

Rating Action: Moody's Public Sector Europe changes outlook on Olsztyn's rating to stable from negative; rating affirmed

Global Credit Research - 15 May 2017

London, 15 May 2017 -- Moody's Public Sector Europe (MPSE) has today changed the outlook on the City of Olsztyn's rating to stable from negative. The long-term issuer rating of Baa1 has been affirmed.

Today's rating action was prompted by the improvement in Poland's credit profile as captured by Moody's recent decision to change the outlook on Poland's A2 government bond rating to stable from negative. For details, please refer to the press release: https://www.moody.com/research/--PR_366374.

RATINGS RATIONALE

RATIONALE FOR THE CHANGES IN OUTLOOK TO STABLE

The outlook change to stable on Poland's A2 government bond rating on 12 May 2017 prompted the outlook change to stable from negative on Olsztyn's rating. The sovereign outlook change indicates improved fiscal strengths, that supports the credit profile of Polish sub-sovereigns due to close financial linkages with the central government.

RATIONALE FOR THE AFFIRMATION

The affirmation of the City of Olsztyn's rating reflects its satisfactory operating performance, improving financial results, declining debt levels and comfortable liquidity position.

The rating of Olsztyn takes into account the fact that it receives the bulk of its operating revenues from the central government. These revenues take the form of national taxes which are collected and then redistributed to cities. Growing proceeds from shared taxes have resulted in an increase in the cities' budget volumes. These growing budget volumes, combined with the City of Olsztyn's disciplined financial management and close oversight of municipal-related service companies, enabled the city to demonstrate good operating performances, with operating surpluses at 10% of operating revenue in 2016 compared with 4.5% in 2015. At the same time, Olsztyn posted a financing surplus at 11% of total revenue compared with a high deficit of 12% at year-end 2015.

Olsztyn's debt decreased to 30% of operating revenue in 2016 from 42% at year-end 2015 driven by lower capital spending, and is projected to remain at similar levels in 2017.

WHAT COULD CHANGE THE RATINGS UP/DOWN

An upgrade of the City of Olsztyn's rating would require an upgrade of the sovereign rating, associated with a significant improvement of the city's operating margin and sustained balanced financial performance. Significant change in the Polish RLGs' revenue and expenditure flexibility and ability to raise additional own-source revenues would also have positive implications for the rating.

A downgrade of Poland's sovereign rating will lead to a similar action on Olsztyn's rating. In addition, a significant deterioration in financial performance and cash reserves and/or an increase in debt levels above 60% of operating revenue may exert downward rating pressure.

The sovereign action required the publication of this credit rating action on a date that deviates from the previously scheduled release date in the sovereign release calendar, published on www.moody.com.

The specific economic indicators, as required by EU regulation, are not available for Olsztyn, City of. The following national economic indicators are relevant to the sovereign rating, which was used as an input to this credit rating action.

Sovereign Issuer: Poland, Government of

GDP per capita (PPP basis, US\$): 27,764 (2016 Actual) (also known as Per Capita Income)

Real GDP growth (% change): 2.7% (2016 Actual) (also known as GDP Growth)

Inflation Rate (CPI, % change Dec/Dec): 0.8% (2016 Actual)

Gen. Gov. Financial Balance/GDP: -2.4% (2016 Actual) (also known as Fiscal Balance)

Current Account Balance/GDP: -0.3% (2016 Actual) (also known as External Balance)

External debt/GDP: [not available]

Level of economic development: High level of economic resilience

Default history: No default events (on bonds or loans) have been recorded since 1983.

On 12 May 2017, a rating committee was called to discuss the rating of the Olsztyn, City of. The main points raised during the discussion were: The systemic risk in which the issuer operates has materially decreased.

The principal methodology used in these ratings was Regional and Local Governments published in January 2013. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

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