

FITCH AFFIRMS POLISH CITY OF KATOWICE AT 'A-'; OUTLOOK STABLE

Fitch Ratings-Warsaw/London/Moscow-30 January 2015: Fitch Ratings has affirmed the Polish City of Katowice's Long-term foreign and local currency Issuer Default Ratings (IDR) at 'A-'. Fitch has also affirmed the city's National Long-term rating at 'AA+(pol)'. The Outlooks are Stable.

KEY RATING DRIVERS

The affirmation reflects Katowice's sound operating performance, which we expect to be maintained in the medium term. The ratings also factor in our expectations that the city's direct debt will be stable, based on its policy of financing investments mainly with own resources. Although this leads to the absorption of the city's significant cash reserves, Katowice has more than sufficient liquidity to ensure smooth debt service.

Fitch expects that the city will continue its positive performance of 2014 over the next two years, with an operating margin of 13%. Based on preliminary data the city reported a better-than-expected operating margin of 13.1% in 2014, due to current spending savings on statutory responsibilities. Katowice expects to have achieved an operating balance of PLN184.1 in 2014, up from PLN147m in 2013. The operating balance would have been sufficient to cover debt service of PLN29.9m (including debt repayments and interest) by 6x. We assume that the city will maintain its policy of limiting opex growth and project an operating balance of PLN200m by 2017.

Fitch expects that Katowice's direct debt to remain moderate and stabilise at below 50% of current revenue in 2015-2017. At end-2014 debt amounted to PLN674.2m or 46% of current revenue (preliminary estimates). The majority of loans are with European Investment Bank (87%) and with European Investment Bank and Council of Europe Development Bank (12%). Katowice's debt is long-term and amortises smoothly, lowering pressure on the city's budget. The debt payback ratio (debt to current balance) was 3.7 years at end-2014 and was significantly lower than the weighted average debt maturity of over 18 years, which is a rating-positive.

We expect the city's capex to average to PLN350m annually or 20% of total expenditure for 2015-2017. As the city aims to finance the investments from own sources mainly we expect that 60% of capex will be funded by capital revenue (mainly EU grants) and the city's current balance. The remainder will be funded by the city's high cash reserves and debt (PLN17m in 2015).

Fitch assumes that Katowice will continue to use its cash reserves to finance investments. In 2014 PLN150m of cash reserves were absorbed by capex. We project cash reserves to decline to about PLN80m at end-2017, from PLN223.3m in 2014, but should still cover annual debt service, by 2x.

RATING SENSITIVITIES

Sustainable sound operating performance and declining pressure to fund capex with debt could lead to a positive rating action.

Conversely, sharper-than-expected deterioration in debt coverage, due to a sustained weakening in the operating margin or a significant rise in the city's net direct risk, could result in a negative rating action.

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Additional information is available on www.fitchratings.com.

Applicable criteria, 'Tax-Supported Rating Criteria', dated 14 August 2012, and 'International Local and Regional Governments Rating Criteria', dated 23 April 2014, are available on www.fitchratings.com.

Applicable Criteria and Related Research:

International Local and Regional Governments Rating Criteria - Outside the United States

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=719656

Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015

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