

Research Update:

City of Goteborg 'AA+/A-1+' Ratings Affirmed; Outlook Stable

September 13, 2019

Overview

- As expected, Göteborg's growing population has caused an increase in operating spending, which is weighing on the city's operating performance and ability to self-finance its investments.
- That said, although Göteborg's fragmented parliamentary situation could hinder necessary policy making, we expect the city to uphold its sound fiscal performance and maintain budgetary discipline.
- We are affirming our 'AA+/A-1+' issuer credit and 'K-1' Nordic regional scale ratings on Göteborg.
- The outlook is stable.

Rating Action

On Sept. 13, 2019, 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.

Outlook

The stable outlook reflects our expectation that Göteborg, despite a challenging parliamentary situation, will maintain its sound financial position through 2021, despite increasing operating spending and high investments caused by the city's growing population. Moreover, we expect the city's management to remain committed to budgetary discipline and conservative debt policies.

Downside scenario

We could consider lowering the ratings if we observed that a deteriorating political situation was preventing the city from making the policy reforms necessary to contain increased spending,

PRIMARY CREDIT ANALYST

Erik A Karlsson
Stockholm
+ 46(0)84405924
erik.karlsson
@spglobal.com

SECONDARY CONTACT

Carl Nynerod
Stockholm
(46) 8-440-5919
carl.nynerod
@spglobal.com

ADDITIONAL CONTACT

EMEA Sovereign and IPF
SovereignIPF
@spglobal.com

leading to a deterioration in the city's overall fiscal position.

Upside scenario

We could raise the ratings if the city's government reinforced its control over the growth in operating spending and structurally improved its operating margins to above 5% of revenues.

Rationale

Göteborg's political situation remains difficult; it has a fragmented parliament and a minority government. Despite this, we expect Göteborg to manage the increase in operating spending caused by demographic factors to maintain a sound fiscal position. It will be supported by Sweden's institutional framework and the city's budgetary discipline. Because of the city's high investments, we expect direct debt to reach 120% of operating revenues in 2021. That said, most of the amount has been onlent to financially strong subsidiaries, mitigating the risk. We regard the city's financial management as prudent and risk minimizing, and we expect that it will keep the city's refinancing risks to a minimum.

Political uncertainty is lingering, but there are signs of improvement

Since the 2018 election, Göteborg has been ruled by a right-center minority government that holds only about 30% of the seats in the local parliament. As a result, parliamentary uncertainty has been noticeable. Although this could impair the city's ability to conduct efficient financial policymaking, a majority of the parliament agreed on the city's financial strategies for the coming years. In addition, we regard the city's civil servants as committed to budgetary discipline, which further mitigates the parliamentary risks.

Sweden's estimated GDP per capita for 2019 is high at \$53,300 and its very favorable macroeconomic fundamentals support our ratings on Göteborg. Furthermore, Göteborg is Sweden's second-largest city and, as an industrial and regional center in a strategic location, it is a natural hub for international trade.

The Swedish institutional framework for local and regional governments (LRGs) underpins our ratings on Göteborg. It displays a high degree of stability and we regard the system as extremely predictable and supportive. In addition, the sector's revenue and expenditure management is largely based on an extensive equalization system, combined with autonomy in setting local taxes.

The growing population weighs on the city's fiscal position

Demographic factors have led to a growing population in Göteborg. We anticipate that the resulting increase in operating spending will depress the city's operating balance throughout our forecast period. Göteborg's operating balance is predicted to average 2.8% of operating revenues in 2019-2021, compared with 4.5% in 2017-2018. At the same time, the city expects to invest heavily in core municipal infrastructure and land development--about Swedish krona (SEK) 5 billion a year over the coming two years. Given its weaker operating performance, we expect Göteborg's ability to self-finance these investments will weaken. Deficits will likely rise slightly to an average of 4.5% of total revenues over the next two years, compared with 1% in 2017-2018.

For several years, Göteborg has extracted dividends from its government-related entities (GREs) to balance its increasing operating spending. Although its political leaders have indicated that

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they want to reduce this dependence on dividends, we estimate the city will extract about SEK500 million annually from these entities through 2021. We do not consider this a sustainable long-term practice because it erodes the GREs' financial flexibility and reduces their ability to manage their own upcoming investments. Göteborg's management will instead need to enforce fiscal discipline to curb rising expenditure.

Owing to high investments by both the city and its GREs, we forecast the city's direct debt will reach 120% of operating revenues by year-end 2021, up from 92% in 2018. In addition to the city's own investments, the housing company Forvaltnings AB Framtiden (AA-/Stable/A-1+; Framtiden) faces large upcoming investments that require a loan from the city treasury. We consider it a mitigating factor that the city has onlent about half its debt to companies that we consider to be financially strong, and that have a commercial business profile. These companies are Framtiden, Göteborg Energi AB (energy), Göteborgs Hamn AB (harbour), and Gryaab (water and waste). Furthermore, we regard Göteborg's contingent liabilities, including the joint and several guarantee extended to Kommuninvest, as limited.

Göteborg's very favorable liquidity position relies on an ample mix of contracted liquidity facilities and liquid assets that covers 147% of the next 12 months' debt service. In our calculation, we include SEK12.2 billion of contracted backups, overdrafts, and facilities with the European Investment Bank (EIB) and Nordic Investment Bank (NIB). We also include SEK3 billion of liquid assets invested in covered bonds and SEK1.6 billion in upcoming funding needs.

We calculate that Göteborg will service SEK9.7 billion of debt and interest in the next 12 months. Like other rated Swedish LRGs, we acknowledge in our assessment of Göteborg's liquidity position that the city has strong and reliable access to external liquidity. In contrast with previous reviews, we no longer consider Göteborg's debt-financed onlending as depressing the liquidity position.

Göteborg's debt and liquidity management is centralized via the in-house bank that caters for the city's funding needs, and those of its GREs. The city has a wide range of funding sources including a SEK6 billion commercial paper program, a €6 billion euro medium-term note program, a \$500 million euro commercial paper program, and loans from Kommuninvest. In addition, the city has loan facilities with the NIB, EIB, and the Council of Europe Development Bank (CEB).

Key Statistics

Table 1

City of Göteborg Selected Indicators

Mil. SEK	2016	2017	2018	2019bc	2020bc	2021bc
Operating revenues	39,098	40,561	41,850	43,240	44,682	46,081
Operating expenditures	37,198	38,522	40,177	41,823	43,548	44,935
Operating balance	1,900	2,039	1,673	1,417	1,134	1,146
Operating balance (% of operating revenues)	4.9	5.0	4.0	3.3	2.5	2.5
Capital revenues	807	1,595	2,363	1,950	1,720	1,720
Capital expenditures	2,920	3,600	4,950	5,130	5,120	5,120
Balance after capital accounts	(213)	34	(914)	(1,763)	(2,266)	(2,254)
Balance after capital accounts (% of total revenues)	(0.5)	0.1	(2.1)	(3.9)	(4.9)	(4.7)
Debt repaid	7,884	5,832	5,939	9,534	9,113	10,819

Table 1

City of Göteborg Selected Indicators (cont.)

Mil. SEK	2016	2017	2018	2019bc	2020bc	2021bc
Gross borrowings	10,333	10,602	6,916	14,509	14,795	17,244
Balance after borrowings	(538)	155	(257)	2	0	(0)
Direct debt (outstanding at year-end)	32,566	37,336	38,313	43,288	48,970	55,395
Direct debt (% of operating revenues)	83.3	92.0	91.5	100.1	109.6	120.2
Tax-supported debt (outstanding at year-end)	32,566	37,336	38,313	43,288	48,970	55,395
Tax-supported debt (% of consolidated operating revenues)	59.2	65.4	66.0	68.5	75.3	82.9
Interest (% of operating revenues)	1.3	1.2	1.2	1.1	1.1	1.1
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	445,182	458,105	473,294	485,433	500,290	517,575

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. N/A--Not applicable.

Ratings Score Snapshot

Table 2

City of Göteborg Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	2
Budgetary performance	3
Liquidity	1
Debt burden	3
Stand-alone credit profile	aa+
Issuer credit rating	AA+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Summary: Sweden, Aug. 23, 2019

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Sovereign Risk Indicators, July 11, 2019. An interactive version is also available at www.spratings.com/sri
- S&P Global Ratings Definitions, July 5, 2019
- A Potential Profit Cap On Private Operators In Sweden's Welfare Sector Could Increase LRG Spending, March 11, 2019
- Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Stable, Feb. 22, 2019
- Public Finance System Overview: Swedish Municipalities And Counties, Jan. 21, 2019
- European Local And Regional Government Risk Indicators, Nov. 9, 2018
- Sweden's Unclear Parliamentary Situation Clouds Local Governments' Future Financial Policy, Oct. 4, 2018
- Swedish Housing Group Framtiden 'AA-/A-1+' And 'K-1' Ratings Affirmed; Outlook Stable, Oct. 23, 2018

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

Ratings Affirmed

Goteborg (City of)

Issuer Credit Rating	AA+/Stable/A-1+
Nordic Regional Scale	--/--/K-1
Senior Unsecured	AA+
Commercial Paper	A-1+
Commercial Paper	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 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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