

RatingsDirect®

Lund (Municipality of)

Primary Credit Analyst:

Dennis Nilsson, Stockholm + 46 84 40 5354; dennis.nilsson@spglobal.com

Secondary Contact:

Carl Nynerod, Stockholm + 46 84 40 5919; carl.nynerod@spglobal.com

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Lund (Municipality of)

This report does not constitute a rating action.

Key Rating Factors

Issuer Credit Rating

AAA/Stable/A-1+
Nordic Regional Scale
--/--/K-1

| Credit context and assumptions | Base-case expectations |
|---|---|
| <p>The supportive central government and robust tax revenue growth underpin Lund's strong performance.</p> <ul style="list-style-type: none">Sweden's central government has provided extensive support to the local and regional government (LRG) sector in response to the COVID-19 pandemic.S&P Global Ratings expects higher tax revenue growth will support operating performance.That said, demographic-related cost pressure will weigh on Lund's budgetary performance. | <p>Investment levels will remain elevated in the coming years, with continued debt buildup.</p> <ul style="list-style-type: none">A large share of debt is on-lent to the financially strong municipal housing company Lunds Kommuns Fastighets AB (LKF).Lund has strong liquidity with ample backup facilities.Management is strongly committed to the municipality's financial stability. |

Outlook

The stable outlook indicates that we expect Lund's local assembly and management will enact and implement the measures necessary to maintain a balanced budget, compliant with regulatory requirements, on a structural level, and weather the effects of the pandemic.

Downside scenario

We could consider lowering the ratings if Lund is unable to curb pressure on its results, stemming from demographic-related spending or conditions caused by the pandemic, resulting in persistent deficits against regulatory requirements or internal surplus targets. We could also lower the rating if systemic support to the Swedish LRG sector remains insufficient.

Rationale

We forecast Lund will uphold relatively strong operating performance through our forecast period to 2023, supported by temporary grants from government support packages, stronger tax revenue growth, and efficiency measures undertaken by the municipality itself. We believe Lund will continue to improve cost efficiency, which will partly offset the negative impact from higher unemployment following the pandemic. Investments, both within the municipality and its companies, will remain sizable, albeit declining through 2023. We further expect Lund will remain committed to prudent debt and liquidity policies, enabling it to control the increasing debt burden and maintain a favorable liquidity position.

Government support mitigates risks from the pandemic, although sector-wide risks remain

Although we consider that the institutional framework is generally supportive of Swedish LRGs, we regard the trend as weakening. In recent years, the Swedish LRG sector's budgetary performance has deteriorated due to increasing expenditure--spurred by central government policymaking--alongside insufficient central government compensation mechanisms and inadequate countermeasures by LRGs.

Nevertheless, we believe the institutional framework remains a key credit strength for Swedish LRGs. In our view, the framework displays a high degree of stability, and the sector's revenue and expenditure management is based on a far-reaching equalization system and autonomy in setting local taxes. Furthermore, we think the central government's swift response to the COVID-19 pandemic, illustrated by increased grants, for instance, supports our opinion.

The incumbent minority administration in Lund has, since taking office in 2018, emphasized the importance of financial sustainability by imposing stricter financial targets. Although Lund breached the Swedish balanced budget requirement in 2019, we note that progress has been made on efficiency measures, and we expect management will act to maintain compliance with regulatory requirements. Furthermore, we believe management's continued focus on financial sustainability will be key in facing the pressure of demographic challenges and navigating the effects of the pandemic.

Lund benefits from Sweden's high wealth levels, illustrated by our estimate of national GDP per capita in 2021 of approximately Swedish krona (SEK) 506,733 (about \$60,800). The municipality also benefits from its wealthy, fast-developing local economy and highly educated labor force.

A focus on financial sustainability is needed to face upcoming demographic pressures as government support is phased out

Similar to 2020, we forecast continued strong operating performance for 2021. This is mainly driven by higher tax revenue growth and COVID-19-related grants to the sector, as well as lower costs in departments such as elderly care that saw lower user volumes amid the pandemic. That said, we still expect cost pressures relating to demographic changes to resume in 2022. We expect operating balances to revert to a structural level below 5% from 2022 as COVID-19-related grants are phased out.

Compared to our last review, the sector's tax revenue growth was higher than expected for both 2020 and 2021, largely due to the substantial government grants and labor-market support schemes. Although tax revenue growth has

proven resilient to the economic downturn, there are still lingering pandemic-related effects facing the sector. For instance, Lund expects (similar to other Swedish municipalities) that school departments will need additional funding in the coming years to accommodate higher student failure rates linked to remote education during the pandemic.

We anticipate Lund's investments will remain sizable throughout the forecast period, since demand for core municipal infrastructure remains high. However, Lund expects a larger portion of planned investments to be carried out in 2021, whereafter investments will decrease in line with updated population growth forecasts. We expect the municipality to see a trend of balanced accounts from about 2024 (balance after capital accounts). Furthermore, we expect municipal companies' borrowing needs will remain sizable, since housing company LKF and the partly owned water utility company VA Syd are in a period of relatively high investments.

The bulk of these investments will be funded from borrowings lent by the municipality, leading us to expect Lund's tax-supported debt to increase moderately over the next two years. The group's debt and liquidity are coordinated and managed via the city treasury, except for Krafringen Energi AB (publ) (A-/Stable/A-2), which funds itself entirely in its own name, and part of LKF's borrowings, which it can choose to fund via guarantee-supported loans from public sector funding agency Kommuninvest i Sverige AB. We regard Lund's contingent liabilities, including its pro-rata ownership share of Krafringen's debt, LKF's external loans, and Lund's extended joint and several guarantee for its Kommuninvest membership, as limited, and not negative for Lund's debt assessment.

Moreover, we consider on-lending to LKF and regulated water utility company VA Syd a mitigant to Lund's overall debt burden because these companies have strong financial and commercial business profiles. Adjusted for these two companies' debt, Lund's tax-supported debt would decrease to about 42% of consolidated operating revenue.

We still regard Lund as having stronger-than-average financial flexibility. The political leadership is committed to fiscal prudence, and has proved itself willing to divest assets such as landholdings or those in its relatively large company sector to comply with its financial targets. Another example is the imposed efficiency measures aimed at improved performance, which we deem a necessity to navigate the currently challenging economic environment.

Lund's liquidity position remains very favorable, primarily supported by ample committed facilities covering 147% of the average coming 12-months' debt service. We also view the municipality as having strong access to external liquidity. In our liquidity calculation, we include about SEK3 billion in committed liquidity facilities, about SEK150 million in cash, and about SEK300 million in financial assets (to which we have applied an appropriate haircut). Moreover, we calculate that Lund has average borrowing needs of about SEK360 million for the coming years, and will need to service about SEK1.7 billion in maturing debt and interest over the coming 12 months, including LKF's maturing borrowings from Kommuninvest. In our view, Lund's financial management is prudent and adheres to conservative debt and liquidity policies.

Key Statistics

Table 1

| Lund (Municipality of) Selected Indicators | | | | | | |
|---|-------------|-------------|-------------|---------------|---------------|---------------|
| (Mil. SEK) | 2018 | 2019 | 2020 | 2021bc | 2022bc | 2023bc |
| Operating revenues | 8,295 | 8,564 | 9,062 | 9,287 | 9,488 | 9,726 |
| Operating expenditures | 7,892 | 8,268 | 8,244 | 8,646 | 9,049 | 9,294 |
| Operating balance | 403 | 296 | 818 | 641 | 439 | 432 |
| Operating balance (% of operating revenues) | 4.9 | 3.5 | 9.0 | 6.9 | 4.6 | 4.4 |
| Capital revenues | 257 | 221 | 136 | 150 | 150 | 150 |
| Capital expenditures | 1,122 | 974 | 879 | 1,111 | 1,022 | 901 |
| Balance after capital accounts | (462) | (457) | 75 | (319) | (433) | (319) |
| Balance after capital accounts (% of total revenues) | (5.4) | (5.2) | 0.8 | (3.4) | (4.5) | (3.2) |
| Debt repaid | 1,300 | 2,600 | 1,800 | 1,550 | 1,950 | 2,600 |
| Gross borrowings | 1,451 | 2,489 | 1,700 | 2,146 | 2,803 | 3,449 |
| Balance after borrowings | 24 | 31 | 75 | (36) | (0) | 0 |
| Direct debt (outstanding at year-end) | 6,100 | 6,100 | 6,000 | 6,596 | 7,449 | 8,297 |
| Direct debt (% of operating revenues) | 73.5 | 71.2 | 66.2 | 71.0 | 78.5 | 85.3 |
| Tax-supported debt (outstanding at year-end) | 6,116 | 6,213 | 6,213 | 6,809 | 7,812 | 8,710 |
| Tax-supported debt (% of consolidated operating revenues) | 67.5 | 67.3 | 63.5 | 67.8 | 76.1 | 82.7 |
| Interest (% of operating revenues) | 0.3 | 0.3 | 0.5 | 0.4 | 0.4 | 0.4 |
| Local GDP per capita (single units) | N/A | N/A | N/A | N/A | N/A | N/A |
| National GDP per capita (single units) | 477,094 | 493,600 | 481,951 | 506,733 | 528,119 | 545,883 |

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. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful. SEK--Swedish krona.

Ratings Score Snapshot

Table 2

| Lund (Municipality of) Ratings Score Snapshot | |
|--|---------------|
| Key rating factors | Scores |
| Institutional framework | 1 |
| Economy | 1 |
| Financial management | 2 |
| Budgetary performance | 2 |
| Liquidity | 1 |
| Debt burden | 2 |
| Stand-alone credit profile | aaa |
| Issuer credit rating | AAA |

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

- Sweden, Aug. 16, 2021

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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Institutional Framework Assessments For International Local And Regional Governments, Sept. 8, 2021
- European Local And Regional Government Risk Indicators, Sept. 1, 2021
- Non-U.S. Local Governments: To What Extent Did Sovereign Support Offset The Pandemic Downturn, July 19, 2021
- Sovereign Risk Indicators, July 12, 2021. An interactive version is available at <http://www.spratings.com/sri>
- Extra Funding In Sweden's 2021 Budget Will Support LRGs, Sept. 24, 2020
- COVID-19: Fiscal Response Will Lift Local And Regional Government Borrowing To Record High, June 9, 2020
- COVID-19 Could Further Strain Swedish LRGs' Budgets, May 20, 2020
- Swedish Government To Mitigate Impact From Coronavirus On Local And Regional Governments, March 11, 2020
- Public Finance System Overview: Swedish Municipalities And Regions, Dec. 3, 2019

Ratings Detail (As Of September 13, 2021)*

Lund (Municipality of)

| | |
|------------------------------|-----------------|
| Issuer Credit Rating | AAA/Stable/A-1+ |
| <i>Nordic Regional Scale</i> | --/--/K-1 |
| Commercial Paper | |
| <i>Local Currency</i> | A-1+ |
| <i>Nordic Regional Scale</i> | K-1 |

Issuer Credit Ratings History

| | |
|--|-----------------|
| 28-Sep-2010 | AAA/Stable/A-1+ |
| 28-Sep-2010 <i>Nordic Regional Scale</i> | --/--/K-1 |

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

Additional Contacts:

Freja L Dobreff, Stockholm; freja.dobreff@spglobal.com
EMEA Sovereign and IPF; SovereignIPF@spglobal.com

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