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Research Update:

Swedish Municipality of Jonkoping 'AA+/A-1+' And 'K-1' Ratings Affirmed On Sound Budgetary Performance; Outlook Stable

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Overview

- We expect the Swedish Municipality of Jönköping to retain sound budgetary performance as municipal investments ease in 2014-2015, resulting in only moderate financing needs after capital accounts.
- However, the municipality's in-house treasury activities for its fully owned companies will likely cause tax-supported debt to approach 60% of consolidated revenues by year-end 2015.
- We are affirming our 'AA+/A-1+' and 'K-1' ratings on Jönköping.
- The stable outlook reflects our expectation of continued sound budgetary performance and moderate financing requirements from municipal investments through 2015.

Rating Action

On Nov. 8, 2013, Standard & Poor's Ratings Services affirmed its 'AA+/A-1+' long- and short-term issuer credit ratings on the Swedish Municipality of Jönköping. The outlook is stable. At the same time, we affirmed our 'K-1' Nordic regional scale rating on Jönköping.

Rationale

The ratings on Jönköping reflect its well-diversified and wealthy local economy, neutral liquidity, and our view of the Swedish institutional framework as predictable and supportive. Jönköping's balanced macroeconomic fundamentals and prudent municipal budget discipline support its sound budgetary performance. We also expect Jönköping's management, which we view as a positive rating factor, to continue to enact strong budget discipline to curtail the budget in 2014. Jönköping has strong revenue flexibility to counteract deteriorating budgetary conditions. We consider this to be important as it counterbalances a fairly inflexible expenditure structure. While Jönköping's municipal investments are set to require only moderate debt financing under our base-case scenario, Jönköping is supplying the new funding of its company group through the municipal treasury. Together with the refinancing of some existing loans held in its holding company Jönköping Rådhus AB, this puts Jönköping's tax-supported debt on an increasing trend. Still, we assess its overall debt position as modest under our base-case scenario through 2015. As most of Jönköping's company group's debt is factored into our tax-supported debt ratio, we consider the municipality to have modest

contingent liabilities.

Jönköping's local economy is well balanced and has a diverse industry structure with an employment profile focused on logistics and trade. We assess the city's employment structure as robust with no large concentrations on key employers or industries sensitive to swings in the economic cycle. In September 2013, Jönköping's unemployment was 5.7%, below the national average of 7.0%. We view Jönköping's growth prospects as robust, with the population set to increase by 0.8% yearly in our base case through 2015, slightly above the national average.

Jönköping's balanced macroeconomic fundamentals and prudent municipal budget discipline have supported the city's stable budgetary performance in recent years. The municipality has a track record of sound operating balances averaging 7.0% of operating revenues from 2010-2012. The robust operating result helped finance the city's capital expenditure (capex), which was substantial in 2012 at Swedish krona (SEK)839 million, resulting in a deficit after capital accounts of 2.8%. Capex has risen over the past three years, with particularly high levels in 2011 and 2012 as some large scale projects have reached completion.

For 2013, we assume under our base-case scenario that Jönköping's tax revenues will grow by about 5.8%, a strong increase due to a tax shift transferring additional responsibilities for domestic health care to the municipal from the county level. Similarly, we expect operating expenditures in 2013 to increase by 5% because of these new responsibilities. Our base case for 2013 also incorporates positive revenue developments from an SEK112 million reimbursement of previously paid health care insurance premiums, which will boost its operating balance to 6.9% of operating revenues. For 2014-2015 we believe some additional spending pressures could come from these new responsibilities in domestic health care which, together with some re-allocation in education expenditures, will likely moderate the municipality's operating balances to an average 5.4% of operating revenues.

However, we also expect the municipality's capex to trend down from the 2012 level and average SEK600 million yearly through 2015, leaving only moderate deficits after capital accounts of about 1.2% on average under our base-case scenario. With regard to budgeting practices, we note that Jönköping's management continues to be strict in enforcing budget discipline. We therefore assess management as a positive factor for the ratings. We consider Jönköping's management practices to be important as we believe the municipality has average budgetary flexibility due to a generally rigid spending structure.

While we expect only modest financing needs relating to Jönköping's capex, we forecast in our base case that investments in the municipality's company sector, particularly in utility Jönköping Energi, will require debt financing of about SEK1.0 billion in 2013-2015. Importantly, Jönköping has pooled the financing of its company group into an in-house treasury function. This function has been legally placed within the holding company, Jönköping Rådhus

AB, (Rådhus) which has carried out funding on municipal guarantees.

In our analysis of Jönköping's tax-supported debt we include guarantees extended to subsidiaries we do not consider self-supporting, as defined in our criteria. In this respect we assess the two largest borrowers--utility Jönköping Energi and housing company Vätterhem--as self-supporting. In line with our expectations, in 2013 Jönköping has acquired funding through its municipal capital market programs by providing new funding for its company sector while refinancing some of Rådhus' loans in the municipal treasury. We expect this strategy to be more pronounced over the coming years. At year-end 2015 we expect Jönköping's tax-supported debt to approach 60% of consolidated revenues, up from 43% in 2012 and driven by financing of company group investments. A substantial part of the increase in debt through 2015 will be due to increased lending to self-supporting entities in Jönköping's company group.

As a member of local government funding agency Kommuninvest i Sverige AB (AAA/Stable/A-1+), Jönköping has signed a joint and several guarantee 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. Overall, we consider the municipality to have modest contingent liabilities.

Liquidity

The short-term rating is 'A-1+'. We assess Jönköping's liquidity as a "neutral" rating factor, owing to the municipality's adequate internal liquidity and committed bank facilities in relation to volumes of maturing debt, supported by strong access to the market.

The municipality normally holds a low cash balance and uses committed credit facilities from banks to handle its liquidity needs and manage refinancing risk. Jönköping's in-house treasury function is primarily situated in holding company Jönköpings Rådhus AB, which historically has conducted the company group's financing on municipal guarantees. Funding is primarily sourced from municipal funding vehicle Kommuninvest, which currently supplies about 70% of Jönköping's total external financing, down from 75% in May 2013. The remainder consists of traditional bank loans and loans under the municipality's capital market programs.

In 2013, Jönköping is increasingly tapping the market through a SEK1.5 billion commercial paper program, and is about to extend its municipal medium-term note (MTN) program to SEK2 billion from SEK800 million. To prepare for this, the municipal treasury has contracted additional liquidity facilities, which are currently SEK1.9 billion, up from SEK1.54 billion in June 2013. As of September 2013, we forecast Jönköping's cash and available committed bank facilities at 55% of debt maturing over the following 12 months, including our expectation of financing required for city investments and loan repayments, including those to Kommuninvest.

We expect that Jönköping will extensively tap its MTN program when its increased program becomes operational and gradually prolong the maturity profile of its loan portfolio. Still, we expect Kommuninvest to remain Jönköping's main loan provider over the medium term.

Outlook

The stable outlook reflects our expectation that Jönköping will post a persistently solid budgetary performance, with low financing requirements from municipal investments through 2015. In our base case, we also incorporate a moderate buildup of debt to fund a new bio-fuel plant at Jönköping Energi and increased onlending activity from the municipal treasury. Still, we expect Jönköping's tax-supported debt ratio to remain below 60% of consolidated revenues by 2015, supported by the fact that the build-up of debt is sourced to self-supporting entities. In light of this debt increase, we expect Jönköping's management to enforce prudent handling of refinancing risks associated with expanded capital market activities and gradually extend the maturity profile of its loan portfolio.

We might consider a positive rating action if we observed Jönköping's management actively working to stabilize the debt of its municipal group, possibly through exercising its flexibilities over asset sales. In line with our upside scenario, we would also expect a significantly improved liquidity position and a further formalization and institutionalization of management practices if we were to consider an upgrade.

We might consider a negative rating action if we observed a severe deterioration in Jönköping's budgetary performance, coupled with pressures on liquidity. Under this downside scenario, if we observed Jönköping's management abstaining from using its budgetary flexibilities to counteract deteriorating performance and ailing liquidity, we would revise down our assessments of management to neutral and lower the long-term rating.

Published Rating Factor Scores

Table 1

Summary Of Published Rating Factor Scores*	
RATING FACTOR	SCORE
Institutional framework	Predictable and supportive
Financial management	Positive
Liquidity	Neutral

*Standard & Poor's ratings on local and regional governments are based on, among other things, a scoring system that covers eight main rating factors, as further explained in our criteria (see below). We publish our scores for the three rating factors above.

Key Statistics

Table 2

Municipality of Jonkoping--Economic Statistics						
	--Fiscal year ended Dec. 31--					
Balance sheet date year	2010	2011	2012	2013bc	2014bc	2015bc
Population	127,382	128,305	129,478	130,550	131,630	132,710
Population growth (%)	N.M.	0.72	0.91	0.83	0.83	0.82
GDP per capita (SEK)	314,913	327,982	331,328	N/A	N/A	N/A
Unemployment rate (%)	5.50	4.80	5.10	5.50	N/A	N/A

SEK--Swedish krona. N/A--Not applicable. N.M.--Not meaningful. Bc--Base case. Sources: Experian Ltd. and Standard & Poor's.

Table 3

Municipality of Jonkoping--Financial Statistics

	--Fiscal year ended Dec. 31--					
(Mil. SEK)	2010	2011	2012	2013bc	2014bc	2015bc
Operating revenues	7,329	7,519	7,677	8,058	8,242	8,454
Operating expenditures	6,760	7,053	7,131	7,501	7,777	8,015
Operating balance	569	466	546	557	465	439
Operating balance (% of operating revenues)	7.76	6.20	7.11	6.91	5.64	5.19
Capital revenues	117	138	63	20	20	20
Capital expenditures (capex)	735	867	839	532	598	682
Balance after capital accounts	(49)	(263)	(230)	45	(113)	(223)
Balance after capital accounts (% of total revenues)	(0.66)	(3.43)	(2.97)	0.56	(1.37)	(2.64)
Debt repaid	175	250	490	150	300	500
Balance after debt repayment and onlending	(477)	(700)	(742)	(705)	(1,413)	(1,623)
Balance after debt repayment and onlending (% of total revenues)	(6.41)	(9.14)	(9.59)	(8.73)	(17.11)	(19.16)
Gross borrowings	270	694	744	705	1,413	1,623
Balance after borrowings	(207)	(6)	2	0	(0)	(0)
Operating revenue growth (%)	N.M.	2.59	2.10	4.96	2.28	2.57
Operating expenditure growth (%)	N.M.	4.33	1.11	5.19	3.68	3.06
Modifiable revenues (% of operating revenues)	69.52	69.85	70.11	70.31	70.27	71.41
Capital expenditures (% of total expenditures)	9.81	10.95	10.53	6.62	7.14	7.85
Direct debt (outstanding at year-end)	610	1,054	1,308	1,863	2,976	4,099
Direct debt (% of operating revenues)	8.32	14.02	17.04	23.12	36.11	48.49
Tax-supported debt (% of consolidated operating revenues)	35.06	39.63	42.88	40.13	50.12	59.69
Interest (% of operating revenues)	0.27	0.53	0.65	0.62	0.62	0.67
Debt service (% of operating revenues)	2.66	3.86	7.03	2.48	4.26	6.58

SEK--Swedish krona. bc--Base case. Base case reflects Standard & Poor's expectations of the most likely scenario. Downside case represents some but not all aspects of Standard & Poor's scenarios that could be consistent with a downgrade. Upside case represents some but not all aspects of Standard & Poor's scenarios that could be consistent with an upgrade.

Key Sovereign Statistics

For latest sovereign statistics, please click here: "Sweden Ratings Affirmed At 'AAA/A-1+'; Outlook Stable," published Oct. 18, 2013.

Related Criteria And Research

- International Local And Regional Governments Default And Transition Study: 2012 Saw Defaults Spike, March 28, 2013
- Public Finance System Overview: Swedish Local And Regional Governments, May 19, 2011
- Principles Of Credit Ratings, Feb. 16, 2011
- Methodology For Rating International Local And Regional Governments, Sept. 20, 2010
- 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, Oct. 15, 2009

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 above). 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 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.

Ratings List

Ratings Affirmed

Municipality of Jonkoping

Issuer Credit Rating

AA+/Stable/A-1+

Nordic Regional Scale

--/--/K-1

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