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## Research Update:

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

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## Overview

- We expect the Swedish Municipality of Jönköping will demonstrate strong budgetary performance in 2017-2019, while continuing to invest in municipal infrastructure.
- The city's intention to decrease the amount of provided guarantees leads us to forecast lower tax-supported debt and gradual growth to a moderate 74% of consolidated operating revenues by 2019.
- We are affirming our 'AA+/A-1+' and 'K-1' ratings on Jönköping.
- The stable outlook reflects our expectation that Jönköping will continue its strong budgetary performance and conservative debt and liquidity management through 2019.

## Rating Action

On April 21, 2017, S&P Global Ratings affirmed its 'AA+' long-term and 'A-1+' 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.

## Outlook

The stable outlook reflects our expectation that Jönköping's strong budgetary performance and conservative debt and liquidity management will continue through 2019. In our base case, we anticipate increasing financing requirements from municipal investments and moderate financing requirements from company sector investments. Still, we expect the ratio of tax-supported debt will remain moderate, below 80% of consolidated revenues by year-end 2019. In light of the expected debt increase, we think that Jönköping's management will prudently manage associated refinancing risks and gradually extend its loan maturity profile.

## Downside Scenario

We could lower the ratings if we observed that Jönköping's financial management had failed to prevent meaningful deterioration in the city's budgetary performance, leading to weakening operating balances, widening deficits after capital accounts, and a subsequent weakening of liquidity.

## Upside Scenario

We could consider raising the ratings if Jönköping's management took resolute action to structurally improve liquidity and formalize prudent practices in managing debt, liquidity, and investments, with other rating factors remaining unchanged.

## Rationale

In our view, the higher demand for municipal services in Jönköping, owing to population growth, will not affect the policy of the city's management to maintain the currently strong budgetary performance and will not lead to material debt accumulation beyond currently moderate levels. The wealthy local economy and very stable and predictable institutional framework will also continue to support the ratings on the city.

### The local economy and equalization system are key strengths

Jönköping's economy is very strong. In our assessment, we use the average national GDP per capita of US\$54,000 for the past three years as a starting point, owing to the comprehensive equalization system within the Swedish institutional framework, which evens out the wealth among Swedish local and regional governments (LRGs). The municipality benefits from diverse industry, with a focus on logistics and trade and no pronounced dependence on key employers or industries sensitive to swings in the economic cycle. In February 2017, Jönköping's unemployment rate was at a relatively low 4.8%, below the national average of 6.7%. With the population set to increase by 1% yearly in our base case through 2019, slightly above the national average, we view Jönköping's growth prospects as healthy.

Nevertheless, the population growth raises demand for municipal services. It leads to higher spending on infrastructure, which the city funds directly from its budget, as well as via its municipal companies.

In our view, the Swedish LRG system has a high degree of institutional stability. The sector's revenue and expenditure management is based on a far-reaching equalization system and autonomy in setting local taxes.

We view positively Jönköping's strong revenue and expenditure management, based on its budget and operating performance. We also anticipate that spending will be contained while tax revenues will increase throughout our forecast period through year-end 2019. We expect that Jönköping's management would use its institutionalized, strong revenue flexibility to mitigate any pronounced budgetary deterioration. This feature is important in light of our assessment of Jönköping's fairly rigid expenditure structure.

### We think budgetary performance will remain stable, despite high investments

Jönköping's balanced economic fundamentals and what we view as prudent municipal budget discipline have supported its historically strong budgetary performance. In 2016, the municipality posted an operating margin of 7.4% of operating revenues, an increase from 6.3% in 2015, partly due to property-building-related grants.

In 2016, capital expenditures (capex) amounted to Swedish krona (SEK) 851 million (about €89 million), on par with 2015, but noticeably higher than past years. The high investment levels, mainly in properties and energy, led to a deficit after capital accounts of 1%. Recognizing the municipality's growing investment needs over the coming years, we expect capex will remain high, at about SEK750 million on

average over our 2017-2019 forecast period. We project the average deficit after capital accounts at 1.5% over the same period.

Jönköping manages the funding of its municipal companies through an in-house treasury, established within Jönköping Rådhus AB, a municipal holding company that provides funding based on municipal guarantees. The funding of the municipal group increasingly comes from the city's direct capital market activity. In our base-case scenario, we expect a moderation of funding needs within Jönköping's company sector, primarily as a result of decreasing financing needs within the city's utility entity, which recently completed a large-scale investment in a waste incineration plant. We expect the majority of the city's onlending in 2017-2019 will be directed to housing entity Vätterhem, which is stepping up new construction, in line with its owner's requirements. Overall, we assess the new funding requirement of Jönköping's company sector as averaging about SEK300 million (about €31 million) yearly in our 2017-2019 base case, with funding supplied by the city treasury. These volumes will add to the city's funding needs resulting from its rising capex, and we expect to see tax-supported debt at 74% of consolidated operating revenues by the end of 2019, up from 69% in 2016.

In our analysis of Jönköping's tax-supported debt, we include guarantees to subsidiaries that are not self-supporting under our criteria. We assess housing company Vätterhem as self-supporting and therefore do not include its guarantees or revenues in our tax-supported debt ratio for the municipality.

As a member of local government funding agency Kommuninvest i Sverige AB, 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. In addition, since we include most of the municipal companies' debt in Jönköping's tax-supported debt, aside from the debt of financially strong housing entity Vätterhem, we consider the municipality to have low contingent liabilities.

We assess Jönköping's liquidity as strong, reflecting both strong market access and committed facilities. Jönköping normally holds moderate cash balances and has contracted committed credit facilities of SEK1.74 billion from banks to manage its liquidity needs and refinancing risk. Kommuninvest continues to be a key source of funding for the municipal group, currently supplying about 40% of total external financing, down from 75% in May 2013. The remainder consists of bank loans and borrowing under the municipality's capital market programs. In March 2017, cash and committed facilities accounted for about 87% of debt service for the ensuing 12 months. We also include our expectation of available European Investment Bank financing in Jönköping's liquidity sources. The municipality taps the markets from its SEK2.5 billion commercial paper program and SEK4 billion medium-term note program. We expect the municipality will maintain a liquidity coverage ratio above 80% over 2017-2019.

Jönköping has recently diversified its funding sources further by signing a loan agreement of SEK500 million with the Nordic Investment Bank. This funding is tied to specific utility company investments. In addition, the municipality has a loan

agreement of SEK700 million with the European Investment Bank, with a large portfolio of approved projects tied to it. We view Jönköping as having strong access to the capital markets.

## Key Statistics

Table 1

Municipality of Jonkoping Key Statistics						
(Mil. SEK)	--Fiscal year ending Dec. 31--					
	2014	2015	2016	2017bc	2018bc	2019bc
Operating revenues	8,066	8,522	9,173	9,472	9,747	10,041
Operating expenditures	7,604	7,955	8,495	8,901	9,145	9,432
Operating balance	462	567	678	571	602	609
Operating balance (% of operating revenues)	5.7	6.7	7.4	6.0	6.2	6.1
Capital revenues	77	151	86	10	10	10
Capital expenditures	620	855	851	779	761	706
Balance after capital accounts	(81)	(137)	(87)	(199)	(149)	(87)
Balance after capital accounts (% of total revenues)	(1.0)	(1.6)	(0.9)	(2.1)	(1.5)	(0.9)
Debt repaid	1,160	1,125	1,415	2,529	2,369	2,388
Gross borrowings	2,895	1,865	1,900	3,018	2,898	2,627
Balance after borrowings	31	133	-14	0	0	0
Modifiable revenues (% of operating revenues)	71.6	71.1	70.1	70.7	71.0	71.1
Capital expenditures (% of total expenditures)	7.5	9.7	9.1	8.1	7.7	7.0
Direct debt (outstanding at year-end)	3,630	4,370	4,855	5,344	5,873	6,112
Direct debt (% of operating revenues)	45.0	51.3	52.9	56.4	60.3	60.9
Tax-supported debt (outstanding at year-end)	7,045	7,575	7,539	8,028	8,557	8,796
Tax-supported debt (% of consolidated operating revenues)	73.2	74.4	69.1	71.4	74.1	74.1
Interest (% of operating revenues)	0.7	0.4	0.3	0.3	0.4	0.5
Local GDP per capita (SEK)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (SEK)	408,180	428,947	444,480	458,978	473,472	486,988

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. SEK--Swedish krona. N/A--Not applicable.

## Ratings Score Snapshot

**Table 2**

**Municipality of Jonkoping Ratings Score Snapshot**

<b>Key rating factors</b>	
Institutional framework	Extremely predictable and supportive
Economy	Very strong
Financial management	Strong
Budgetary flexibility	Average
Budgetary performance	Strong
Liquidity	Strong
Debt burden	Moderate
Contingent liabilities	Low

\*S&P Global Ratings' credit ratings on local and regional governments 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 government's foreign currency rating.

## Key Sovereign Statistics

Sovereign Risk Indicators - April 10, 2017. An interactive version is available at [www.spratings.com/sri](http://www.spratings.com/sri)

## Related Criteria And Research

### Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07, 2017
- 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 - April 10, 2017. An interactive version is available at [www.spratings.com/sri](http://www.spratings.com/sri)
- 2016 Annual Sovereign Default Study And Rating Transitions - April 4, 2017
- 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
- Public Finance System Overview: Swedish Local And Regional Governments - January 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
Jonkoping (Municipality of)		
Issuer Credit Rating		
Foreign and Local Currency	AA+/Stable/A-1+	AA+/Stable/A-1+
Nordic Regional Scale	--/--/K-1	--/--/K-1

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