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## Research Update:

# Stockholm County Council Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable

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## Overview

- We expect Stockholm County Council to maintain a strong operating balance and liquidity, although we forecast higher investment needs than in 2012-2014 in our base case through 2017.
- The county council's debt will likely increase rapidly to fund investments, but we expect its tax-supported debt to peak at moderate levels over that period.
- We are affirming our 'AA+/A-1+' and 'K-1' ratings on Stockholm County Council.
- The stable outlook reflects our expectation that in 2015-2017 the county council will maintain average budgetary performance, tax-supported debt below 85% of consolidated operating revenues, and strong liquidity.

## Rating Action

On Oct. 16, 2015, Standard & Poor's Ratings Services affirmed its 'AA+' long-term and 'A-1+' short-term issuer credit ratings on Sweden's Stockholm County Council. The outlook is stable.

At the same time, we affirmed our 'K-1' short-term Nordic regional scale rating on Stockholm County Council.

## Rationale

The ratings reflect our view of Stockholm County Council's very strong economy and very low contingent liabilities, and Sweden's extremely predictable and supportive institutional framework. The ratings are further supported by our assessments of the county council's strong financial management, budgetary flexibility, and liquidity. These positive rating factors are balanced by Stockholm County Council's average budgetary performance and high debt burden, in our view. The long-term rating on Stockholm County Council is at the same level as its stand-alone credit profile, which we assess at 'aa+'.

Stockholm County Council's dynamic local economy has very strong economic fundamentals. Wealth and income levels are high and the county council's per capita GDP exceeds the national average. The local economy is well balanced and has a diverse industry structure, signaling its importance as a regional growth center. Population growth is strong, averaging 1.7% over the past three years. However, since the Swedish equalization system significantly balances wealth levels among local and regional governments (LRGs), we use Sweden's national GDP per capita of US\$59,053 as the starting point for our analysis.

Even though the county's increasing population adds to its operating expenditures, the county council has a track record of robust budgetary performance, with average

operating balances of 7.9% in 2012-2014. This was partly due to positive revenue developments on the back of a strong increase in tax revenues and sectorwide reimbursements of health insurance premiums. Still, high capital expenditures led to deficits after capital accounts averaging 4.8% for the period.

In our base case, we continue to anticipate a pick-up in tax revenue growth in 2015. Nevertheless, we expect that structural deficits at several of the county's hospitals and increased contributions to the Swedish LRG equalization system will reduce the county's operating balance to an average 5.2% of operating revenues during the 2015-2017 planning period. We factor into our base case that Stockholm County Council will reduce the deficits at several hospitals and contain the growth in operating expenditures by improving efficiency by year-end 2017. We expect that this, together with higher tax revenues, will lead to stabilization of its operating performance by that time.

Under our 2015-2017 base case, we project that Stockholm County Council's capital expenditures will continue increasing from their 2012-2014 levels. Our forecasts for the county's investments largely relate to property equipment upgrades, new buildings at a number of hospitals, and increased investments in public transportation. We expect investments to average a high 14.2% of total expenditures, leading to an average deficit after capital accounts of 10.3% of revenues through 2017. However, we expect capital expenditures to reach a peak during this period and to subsequently moderate to lower levels.

Although, in our view, Sweden's LRG equalization system has hampered Stockholm County Council, we consider it extremely predictable and supportive and a key component of our ratings on the county council. In our view, the system displays a high degree of institutional stability. The LRG sector's revenue and expenditure management is based on this far-reaching equalization system and on LRGs' autonomy in setting local taxes.

We view Stockholm County Council in particular as having strong revenue flexibility, which is important in light of its fairly rigid expenditure structure. We consider Stockholm County Council's financial management to be positive for the ratings and expect it to use this flexibility to counteract any potential budgetary deterioration.

Stockholm County Council has institutionalized strong debt management to handle its increasing loan portfolio, with diversified funding sources. In our base case for 2015-2017, we assume a high level of capital expenditures, due to significant infrastructure investments. Consequently, we forecast additional net new borrowings and expect that the county council's tax-supported debt will increase to about 83% of consolidated revenues by year-end 2017, from 57% in 2014. We factor in our assessment of Stockholm County Council's tax-supported debt our estimate of the present value of capital and funding costs stemming from its public-private partnership agreement for New Karolinska Hospital.

We assess Stockholm County Council on a consolidated basis, including transport company AB Storstockholms Lokaltrafik. As a result, we consider the county council's contingent liabilities to be very low.

## **Liquidity**

The short-term rating is 'A-1+'. We assess Stockholm County Council's liquidity as strong, as defined in our criteria, based on the county council's adequate debt-service coverage ratio over the next 12 months, including the expected financing of investments, with cash and external liquidity accounting for 103% of debt service for the 12 months started Sept. 30, 2015. We also incorporate in our liquidity assessment our view of the council's strong access to external liquidity.

In calculating Stockholm County Council's debt-service coverage ratio, we take into account its credit facilities: committed bank lines of Swedish krona (SEK) 1 billion (about €107 million) and a checking account with SEK3 billion. Furthermore, the county council has loan agreements with the European Investment Bank (EIB) linked to specific infrastructure investment plans. We include as a liquidity source part of the available amount under the EIB loans, taking into account that the EIB program extends beyond one year.

Refinancing risk is further reduced by the county council's range of funding alternatives. Funding is largely through a SEK5 billion commercial paper program, a SEK10 billion medium-term note program, and a €3 billion euro medium-term note program. Consequently, we acknowledge Stockholm County Council's strong and reliable capital market access in assessing its overall liquidity position.

We view Stockholm County Council's financial management as strong and expect it to continue its prudent approach to debt and liquidity management to handle its large loan portfolio. Liquidity will therefore likely remain strong through 2017.

## **Outlook**

The stable outlook reflects our expectation that Stockholm County Council will maintain average budgetary performance in 2015-2017, despite increasing capital investments and rising deficits after capital accounts. In our base-case scenario for the period, we do not expect the county's tax-supported debt to exceed 85% of consolidated operating revenues. The stable outlook also incorporates our expectation of continued prudent debt and liquidity management, with liquidity remaining a strong rating factor.

We could raise the ratings if, in line with our upside case, Stockholm County Council's financial management improved to the very strong category, from strong currently. This could happen if the county council strengthens its budgetary performance to the strong category, most likely by reducing deficits after capital accounts to below 5% of operating revenues, while maintaining operating balances over 5% of revenues. This, combined with exceptional liquidity, could lead to an upgrade.

The ratings could come under pressure if the county council's budgetary performance was worse than we currently expect, with deficits after capital expenditures on average higher than 10% of operating revenues. If, together with this, we saw the county council's liquidity deteriorating, with cash and committed back-up facilities structurally covering less than 80% of debt service, we could revise our assessment of financial management and liquidity downward and lower the ratings.

## Key Statistics

Table 1

Stockholm County Council Financial Statistics					
(Mil. SEK)	--Fiscal year ending Dec. 31--				
	2013	2014	2015bc	2016bc	2017bc
Operating revenues	80,913	82,604	86,157	89,540	93,722
Operating expenditures	74,617	76,528	81,991	84,953	88,465
Operating balance	6,296	6,076	4,166	4,587	5,257
Operating balance (% of operating revenues)	7.8	7.4	4.8	5.1	5.6
Capital revenues	533	153	100	100	100
Capital expenditures	9,813	13,553	13,530	14,015	14,595
Balance after capital accounts	(2,984)	(7,324)	(9,264)	(9,328)	(9,238)
Balance after capital accounts (% of total revenues)	(3.7)	(8.9)	(10.7)	(10.4)	(9.8)
Debt repaid	2,100	4,100	3,262	3,242	4,873
Balance after debt repayment and onlending	(2,249)	(10,569)	(12,526)	(12,570)	(14,111)
Balance after debt repayment and onlending (% of total revenues)	(2.8)	(12.8)	(14.5)	(14.0)	(15.0)
Gross borrowings	1,573	9,062	13,562	12,570	14,111
Balance after borrowings	(676)	(1,507)	1,036	0	0
Operating revenue growth (%)	4.8	2.1	4.3	3.9	4.7
Operating expenditure growth (%)	5.8	2.6	7.1	3.6	4.1
Modifiable revenues (% of operating revenues)	81.1	82.2	83.1	84.4	84.3
Capital expenditures (% of total expenditures)	11.6	15.0	14.2	14.2	14.2
Direct debt (outstanding at year-end)	28,187	31,438	41,738	51,066	60,304
Direct debt (% of operating revenues)	34.8	38.1	48.4	57.0	64.3
Tax-supported debt (% of consolidated operating revenues)	55.5	57.2	66.6	73.8	82.9
Interest (% of operating revenues)	1.6	1.1	1.4	1.9	2.5
Debt service (% of operating revenues)	4.2	6.1	5.1	5.5	7.7

The data and ratios above result in part from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's 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 Standard & Poor's expectations of the most likely scenario. SEK--Swedish krona.

**Table 2**

<b>Stockholm County Council Economic Statistics</b>						
	<b>--Fiscal year ending Dec. 31--</b>					
	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015bc</b>	<b>2016bc</b>	<b>2017bc</b>
Population	2,127,006	2,163,042	2,199,949	2,242,335	2,285,227	2,327,818
Population growth (%)	1.7	1.7	1.7	1.9	1.9	1.9
GDP per capita (SEK)	518,326	527,167	N/A	N/A	N/A	N/A
Real GDP growth (%)	N/A	N/A	N/A	N/A	N/A	N/A
Unemployment rate (%)	5.0	5.4	5.1	5.1	N/A	N/A

The data and ratios above result in part from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. bc--Base case: reflects Standard & Poor's expectations of the most likely scenario. SEK--Swedish krona. N/A--Not applicable. Sources typically include national statistical offices, Eurostat, and Experian Ltd.

## Ratings Score Snapshot

**Table 3**

<b>Stockholm County Council Ratings Score Snapshot</b>	
<b>Key rating factors</b>	
Institutional framework	Extremely predictable and supportive
Economy	Very strong
Financial management	Strong
Budgetary flexibility	Strong
Budgetary performance	Average
Liquidity	Strong
Debt burden	High
Contingent liabilities	Very low

\*Standard & Poor's ratings on local and regional governments (LRGs) are based on eight main rating factors listed in the table above. Section A of Standard & Poor's "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

Sovereign Risk Indicators - October 12, 2015. Interactive version available at <http://www.spratings.com/sri>

## Related Criteria And Research

### Related Criteria

- General Criteria: Standard & Poor's National And Regional Scale Mapping Tables - September 30, 2014
- General Criteria: National And Regional Scale Credit Ratings - September 22, 2014

*Research Update: Stockholm County Council Ratings Affirmed At 'AA+/A-1+' And 'K-1'; Outlook Stable*

- 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
- Criteria - Governments - International Public Finance: Methodology And Assumptions: The Impact Of PPP Projects On International Local And Regional Governments: Refined Accounting Treatment - December 15, 2008

**Related Research**

- Sovereign Risk Indicators - October 12, 2015. An interactive version is available at [www.spratings.com/sri](http://www.spratings.com/sri).
- Swedish Local And Regional Government Risk Indicators: May 2015 - May 28, 2015
- Sweden's New Equalization System Will Hurt Some LRGs' Finances But Not Their Credit Quality - February 9, 2015

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

To

From

Stockholm County Council

Issuer credit rating

## Ratings List Continued...

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		
Commercial Paper		
Nordic Regional Scale	K-1	K-1

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