

Research Update:

Swedish Municipality of Lund 'AAA/A-1+' Ratings And 'K-1' Ratings Affirmed; Outlook Stable

September 11, 2020

Overview

- We believe central government support packages will shield Lund's tax-revenue growth in 2020, which in tandem with increased state grants and efficiency measures undertaken by Lund, will support performance over the coming two years.
- Downside risk remains, and we expect Lund, supported by the central government, will act prudently and counterbalance any major pressure that might arise from the pandemic.
- We are therefore affirming our 'AAA/A-1+' and 'K-1' ratings on Lund. The outlook is stable.

Rating Action

On Sept. 11, 2020, S&P Global Ratings affirmed its 'AAA' long-term and 'A-1+' short-term issuer credit ratings on the Swedish Municipality of Lund. The outlook is stable.

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

Outlook

The stable outlook indicates that we expect Lund's local assembly and management will enact and implement the measures necessary to restore a balanced budget, compliant with regulatory requirements, and weather the COVID-19-induced economic downturn.

Downside scenario

We could consider lowering the ratings if Lund is unable to curb pressure on its results, stemming from demographic-related spending or weaker economic 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.

PRIMARY CREDIT ANALYST

Carl Nyrerod
Stockholm
(46) 8-440-5919
carl.nyrerod
@spglobal.com

SECONDARY CONTACT

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

ADDITIONAL CONTACT

EMEA Sovereign and IPF
SovereignIPF
@spglobal.com

Rationale

We forecast Lund will be able to uphold its relatively strong operating performance through our forecast period to 2022, supported by central government support packages, including increased grants and amendments to furlough schemes, alongside 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 and relatively weak tax-revenue growth over the coming two years. Investments, both within the municipality and its companies, will remain sizable, and we expect Lund will remain committed to prudent debt and liquidity policies, enabling it to control the increasing debt burden and maintain its favorable liquidity position.

Government support mitigates risks from the pandemic, although sectorwide risks remain

Although we consider that the institutional framework is generally supportive of Swedish local and regional governments (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 the 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 restore compliance with internal surplus targets and regulatory requirements. Furthermore, we believe management's continued focus on financial sustainability will be key in navigating the effects of the pandemic.

Lund benefits from Sweden's high wealth levels, illustrated by our estimate of national GDP per capita in 2020 of approximately Swedish krona (SEK) 468,000 (about \$51,100). The Swedish economy has proven relatively resilient, and we forecast GDP per capita will contract by about 5.8% in 2020, compared with 7.8% in the eurozone. In addition, Lund benefits from its wealthy, fast-developing local economy and highly educated labor force.

A focus on financial sustainability and government support mitigate fallout from the pandemic

Compared with our last review, we forecast stronger operating performance. The sector's 2020 tax-revenue growth has proven to be fairly resilient to the economic downturn, given that policy reforms undertaken by the central government, such as improvements of furlough schemes, are supporting taxable income levels, despite a reduction in the number of hours worked and employment. In addition, the central government has increased grants to the sector, and committed itself to cover certain COVID-19-related expenditure. In combination with Lund's own efficiency measures, we expect operating performance will temporarily soar in 2020.

Research Update: Swedish Municipality of Lund 'AAA/A-1+' Ratings And 'K-1' Ratings Affirmed; Outlook Stable

Although we expect some economic recovery in 2021 and 2022, we estimate tax-revenue growth will remain hampered, since some of the support packages will come to an end, and at the same time we factor in higher operating spending, caused by rising unemployment. Consequently, we believe Lund's operating margins will come down from the expected peak in 2020. That said, we expect Lund, supported by the central government, will make necessary policy reforms to curb the pressure from a worsened economic downturn, should it arise.

We anticipate Lund's investments will remain sizable over the coming two years, since demand for core municipal infrastructure remains high. A limit on annual investment was imposed in 2018, and we expect investments to be roughly on par with those made in 2019, leading to narrower, yet still noticeable, deficits after capital accounts. Furthermore, we expect municipal companies' borrowing needs will remain sizable, since the housing company (Lunds Kommunala Fastighets AB; LKF) and the partly owned water utility company VA Syd are in a period of relatively high investments.

Since the bulk of these investments will be funded from borrowings lent by the municipality, we expect Lund's tax-supported debt to increase moderately over the coming two years. The group's debt and liquidity is coordinated and managed via the city treasury, except for Krafringen Energi AB (publ) (BBB+/Stable/A-2), which funds itself entirely in its own name, and parts of LKF's borrowings, which it can choose to fund via guarantee-supported loans from the 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 regard onlending to LKF and the regulated water utility company VA Syd as 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 139% of 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 and about SEK325 million in cash and financial assets (to which we have applied an appropriate haircut). Moreover, we calculate that Lund has an average borrowing need of about SEK300 million, and will need to service about SEK2.2 billion in maturing debt and interests 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	--Year ended Dec. 31--					
	2017	2018	2019	2020bc	2021bc	2022bc
Operating revenues	8,006	8,295	8,564	9,049	9,295	9,484
Operating expenditures	7,467	7,892	8,268	8,511	8,806	9,011
Operating balance	539	403	296	538	489	473
Operating balance (% of operating revenues)	6.7	4.9	3.5	5.9	5.3	5.0
Capital revenues	58	257	221	139	150	150
Capital expenditures	873	1,122	974	945	1,006	938
Balance after capital accounts	(276)	(462)	(457)	(268)	(368)	(315)
Balance after capital accounts (% of total revenues)	(3.4)	(5.4)	(5.2)	(2.9)	(3.9)	(3.3)
Debt repaid	1,450	1,300	2,600	1,800	1,750	1,950
Gross borrowings	2,050	1,451	2,489	2,022	2,366	2,546
Balance after borrowings	(114)	24	31	39	(30)	(0)
Direct debt (outstanding at year-end)	5,950	6,100	6,100	6,322	6,938	7,534
Direct debt (% of operating revenues)	74.3	73.5	71.2	69.9	74.6	79.4
Tax-supported debt (outstanding at year-end)	5,966	6,116	6,116	6,595	7,291	8,007
Tax-supported debt (% of consolidated operating revenues)	68.0	67.5	66.2	68.1	73.3	78.8
Interest (% of operating revenues)	0.3	0.3	0.3	0.3	0.4	0.5
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	462,734	477,094	490,783	467,584	491,779	511,257

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. SEK--Swedish krona.

Ratings Score Snapshot

Table 2

Lund (Municipality of) Ratings Score Snapshot

Key rating factors

Institutional framework	1
Economy	1
Financial management	2
Budgetary performance	2
Liquidity	1
Debt burden	2

Table 2

Lund (Municipality of) Ratings Score Snapshot (cont.)

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

- Research Update: Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Remains Stable, Aug. 14, 2020

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

- European Local And Regional Government Risk Indicators, June 30, 2020
- Sovereign Risk Indicators, July 14, 2020. An interactive version is also available at <http://www.spratings.com/sri>
- 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
- 2018 Annual International Public Finance Default And Rating Transition Study, Aug. 19, 2019
- Institutional Framework Assessments For International Local And Regional Governments, July 4, 2019
- Public Finance System Overview: Swedish Municipalities And Regions, Dec. 3, 2019
- Sweden's Local Governments To Get A Slight Boost From 2020 Budget, Sept. 20, 2019
- Sweden's Municipal Sector Faces An Equalization Shake-Up, Sept. 13, 2019
- A Potential Profit Cap On Private Operators In Sweden's Welfare Sector Could Increase LRG Spending, March 11, 2019
- Kraftringen Energi AB (publ), May 12, 2020.

Research Update: Swedish Municipality of Lund 'AAA/A-1+' Ratings And 'K-1' Ratings Affirmed; Outlook Stable

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

Lund (Municipality of)

Issuer Credit Rating	AAA/Stable/A-1+
Nordic Regional Scale	--/--/K-1
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. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 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.

Copyright © 2020 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.