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## Research Update:

# City Of Goteborg Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable

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## Table Of Contents

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Overview

Rating Action

Rationale

Outlook

Key Statistics

Ratings Score Snapshot

Key Sovereign Statistics

Related Criteria And Research

Ratings List

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## Overview

- In our base-case scenario until 2018, we expect the Swedish City of Göteborg's strong management to navigate budgetary pressures and present adequate budgetary performance in spite of significantly rising investment needs from a rapidly increasing population.
- We expect Göteborg's prudent financial management to uphold conservative debt and liquidity management in order to manage the city's increasing direct debt as it continues to centralize the funding of its company sector in the city treasury in the coming years.
- We are affirming our 'AA+/A-1+' issuer credit and 'K-1' Nordic regional scale ratings on Göteborg.
- The stable outlook reflects our expectation that Göteborg will maintain adequate budgetary performance until 2018, as well as prudent treasury management supporting a continued strong overall liquidity position.

## Rating Action

On Sept. 16, 2016, S&P Global Ratings affirmed its 'AA+' long-term and 'A-1+' short-term issuer credit ratings on the Swedish City of Göteborg. The outlook is stable. We also affirmed our 'K-1' short-term Nordic regional scale rating on the city.

## Rationale

The ratings are supported by our assessments of Göteborg's very strong local economy, strong liquidity, and our view of the Swedish institutional framework as extremely predictable and supportive. Göteborg's strong financial management, strong budgetary flexibility, and low contingent liabilities further underpin the ratings. These positive rating factors are balanced by the city's average budgetary performance and the rising levels of its currently moderate debt burden. The long-term rating on Göteborg mirrors our 'aa+' assessment of its stand-alone credit profile.

With more than 500,000 inhabitants, Göteborg is Sweden's second-largest city and the regional center of western Sweden. In an international context, Göteborg's economy is very strong. An expanding services sector and increased diversification have contributed to a more robust macroeconomic structure in recent years. Because of the country's comprehensive equalization system, which evens out the wealth among Swedish local and regional governments (LRGs), we use the national GDP per capita of US\$52,700 as a starting point for our analysis.

Göteborg's historically robust budgetary performance is supported by its strong management and stable economic fundamentals. The city's operating balance has historically been sound, with an average of 5.4% over 2013-2015. Due to the

increasing population, which puts pressure on core public services spending, we expect Göteborg's operating balance to decline to an average of 3.6% over 2016-2018. The rising population will also increase the city's need to make investments in the coming years, further accentuated by a number of key infrastructure projects to which it contributes. As such, we expect deficits in the capital account to widen in the coming years to average 5.1% of total revenues over 2016-2018, compared with 2013-2015 when the average deficit was only 0.6% mainly due to high capital revenues.

We view the Swedish equalization system as extremely predictable and supportive and consider it to be a key component of our ratings on Göteborg. In our view, the system displays a high degree of institutional stability. The LRG sector's revenue and expenditure management is based on a far-reaching equalization system and autonomy in setting local taxes. In this regard, we assess the city as having overall strong budgetary flexibility, with modifiable revenues above 70% of revenues. In our view, Göteborg has institutionalized revenue flexibility to mitigate any significant budgetary deterioration, which is important in light of our assessment of a fairly rigid expenditure structure. Further support to its strong revenue flexibility stems from the city's asset-rich company sector, which we consider holds scope for divestments.

We consider Göteborg's management as strong. Since the election in 2014, Göteborg has been run by a minority government. This could lead to strains on effective decision making. In spite of this, we expect broad agreements to be struck across the city's political parties. Moreover, we note a consensus on the importance of fiscal discipline, which is being enforced by Göteborg's civil servants. With the budgetary challenges on both the operating and capital side, we believe the incumbent political leadership would use its revenue flexibilities if necessary to balance budgets for example by extracting dividends or from outright divestment of assets. We consider the city's financial management to be very prudent with professional, conservative, and active debt and liquidity management. Over the past year, the city has become a renowned issuer of green bonds, which has generated significant investor interest and broadened its investor base.

In assessing the city's debt position, we view our tax-supported debt metric as distorted by the inclusion of the substantial revenues of Göteborg's company sector. We consider the city's direct debt as a better metric for our assessment, reflecting the risk associated with the external loans held in the city treasury. In this regard, the city's increasing investments will cause its direct debt to gradually rise until 2018. In addition, the debt in the city treasury continues to increase due to an expanding in-house treasury and onlending functions. Over the next three years, Göteborg plans to complete the process of gradually assuming the debt stock of its housing company, Forvaltnings AB Framtiden, (AA-/Stable/A-1+) into the city treasury.

As such, we expect that Göteborg's direct debt will increase to 117% of operating revenues by 2018 from 80% in 2015. However, we consider Framtiden as self-supporting, and view the debt lent to this company as positive. We anticipate that the city's management will continue its prudent work in containing the increase in

debt as investments increase. In spite of this, we expect Göteborg's direct debt to continue increasing beyond 2018 and take this into account in our assessment of the city's moderate debt burden. We assume that Framtiden's loans will be fully transferred into the city treasury during 2018.

As a member of Sweden's local government funding agency, Kommuninvest i Sverige AB (AAA/Stable/A-1+), Göteborg has signed joint and several guarantees of 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. In addition, Göteborg holds a large company sector relative to its size. However, we consider the city to hold low contingent liabilities, since the debt of the company sector is already integrated into the city treasury and we assess the need for financial support as limited.

## **Liquidity**

We assess Göteborg's liquidity as strong, owing to the city's ample committed bank facilities relative to its volume of maturing debt and strong access to the market.

Göteborg's committed bank facilities amount to Swedish krona (SEK) 9 billion (about €1 billion). The city furthermore has a facility with the European Investment Bank, of which we expect it to draw down its remaining SEK700 million by year-end 2016. In addition, over the coming month, we expect Göteborg to finalize discussions and put in place loan facility of SEK1 billion with the Nordic Investment Bank and factor this into our liquidity analysis. We also acknowledge that the city is conducting discussions with the Council of Europe Development Bank (CEDB) and the EIB for associated loan facilities. Considering that these discussions are at an early stage, we have not included them in our liquidity assessment.

On Sept. 8, the city conducted buybacks of two bonds totalling SEK1.2 billion while issuing new debt of SEK2.0 billion and proactively limiting its short-term refinancing need. Following the buyback, Göteborg's cash, liquid assets, and available committed credit lines amounted to 113% of debt and interest coming due over the following 12 months, including our expectation of financing needs for municipal investments. Because the city is committed to refinancing the debt of its housing subsidiary Framtiden with the city treasury, we include these loans in our proxy for the city's upcoming financing needs.

Göteborg has a range of funding options that help to reduce refinancing risk. Importantly, as it is continuing the process of centralizing housing subsidiary Framtiden's funding into the city treasury, the city has increased its capital market programs. It generally obtains funding through a SEK6 billion commercial paper (CP) program, a €6 billion euro medium-term note program, a US\$0.5 billion euro CP program, and loans from Kommuninvest. Consequently, we acknowledge Göteborg's strong and reliable capital market access in assessing its overall liquidity.

We expect the city to continue to exercise prudent debt and liquidity management to handle its increasing loan portfolio. As a result, we expect its liquidity to remain strong over the next two years.

## Outlook

The stable outlook reflects our expectation that Göteborg will maintain adequate budgetary performance through 2018. As the city completes the transfer of its company sector debt into the city treasury, we foresee that its direct debt will gradually increase and likely reach a moderate level by year-end 2019. In addition, despite the increased treasury activities, the stable outlook incorporates our expectation of continued prudent debt and liquidity management to the extent that liquidity will likely remain strong over the coming 24 months.

We could raise the ratings if, in line with our upside scenario, we observed a strengthening of management practices--for example with regard to long-term capital planning--leading us to revise our view of Göteborg's management upward. A combination of strengthening management practices and liquidity improving to a level we would consider exceptional could lift our assessments of the city's liquidity and management, and trigger an upgrade.

We could consider a downgrade if we observed that Göteborg's management was unable to control spending, and faltering capital expenditure planning and lax debt and liquidity management led to strains on liquidity. In this case, we could revise downward our view of the city's financial management and liquidity, and consequently lower the ratings.

## Key Statistics

Table 1

City of Goteborg Financial Statistics						
	--Fiscal year end Dec. 31--					
(Mil. SEK)	2013	2014	2015	2016bc	2017bc	2018bc
Operating revenues	33,642	34,703	36,725	37,542	39,622	40,856
Operating expenditures	31,672	32,974	34,767	36,233	38,193	39,321
Operating balance	1,970	1,729	1,958	1,309	1,429	1,535
Operating balance (% of operating revenues)	5.9	5.0	5.3	3.5	3.6	3.8
Capital revenues	1,792	1,271	375	350	350	350
Capital expenditures	3,712	3,060	3,013	3,400	3,900	4,125
Balance after capital accounts	50	(60)	(680)	(1,741)	(2,121)	(2,240)
Balance after capital accounts (% of total revenues)	0.1	(0.2)	(1.8)	(4.6)	(5.3)	(5.4)
Debt repaid	7,847	6,858	8,106	7,729	6,231	5,144
Net budget loans	1,935	(5,775)	(1,237)	(2,759)	(5,335)	(4,629)
Balance after debt repayment and onlending	(5,862)	(12,693)	(10,023)	(12,229)	(13,687)	(12,013)
Balance after debt repayment and onlending (% of total revenues)	(16.5)	(35.3)	(27.0)	(32.3)	(34.2)	(29.2)

**Table 1**

<b>City of Goteborg Financial Statistics (cont.)</b>						
<b>(Mil. SEK)</b>	<b>--Fiscal year end Dec. 31--</b>					
	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016bc</b>	<b>2017bc</b>	<b>2018bc</b>
Gross borrowings	7,390	11,733	10,301	11,591	13,687	12,013
Balance after borrowings	1,528	(960)	278	(638)	0	0
Operating revenue growth (%)	3.8	3.2	5.8	2.2	5.5	3.1
Operating expenditure growth (%)	2.3	4.1	5.4	4.2	5.4	3.0
Modifiable revenues (% of operating revenues)	70.9	71.0	70.5	73.2	72.4	72.9
Capital expenditures (% of total expenditures)	10.5	8.5	8.0	8.6	9.3	9.5
Direct debt (outstanding at year-end)	24,437	27,526	29,571	33,433	40,889	47,758
Direct debt (% of operating revenues)	72.6	79.3	80.5	89.1	103.2	116.9
Tax-supported debt (% of consolidated operating revenues)	48.5	64.8	64.8	70.7	80.9	90.6
Interest (% of operating revenues)	3.5	2.9	1.5	1.6	1.5	1.5
Debt service (% of operating revenues)	26.9	22.6	23.6	22.2	17.2	14.1

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

**Table 2**

<b>City of Goteborg Economic Statistics</b>						
	<b>--Fiscal year end Dec. 31--</b>					
	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016bc</b>	<b>2017bc</b>	<b>2018bc</b>
Population	533,060	541,145	548,190	556,948	567,219	578,558
Population growth (%)	1.3	1.5	1.3	1.6	1.8	2.0
Unemployment rate (%)	7.1	6.6	6.3	5.8	N/A	N/A

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. Sources typically include national statistical offices, Eurostat, and Experian Limited. bc--Base case.

## Ratings Score Snapshot

**Table 3**

### City of Goteborg Ratings Score Snapshot

#### Key rating factors

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

\*The ratings of S&P Global 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," published on June 30, 2014, summarizes how the eight factors are combined to derive the foreign currency rating on an LRG.

## Key Sovereign Statistics

- Kingdom of Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Stable - September 02, 2016

## 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

- High Investments Underpin Growing Debt Levels For Swedish Local And Regional Governments - February 10, 2016
- Sovereign Risk Indicators - July 6, 2016. An interactive version is available at [www.spratings.com/sri](http://www.spratings.com/sri)
- 2015 Annual Sovereign Defaults And Rating Transitions - May 24, 2016
- Public Finance System Overview: Swedish Local And Regional Governments - Jan 21, 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
Goteborg (City 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+
Short-Term Debt		
Foreign and Local Currency	A-1+	A-1+
Commercial Paper		
Foreign and Local Currency	A-1+	A-1+
Nordic Regional Scale	K-1	K-1

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](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.globalcreditportal.com](http://www.globalcreditportal.com) and at [spcapitaliq.com](http://spcapitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public Web site at

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