Research Update:

City of Oslo Outlook Revised To Negative On Potentially Larger Deficits; Ratings Affirmed At 'AAA'

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Overview

- We expect Oslo's operating performance will improve this year thanks to stronger tax revenue growth and moderating cost pressure, but to remain weaker than historical levels through 2026.
- Oslo's continued high investment needs in municipal properties and infrastructure projects will contribute to sustained budgetary deficits and debt accumulation.
- Because the operating performance improvements may not be enough to cover potentially increasing investment needs, Oslo could face wider-than-anticipated deficits and faster debt build-up.
- We therefore revised to negative from stable the outlook on Oslo and affirmed the 'AAA' ratings.

Rating Action

On May 10, 2024, S&P Global Ratings revised the outlook to negative from stable on the long-term issuer credit rating on the Norwegian City of Oslo. At the same time, we affirmed the 'AAA' long-term issuer credit ratings.

We also affirmed our 'AAA' issue ratings on Oslo's senior unsecured debt.

Outlook

The negative outlook reflects an increased risk that Oslo's deficits will widen structurally if fairly stable operating performance and capital grants are insufficient to cover consistently large investment needs and related spending.

Downside scenario

We could lower the rating on Oslo over the coming 24 months if the city's high capital expenditure (capex) resulted in structurally wider deficits. This would accelerate debt accumulation and reflect an increased risk appetite, which might affect our view on the city's fiscal management.

We could also lower the rating if systemic support to Norwegian local and regional governments (LRGs) became insufficent and central government policies do not adequately address any build-up of debt in the sector.

Upside scenario

We could revise the outlook to stable if the city's management sucessfully contains deficits after capital accounts, for instance by strenghening operating performance and stabilizing capex.

Rationale

The outlook revision to negative captures the risk that persistently high investments may keep deficits wider and for longer than we currently project. Oslo's operating performance weakened more than we expected in 2023 because of inflationary pressure on operating costs and capex, widening the deficit after capital accounts to 7.5% of total revenue from 5.0% at end-2022. Although we assume the city management's efforts to contain costs and stabilize capex will give way to gradually narrower deficits in 2024-2026, local infrastructure projects--mainly related to transportation and water and sewage--to keep up with continued population growth and to update old facilities could incur higher costs than expected at this time.

Oslo's very wealthy local economy is a fundamental credit strength

We continue to regard the institutional framework for Norwegian LRGs as extremely predictable and supportive. That said, we revised the trend to weakening to reflect our view of persistent mismatches between revenue and total expenditure, particularly in the capital accounts. These mismatches have caused Norwegian LRGs to accumulate debt, and central government policies have not adequately addressed this build-up. Still, the very strong system support provides Norwegian LRGs a high degree of institutional stability, and there are mechanisms in place to ensure that they do not experience financial distress. If debt continues to climb, however, the resulting uncertainty about the sector's debt burden, alongside the LRGs' limited autonomy to adjust revenues, would raise questions about the system's predictability.

With an eye on maintaining budgetary strength, Oslo's management has implemented an exhaustive review of its operations and the use of resources for potential inefficiencies. The city's prudent debt-management strategy, which stipulates that most funding is through fixed-rate, long-term bonds, remains intact, providing it with a very predictable debt-maturity profile. Conservative and liberal parties, with support from the Christian Democrats and the Progress Party, have governed Oslo since the local election in fall 2023. The coalition has ambitious targets to reduce the environmental footprint and lower property taxes, which could lead to increased debt funding in the near term as capex will remain high. We understand the coalition will remain committed to the city's long-term strategies and will focus largely on gains from operational efficiency to fund its reforms.

Importantly, Oslo benefits from Norway's very high wealth levels. We estimate a national GDP per capital estimate of about $87,000 in 2024. As Norway's capital, Oslo has a very diversified and wealthy local economy, hosting a broad range of government functions, financial services, and corporate sectors.

Continued high capex amid slightly weaker-than-historical operating performance will accelerate debt accumulation

We expect operating performance will strengthen this year after a temporary weakening in 2023. The city's operating balance will reach 5.5% of operating revenue in 2024, from 4.4% in 2023, before stabilizing at an average of 6.0% in 2025-2026. We think that, from 2024 on, the city's tax revenue will resume growing in line with the economy, thereby helping to strengthen and stabilize operating balances, even though performance remains slightly weaker than historical levels. We understand changes to the equalization system could be announced in May, when the central government publishes its municipal proposition 2025. We assume revisions could include larger transfers from cities to rural areas and that they would be gradually implemented or be accompanied by compensation during the transition.

Sustained high capex could accelerate debt accumulation and widen deficits further. We expect Oslo's annual capex will average Norwegian krone (NOK) 17.7 billion in 2024-2026, with a slight decreasing trend. About half of this capex will go to transport and municipal technical facilities, related to water and sewage, for instance, while about 25% will be spent on schools and kindergartens. The remainder will go to sheltered/municipal housing and urban development, among other items. Considering the capex peak in 2023 and the ensuing deficit after capital accounts of 7.5% of revenue, we assume the metric will stabilize around 4.0% by 2026.

Oslo has high capex relative to its domestic peers since it operates as both a region and municipality. However, some capex is financed with capital grants from the central government, which are roughly equal to funding from cash flow from the city's operations and debt uptake. Consequently, we think debt will reach 93% of operating revenue by 2026, from 85% in 2023. We regard the city's contingent liabilities, including the debt of fully owned energy company Hafslund Eco AS, as limited, with contingent debt corresponding to 15% of aggregated revenues.

We consider the city's liquidity to be strong despite the weaker-than-peers' debt-service coverage ratio, supported by strong liquidity access through the capital markets and KBN Kommunalbanken Norway, a public sector funding agency owned by the central government. We estimate that Oslo's liquidity sources will cover 64% of the average debt service for the coming 12 months. Our calculation of internal liquidity sources includes about NOK6 billion of cash and NOK2 billion in committed facilities. We estimate that the city has net borrowing needs of about NOK2.9 billion over the coming 12 months, in addition to the NOK7.0 billion of maturing debt and interest payments. We also note Oslo Pensjonsforsikring AS, the pension fund for public employees at the City of Oslo, represents a source of contingent liquidity; this is because it could lend to the city by investing in its bond issuance, if needed, as an emergency alternative to rolling over debt. However, we do not include this in our sources-to-uses liquidity ratio, as it's an emergency option.

Key Statistics

Table 1

City of Oslo--Selected Indicators

Mil. NOK	2021	2022	2023	2024bc	2025bc	2026bc
Operating revenues	84,596	87,922	91,479	95,909	99,049	101,849
Operating expenditures	77,952	80,951	87,496	90,610	93,146	95,790

Table 1

City of Oslo--Selected Indicators (cont.)

Mil. NOK	2021	2022	2023	2024bc	2025bc	2026bc
Operating balance	6,644	6,971	3,983	5,298	5,903	6,059
Operating balance (% of operating revenues)	7.9	7.9	4.4	5.5	6.0	5.9
Capital revenues	4,468	5,049	7,224	7,013	6,840	7,004
Capital expenditures	13,989	16,698	18,599	18,301	17,270	17,486
Balance after capital accounts	(2,877)	(4,678)	(7,392)	(5,990)	(4,527)	(4,423)
Balance after capital accounts (% of total revenues)	(3.2)	(5.0)	(7.5)	(5.8)	(4.3)	(4.1)
Debt repaid	5,000	4,500	4,000	5,000	4,735	6,500
Gross borrowings	9,500	10,000	10,463	11,500	10,500	11,500
Balance after borrowings	1,431	33	(491)	(240)	488	(173)
Direct debt (outstanding at year-end)	62,548	68,819	77,630	84,130	89,895	94,895
Direct debt (% of operating revenues)	73.9	78.3	84.9	87.7	90.8	93.2
Tax-supported debt (outstanding at year-end)	62,548	68,819	77,630	84,130	89,895	94,895
Tax-supported debt (% of consolidated operating revenues)	73.9	78.3	84.9	87.7	90.8	93.2
Interest (% of operating revenues)	1.4	1.7	2.3	2.2	2.6	3.0
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	802,010	1,052,149	934,351	905,257	929,538	955,914

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.

Ratings Score Snapshot

Table 2

City of Oslo--Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	1
Budgetary performance	2
Liquidity	2
Debt burden	3
Stand-alone credit profile	aaa

Table 2

City of Oslo--Ratings Score Snapshot (cont.)

Key rating factors	Scores
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 our "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

Sovereign Risk Indicators, April 8, 2024. An interactive version is available at www.spratings.com/sri.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Rising Debt Points To A Weakening Trend For Norwegian LRGs, March 21, 2024
- Full Analysis: Norway, March 11, 2024
- Subnational Debt 2024: Focus on Debt Sustainability, Feb. 29, 2024
- Subnational Debt 2024: Infrastructure Spending Succumbs To Economic Slowdown, Feb. 29, 2024
- Subnational Debt 2024: Global LRGs Can Handle Rising Interest Expenses, Feb. 29, 2024

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

Outlook Action; Ratings Affirmed

	To	From
Oslo (City of)		
Issuer Credit Rating	AAA/Negative/--	AAA/Stable/--
Senior Unsecured	AAA	AAA