios and supplemental data                             |           |          |          |          |          |
| Total investment return at net asset value (%) (a)       | 7.90      | 7.73     | 3.16     | 7.90     | 2.57     |
| Net assets, end of period (in thousands)                 | \$100,806 | \$98,307 | \$96,110 | \$98,418 | \$95,587 |
| Ratio of expenses to average net assets (%) (b)          | 1.01      | 1.03     | 1.01     | .99      | 1.03     |
| Ratio of net investment income to average net assets (%) | 4.89      | 5.32     | 5.26     | 5.85     | 5.60     |
| Portfolio turnover (%)                                   | 10.67     | 50.80    | 109.85   | 58.18    | 28.19    |

+ Commencement of operations.

\* Not annualized.

(a) Total investment return assumes dividend reinvestment and does not reflect the effect of sales charges.

(b) The ratio of expenses to average net assets for the year ended May 31, 1996 and thereafter, includes amounts paid through expense offset arrangements. Prior period ratios exclude these amounts (Note 2).

</TABLE>

<TABLE>  
<CAPTION>

Financial highlights  
(For a share outstanding throughout the period)

CLASS B

| Per-share operating performance                        | Year ended May 31 |        |        |        | For the period July 15, 1993+ to May 31 |
|--|-------------------|--------|--------|--------|---|
|  | 1998              | 1997   | 1996   | 1995   | 1994                                    |
| <S>  | <C>               | <C>    | <C>    | <C>    | <C>                                     |
| Net asset value, beginning of period                   | \$8.92            | \$8.73 | \$8.92 | \$8.77 | \$9.18                                  |
| Investment operations                                  |                   |        |        |        |   |
| Net investment income                                  | .39               | .41    | .41    | .45    | .39                                     |
| Net realized and unrealized gain (loss) on investments | .24               | .19    | (.19)  | .15    | (.41)                                   |
| Total from investment operations                       | .63               | .60    | .22    | .60    | (.02)                                   |

| Less distributions:            |        |        |        |        |        |
|--------------------------------|--------|--------|--------|--------|--------|
| From net investment income     | (.39)  | (.41)  | (.41)  | (.45)  | (.39)  |
| Total distributions            | (.39)  | (.41)  | (.41)  | (.45)  | (.39)  |
| Net asset value, end of period | \$9.16 | \$8.92 | \$8.73 | \$8.92 | \$8.77 |

Ratios and supplemental data

|  |          |          |          |          |         |
|--|----------|----------|----------|----------|---------|
| Total investment return at net asset value (%) (a)       | 7.20     | 7.04     | 2.49     | 7.17     | (.32)*  |
| Net assets, end of period (in thousands)                 | \$44,100 | \$35,333 | \$30,149 | \$19,698 | \$8,873 |
| Ratio of expenses to average net assets (%) (b)          | 1.66     | 1.68     | 1.67     | 1.63     | 1.47*   |
| Ratio of net investment income to average net assets (%) | 4.22     | 4.67     | 4.57     | 5.15     | 4.23*   |
| Portfolio turnover (%)                                   | 10.67    | 50.80    | 109.85   | 58.18    | 28.19   |

+ Commencement of operations.

\* Not annualized.

(a) Total investment return assumes dividend reinvestment and does not reflect the effect of sales charges.

(b) The ratio of expenses to average net assets for the year ended May 31, 1996 and thereafter, includes amounts paid through expense offset arrangements. Prior period ratios exclude these amounts (Note 2).

</TABLE>

<TABLE>  
<CAPTION>

Financial highlights  
(For a share outstanding throughout the period)

CLASS M

| Per-share operating performance                        | Year ended May 31 |        |        | For the period April 3, 1995+ to May 31 |  |
|--|-------------------|--------|--------|---|--|
|  | 1998              | 1997   | 1996   | 1995                                    |  |
| Net asset value, beginning of period                   | \$8.94            | \$8.76 | \$8.95 | \$8.77                                  |  |
| Investment operations                                  |                   |        |        |   |  |
| Net investment income                                  | .42               | .45    | .43    | .08                                     |  |
| Net realized and unrealized gain (loss) on investments | .26               | .18    | (.18)  | .17                                     |  |
| Total from investment operations                       | .68               | .63    | .25    | .25                                     |  |
| Less distributions:                                    |                   |        |        |   |  |
| From net investment income                             | (.43)             | (.45)  | (.44)  | (.07)                                   |  |
| Total distributions                                    | (.43)             | (.45)  | (.44)  | (.07)                                   |  |
| Net asset value, end of period                         | \$9.19            | \$8.94 | \$8.76 | \$8.95                                  |  |
| Ratios and supplemental data                           |                   |        |        |   |  |
| Total investment return at net asset value (%) (a)     | 7.70              | 7.29   | 2.82   | 2.89*                                   |  |

|   |         |         |        |       |
|---|---------|---------|--------|-------|
| Net assets, end of period<br>(in thousands)                 | \$1,492 | \$1,106 | \$913  | \$1   |
| Ratio of expenses to<br>average net assets (%) (b)          | 1.31    | 1.33    | 1.32   | .21*  |
| Ratio of net investment income<br>to average net assets (%) | 4.64    | 5.01    | 4.72   | .93*  |
| Portfolio turnover (%)                                      | 10.67   | 50.80   | 109.85 | 58.18 |

+ Commencement of operations.

\* Not annualized.

(a) Total investment return assumes dividend reinvestment and does not reflect the effect of sales charges.

(b) The ratio of expenses to average net assets for the year ended May 31, 1996 and thereafter, includes amounts paid through expense offset arrangements. Prior period ratios exclude these amounts (Note 2).

</TABLE>

Notes to financial statements  
May 31, 1998

Note 1  
Significant accounting policies

Putnam Minnesota Tax Exempt Income Fund (the "fund") is registered under the Investment Company Act of 1940, as amended, as a diversified, open-end management investment company. The fund seeks as high a level of current income exempt from federal income tax and Minnesota personal income tax as the fund's Manager, Putnam Investment Management, Inc. ("Putnam Management"), a wholly-owned subsidiary of Putnam Investments, Inc., believes is consistent with preservation of capital by investing primarily in a portfolio of Minnesota tax-exempt securities.

The fund offers class A, class B and class M shares. Class A shares are sold with a maximum front-end sales charge of 4.75%. Class B shares, which convert to class A shares within approximately six to eight years, do not pay a front-end sales charge, but pay a higher ongoing distribution fee than class A shares, and are subject to a contingent deferred sales charge, if those shares are redeemed within six years of purchase. Class M shares are sold with a maximum front-end sales charge of 3.25% and pay an ongoing distribution fee that is lower than class B shares and higher than class A shares.

Expenses of the fund are borne pro-rata by the holders of each class of shares, except that each class bears expenses unique to that class (including the distribution fees applicable to such class). Each class votes as a class only with respect to its own distribution plan or other matters on which a class vote is required by law or determined by the Trustees.

Shares of each class would receive their pro-rata share of the net assets of the fund, if the fund were liquidated. In addition, the Trustees declare separate dividends on each class of shares.

The following is a summary of significant accounting policies consistently followed by the fund in the preparation of its financial statements. The preparation of financial statements is in conformity with generally accepted accounting principles and requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. Actual results could differ from those estimates.

A) Security valuation Tax-exempt bonds and notes are stated on the basis of valuations provided by a pricing service, approved by the Trustees, which uses information with respect to transactions in bonds, quotations from bond dealers, market transactions in comparable securities and various relationships between securities in determining value.

B) Security transactions and related investment income Security transactions are accounted for on the trade date (date the order to buy or sell is executed). Interest income is recorded on the accrual basis.

C) Futures and options contracts The fund may use futures and options contracts to hedge against changes in the values of securities the fund owns or expects to purchase. The fund may also write options on securities it owns or in which it may invest to increase its current returns.

The potential risk to the fund is that the change in value of futures and options contracts may not correspond to the change in value of the hedged instruments. In addition, losses may arise from changes in the value of the underlying instruments, if there is an illiquid secondary market for the

contracts, or if the counterparty to the contract is unable to perform. When the contract is closed, the fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value at the time it was closed. Realized gains and losses on purchased options are included in realized gains and losses on investment securities.

Futures contracts are valued at the quoted daily settlement prices established by the exchange on which they trade. Exchange traded options are valued at the last sale price, or if no sales are reported, the last bid price for purchased options and the last ask price for written options. Options traded over-the-counter are valued using prices supplied by dealers.

D) Line of credit The fund has entered into a committed line of credit with certain banks. This line of credit agreement includes restrictions that the fund maintain an asset coverage ratio of at least 300% and borrowings must not exceed prospectus limitations. For the year ended May 31, 1998, the fund had no borrowings against the line of credit.

E) Federal taxes It is the policy of the fund to distribute all of its income within the prescribed time and otherwise comply with the provisions of the Internal Revenue Code applicable to regulated investment companies. It is also the intention of the fund to distribute an amount sufficient to avoid imposition of any excise tax under Section 4982 of the Internal Revenue Code of 1986, as amended. Therefore, no provision has been made for federal taxes on income, capital gains or unrealized appreciation on securities held nor for excise tax on income and capital gains.

At May 31, 1998, the fund had a capital loss carryover of approximately \$1,719,000 available to offset future capital gains, if any. The amount of the carryover and the expiration dates are:

| Loss Carryover | Expiration   |
|----------------|--------------|
| -----          | -----        |
| \$723,000      | May 31, 2003 |
| 832,000        | May 31, 2004 |
| 164,000        | May 31, 2006 |

F) Distributions to shareholders Distributions to shareholders from net investment income are recorded by the fund on the ex-dividend date. Capital gain distributions, if any, are recorded on the ex-dividend date and paid at least annually. The amount and character of income and gains to be distributed are determined in accordance with income tax regulations which may differ from generally accepted accounting principles. These differences include temporary and permanent differences of post October losses, dividends payable and unrealized gains and losses on certain futures contracts. Reclassifications are made to the fund's capital accounts to reflect income and gains available for distribution (or available capital loss carryovers) under income tax regulations. For the year ended May 31, 1998, the fund required no such reclassifications.

G) Amortization of bond premium and accretion of bond discount Any premium resulting from the purchase of securities in excess of maturity value is amortized on a yield-to-maturity basis. Discounts on zero coupon bonds and original issue discount bonds are accreted according to the yield-to-maturity basis.

#### Note 2

Management fee, administrative services and other transactions

Compensation of Putnam Management, for management and investment advisory services is paid quarterly based on the average net assets of the fund. Such fee is based on the following annual rates: 0.60% of the first \$500 million of average net assets, 0.50% of the next \$500 million, 0.45% of the next \$500 million, 0.40% of the next \$5 billion, 0.375% of the next \$5 billion, 0.355% of the next \$5 billion, 0.34% of the next \$5 billion, and 0.33% thereafter.

The fund reimburses Putnam Management an allocated amount for the compensation and related expenses of certain officers of the fund and their staff who provide administrative services to the fund. The aggregate amount of all such reimbursements is determined annually by the Trustees.

Custodial functions for the fund's assets are provided by Putnam Fiduciary Trust Company (PFTC), a subsidiary of Putnam Investments, Inc. Investor servicing agent functions are provided by Putnam Investor Services, a division of PFTC.

For the year ended May 31, 1998, fund expenses were reduced by \$72,782 under expense offset arrangements with PFTC. Investor servicing and custodian fees reported in the Statement of operations exclude these credits. The fund could have invested a portion of the assets utilized in connection with the expense offset arrangements in an income producing asset if it had not entered into such arrangements.

Each Trustee of the fund receives an annual Trustee fee, of which \$330 has

been allocated to the fund, and an additional fee for each Trustee's meeting attended. Trustees who are not interested persons of Putnam Management and who serve on committees of the Trustees receive additional fees for attendance at certain committee meetings.

The fund has adopted a Trustee Fee Deferral Plan (the "Deferral Plan") which allows the Trustees to defer the receipt of all or a portion of Trustees Fees payable on or after July 1, 1995. The deferred fees remain in the fund and are invested in certain Putnam funds until distribution in accordance with the Deferral Plan.

The fund has adopted an unfunded noncontributory defined benefit pension plan (the "Pension Plan") covering all Trustees of the fund who have served as Trustee for at least five years. Benefits under the Pension Plan are equal to 50% of the Trustee's average total retainer and meeting fees for the three years preceding retirement. Pension expense for the fund is included in Compensation of Trustees in the Statement of operations. Accrued pension liability is included in Payable for compensation of Trustees in the Statement of assets and liabilities.

The fund has adopted distribution plans (the "Plans") with respect to its class A, class B and class M shares pursuant to Rule 12b-1 under the Investment Company Act of 1940. The purpose of the Plans is to compensate Putnam Mutual Funds Corp., a wholly-owned subsidiary of Putnam Investments Inc., for services provided and expenses incurred by it in distributing shares of the fund. The Plans provide for payments by the fund to Putnam Mutual Funds Corp. at an annual rate up to 0.35%, 1.00% and 1.00% of the average net assets attributable to class A, class B and class M shares, respectively. The Trustees currently limit payment by the fund to an annual rate of 0.20%, 0.85% and 0.50% of the average net assets attributable to class A, class B and class M shares respectively.

For the year ended May 31, 1998, Putnam Mutual Funds Corp., acting as underwriter received net commissions of \$17,156 and \$161 from the sale of class A and class M shares, respectively, and \$67,726 in contingent deferred sales charges from redemptions of class B shares. A deferred sales charge of up to 1% is assessed on certain redemptions of class A shares that were purchased without an initial sales charge as part of an investment of \$1 million or more. For the year ended May 31, 1998, Putnam Mutual Funds Corp., acting as underwriter received \$10,651 on class A redemptions.

Note 3  
Purchases and sales of securities

During the year ended May 31, 1998, purchases and sales of investment securities other than short-term investments aggregated \$24,067,832 and \$14,668,392, respectively. There were no purchases and sales of U.S. government obligations. In determining the net gain or loss on securities sold, the cost of securities has been determined on the identified cost basis.

Note 4  
Capital shares

At May 31, 1998, there was an unlimited number of shares of beneficial interest authorized. Transactions in capital shares were as follows:

|  | Year ended<br>May 31, 1998 |              |
|--|----------------------------|--------------|
| Class A  | Shares                     | Amount       |
| Shares sold  | 1,312,937                  | \$12,011,038 |
| Shares issued in connection with reinvestment of distributions | 370,581                    | 3,391,346    |
|  | 1,683,518                  | 15,402,384   |
| Shares repurchased   | (1,703,692)                | (15,576,477) |
| Net decrease   | (20,174)                   | \$ (174,093) |

|                                  | Year ended<br>May 31, 1997 |              |
|----------------------------------|----------------------------|--------------|
| Class A                          | Shares                     | Amount       |
| Shares sold                      | 1,283,188                  | \$11,437,737 |
| Shares issued in connection with |                            |              |

|                               |             |              |
|-------------------------------|-------------|--------------|
| reinvestment of distributions | 389,142     | 3,468,329    |
|                               | 1,672,330   | 14,906,066   |
| Shares repurchased            | (1,654,928) | (14,754,582) |
| Net increase                  | 17,402      | \$ 151,484   |

Year ended  
May 31, 1998

| Class B  | Shares    | Amount       |
|--|-----------|--------------|
| Shares sold  | 1,212,364 | \$11,053,422 |
| Shares issued in connection with reinvestment of distributions | 123,282   | 1,124,947    |
|  | 1,335,646 | 12,178,369   |
| Shares repurchased   | (484,197) | (4,416,317)  |
| Net increase   | 851,449   | \$ 7,762,052 |

Year ended  
May 31, 1997

| Class B  | Shares    | Amount       |
|--|-----------|--------------|
| Shares sold  | 790,026   | \$ 7,019,605 |
| Shares issued in connection with reinvestment of distributions | 111,269   | 988,567      |
|  | 901,295   | 8,008,172    |
| Shares repurchased   | (391,861) | (3,478,216)  |
| Net increase   | 509,434   | \$4,529,956  |

Year ended  
May 31, 1998

| Class M  | Shares   | Amount    |
|--|----------|-----------|
| Shares sold  | 81,529   | \$740,471 |
| Shares issued in connection with reinvestment of distributions | 7,025    | 64,302    |
|  | 88,554   | 804,773   |
| Shares repurchased   | (49,798) | (457,379) |
| Net increase   | 38,756   | \$347,394 |

Year ended  
May 31, 1997

| Class M  | Shares | Amount    |
|--|--------|-----------|
| Shares sold  | 21,421 | \$191,695 |
| Shares issued in connection with reinvestment of distributions | 5,478  | 48,811    |
|  | 26,899 | 240,506   |

|                    |         |           |
|--------------------|---------|-----------|
| Shares repurchased | (7,453) | (66,515)  |
| -----              |         |           |
| Net increase       | 19,446  | \$173,991 |
| -----              |         |           |

Federal tax information  
(Unaudited)

The fund has designated 100% of dividends paid from net investment income during the fiscal year as tax exempt for Federal income tax purposes.

The Form 1099 you receive in January 1999 will show the tax status of all distributions paid to your account in calendar 1998.

PUTNAM GROWTH FUNDS

Asia Pacific Growth Fund

Capital Appreciation Fund [DOUBLE DAGGER]

Capital Opportunities Fund

Diversified Equity Trust

Europe Growth Fund

Global Growth Fund

Global Natural Resources Fund

Growth Opportunities Fund

Health Sciences Trust

International Growth Fund

International New Opportunities Fund

Investors Fund

New Opportunities Fund [DOUBLE DAGGER]

OTC & Emerging Growth Fund

Research Fund

Vista Fund

Voyager Fund

Voyager Fund II

PUTNAM GROWTH  
AND INCOME FUNDS

Balanced Retirement Fund

Convertible Income-Growth Trust

Equity Income Fund

The George Putnam Fund of Boston

Global Growth and Income Fund

The Putnam Fund for Growth and Income

Growth and Income Fund II

International Growth and Income Fund

New Value Fund

Utilities Growth and Income Fund

PUTNAM INCOME FUNDS

American Government Income Fund

Diversified Income Trust

Strategic Income Fund \*

High Quality Bond Fund +

Global Governmental Income Trust

High Yield Advantage Fund [DOUBLE DAGGER]

High Yield Total Return Fund

High Yield Trust [DOUBLE DAGGER]

High Yield Trust II

Income Fund

Money Market Fund \*\*

Intermediate U.S. Government  
Income Fund

Preferred Income Fund

U.S. Government Income Trust

PUTNAM TAX-FREE  
INCOME FUNDS

Municipal Income Fund

Tax Exempt Income Fund

Tax Exempt Money Market Fund \*\*

Tax-Free High Yield Fund

Tax-Free Insured Fund

State tax-free income funds [SECTION MARK]

Arizona, California, Florida, Massachusetts,  
Michigan, Minnesota, New Jersey, New York,  
Ohio and Pennsylvania

State tax-free money market funds [SECTION MARK]

California, New York

LIFESTAGE SM FUNDS

Putnam Asset Allocation Funds—three investment  
portfolios that spread your money across a variety  
of stocks, bonds, and money market investments.

The three portfolios:

Asset Allocation: Balanced Portfolio

Asset Allocation: Conservative Portfolio

Asset Allocation: Growth Portfolio

\* Formerly Putnam Diversified Income Trust II

+ Formerly Putnam Federal Income Trust

[DOUBLE DAGGER] Closed to new investors. Some exceptions may apply.  
Contact Putnam for details.

[SECTION MARK] Not available in all states.

\*\* An investment in a money market fund is neither insured  
nor guaranteed by the U.S. government. These funds are  
managed to maintain a price of \$1.00 per share, although  
there is no assurance that this price will be maintained  
in the future.

Please call your financial advisor or Putnam at 1-800-225-1581 to  
obtain a prospectus for any Putnam fund. It contains more complete  
information, including charges and expenses. Please read it carefully  
before you invest or send money.

Fund information

INVESTMENT MANAGER

Putnam Investment  
Management, Inc.  
One Post Office Square  
Boston, MA 02109

MARKETING SERVICES

Putnam Mutual Funds Corp.  
One Post Office Square  
Boston, MA 02109

CUSTODIAN

Putnam Fiduciary Trust Company

LEGAL COUNSEL

Ropes & Gray

INDEPENDENT ACCOUNTANTS

PricewaterhouseCoopers LLP

TRUSTEES

George Putnam, Chairman  
William F. Pounds, Vice Chairman  
Jameson Adkins Baxter  
Hans H. Estin  
John A. Hill  
Ronald J. Jackson  
Paul L. Joskow  
Elizabeth T. Kennan  
Lawrence J. Lasser  
John H. Mullin III  
Robert E. Patterson  
Donald S. Perkins  
George Putnam, III  
A.J.C. Smith  
W. Thomas Stephens  
W. Nicholas Thorndike

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Executive Vice President

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Senior Vice President

John D. Hughes  
Senior Vice President and Treasurer

Lawrence J. Lasser  
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Vice President

Leslie J. Burke  
Vice President and Fund Manager

William N. Shiebler  
Vice President

John R. Verani

Vice President

Beverly Marcus  
Clerk and Assistant Treasurer

This report is for the information of shareholders of Putnam Minnesota Tax Exempt Income Fund. It may also be used as sales literature when preceded or accompanied by the current prospectus, which gives details of sales charges, investment objectives, and operating policies of the fund, and the most recent copy of Putnam's Quarterly Performance Summary. For more information or to request a prospectus, call toll free: 1-800-225-1581. You can also learn more at Putnam Investments' website: <http://www.putnaminv.com>.

Shares of mutual funds are not deposits or obligations of, or guaranteed or endorsed by, any financial institution; are not insured by the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve Board, or any other agency; and involve risk, including the possible loss of the principal amount invested.

[LOGO OMITTED]

PUTNAM INVESTMENTS

The Putnam Funds  
One Post Office Square  
Boston, Massachusetts 02109

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Bulk Rate  
U.S. Postage  
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Putnam  
Investments  
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