

Research

Russian City of Novosibirsk 'BB+' And 'ruAA+' Ratings Affirmed; Outlook Negative

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OVERVIEW

- Continuing support from Novosibirsk Oblast, coupled with management's cautious spending and debt policies, will likely underpin the City of Novosibirsk's average financial performance, adequate liquidity, and low debt over the next three years.
- We are therefore affirming our 'BB+' and 'ruAA+' ratings on the City of Novosibirsk.
- The negative outlook on Novosibirsk solely mirrors that on Russia. We could take a negative rating action on the city if we took a negative rating action on Russia.

RATING ACTION

On Sept. 25, 2015, Standard & Poor's Ratings Services affirmed its 'BB+' long-term issuer credit rating on Russia's City of Novosibirsk. The outlook is negative.

At the same time, we affirmed our 'ruAA+' Russia national scale rating on the city and our 'BB+' and 'ruAA+' issue ratings on the city's senior unsecured bonds.

RATIONALE

The ratings are constrained by what we see as Novosibirsk's relatively weak economy and Russia's volatile and unbalanced institutional framework, which limits the city's budgetary flexibility to weak. These constraints are mitigated by Novosibirsk's satisfactory management quality and reasonable cost control, which

results in average budgetary performance, adequate liquidity, low debt, and very low contingent liabilities.

The issuer credit rating on the city is equal to its stand-alone credit profile.

The economy of Novosibirsk, Russia's third-largest city, is weak, but relatively diversified. The wealth levels are low compared with international peers; GDP per capita stands at about \$12,000, which is in line with the Russian average. Novosibirsk's economy is constrained by low industrial productivity and the poor state of its municipal infrastructure remains a long-term challenge. These constraints are somewhat mitigated by the relatively diverse nature of the city's economy. It has an expanding services sector, transport, and research and development activities. The city's 10 largest enterprises contribute about 3% of total employment and about 8% of Novosibirsk's tax revenues.

We view Novosibirsk's budgetary flexibility as weak compared with international peers because of its exposure to federal and regional government decisions regarding the city's share of taxes, the allocation of transfers, and the redistribution of spending responsibilities.

The majority of the municipal revenues are not regulated by the city, and it is difficult to predict decision-making at the Novosibirsk Oblast and federal government level. In the oblast's budget, it decides what share of personal income tax the city will receive in addition to the amount outlined in the federal budget code. This share represented about 25% of the city's operating revenues in 2014.

Despite limited budgetary flexibility, the city's financial management has demonstrated reasonable cost control and prudent debt and liquidity policies. We observed no changes in Novosibirsk's established managerial procedures following mayoral elections in April 2014. As a result, we maintain our assessment of the city's management as satisfactory, which is higher than average in Russia.

Owing to the City of Novosibirsk's prudent approach to expenditure and continuing support from Novosibirsk Oblast, we expect the city to maintain average budgetary performance in the medium term. We believe the city will continue to benefit from Novosibirsk Oblast's support because it accounts for more than 55% of the oblast's population. The oblast's support, coupled with the city management's cautious spending policy, will likely mitigate the effect of slowing revenues due to economic recession. Under our base case, we assume that the city will post an average operating surplus of about 2.5% of operating revenues over 2015-2017, compared with 5% on average in 2012-2014.

In our base case, we anticipate that the city will fund about half of its investment program with capital transfers from the oblast and the federal budget. For this reason, our base-case scenario envisages only modest deficits after capital accounts of about 3% of total revenues on average in 2015-2017, similar to the 2012-2014 average of 4%.

Owing to modest deficits, tax-supported debt will likely stay below 50% of consolidated operating revenues by the end of 2017, which we see as low by international standards. The city's limited involvement in the local economy and the relatively stable financial position of its government-related entities translate into very low contingent liabilities.

LIQUIDITY

We view Novosibirsk's liquidity as adequate, according to our criteria. We base our assessment on the strong debt-service coverage, adjusted for limited access to external liquidity.

In our base-case scenario, we forecast that over the next 12 months, Novosibirsk's free cash reserves, together with available committed credit facilities, net of the deficit after capital accounts, will average about Russian ruble (RUB) 6.4 billion (about \$98 million at the time of publication). This amount covers 170% of city's debt service falling due in the next 12 months.

We expect that, in 2016-2017, Novosibirsk will continue to rely on medium- to long-term borrowings (bonds and bank lines) for refinancing and liquidity purposes, which it usually organizes during the budget year, well ahead of debt maturity dates. The terms of Novosibirsk's access to bank lending are more favorable than those of other entities in Russia.

Nevertheless, under our methodology, we qualify all Russian local and regional governments' access to external liquidity as "limited" by international standards because of what we see as Russia's weak banking system and limited development of the domestic capital market (see "Various Rating Actions Taken On Russian Banks Due To Rising Economic Risk," published on Feb. 24, 2015, on RatingsDirect).

OUTLOOK

The negative outlook on Novosibirsk solely mirrors that on Russia. We could take a negative rating action on the city if we took a negative rating action on Russia.

We could also take a negative rating action if the city's management drew back from its cautious spending and refinancing policies, leading to higher deficit after capital expenditure and/or causing it to fail to secure new bank lines well ahead of maturity. This would lead us to revise down our view of the city's management to weak and/or our view of the city's liquidity to less than adequate.

We would revise the outlook back to stable following a similar action on Russia, if the city also performs in line with our base-case scenario.

KEY STATISTICS

Table 1

City of Novosibirsk Financial Statistics						
	--Fiscal year end Dec. 31--					
(Mil. RUB)	2012	2013	2014	2015bc	2016bc	2017bc
Operating revenues	28,838	29,820	32,544	31,546	33,817	35,852
Operating expenditures	27,209	28,632	30,169	30,821	32,851	34,861
Operating balance	1,629	1,188	2,375	725	966	990
Operating balance (% of operating revenues)	5.6	4.0	7.3	2.3	2.9	2.8
Capital revenues	7,452	9,677	5,438	5,000	5,500	6,000
Capital expenditures	9,961	13,511	9,180	7,000	7,500	8,000
Balance after capital accounts	(880)	(2,645)	(1,367)	(1,275)	(1,034)	(1,010)
Balance after capital accounts (% of total revenues)	(2.4)	(6.7)	(3.6)	(3.5)	(2.6)	(2.4)
Debt repaid	4,655	4,215	1,350	2,178	3,200	1,450
Balance after debt repayment and onlending	(5,535)	(6,860)	(2,717)	(3,453)	(4,234)	(2,460)
Balance after debt repayment and onlending (% of total revenues)	(15.3)	(17.4)	(7.2)	(9.4)	(10.8)	(5.9)
Gross borrowings	5,875	6,515	2,930	3,478	4,300	2,500
Balance after borrowings	340	(345)	213	25	66	40
Operating revenue growth (%)	8.1	3.4	9.1	(3.1)	7.2	6.0
Operating expenditure growth (%)	2.8	5.2	5.4	2.2	6.6	6.1
Modifiable revenues (% of operating revenues)	30.7	30.4	29.4	32.5	32.6	32.8
Capital expenditures (% of total expenditures)	26.8	32.1	23.3	18.5	18.6	18.7
Direct debt (outstanding at year-end)	10,468	12,768	14,348	15,648	16,748	17,798
Direct debt (% of operating revenues)	36.3	42.8	44.1	49.6	49.5	49.6
Tax-supported debt (% of consolidated operating revenues)	35.4	40.1	41.4	46.0	46.0	46.2
Interest (% of operating revenues)	1.6	1.9	3.0	3.3	3.8	3.9
Debt service (% of operating revenues)	17.8	16.1	7.2	10.2	13.3	8.0

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. Base case reflects Standard & Poor's expectations of the most likely scenario. Downside case represents some but not all aspects of Standard & Poor's scenarios that could be consistent with a downgrade. Upside case represents some but not all aspects of Standard & Poor's scenarios that could be consistent with an upgrade.

Table 2

City of Novosibirsk Economic Statistics

	--Fiscal year end Dec. 31--					
	2012	2013	2014	2015bc	2016bc	2017bc
Population	1,511,361	1,535,909	1,557,499	1,575,069	1,591,002	1,606,929
Population growth (%)	1.6	1.6	1.4	1.1	1.0	1.0
GDP per capita (RUB)	385,430	427,846	455,165	464,689	501,590	531,879
Officially registered unemployment rate (%)	0.58	0.48	0.44	0.43	0.41	0.4

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. Sources typically include national statistical offices, Eurostat, and Experian Ltd.

RATINGS SCORE SNAPSHOT

Table 3

City of Novosibirsk Ratings Score Snapshot

Key Rating Factors	
Institutional framework	Volatile and un-balanced
Economy	Weak
Financial management	Satisfactory
Budgetary flexibility	Weak
Budgetary performance	Average
Liquidity	Adequate
Debt burden	Low
Contingent liabilities	Very low

*Standard & Poor's ratings on local and regional governments 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," published on June 30, 2014, summarizes how the eight factors are combined to derive the government's foreign currency rating.

KEY SOVEREIGN STATISTICS

Sovereign Risk Indicators, June 30, 2015. An interactive version is also available at <http://www.spratings.com/sri>.

RELATED CRITERIA AND RESEARCH

Related Criteria

- Criteria - Governments - International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign - December 15, 2014
- 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
- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments - June 30, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions - November 19, 2013

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
Novosibirsk (City of)		
Issuer credit rating		
Foreign and Local Currency	BB+/Negative/--	BB+/Negative/--
Russia National Scale	ruAA+/--/--	ruAA+/--/--
Senior Unsecured		
Local Currency	BB+	BB+
Russia National Scale	ruAA+	ruAA+

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