

Municipality of Burgas

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	Initial Rating 17.04.2015
Credit Rating of Municipality of Burgas	
Long-term Rating:	BBB-
Outlook:	stable
Short-term Rating:	A-3
National-scale long-term Rating:	AAA (BG)
Outlook:	stable
National-scale short-term Rating:	A-1+ (BG)

BCRA - Credit Rating Agency (BCRA) is the third qualified rating agency in the EU, registered under Regulation (EC) 1060/2009 of the European Parliament and of the Council. The credit ratings, assigned by BCRA, are recognized throughout the EU, and are entirely equal with the other ratings, recognized by European Securities and Markets Authority (ESMA), without any territorial or other restrictions.

„BCRA – Credit Rating Agency” AD (BCRA) assigns to Municipality of Burgas the ratings below:

- **Long-term credit rating BBB-, outlook: stable, short-term credit rating A-3;**
- **National-scale long-term AAA (BG), outlook: stable, national-scale short-term rating A-1+ (BG).**

The officially adopted by BCRA methodology for assigning a credit rating to municipalities is applied (http://www.bcra-bg.com/files/file_319.pdf).

In order to elaborate the credit report and to assign the credit rating, BCRA uses information, provided by the rated municipality, Ministry of Finance, NSI, National Employment Agency, its own database, consultants and other sources of public information.

The analyzed period (2010-2014) is distinguished with gradual fading of the economic crisis. The gradual recovery of Bulgaria from the crisis is running slowly and tentatively, and it strongly

depends on the volume of exports (mainly by the recovery rates of EU's economy), growing unemployment, low domestic consumption and investment activity.

Despite the growth of the debts, the ratio Government debt/GDP, which is expected to reach about 30% during 2015, remains considerably lower than 60%, adopted in the EU. As a result of the unfavourable development of the economic environment in the country, there is a potential opportunity for taking new loans during the upcoming year with the aim at stimulating the economy.

The lack of the reforms over the last years, the political and institutional instability are the main factors, which determine the worse investment climate in the country and cause a strongly negative effect upon its economic development. At the end of 2014, the government in power, took steps to revise the forecasts made by the prior government, restructure the state budget and limit the budget deficit.

During the last years, there was a number of changes in the legal framework, related to the activity of the municipalities, as among the most considerable changes was the adoption of the Public Finance Act (promulgated on 15.02.2013). The new law regulates the budget framework, the common pattern and structure of the public finance, defining the scope, structure and main indicators of the consolidated fiscal policy, the fiscal rules and restrictions, regime of the accounts for EU funds, reporting of the budget

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organizations, etc. The Law came into force since early 2014 and abolished the State Budget Law and Municipal Budgets Law.

The economic crisis had an influence on income and expense section in the municipal budgets, as a slight improvement was observed over last 1-2 years. The total income of the municipalities followed a downtrend during 2012 (a 13.5% decline in the period 2009-2012), then during the last year a growth of 11.4% was observed. A positive change was observed in the own income during 2011 (a growth of 9.5% compared to the previous year), but we should have in mind that partially it was due to the measures that the municipalities took to strengthen enhancing the collection. To a great extent, the crisis affected the sales property income, which decreased cumulatively during the period 2009-2012 by 32.1%. A growth of 21.0% was observed during the last year.

The current expenses for local activities and supplementary funds of the state activities followed a downtrend up to 2012 (a cumulative decline of 19.3% during 2009-2012), then an increase was reported of 5.6% during 2013. The decline in the capital expenses also continued up to 2012 (cumulatively 56.5% during 2009-2012). There was a growth of 15.1% during 2013.

The population of Municipality of Burgas reported a positive change over the years within the period under review with the exception of 2012, when a decline of 0.30% was observed. This dynamics was outlined in the background of a negative change of the population in the country. The share of the active population in the municipality followed a trend of a slight decrease of 66.72% during 2009 to 64.48% during 2013. For all years this share was higher than the average in the country. A positive factor is the higher share of under active population in Burgas compared to the average in the country.

On the basis of the NSI's data in 2014, the unemployment rate in Burgas District for persons aged 15-64 was 11.1%, compared to 11.5% on average in the country, as the district occupied the tenth position among total 28 districts in Bulgaria.

The output of the companies in Municipality of Burgas followed an uptrend to 2012, as reported a 43.7% cumulative growth. During the entire period, the processing industry dominated. The investments in FTA of the companies in the municipality registered a decline only during 2010

(37.8%). During the next three years, the level of the indicator increased reaching 81.2%. The processing industry dominated.

Municipality of Burgas reported an increasing operating result during the period 2010-2014, which was positive over the years. The result from investment activity was negative, as the capital expenses exceeded the income with a capital character. The Net Cash Flow was negative during the first two years during the period, and it was positive during the last three years, but its value increased, as during the last 2014 was 2.8% of the income for local activities.

The own income of Municipality of Burgas increased by 24.8% cumulatively for the period 2010-2014, as the growth was the highest during the last year – 8.0%. Their relative share in the income for local activities varied from 85% to 98%, as the highest was during 2012 (97.4%), and the lowest – during the last year (85.0%). The decreased share during the last year was determined by a comparatively large size of the capital subsidiary.

The tax income increased by 29.9% during the analyzed period and was dominated by the real estate tax and vehicle tax.

During the five-year period under review, the non-tax income reported a growth of 21.8%. The taxes (53%-75%) dominated by the domestic waste tax (a share of 69.2% during 2014) reported the highest share.

The income from municipal property sales decreased to 2013, which is not considered to be negative with the view of that this source was changeable. A more considerable decline was observed during 2011 (65.1% on an annual basis). During the last year, a considerable growth was observed, more than 380%. The sales property income reached BGN 5 485 thousand.

During the period 2011-2013, the current expenses of Municipality of Burgas were at level of 59 millions leva annually. During the last year, a growth of 4.4% was observed and they reached 61.5 million leva. The maintenance for the entire period was dominated with a share of 71.1% over the last year. The capital expenses with budget funds during the period were volatile, as over the last two years increased, and during 2014 reached the highest level – 25 004 thousand leva.

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Municipality of Burgas did not report overdue liabilities as of the end of 2014.

The structure of the expenses on functions is dominated by the utility expenses. Their share decreased during the period – from 53.6% during 2009 to 39.8% during 2013. During 2014 a growth was observed of 5.4 p.p. to 45.2%.

A positive factor is the considerable capital expenses in education during 2013 (7 312 thousand leva budgetary funds). The final result is renovation of the entire educational infrastructure of the municipality and lower energy expenses. At the end of 2013, the children's homes were renovated in 100%.

The utility current expenses were dominated by the maintenance of cleanliness, which increased from 11 429 thousand leva during 2010 to 14 478 thousand leva during 2012, then it started decreasing to 13 045 thousand leva during 2014. Over the last three years, their share in the utility current expenses was from 47% to 50%. The capital expenses on the function were the largest during 2011 and 2014, respectively BGN 12 276 thousand and 12 845 thousand leva which were 71.8% and 51.4% of the total capital expenses.

The municipality reported considerably larger by size off-budget funds (on OPs). Among the largest projects is the integrated public transport project with a total budget of 131 million leva and deadline - April 2015. The project for implementing a regional waste depot in Bratovo is in its final stage. The partners of the project are the municipalities Aitos, Kameno, Karnobat, Pomorie, Ruen, Sredets, Sungurlare and Waste Management Organization – Burgas district. The total budget is in the amount of BGN 43 millions. A number of water projects are in a process of realization.

Municipality of Burgas is marked by the financing of a comparatively large part of the capital programme with attracted funds on OPs, which is a positive factor: their share is the lowest during 2011 (38%), and during 2013 increased to 77%. During 2014, it was 67%. Over the last three years, the share of the bank financing was low – during 2012 and 2013, it was from 3% to 5%, and during the last year – over 1%.

A considerable growth of the total capital programme during the last two years – during 2013 it was in the amount of 70 789 thousand leva compared to 24 374 thousand leva during 2012

and by 28-29 million leva during the last two years, and during 2014 reached nearly 79 million leva.

The position of Municipality of Burgas was reviewed in a comparative aspect by a set of indicators calculated per capita of the population. Burgas has taken a favourable position during the whole period compared to the average levels in the country, as the average in the group of municipalities, which are districts. The comparison with Municipality of Varna (as a municipality with a similar character shows that both municipalities occupy very close positions.

During the analyzed period a Mayor of Municipality of Burgas was Mr. Dimitar Nikolov. Currently, his second mandate is running which launched after the local elections during October 2011, when he was elected at the first round by 70.86% of the votes. The management works actively to implement projects and provide financial aid in order to improve the municipal infrastructure. We should take into account the efforts to diversify Burgas not only as an industrial centre but also as a tourist destination with cultural attractions and leisure facilities.

BCRA makes a financial forecast of the municipality for the period 2015-2017. The results show that in development similar to the forecast, Burgas will realize a positive operating result during the entire forecast period. The free cash flow is positive during the first year and negative over the next two years, as the cash on accounts cover it. The forecast is based on comparatively conservative assumptions.

As far as the rating of Municipality of Burgas is limited by the rating of Bulgaria, a favourable influence upon the rating could have a possible increase of the sovereign rating, which however, with the view of the negative outlook at present, we assess as unlikely.

A negative influence on the rating of Municipality of Burgas might cause a future accumulation of overdue liabilities, generation of a negative operating result, as well considerable reduction of the own income.

Main Financial Indicators in BGN

	(лева)	2014	2013	2012
Income for local activities incl.		88 944 818	76 676 153	69 132 341
Own income:		75 572 176	69 954 414	67 328 443
- tax income		28 992 331	26 889 533	26 088 239
- non-tax income		46 579 845	43 064 881	41 240 204
Subsidiaries and transfers for local activities		13 372 642	6 721 739	1 803 898
Capital Expenses		25 004 412	15 103 394	7 055 497
Operating Result		9 820 834	9 610 253	5 697 064
Operating Result before Taxation		10 654 798	10 445 076	6 624 896
Result from Investment Activity		-7 374 759	-6 967 712	-2 776 732
Deficit/Surplus for Local Activities		2 446 075	2 642 541	2 920 332

Resume of the Minutes of the Rating Committee:

The members of the Rating Committee reviewed the credit rating report of Municipality of Burgas and discussed the factors which defined its credit rating in the context of the changed during July 2014 Methodology for assigning a credit rating to a municipality.

Due to the specific risk profile of the municipality, as well the condition of the legal regulation of the municipalities in Bulgaria, the base rating¹ was defined at level A-.

The evaluation of the sovereign risk of the country and its level of impact upon Municipality of Burgas limited the assigned long-term credit rating to BBB- and short-term A-3.

The long national-scale rating AAA (BG) and short-term national-scale rating A-1+ (BG) were assigned on the basis of the position of the rating characteristics of the municipality in a comparative aspect compared to the other municipalities in Bulgaria.

¹ The base rating is an intermediate step in assigning a credit rating to the municipality according to the adopted methodology.