

City of Lviv

Key Rating Drivers

Outlook Reflects Sovereign's: Fitch Ratings has revised the Outlook on the City of Lviv's Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) to Stable from Positive and affirmed the IDR at 'B'. The revision of the Outlook follows that on Ukraine as we continue to view Lviv's ratings as constrained by that of the sovereign.

Rating Derivation Summary: Lviv's 'b+' Standalone Credit Profile (SCP) reflects a combination of a 'Vulnerable' risk profile and an 'aa' debt sustainability assessment. The SCP also factors in national peer comparison. The IDRs are not affected by any asymmetric risk or extraordinary support from the central government, but they remain capped by the Ukrainian sovereign IDRs at 'B'.

Risk Profile - 'Vulnerable': Fitch continues to assess Lviv's risk profile as 'Vulnerable', reflecting an unchanged 'Weaker' assessment of the six key risk factors in combination with the sovereign rating at 'B'.

Revenue Framework - 'Weaker': The city's revenue framework continues to evolve alongside changes to tax and budgetary regulation. Its tax base is exposed to a weak economic environment and negative trends in the local economy caused by the coronavirus pandemic, which together with inter-governmental transfers from the financially weak sovereign, drives our 'Weaker' assessment of the city's revenue robustness.

Fitch views Lviv's ability to generate additional revenue in response to economic downturns as limited. The city's formal tax-setting authority over several local taxes and fees is constrained by both legally set ceilings and high social-political sensitivity to tax increases.

Expenditure Framework - 'Weaker': The city's expenditure framework is fragile and characterised by frequent reallocation of responsibilities between government tiers. Part of individual spending items in key sectors, such as education, healthcare and social policy, have been transferred to the local level without a simultaneous transfer of funding sources. The city has a rigid expenditure structure and overall low per-capita spending compared with international peers, which limits its ability to curb spending in response to shrinking revenue.

Debt Sustainability - 'aa' Category: Under Fitch's new rating case, the debt payback ratio will deteriorate to 4.1x in 2024 from current 0.8x, but remaining in line with an 'aaa' assessment. However, short debt maturity, together with tightened conditions on the capital market caused by the pandemic, could put further pressure on an actual debt service coverage ratio (ADSCR), which we estimate to fall to 1.7x in the rating case, equal to an 'a' assessment.

This, plus a fiscal debt burden (net adjusted debt-to-operating revenue), which we expect to gradually increase to 66% in 2024, lead us to an overall 'aa' debt sustainability assessment.

ESG Considerations: The city has an ESG Relevance Score of '4' for Political Stability and Rights due to its exposure to the impact of political pressure or instability on operations and a tendency towards unpredictable policy shifts, which, in combination with other factors, affects the rating.

Rating Sensitivities

Constrained Ratings: Any action on Ukraine's sovereign ratings would lead to a respective rating action on Lviv's ratings.

Worsened Payback: A multiple-notch downward revision of the SCP below 'b', driven by material deterioration in debt metrics, particularly a debt payback sustainably above 5x under Fitch's rating case would lead to a negative rating action.

Ratings

Foreign Currency	
Long-Term IDR	B

Local Currency	
Long-Term IDR	B

National rating	AA-(ukr)
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Outlooks

Long-Term Foreign-Currency IDR	Stable
Long-Term Local-Currency IDR	Stable
National Rating	Stable

Issuer Profile

Lviv is the biggest city in the western part of Ukraine with 700,000 inhabitants. It is the capital of the Lviv Region, which contributed 5% to Ukraine's GDP in 2017 and 6% of the total population. Lviv is well-positioned among domestic peers, but the economy significantly lags behind international peers, with gross regional product per capita well below the EU average. Fitch classifies it as a 'Type B' local and regional government, meaning that it is required to cover debt service from cash flow on an annual basis.

Financial Data

City of Lviv (UAHm)	2019	2024rc
Payback (x)	0.8	4.1
ADSCR (x)	28.6	1.7
Fiscal debt burden (%)	17.7	65.8
Net adjusted debt	1,733	6,635
Operating balance	2,246	1,627
Operating revenue	9,773	10,089
Debt service	79	979

rc: Fitch's rating-case scenario
^a Fitch's calculation (see Appendix C)
 Source: Fitch Ratings, City of Lviv

Applicable Criteria

[Rating Criteria for International Local and Regional Governments \(September 2019\)](#)
[National Scale Ratings Criteria \(July 2018\)](#)

Related Research

[Ukraine \(May 2020\)](#)

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Appendix A

City of Lviv

(UAHm)	2016	2017	2018	2019	2020rc	2024rc
Taxes	3,286	4,324	5,352	6,404	6,236	7,869
Transfers received	2,642	3,607	3,478	2,739	1,444	1,775
Fees, fines and other operating revenues	362	485	552	630	332	445
Operating revenue	6,290	8,416	9,382	9,773	8,012	10,089
Operating expenditure	-4,583	-6,512	-7,471	-7,527	-6,634	-8,462
Operating balance	1,707	1,903	1,911	2,246	1,378	1,627
Interest revenue	94	51	56	51	0	0
Interest expenditure	0	0	-39	-79	-137	-259
Current balance	1,801	1,954	1,927	2,219	1,241	1,368
Capital revenue	132	144	225	456	444	594
Capital expenditure	-2,049	-2,006	-2,661	-2,992	-2,438	-2,607
Capital balance	-1,917	-1,862	-2,436	-2,536	-1,994	-2,013
Total revenue	6,516	8,610	9,663	10,280	8,456	10,683
Total expenditure	-6,632	-8,518	-10,172	-10,597	-9,209	-11,328
Surplus (deficit) before net financing	-116	92	-509	-317	-753	-645
New direct debt borrowing	0	0	440	300	800	1,370
Direct debt repayment	-2	-2	-1	0	0	-720
Net direct debt movement	-2	-2	439	300	800	650
Overall results	-118	90	-70	-17	47	5
Debt						
Short-term debt	0	0	0	0	0	0
Long-term debt	3	2	441	740	1,540	3,200
Intergovernmental debt	0	0	0	0	0	0
Direct debt	3	2	441	740	1,540	3,200
Other Fitch-classified debt	1,435	1,439	1,195	1,224	2,000	3,500
Adjusted debt	1,439	1,440	1,635	1,964	3,540	6,700
Guarantees issued (excl. adjusted debt portion)	0	0	0	0	0	0
Majority-owned GRE debt	240	240	240	240	240	240
Overall adjusted debt	1,678	1,680	1,875	2,204	3,780	6,940
Total cash, liquid deposits	268	331	260	231	278	65
Restricted cash	0	0	0	0	0	0
Unrestricted cash	268	331	260	231	278	65
Net adjusted debt	1,171	1,109	1,376	1,733	3,262	6,635
Net overall debt	1,410	1,349	1,615	1,972	3,502	6,875

rc: Fitch's rating case, based on conservative assumptions. 2024 is the last year of the rating case scenario.
Source: Fitch Ratings, City of Lviv

Rating History

Date	Long-Term Foreign-Currency IDR	Outlook
20 Apr 20	B/Stable	B/Stable
13 Sep 19	B/Positive	B/Positive
12 Jan 18	B-/Stable	B-/Stable

Socioeconomic Indicators

	Lviv Region*	Ukraine
Population, Sep 2019 (m)	2.5	41.9
GRP per capita, 2018 (UAH 000)	70.2	82.2
Unemployment rate, Mar 2019 (%)	7.6	9.6

* No data for the city of Lviv, data for the Lviv region act as a proxy

Source: State Statistics Service of Ukraine

Appendix B

City of Lviv

	2016	2017	2018	2019	2020rc	2024rc
Fiscal Performance Ratios						
Operating balance/operating revenue (%)	27.1	22.6	20.4	23.0	17.2	16.1
Current balance/current revenue (%)	28.2	23.1	20.4	22.6	15.5	13.6
Operating revenue growth (annual % change)	31.7	33.8	11.5	4.2	-18.0	6.8
Operating expenditure growth (annual % change)	30.5	42.1	14.7	0.7	-11.9	8.0
Surplus (deficit) before net financing/total revenue (%)	-1.8	1.1	-5.3	-3.1	-8.9	-6.0
Surplus (deficit) before net financing/GDP (%)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total revenue growth (annual % change)	32.0	32.1	12.2	6.4	-17.7	6.9
Total expenditure growth (annual % change)	44.4	28.4	19.4	4.2	-13.1	8.6
Debt Ratios - Type B						
Primary Metrics						
Payback ratio (x)	0.7	0.6	0.7	0.8	2.4	4.1
Enhanced payback ratio (x)	0.7	0.6	0.7	0.8	2.4	4.1
Overall payback ratio (x)	0.8	0.7	0.8	0.9	2.5	4.2
Enhanced overall payback ratio (x)	0.8	0.7	0.8	0.9	2.5	4.2
Secondary Metrics						
Fiscal debt burden (%)	18.6	13.2	14.7	17.7	40.7	65.8
Synthetic debt service coverage ratio (x)	15.4	19.2	7.1	8.3	2.9	2.0
Actual debt service coverage ratio (x)	898.3	1,057.4	47.4	28.6	10.1	1.7
Other Debt Ratios						
Liquidity coverage ratio (x)	1,107.4	1,206.3	55.6	31.9	11.7	1.7
Direct debt maturing in one year/total direct debt (%)	0.0	100.0	0.0	0.0	0.0	0.0
Direct debt (annual % change)	-33.3	-50.0	25,823.5	67.9	108.1	25.5
Apparent cost of direct debt (interest paid/direct debt) (%)	4.7	3.9	17.8	13.3	12.0	9.0
Revenue Ratios						
Tax revenue/total revenue (%)	50.4	50.2	55.4	62.3	73.7	73.7
Current transfers received/total revenue (%)	40.5	41.9	36.0	26.6	17.1	16.6
Interest revenue/total revenue (%)	1.4	0.6	0.6	0.5	0.0	0.0
Capital revenue/total revenue (%)	2.0	1.7	2.3	4.4	5.3	5.6
GDP deflated total revenue growth (annual % change)	12.7	8.3	1.1	-5.3	-20.2	n.a.
Expenditure Ratios						
Staff expenditure/total expenditure (%)	24.4	21.8	23.0	26.5	0.0	0.0
Current transfers made/total expenditure (%)	30.1	35.1	34.5	31.9	0.0	0.0
Interest expenditure/total expenditure (%)	0.0	0.0	0.4	0.7	1.5	2.3
Capital expenditure/total expenditure (%)	30.9	23.5	26.2	28.2	26.5	23.0
GDP deflated total expenditure growth (annual % change)	23.3	5.2	7.6	-7.2	-15.7	n.a.

rc: Fitch's rating case, based on conservative assumptions. The last year of the rating-case scenario is 2024.

Source: Fitch Ratings, City of Lviv

Appendix C: Data Adjustments

Net Adjusted Debt Calculation

Fitch includes the guaranteed incurred debt of municipal companies into “other Fitch-classified debt” and thus in Lviv’s adjusted debt calculation. This is because many of those companies have been posting losses in recent years and the city provides them with capital injections, including amounts equal to the guaranteed debt coming due in a given year.

The actual debt incurred by municipal companies was UAH1.2 billion at end-2019. Under Fitch’s rating case, we expect the latter to rise to UAH2 billion in 2020 and UAH3.5 billion in 2024, albeit subject to the pace of project implementation.

Fitch does not include budget loans received from the central government in 2010-2013 in the city’s adjusted debt, in line with other national peers. These loans, which were UAH240 million for Lviv, are not serviced and are subject to write-off when expected regulation comes into force. The loans are included in the city’s contingent liabilities.

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