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Research Update:

City of Barcelona 'BBB+' Rating Affirmed; Outlook Remains Stable

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Overview

- Supportive economic conditions and Barcelona's experienced management contribute to a strong financial position marked by low levels of debt, sustained budgetary surpluses, and high levels of cash reserves.
- However, due to the institutional arrangements in place, Barcelona, similarly to other Spanish cities, does not qualify to be rated above our current long-term rating on Spain.
- As a result, we are affirming our 'BBB+' long-term rating on Barcelona.
- The outlook remains stable, reflecting our expectation that our rating on Barcelona will continue move in line with our sovereign rating on Spain.

Rating Action

On March 17, 2017, S&P Global Ratings affirmed its 'BBB+' long-term issuer credit rating on the Spanish City of Barcelona. The outlook remains stable.

Outlook

The rating on Barcelona is capped by the ratings on Spain, and therefore the stable outlook is a reflection of our current outlook on the Kingdom of Spain (BBB+/Stable/A-2).

Downside scenario

If we were to downgrade Spain, we would downgrade Barcelona, as well. Apart from a potential sovereign downgrade, we would lower the rating on Barcelona if we revised our assessment of its stand-alone credit profile (SACP; our assessment of an issuer's intrinsic credit characteristics), to 'bbb' or lower. The SACP for Barcelona currently stands at 'aa'. Such a multi-notch deterioration appears highly unlikely, however.

Upside scenario

We would raise our rating on Barcelona if, all things remaining equal, we upgraded Spain to 'A-' or higher.

Rationale

We have updated our base-case scenario for Barcelona and extended our forecasting horizon through 2019. We think Barcelona will continue to show very strong credit metrics, thanks to a sustained commitment to financial stability and deficit containment. While it aims to increase spending on social programs and a newly

established investment program, the city will also limit its debt issuance to refinancing purposes--thus keeping the debt burden at a low level. As a result, we expect Barcelona's SACP to remain in line with the 'aa' category. The issuer credit rating continues to be capped by the 'BBB+' sovereign rating on Spain.

- Prudent financial management and a buoyant local economy support Barcelona's creditworthiness

With 1.6 million residents, Barcelona is Spain's second-largest city and business center. The local economy is strong and diversified. It is growing substantially with strong migration inflows, a return to job creation, and an ability to benefit from its position as one of Europe's leading tourism destinations.

The city operates within an institutional framework that is marked by a high level of central government control and support. Since the European debt crisis, the Spanish government has increased the level of controls on local and regional governments (LRGs), including cities, imposing spending and debt ceilings, and deficit rules. This increased surveillance was implemented alongside supportive measures, such as the extension of central government loans to clear supplier debts, or increased tax flexibility on some fiscal items.

We expect Barcelona will continue to draw benefits from the central government's supportiveness in this context, while also maintaining prudent financial management. Following a political agreement in May 2016, the minority government was enlarged and now includes two political parties in a ruling coalition that has continued with the city's longstanding internal budgetary and debt targets.

- Financing needs will remain low, reflecting balanced budgets and high cash reserves

In line with its own targets, we expect the city to post operating surpluses in excess of 15% of operating revenues through 2019. A move by the city to increase its operating expenses--especially on social-related items, is unlikely to dent the operating margin. We expect fiscal revenues will continue to benefit from the local buoyancy, and government transfers will continue to contribute to revenue growth.

We continue to forecast the city will gradually increase its capital commitments to €500 million by 2019. Among others, these amounts include a major housing program carried out by the city's social housing operator, Patronat Municipal del Habitatge (PMHB). Despite this capital expenditure ramp up, we expect the city will continue to post sustained, though reducing, surpluses. The high operating surplus described above, along with capital subsidies, will likely cover most of the spending.

As a result, the city's financing needs will be limited. Tax-supported debt is set to grow slightly, owing to the significant investments carried out by PMHB. Meanwhile, we expect the direct debt stock to start declining from 2018, as the city starts covering some of the amortizations with its own cash, instead of the full refinancing that has been observed in the past. While this might reduce the cash reserves, it will not significantly change the liquidity profile in the short term, given the very high starting point.

Indeed, we forecast Barcelona's debt-servicing ratio of free cash and liquid assets over the next 12 months to be over four times the city's next 12 months' debt and interest payments. We expect Barcelona to hold about €600 million in unrestricted cash and liquid assets over the next 12 months. These assets could comfortably cover debt maturing within the next 12 months of €126 million and interest of €20 million. The city actively manages its liquidity and has been able to significantly reduce the period of payments to suppliers. Additionally, we believe it could have access to short-term bank financing in case of need.

Our assessment of the city's contingent liabilities factors in the risks stemming from the links with the Autonomous Community of Catalonia (B+/Negative/B), Barcelona's home region. We understand that the city has taken an active approach to managing cross flows between the two governments, signing an arrears clearance agreement in 2014, and monitoring joint projects. Our base case rests on the assumption that the city will not fund Catalonia's projects and operations without a transfer of underlying assets.

- Rating on Spain still constrains that on Barcelona

We assess Barcelona's SACP at 'aa'. The SACP is not a credit rating but a means to assess the intrinsic creditworthiness of an LRG under the assumption that the rating on the sovereign is not a constraint. The SACP results from the combination of our assessment of an LRG's individual credit profile and the institutional framework under which it operates.

We cap our long-term rating on Barcelona at the level of the long-term rating on Spain. In our view, Barcelona does not meet the criteria under which we would rate an LRG higher than the related sovereign. We believe the city lacks sufficient financial autonomy to effectively resist significant sovereign intervention, such as reductions or delays in central government transfers. We do not believe that the city's credit quality could withstand the stress of a sovereign default, given its reliance on central government transfers (about 40% of operating revenues) and tax transfers (an additional 10%). Like all Spanish cities, Barcelona has no substantial legislative power over its financial framework.

Key Statistics

Table 1

City of Barcelona Financial Statistics

(Mil. €)	--Fiscal year ending Dec. 31--				
	2015	2016e	2017bc	2018bc	2019bc
Operating revenues	2,709	2,655	2,744	2,830	2,922
Operating expenditures	2,124	2,163	2,228	2,294	2,393
Operating balance	585	492	516	536	529
Operating balance (% of operating revenues)	21.6	18.5	18.8	18.9	18.1
Capital revenues	49	45	42	42	42

Table 1

City of Barcelona Financial Statistics (cont.)					
(Mil. €)	--Fiscal year ending Dec. 31--				
	2015	2016e	2017bc	2018bc	2019bc
Capital expenditures	476	458	467	489	500
Balance after capital accounts	158	79	91	89	71
Balance after capital accounts (% of total revenues)	5.7	2.9	3.3	3.1	2.4
Debt repaid	156	156	126	49	51
Balance after debt repayment and onlending	2	(77)	(35)	39	20
Balance after debt repayment and onlending (% of total revenues)	0.1	(2.9)	(1.3)	1.4	0.7
Gross borrowings	156	156	126	0	0
Balance after borrowings	158	79	91	39	20
Operating revenue growth (%)	7.3	(2.0)	3.4	3.1	3.3
Operating expenditure growth (%)	8.4	1.8	3.0	3.0	4.3
Modifiable revenues (% of operating revenues)	51.4	54.0	53.8	53.7	53.6
Capital expenditures (% of total expenditures)	18.3	17.5	17.3	17.6	17.3
Direct debt (outstanding at year-end)	836	836	835	786	735
Direct debt (% of operating revenues)	30.9	31.5	30.4	27.8	25.2
Tax-supported debt (% of consolidated operating revenues)	34.7	34.4	33.4	32.7	32.2
Interest (% of operating revenues)	0.9	0.7	0.7	0.7	0.6
Debt service (% of operating revenues)	6.6	6.6	5.3	2.4	2.4

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. e--Estimate. bc--Base case: reflects S&P Global Ratings' expectations of the most likely scenario.

Table 2

City of Barcelona Economic Statistics						
	--Fiscal year ending Dec. 31--					
	2014	2015	2016e	2017bc	2018bc	2019bc
Population	1,602,386	1,605,000	N/A	N/A	N/A	N/A
Population growth (%)	(0.6)	0.2	N.M.	N.M.	N.M.	N.M.
GDP per capita (€)	26,557	27,584	28,610	29,610	30,635	31,696
Unemployment rate (%)	18.9	13.3	11.6	N/A	N/A	N/A

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. Sources typically include national statistical offices, Eurostat, and Experian Ltd. bc--Base case: reflects S&P Global Ratings' expectations of the most likely scenario. N.M.--Not meaningful. N/A--Not applicable.

Ratings Score Snapshot

Table 3

City of Barcelona Ratings Score Snapshot

Key rating factors	
Institutional Framework	Evolving but balanced
Economy	Strong
Financial Management	Very strong
Budgetary Flexibility	Strong
Budgetary Performance	Very strong
Liquidity	Exceptional
Debt Burden	Very low
Contingent Liabilities	Low

*S&P Global Ratings' credit 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" summarizes how the eight factors are combined to derive the rating.

Key Sovereign Statistics

- Sovereign Risk Indicators - December 14, 2016. An interactive version is also available at <http://www.spratratings.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
- 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
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs - October 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Kingdom of Spain 'BBB+/A-2' Ratings Affirmed; Outlook Stable - September 30, 2016
- 2015 Annual International Public Finance Default Study And Rating Transitions - June 30, 2016

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

	Rating	
	To	From
Barcelona (City of)		
Issuer Credit Rating		
Foreign and Local Currency	BBB+/Stable/--	BBB+/Stable/--

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. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public Web site 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.

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