

ISSUER IN-DEPTH

9 November 2016

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RATINGS

Belgrade, City of

Long Term Rating	B1
Outlook	Positive

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Belgrade, City of

Key drivers behind the City of Belgrade's B1 issuer rating

On 25 October 2016, Moody's assigned a B1 issuer rating to City of Belgrade, with a positive outlook. The rating reflects Belgrade's track record of prudent budgetary management, which has delivered solid operating surpluses and financial results, as well as its liquidity levels, which exceed the median for the peer group. These credit strengths are partly offset by debt and debt service levels in excess of the peer group median. Moody's currently rates three cities in Serbia, whose ratings span from B2 to B1.

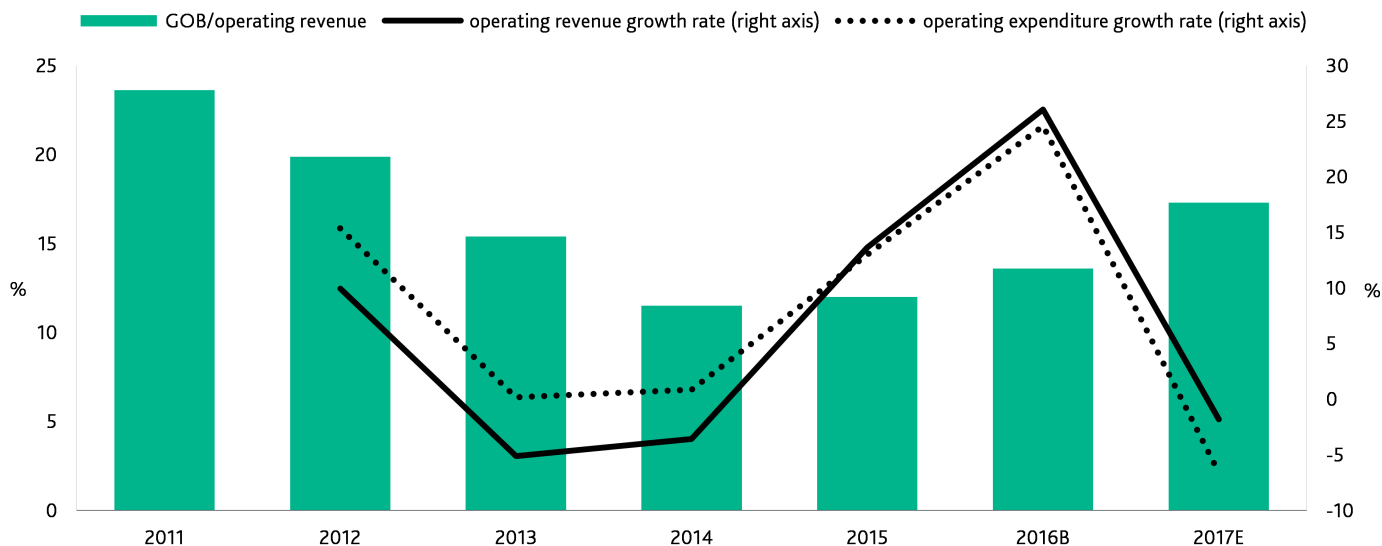
- » **Satisfactory operating performance.** Belgrade's fiscal discipline has delivered double-digit operating surpluses over the last five years. In 2016 and 2017, Moody's expects the city's operating margin to improve to 14% and 16% of operating revenue respectively, from 12% in 2015. The improvement reflects national economic expansion and slower spending growth.
- » **Improving financial results.** Belgrade reported annual surpluses of between 3% and 7% of total revenues in 2013-15, compared with deficits of 7% and 18% in 2012 and 2011 respectively. The improvement largely reflected reduced capital investment. However, the city plans substantial capital expenditure (capex) in 2016-17 which could push its financial result back into negative territory.
- » **High but declining debt levels.** Belgrade's direct debt stock was equivalent to 76% of operating revenues at year-end 2015. While this surpasses the debt ratios of the other rated Serbian cities, we regard it as manageable. We expect Belgrade's debt ratio to decline to around 51% by year-end 2017 as the city plans to fund most of its capex from its own revenues, asset sales, and central government transfers, rather than debt.
- » **Comfortable liquidity position.** Belgrade's accumulated cash reserves averaged 17% of operating revenues in the first three quarters of 2016, equivalent to 1.5x projected debt servicing costs. We expect the city's liquidity to remain satisfactory, with cash reserves above RSD10 billion (EUR81 million) in 2016-17. This provides the city with sufficient funds to cover its financial liabilities.

Satisfactory operating performance

Belgrade has over the past five years delivered a consistently sound fiscal performance, generated double-digit operating surpluses. We expect the city's shared tax receipts and own-source revenues to rise further on the back of solid economic growth, lifting its gross operating balance (GOB) to around 14% and 16% of operating revenue in 2016 and 2017 respectively, from 12% in 2015 (Exhibit 1).

Exhibit 1

Belgrade has generated operating surpluses over the last five years



Source: City of Belgrade, Moody's; B=Budget, E=Estimation

Belgrade has a slightly higher operating margin than rated peers Novi Sad (B1 positive) and Valjevo (B2 positive), whose GOBs are projected to improve to about 15% of operating revenues by 2017 from 11% and 10% respectively in 2015.

Of the three cities, Belgrade has the greatest capacity to generate own-source revenues. Local taxes and other own-source revenues accounted for 45% of Belgrade's operating revenues in 2015, compared to 40% and 30% for Novi Sad and Valjevo respectively.

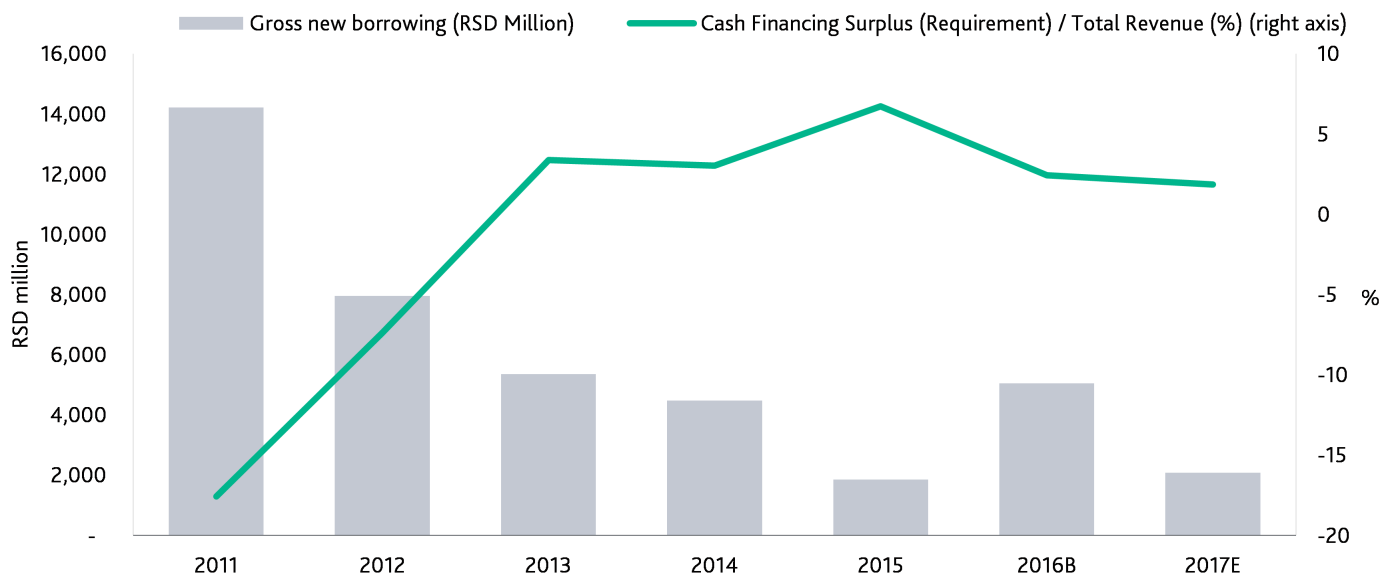
Belgrade and Novi Sad's larger and faster-growing economies give them a budgetary advantage over Valjevo. Of the three cities, Belgrade has by far the highest GDP per capita at around 170% of the national average, compared with 102% for Novi Sad, and just 68% for Valjevo. Belgrade also has a larger balance sheet and higher budget revenues than Novi Sad or Valjevo.

Improving financing results

Moody's expects Belgrade to post a financing surplus again in 2016-17, although a planned increase in capital expenditure could weaken city's financial performance. In 2013-15, sound operating margins combined with stable cash flows and reduced capital investments led to consecutive financing surpluses of between 3% and 7% of total revenues. This marked a strong improvement from financing deficits of 18% and 7% in 2011 and 2012 respectively (see Exhibit 2).

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody.com for the most updated credit rating action information and rating history.

Exhibit 2

Belgrade's financing results are improving

Source: City of Belgrade, Moody's; B=Budget, E=Estimation

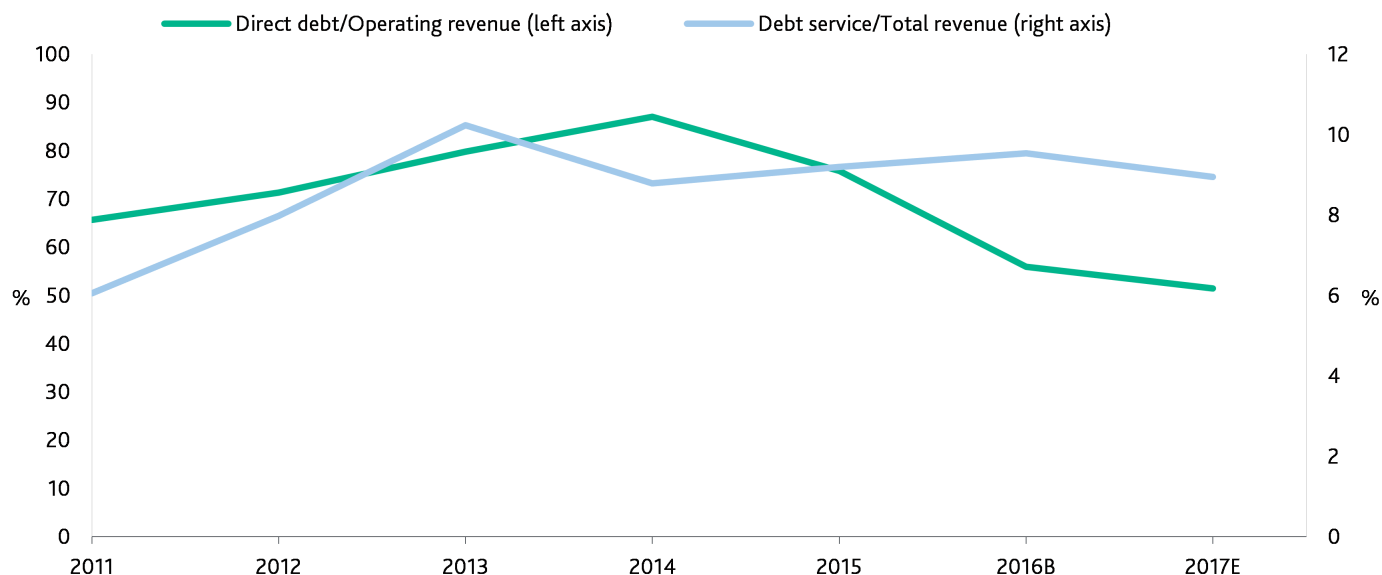
If fully implemented, the city's 2016 and 2017 capex programme will absorb 21% and 27% of total spending for 2016 and 2017, compared with an average of just 17% between 2013 and 2015. The capex plan consists of projects focusing mostly on urban transportation infrastructure, including the construction of new bridges and tunnels. It also aims to extend the city's sewage system and reconstruct parts of its water supply network.

High but declining debt levels

Moody's expects Belgrade's debt to fall to about RSD45.8 billion by year-end 2016 from RSD49.2 billion a year earlier, reducing the city's debt to operating revenue ratio to 56% from a relatively high 76% at year-end 2015 (see Exhibit 3).

We expect Belgrade's debt to continue declining throughout 2017, as set out in the city's own projections, as stronger operating balances and tightly-controlled operating expenditure limit its borrowing needs. By year-end 2017, Belgrade's debt stock should fall to 51% of operating revenue, still ahead of the projected median of about 30% for all other Serbian local governments.

Exhibit 3

Belgrade's debt to decline in 2016-17

Source: City of Belgrade, Moody's; B=Budget, E=Estimation

In 2017, the city expects to draw down one tranche of a RSD2.1 billion European Investment Bank (EIB) loan to help fund its investment programme. However, over 90% of Belgrade's investment funding will come from the city's own revenues, its available cash reserves, the proceeds of asset sales, or from central government grants.

We regard Belgrade's debt burden as manageable, and expect its debt service costs to total around 9% of total revenues in 2016-17. Our estimate is based on the favourable maturity profile of the city's direct debt, which is made up long-term amortising loans.

Novi Sad and Valjevo will also limit their debt growth, although their debt levels are already significantly lower than Belgrade's. We expect Novi Sad's debt to account for a moderate 28% of operating revenue by 2016, down from 32% in 2015. Valjevo's debt will fall to a comparatively low 20% of operating revenues in 2016 from 22% in 2015.

Comfortable liquidity position

Moody's expects Belgrade's liquidity to remain satisfactory in 2016-17. The month-end balance on its accounts was RSD10.7 million on average in first three quarters of 2016, up from RSD7 million in 2015. This is equivalent to a solid 17% of operating revenues, or 1.5x annual debt service, and provides the city with sufficient funds to meet its financial liabilities. Belgrade's liquidity level is above the median for its peer group, with Novi Sad holding cash reserves equivalent to 16% of operating revenues, and Valjevo 11% projected for 2016.

The improvement in Belgrade's cash reserves largely reflects operating expenditure controls as well as reductions in capital spending, which have reduced its borrowing requirement. The city has not held uncommitted credit lines in the last few years, reflecting the accumulation of positive cash balances.

We expect Belgrade's increased capital expenditure plan for 2016-17, much of it self-funded, to erode its liquidity position. Nevertheless, cash reserves should remain above RSD10 billion, a cushion well in excess of Belgrade's debt service requirements over the next two years.

Moody's Related Research

Credit Opinions

- » [Credit Opinion: Belgrade, City of \(October 2016\)](#)
- » [Credit Opinion: Novi Sad, City of \(March 2016\)](#)
- » [Credit Opinion: Valjevo, City of \(March 2016\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

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REPORT NUMBER 1048389