S&P Global Ratings

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Research Update:

Austrian State Of Burgenland 'AA/A-1+' Ratings Affirmed; Outlook Stable

April 23, 2021

Overview

- We believe the Austrian state of Burgenland will implement savings measures to mitigate the financial effects of the pandemic.
- At the same time, projected sluggish tax revenue growth will prolong the period of fiscal deficits until at least 2023.
- The state will continue to cover its funding needs with federal treasury loans.
- We are therefore affirming our 'AA/A-1+' ratings on Burgenland and maintaining the stable outlook.

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Rating Action

On April 23, 2021, S&P Global Ratings affirmed its 'AA/A-1+' long- and short-term issuer credit ratings on Austria's State of Burgenland. The outlook is stable.

Outlook

The stable outlook reflects our view that Burgenland has a relatively high capacity to weather the financial effects of the COVID-19 pandemic. We assume that the widening of the state's budget deficit will be temporary and the deficit will start shrinking from 2022 due to recovering tax revenue. We believe the resulting debt accumulation will be short-lived and Burgenland's debt burden will not substantially increase above moderate levels of about 60% of operating revenue over the period to 2023.

Downside scenario

We would consider lowering our ratings on Burgenland if its management doesn't succeed in adapting its expenditure structure to the lower revenue base. This would likely result in a pronounced depletion of the state's currently ample liquidity and debt accumulation well beyond our current expectation.

Upside scenario

Ratings uplift could stem from an improvement of Burgenland's economic profile that aligned it with the national average, or a more supportive and predictable institutional framework for all Austrian states.

Rationale

Our ratings on Burgenland are supported by the state's exceptional access to liquidity via the Austrian federal debt management agency, OeBFA, and commercial banks, which provides the state with a stable source of funding for the upcoming deficits. In addition, the reliable institutional framework protects individual states from above-average shocks to its revenue base. Major tax shortfalls forecast for 2021 due to the pandemic will keep Burgenland's budgetary performance in deficit after a decade of deleveraging. We believe that the state will therefore deviate from its previous policy of yearly net debt reduction and accumulate direct debt from 2020. However, we expect that the debt increase will remain moderate in a national and international comparison.

We believe that the state's finances might benefit from the upcoming reform of the interstate equalization system, which is currently on hold to digest the effects of the pandemic. We also take into account Burgenland's lower economic wealth than other Austrian states.

Lower tax revenue expected for 2021

The economic recession in 2020, after lockdown measures to restrict the spread of COVID-19 in Austria, will lead to tax shortfalls for all Austrian states in 2021, similar to 2020. In addition, the ongoing national tax reform is leading to lower tax revenue than previous years. Although we expect economic growth will rebound in 2021 following the beginning of vaccinations, tax collection and distribution mechanics mean that tax revenue will be similarly affected as in 2020, effectively delaying the recovery of public finances. In particular, we have reduced our economic forecast for Austria in 2021, based on continued restrictions on economic activities in early 2021, especially in the eastern parts of Austria. We currently anticipate Austria's national GDP will rebound by 2.5% in 2021, after the 6.6% decline in 2020, with the regional economy following national trends. The Austrian fiscal system collects taxes nationally and distributes revenue to the states according to their relative population, therefore the Austrian states share the burden of tax shortfalls with the central government. The fiscal system also shields Burgenland from above-average shocks to its regional tax base, since taxes are distributed irrespective of where they were collected. Despite the pandemic-induced drop, Austria's national GDP per capita remains high at €42,200 (equivalent to about $51,000) in 2020.

We generally regard the legal framework in which Austrian states operate as predictable and supportive. Given that the states and the federal government depend on the same bucket of tax revenue, decisions taken at the federal level on tax rates have immediate effects for the states. Updates to the tax distribution system are regularly implemented, with negotiations for the next reform likely to start once the pandemic effects have diminished. The national fiscal equalization mechanism (Finanzausgleich), which determines the allocation of shared taxes between the federal, state, and local levels, was originally scheduled to be renegotiated by 2022. Given limited resources for renegotiations, we believe that the existing formula might be extended for two additional years. If the Austrian federal legislators enact further meaningful changes to the tax code, this could be compensated by either additional one-off transfers to the states or systemic improvements in the distribution of tax revenue and expenditure tasks.

Burgenland's government consists of members of one party that has an absolute majority in the state parliament. This should allow the government to implement savings measures, even if state laws need to be changed, or raise revenue by tax or fee increases if these are deemed politically feasible. We understand that the prudent deleveraging policy of recent years is currently on hold, given the vast tax shortfalls. Nevertheless, management intends to safeguard its budgetary performance by looking for savings measures and revenue-raising possibilities. We therefore deem it likely that the state will implement savings measures and actually outperform its current financial planning.

Excellent access to the federal treasury limits financing risks considerably

In our base-case scenario through 2023, we anticipate that Burgenland will gradually improve its budgetary performance by using its limited revenue flexibility and strict expenditure controls. Compared with our previous expectation, we now believe that the recovery will be more gradual due to a slow recovery of tax revenue. National tax revenue should improve to pre-pandemic levels by 2023 only, despite our assumption of economic recovery before then. Potential upside to our forecast could stem from increased consolidation measures or additional funds allotted to states in the upcoming revision of the national tax equalization. We currently think the revision is unlikely to be realized over the next three years, however.

According to preliminary results for 2020, as expected Burgenland posted a considerably higher deficit after capital accounts than in previous years. We expect that final figures, including transfers to and from reserves, will not significantly alter the preliminary results. We believe that the state will achieve a slightly weaker result in 2021, based on lagging tax revenue and continued expenditure needs for the pandemic. Unlike German peers, Burgenland has not announced major additional expenditure or guarantee measures funded by its own means.

Our assessment of budgetary performance reflects ongoing payments for unfunded, pay-as-you-go pension liabilities that, although not excessively large, will also weigh on results for the foreseeable future. We estimate the net present value of pensions at about €900 million, and believe that yearly payments of about 3% of operating revenue to retired special status civil servants will continue to burden the state's finances for years to come.

Even though we project an increase in debt through 2023 at least, Burgenland's direct debt burden is low, both in a national and international comparison, following constant deleveraging over the past decade. All direct debt is in domestic currency at fixed interest rates with the federal treasury, which limits risks considerably. In our calculation of tax-supported debt, we include the debt of BELIG, the state's real estate company, and KRAGES, the state's hospital institution, as well as our projections for the cost of an hospital currently under construction. We assess the state's contingent liability risk as limited in size and probability. Unlike most rated Austrian peers, Burgenland bears no contingent risk from guarantees or ownership of a public sector bank. We consider that Burgenland's outsourced companies, including but not limited to the state's holding company Landesholding Burgenland GmbH, represent the state's largest contingency risk. In addition, Burgenland is facing a currently negative market revaluation of derivatives, which the state is trying to negotiate with banks.

We consider the state's liquidity as exceptional, based on cash, liquid assets, and committed credit lines well in excess of 100% of debt service over the coming 12 months. Burgenland has two liquidity lines totaling €80 million with banks. The state only rarely uses commercial banks for short-term credit in limited amounts. The state also benefits from established access to funding from OeBFA and the Austrian capital market.

Key Statistics

Table 1

Burgenland (State of) Selected Indicators

	--Year ended Dec. 31--						
Mil. €	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**	**2023bc**
Operating revenues	1,106	1,146	1,212	1,144	1,128	1,229	1,262
Operating expenditures	1,023	1,018	1,156	1,094	1,079	1,160	1,189
Operating balance	83	128	56	50	49	69	73
Operating balance (% of operating revenues)	7.5	11.2	4.6	4.4	4.3	5.6	5.8
Capital revenues	24	30	37	18	23	23	33
Capital expenditures	119	101	120	150	169	154	136
Balance after capital accounts	(12)	57	(27)	(82)	(97)	(62)	(31)
Balance after capital accounts (% of total revenues)	(1.0)	4.8	(2.2)	(7.0)	(8.4)	(4.9)	(2.4)
Debt repaid	76	31	81	83	99	89	106
Gross borrowings	74	73	77	166	180	130	130
Balance after borrowings	(14)	99	(30)	2	(16)	(21)	(7)
Direct debt (outstanding at year-end)	274	272	269	352	433	474	498
Direct debt (% of operating revenues)	24.8	23.7	22.2	30.8	38.4	38.6	39.5
Tax-supported debt (outstanding at year-end)	400	422	508	617	723	789	838
Tax-supported debt (% of consolidated operating revenues)	31.6	31.9	36.5	46.6	55.3	56.0	58.1
Interest (% of operating revenues)	1.4	1.3	1.3	1.6	2.4	2.1	2.1
Local GDP per capita (single units)	30,000	30,700	31,600	29,846	31,500	32,394	33,285
National GDP per capita (single units)	42,100	43,681	44,879	42,193	43,882	45,898	47,338

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

Ratings Score Snapshot

Table 2

Burgenland (State of) Ratings Score Snapshot

Key rating factors	
Institutional framework	2

Table 2

Burgenland (State of) Ratings Score Snapshot (cont.)

Economy	2
Financial management	2
Budgetary perfomance	4
Liquidity	1
Debt burden	2
Stand-alone credit profile	aa
Issuer credit rating	AA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

Sovereign Risk Indicators, April 12, 2021; a free interactive version is available at http://www.spratings.com/sri

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Institutional Framework Assessments For International Local And Regional Governments, April 13, 2021
- Research Update: Austria Ratings Affirmed At 'AA+/A-1+'; Outlook Stable, March 12, 2021
- European Economic Snapshot: Policy Is Keeping The Impact Of The Second COVID Wave At Bay, Dec. 16, 2020
- Local And Regional Governments Outlook 2021: Gradual Recovery Will Test Rating Resilience, Dec. 10, 2020
- Default, Transition, and Recovery: 2019 Annual International Public Finance Default And Rating Transition Study, Dec. 8, 2020
- Institutional Framework Assessment: Austrian States, Oct. 13, 2020

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

Ratings Affirmed	
Burgenland (State of)	
Issuer Credit Rating	AA/Stable/A-1+

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. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website 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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