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Research Update:

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

Primary Credit Analyst:

Emelie Rosencrantz, London + 44(0)2071763733; emelie.rosencrantz@spglobal.com

Secondary Contact:

Gabriel Forss, Stockholm (46) 8-440-5933; gabriel.forss@spglobal.com

Research Contributor:

JOHANNA MELINDER, Stockholm + 46(0)84405926; johanna.melinder@spglobal.com

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Overview

- We expect that Örebro will continue demonstrating satisfactory budgetary performance in 2018-2020 by prudently managing pressures on operating expenditures and higher investment needs stemming from its increasing population.
- Given the municipality's extensive capital program for the coming years, we expect its financial management to remain committed to prudent debt and liquidity management, such that debt accumulation is moderate and liquidity stays strong.
- We are affirming our 'AA+/A-1+' global scale and 'K-1' regional scale ratings on Örebro.
- The outlook remains stable.

Rating Action

On April 6, 2018, S&P Global Ratings affirmed its 'AA+' long-term and 'A-1+' short-term global scale issuer credit ratings on the Swedish municipality of Örebro. The outlook is 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 Örebro's budgetary performance will remain stable, with cost-control measures and increasing tax revenues balancing expenditure pressure arising from rapid population growth and demographic challenges. We further expect that Örebro's financial management will remain prudent, securing strong liquidity and moderate debt accumulation.

Downside Scenario

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

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 strong liquidity.

Rationale

Örebro benefits from the very supportive institutional framework in Sweden, a wealthy and developing local economy, and its budgetary flexibility. These factors underpin its satisfactory budgetary performance, which we forecast will remain largely stable, in spite of expenditure pressures resulting from an aging population, immigration, and a general pickup in demand for public services from a notably growing population. As a consequence, we foresee that debt-funded investment for the municipality and its company sector, which conducts much of the investments in necessary municipal property infrastructure, will result in increasing debt levels over the next three years. Given this, we consider the management's dedication to securing stable debt-servicing and strong liquidity, as well as the municipality's large liquidity reserves, as central to the affirmation of our ratings.

Very supportive institutional framework and Örebro's strong financial management underpin credit-worthiness

In an international comparison, Örebro's economy is very strong, with a well-balanced and 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, and unemployment rates have converged toward the national average. Through 2020, we expect the population to increase by 1.4% on average annually, outpacing national population growth. However, since the Swedish equalization system significantly balances wealth levels among the local and regional governments (LRGs), we use the 2018 national GDP per capita of \$54,100 as the starting point for our analysis.

Sweden's institutional framework for LRGs is a key strength for our ratings on Örebro. The framework displays a high degree of institutional stability, and we consider it one of the strongest and most predictable globally. Management of revenues and expenditures within the system is based on a far-reaching equalization system and LRGs' autonomy in setting local taxes, and we consider that this promotes high levels of reporting and disclosure, as well as fiscal discipline among all Swedish LRGs.

We view Örebro's financial management as prudent and competent, with a robust track record of budget execution. In particular, we expect that 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, thanks to good long-term planning, cost controls, and conservative debt and liquidity management. We also expect the municipality will be able to maintain a collaborative political environment and continue its policy of fiscal stringency beyond the upcoming election in September 2018.

Robust revenue flexibility and proactive management balance risk from high expenditures and debt repayments

Örebro's sound economic fundamentals will continue to support revenue growth and operating budget surpluses. However, strong population growth and demographic challenges will increase demand for public services, putting pressure on both investment needs and operating expenditures. 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, and we would expect Örebro's management to use its flexibility to counteract any material budgetary deterioration, should it emerge.

As such, we expect Örebro's budgetary performance will remain sound overall, although slightly weakening over the next three years. In our base-case scenario for 2018-2020, we envisage Örebro's operating balance standing at 3.5% of adjusted operating revenues on average, and balance after capital accounts at just below 1% of total revenues. However, when 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 companies the municipality owns. This reduces the municipality's capital expenditures and artificially improves balances after capital accounts.

On the back of rapid growth, we note a significant pickup in the municipality's core investments. In particular, significant investments relate to the building and refurbishment of schools, following the municipality's assessment that it needs to build one new school per year over the medium term. As a result, we project increasing nominal debt during our forecast period through 2020. Although the municipality's financing needs are rising, we think management will prudently manage the expanding loan portfolio.

The inclusion of the municipal companies' substantial revenues distorts our measure of Örebro's tax-supported debt. Consequently, we consider that the municipality's direct debt, which we forecast at 148% of operating revenues in 2020 compared with about 127% in 2017, better reflects the risk associated with the external loans held at the municipality's treasury. However, more than 40% of this debt is onlent to Örebro's housing entity, Örebro Bostäder, which we consider to be self-supporting. As this lending is associated with lower risk and the proportion is material, we view this as dampening to the overall risk of the municipality's debt position.

All municipal companies' debt are included in our debt risk analysis. As such, we believe that Örebro has very limited contingent liabilities stemming from its company sector. As a member of the Swedish local government funding agency 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. We therefore consider Örebro's contingent liabilities low overall.

Örebro's liquidity position remains supportive to the rating, underpinned by its large liquidity reserves and strong market access. The municipality currently has about Swedish krona (SEK) 4.7 billion (€680.4 million) in liquid assets such as cash, bonds and equity, including assets invested to cover future payments for pension liabilities. In addition, Örebro holds about SEK2 billion in checking accounts and committed bank lines, as well as credit facilities with the European Investment Bank. Incorporating our estimate of financing for capital expenditures, we forecast the municipality's liquid holdings will cover about 96% of debt maturing within the

next 12 months. Moreover, Örebro's strong and reliable access to the capital markets is supportive to our view of their liquidity position, which we consider to be strong.

That said, we note that the municipality faces higher debt maturities over the forecast period. Absent changes in credit facilities, this is likely to weigh on our debt-service coverage projections. However, we expect that management will adhere to prudent and proactive refinancing strategies and actively decrease exposure to short-term borrowing in addition to refinancing large upcoming maturities proactively. This risk-mitigating strategy is essential to our expectations of continued strong liquidity.

Key Statistics

Table 1

Municipality of Örebro Key Statistics

(Mil. SEK)	--Fiscal year end Dec. 31--				
	2016	2017	2018bc	2019bc	2020bc
Operating revenues	10,121	10,707	11,069	11,465	11,937
Operating expenditures	9,541	10,063	10,607	11,085	11,585
Operating balance	579	644	462	379	352
Operating balance (% of operating revenues)	5.7	6.0	4.2	3.3	2.9
Capital revenues	329	294	250	250	250
Capital expenditures	551	688	669	508	459
Balance after capital accounts	357	250	43	121	143
Balance after capital accounts (% of total revenues)	3.4	2.3	0.4	1.0	1.2
Debt repaid	3,925	4,800	5,850	4,900	7,215
Gross borrowings	3,425	4,555	7,000	6,375	8,652
Balance after borrowings	(1,134)	(1,047)	(167)	(24)	(35)
Modifiable revenues (% of operating revenues)	66.6	66.0	66.0	66.0	65.5
Capital expenditures (% of total expenditures)	5.5	6.4	5.9	4.4	3.8
Direct debt (outstanding at year-end)	12,260	13,613	14,763	16,238	17,675
Direct debt (% of operating revenues)	121.1	127.1	133.4	141.6	148.1
Tax-supported debt (outstanding at year-end)	13,080	14,368	15,518	16,993	18,430
Tax-supported debt (% of consolidated operating revenues)	102.6	106.0	110.6	116.9	121.8
Interest (% of operating revenues)	0.1	0.1	0.2	0.2	0.2
National GDP per capita (single units)	447,142	460,644	477,049	491,629	506,407

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. SEK--Swedish krona. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

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

- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments - June 30,2014
- General Criteria: National And Regional Scale Credit Ratings - September 22,2014
- 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: S&P Global Ratings' National And Regional Scale Mapping Tables - August 14,2017
- General Criteria: Use Of CreditWatch And Outlooks - September 14,2009
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07,2017

Related Research

- Sovereign Risk Indicators, Dec. 14, 2017. An interactive version is available at www.spratings.com/sri
- Swedish Local And Regional Government Risk Indicators: April 2017 Update - April 5, 2017
- Default, Transition, and Recovery: 2016 Annual Non-U.S. Local And Regional Government Default Study And Rating Transitions - May 8, 2017
- Institutional Framework Assessments For Non-U.S. Local And Regional Governments - September 21, 2017

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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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website 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) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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Additional Contact:

International Public Finance Ratings Europe; PublicFinanceEurope@spglobal.com

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