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Research Update:

Swedish Municipality of Orebro Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable

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Table Of Contents

Overview

Rating Action

Outlook

Rationale

Key Statistics

Ratings Score Snapshot

Key Sovereign Statistics

Related Criteria And Research

Ratings List

Research Update:

Swedish Municipality of Örebro Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable

Overview

- We expect that the Swedish municipality of Örebro will manage pressures on operating expenditures and higher investment needs stemming from the increasing population, and therefore continue demonstrating satisfactory budgetary performance in 2017-2019.
- Recognizing the city's extensive capital program over the coming years, we expect the city will tap its cash reserves to fund part of these investments, while maintaining a strong overall liquidity position, underpinned by its strong market access.
- We are affirming our 'AA+/A-1+' and 'K-1' ratings on Örebro.
- The stable outlook reflects our view that the city's financial management and liquidity will counterbalance any risks arising from heightened spending, investment needs, and demographic pressures.

Rating Action

On April 7, 2017, S&P Global Ratings affirmed its 'AA+' long-term and 'A-1+' short-term issuer credit ratings on the Swedish municipality of Örebro. The outlook remains stable.

At the same time, we affirmed our 'K-1' short-term Nordic regional scale rating on Örebro.

Outlook

The stable outlook reflects our expectation that through to year-end 2019 Örebro's financial management will remain committed to sound budgetary performance and moderate debt accumulation, while implementing its infrastructure spending via municipal companies. We also assume that the city's liquidity will remain strong.

Downside Scenario

The ratings could come under pressure if we observed that changes in Örebro's liquidity management and policies were leading to a significant deterioration of its liquidity position.

Upside Scenario

We could raise the ratings if we observed that Örebro's tighter control over operating spending was leading to notably stronger budgetary performance, with operating balances consistently higher than 5% of revenues and positive balances after capital accounts, resulting in structurally exceptional liquidity.

Rationale

The affirmation reflects our opinion that Örebro will continue to benefit from a very predictable and supportive institutional framework and its wealthy economy. In our view, these factors support Örebro's budgetary performance and its consistently sound liquidity position, despite increased expenditures and investment needs stemming from the city's rapidly growing population. Although we believe that debt-funded investments for the city and its company sector will result in higher debt over the next three years, we consider management's prudent approach to securing stable debt-servicing ability and strong liquidity to be central to our base case.

The supportive institutional framework and Örebro's wealthy economy underpin the ratings

Sweden's institutional framework for local and regional governments (LRGs) is a key strength for our ratings on Örebro. The framework displays a high degree of institutional stability, and we note that the main tools for balancing revenues and expenditures are Sweden's far-reaching equalization system and the autonomy LRGs enjoy in setting local taxes.

In an international comparison, Örebro's economy is very strong, being well balanced and having a dynamic industry structure, signaling its importance as a regional growth center. Örebro's expanding services sector and increased diversification have facilitated a more robust economic structure in recent years. However, because the Swedish equalization system significantly balances wealth levels among the LRGs, we use the 2016 national GDP per capita of \$52,200 as the starting point for our analysis.

We consider that Örebro has a prudent and competent financial management team, and a robust track record of budget execution. In particular, we expect Örebro's financial management will be able to navigate through a period of heightened spending with limited weakening of budgetary performance and only a moderate build-up of debt, due to good long-term planning, cost controls, and conservative debt and liquidity management. In addition, in our view, the municipality enjoys strong revenue flexibility from its asset-rich municipal companies, which report significant surplus values. We consider this revenue flexibility important in light of Örebro's fairly rigid expenditure structure, leading to our overall view of the municipality's budgetary flexibility as average. However, we would expect Örebro's management to use its flexibility to counteract any material budgetary deterioration, should it emerge.

Örebro's rapidly rising population poses fiscal challenges as investment needs and expenditure pressures build

Population growth in Örebro is expected to average a high 1.3% annually over the coming three years, leading to higher expenditure and the need for increased investment. As a result, we expect the city's budgetary performance will weaken slightly, but remain relatively sound over the next three years. In our base-case scenario for 2017-2019, we envisage Örebro's operating balance standing at 3.8% of adjusted operating revenues on average, with slight deficits after capital accounts. Moreover, we expect that during that period, the city will exercise sound cost

control to manage expenditure needs related to the increased demand for public services and changing demographics. We also note that the city's core investments are increasingly significant, signaling that overall municipal investment needs are substantial. In particular, we see a pick-up in investments related to building and refurbishing schools, following an assessment that the city needs to build one new school per year over the medium term to cater for the growing population. In addition, we observe a temporary elevation of investments in water and sewage in 2017 and 2018; although, in this regard we note that water and sewage activities are financed by user fees and mandated by specific legislation that ensures full cost compensation over time.

We note that 2016 was a financially strong year for Örebro. To address upcoming spending and investment needs, the city increased the local tax rate at the start of the year to strengthen its revenues. Furthermore, a series of onetime revenue items, most notably extensive capital revenues from land sales during the year, as well as central government grants for the reception of refugees and construction of housing, helped improve the balances after capital accounts. The positive developments on the revenue side counterbalanced our concerns about continued deficits related to social and home care.

Overall, the city closed 2016 with a surplus after capital accounts of 3% of total revenues. In assessing Örebro's budgetary performance, we take into account that a significant portion of investments in key municipal infrastructure, for example facilities for education, are carried out by the companies the city owns. This reduces the city's capital expenditure and artificially improves balances after capital accounts.

As a result of Örebro's comprehensive investment plans, we project that its debt metrics will worsen through to year-end 2019. The inclusion of the municipal companies' substantial revenues distorts our measure of Örebro's tax-supported debt. Consequently, we consider that the city's direct debt, which we forecast at about 140% of operating revenues in 2019 compared with about 122% in 2016, better reflects the risk associated with the external loans held at the city's treasury. We consider Örebro's housing entity, Örebro Bostäder, to be self-supporting, and regard the proportion of lending to this entity as material enough to have a positive effect on our assessment of the city's debt position.

Örebro holds large liquidity reserves following the replacement of Swedish krona (SEK) 2.2 billion (about €230 million) of onlent cash with external borrowing in 2014. We expect the city will draw on these reserves in the coming years to fund investments. Although the city's financing needs are on the increase, we consider that its competent and sophisticated debt management will be able to handle its expanding loan portfolio. Consequently, we assess Örebro's liquidity as strong, based on adequate debt-service coverage, with cash and committed facilities that in April 2017 covered about 94% of the city's debt service, including our estimate of new investment financing for the next 12 months. Another positive factor, in our view, is Örebro's strong and reliable capital market access.

In addition to the city's ample resources of available committed bank facilities and checking accounts containing over SEK2 billion, liquidity support is reinforced by Örebro's membership of the national municipal funding agency Kommuninvest i Sverige AB and by a SEK1.5 billion loan agreement from the European Investment Bank. Moreover, we anticipate that Örebro could add further supranational lenders to its sources of financing over 2017.

As a member of Kommuninvest, Örebro has signed joint and several guarantees for Kommuninvest's obligations. Currently, we do not envisage a scenario in which Kommuninvest's operations would falter to the extent that these guarantees would be called upon.

Overall, because we include all the municipal companies' debt in our debt analysis, we believe Örebro has low contingent liabilities.

Key Statistics

Table 1

Municipality of Örebro Key Statistics

(Mil. SEK)	--Fiscal year end Dec. 31--				
	2015	2016	2017bc	2018bc	2019bc
Operating revenues	9,560.0	10,079.0	10,706.0	11,049.0	11,410.0
Operating expenditures	9,173.0	9,603.0	10,202.0	10,636.0	11,066.0
Operating balance	387.0	476.0	504.0	413.0	344.0
Operating balance (% of operating revenues)	4.1	4.7	4.7	3.7	3.0
Capital revenues	381.0	387.0	190.0	190.0	190.0
Capital expenditures	638.0	551.0	728.0	624.0	630.0
Balance after capital accounts	131.0	312.0	(34.0)	(21.0)	(96.0)
Balance after capital accounts (% of total revenues)	1.0	3.0	0.0	0.0	(1.0)
Debt repaid	2,458.0	3,000.0	4,950.0	5,000.0	4,900.0
Gross borrowings	4,506.0	3,425.0	6,403.0	6,408.0	5,983.0
Balance after borrowings	530.2	(217.7)	(33.5)	(20.8)	(95.3)
Modifiable revenues (% of operating revenues)	65.2	66.8	65.7	65.9	65.9
Capital expenditures (% of total expenditures)	6.5	5.4	6.7	5.5	5.4
Direct debt (outstanding at year-end)	11,835.4	12,260.0	13,577.0	14,841.0	15,964.0
Direct debt (% of operating revenues)	123.8	121.6	126.8	134.3	139.9
Tax-supported debt (outstanding at year-end)	12,714.4	13,080.0	14,288.0	15,552.0	16,675.0
Tax-supported debt (% of consolidated operating revenues)	105.6	103.3	107.5	113.7	118.3
Interest (% of operating revenues)	0.2	0.4	0.9	1.1	1.2
National GDP per capita (SEK)	428,947.4	444,479.8	458,978.0	473,472.4	486,988.2

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. SEK--Swedish krona.

Ratings Score Snapshot

Table 2

Municipality of Orebro Ratings Score Snapshot

Key rating factors

Institutional framework	Extremely predictable and supportive
Economy	Very strong
Financial management	Strong
Budgetary flexibility	Average
Budgetary performance	Average
Liquidity	Strong
Debt burden	Moderate
Contingent liabilities	Low

*Our ratings on local and regional governments (LRGs) are based on eight main rating factors listed in the table above. Section A of S&P Global Ratings' "Methodology For Rating Non-U.S. Local And Regional Governments" summarizes how the eight factors are combined to derive the foreign currency rating on an LRG.

Key Sovereign Statistics

- Research Update: Kingdom of Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Stable, March 3, 2017

Related Criteria And Research

Related Criteria

- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables - June 01, 2016
- General Criteria: National And Regional Scale Credit Ratings - September 22, 2014
- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments - June 30, 2014
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs - October 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Sovereign Risk Indicators, Dec. 14, 2016. An interactive version is available at www.spratings.com/sri
- Swedish Local And Regional Government Risk Indicators: February 2016 Update - February 10, 2016
- High Investments Underpin Growing Debt Levels For Swedish Local And Regional Governments - February 10, 2016

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

	Rating	
	To	From
Orebro (Municipality of)		
Issuer Credit Rating		
Foreign and Local Currency	AA+/Stable/A-1+	AA+/Stable/A-1+
Nordic Regional Scale	--/--/K-1	--/--/K-1
Senior Unsecured		
Foreign and Local Currency	AA+	AA+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-

Research Update: Swedish Municipality of Orebro Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable

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