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Municipal Guarantee Board

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Municipal Guarantee Board

Major Rating Factors

Issuer Credit Rating
AA+/Stable/A-1+

Strengths	Weaknesses
<ul style="list-style-type: none"> • Joint support from Finland's local government sector through ultimate guarantee of obligations. • Special public-policy status highlighted by government act, which currently limits extension of guarantees to sole beneficiary, Municipality Finance PLC. • Strong risk awareness with active strategy and sophisticated monitoring mechanisms to account for assessed risk in guarantee exposures. • Proactive approach to preempt regulatory risk. • Very strong risk profile of Municipality Finance, which limits likelihood of guarantee being exercised. 	<ul style="list-style-type: none"> • Possibility that last-resort claim on municipalities might not be timely. • Weak liquidity and capitalization in relation to total guarantee commitments.

Outlook

S&P Global Ratings' stable outlook on Finland-based Municipal Guarantee Board (MGB) partly reflects that on the sovereign. If we were to lower our ratings on Finland, we would also lower our ratings on MGB. However, if we were to raise our ratings on Finland, a possible upgrade of MGB would hinge on our view of MGB's and Municipality Finance's joint creditworthiness.

Our ratings on MGB continue to reflect our two-year expectation that the structure of Finland's joint municipal funding system will remain in its current form, and that Municipality Finance will remain the sole recipient of MGB's guarantees. In addition, we anticipate that the creditworthiness of the Finnish municipal sector, even after introduction of a possible reform of the LRG structure, will remain stable and the current legislative structure--including the MGB Act and MGB's status as a special public-policy agency--will remain broadly unchanged.

Independently of any rating action on the sovereign, we could lower the ratings on MGB if its legal status or institutional set-up were to change or if Municipality Finance's credit quality were to deteriorate significantly. Similarly, the ratings could come under pressure if other credit institutions were allowed to benefit from MGB's guarantees. We could also downgrade MGB if we thought the credit quality of the Finnish local government sector was declining.

Rationale

The ratings reflect the joint support of Finland's local government sector, which strongly backs the guarantees that MGB extends on Municipality Finance's senior debt funding. This is done via a joint and pro rata guarantee from MGB's member municipalities, which represent all of mainland Finland's population (that is, excluding the autonomous Åland Islands). Hence, as one of the main pillars of the municipal funding system, MGB is closely linked to the local government sector, in our view; therefore, our ratings on MGB are capped by the ratings on the sovereign, in line with our approach for individual local and regional governments (LRGs). We use our principles of credit ratings to analyze MGB, whereby we assess the strength of the joint guarantee structure and the stand-alone credit profile of Municipality Finance PLC, which MGB exclusively extends guarantees to.

The ratings on MGB are underpinned by our view of the robust creditworthiness of the Finnish local government sector, thanks to strong systemic support features and the institutionalized and unlimited ability of municipalities to increase local income tax rates. We also consider MGB's special public-policy role and status--as described in specific legislation--within the funding system for Finnish local governments, as well as its proactive approach to risk management. In addition, the ratings reflect MGB's focus on providing guarantees solely for the financial obligations of Municipality Finance, which under the current set-up is the primary credit institution for Finnish local governments and the central government's subsidized housing sector. Importantly, we believe it is highly unlikely that MGB will be called upon to honor its guarantees of Municipality Finance because Municipality Finance has a very solid financial standing and very low risk in its operations. These strengths are somewhat mitigated by some uncertainty about the timeliness of the pro rata guarantee from MGB's member municipalities. In addition, we note MGB's thin capitalization and financial resources compared with the amount of guarantees outstanding.

MGB's role and scope of activities are regulated by specific legislation, the MGB Act, which defines the agency's special public-policy role and sole mission of ensuring the viability of a joint funding system for Finnish local governments. Essentially, this means MGB provides guarantees solely for Municipality Finance's financial obligations, and we are not aware of any concrete plans to extend the scope of MGB's remit. If Municipality Finance were to default on its financial obligations, MGB could, without a court order, turn to its members on a pro rata basis to obtain funds, which it would receive through the guarantee mechanism for repaying investors.

We note that, unlike a joint and several guarantee commitment, there could be a time lag in determining and acquiring the required pro rata amount from each member local government if the guarantee were to be triggered. Although it has yet to be tested, we believe the process could take up to one month. Even so, if the guarantee were called, we anticipate that MGB would remain proactive and secure timely payment through the flexibilities that exist within the MGB Act. In addition, MGB has its own liquidity in the form of securities and liquid funds, which totaled €17.7 million in June 2016, together with a committed credit line of €150 million. These liquidity sources serve as a first line of defense, allowing for the injection of capital into Municipality Finance in the unlikely event that it faced financial difficulty. We expect that MGB will revise its liquidity position at certain intervals to keep pace with its expanding guarantee commitments to Municipality Finance and its assessment of risk related to Municipality Finance's derivatives portfolio. As a second level of defense, MGB may be able to obtain additional funds from its members if its

own liquidity sources were to prove insufficient.

As of June 30, 2016, MGB's outstanding guarantees totaled €27.4 billion, compared with its current maximum guarantee limit of €39.1 billion. Although the volume of outstanding guarantees appears very high relative to MGB's capital base and liquidity facilities, we believe that ultimately MGB's ability to fulfill its guarantee commitment to Municipality Finance depends on the creditworthiness of Finland's local government sector. Furthermore, we believe the likelihood of the guarantee ever being called is very low, given Municipality Finance's very strong asset quality, capitalization, and liquidity, as well as its low-risk lending and prudent asset-liability management.

We view MGB as having a proactive approach to risk management. Since 2010, MGB has performed quantitative analyses of the risk held in Municipality Finance's swap portfolio. This created differing target levels for MGB's equity fund, depending on the stresses applied in the scenario analyses, and MGB is gradually increasing its equity fund in response to the conclusions of its risk analyses. In addition, we think MGB and Municipality Finance continue to proactively manage regulatory risk.

We note that there are ongoing discussions about reorganization of Finland's public sector by establishing county councils whose main responsibility will be health care. If this reform were to be implemented, MGB would not, without an amendment to the MGB Act, automatically be in scope of extending guarantees for the benefit of loans to entities belonging to this new tier of government. We will monitor the developments and assess possible implications for MGB.

Table 1

Municipal Guarantee Board--Balance Sheet Statistics														
('000 €)	2015	2014	2013	2012	2011	2010	2009	--Breakdown as a share of assets (%)--						
								2015	2014	2013	2012	2011	2010	2009
Assets														
Liquid funds	137.4	77.9	83.0	126.0	94.0	114.0	50.0	1.4	0.3	0.5	0.9	0.7	0.9	0.4
Securities	17,574.0	16,222.9	14,990.0	13,505.0	12,211.0	11,933.0	10,854.0	92.8	93	94.1	93.8	93.3	93.7	93.5
Intangibles		--	--	--	--	--	--	--	--	--	--	--	--	--
Fixed assets	226.4	248.6	149.0	165.0	170.0	165.0	185.0	1.3	1.5	0.9	1.1	1.3	1.3	1.6
All other assets	681.2	667.4	702.0	595.0	609.0	530.0	519.0	4.4	5.1	4.4	4.1	4.7	4.2	4.5
Total assets	18,619.0	17,216.8	15,925.0	14,392.0	13,084.0	12,743.0	11,608.0	100.0	100	100	100	100	100	100
								--Breakdown as a % of liabilities + equity--						
	2015	2014	2013	2012	2011	2010	2009	2015	2014	2013	2012	2011	2010	2009
Liabilities and equity														
Total liabilities	122.3	108.8	149.1	218.0	158.0	135.0	58.0	1.0	1.6	0.9	1.5	1.2	1.1	0.5
Fund	17,350.8	16,296.3	15,247.0	14,072.0	13,105.0	11,958.0	11,288.0	92.2	93.8	95.7	97.8	100.2	93.8	97.2
revaluation reserve	1,145.8	811.7	529.0	102.0	(179.0)	649.0	262.0	6.9	4.6	3.3	0.7	(1.4)	5.1	2.3
Total capital and reserves	18,496.6	17,108.1	15,775.6	14,290.0	12,926.0	12,607.0	11,550.0	99.0	98.4	99.1	99.3	98.8	98.9	99.5
Total liabilities and equity	18,619.0	17,216.8	15,924.7	14,392.0	13,084.0	12,743.0	11,608.0	100.0	100	100	100	100	100	100

Table 2

Municipal Guarantee Board--Ratio Analysis							
	--Year ended Dec. 31--						
	2015	2014	2013	2012	2011	2010	2009
Cost/revenue analysis (%)							
Guarantee fee/operating revenues	81.2	90.1	88.2	87.7	85.2	80.1	86.5
net interest income/operating revenues	15.0	9.9	11.8	12.3	14.8	19.9	13.5
Personnel expense/operating revenues	21.2	25.4	22.3	24.0	19.9	23.8	22.8
Cost/income	72.7	63.9	54.9	57.6	51.0	64.0	57.0
Guarantee fee/avg. guaranteed funding	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest income/avg. total securities	3.2	1.7	2.2	2.2	2.9	3.3	2.3
Liquidity (%)							
(Liquid funds + Securities + credit line)/guaranteed funding	0.6	0.5	0.7	0.8	0.9	0.7	1.2
(Liquid funds + Securities + credit line)/biggest exposure	18.2	19.6	21.8	32.0	29.8	46.4	27.4
(Liquid funds + Securities + credit line)/biggest individual loan	83.7	83.1	82.7	81.8	81.2	81.0	268.2
Capitalization (%)							
Equity/guaranteed funding	0.1	0.0	0.1	0.1	0.1	0.1	0.1
Equity/biggest exposure	1.9	1.9	2.1	2.6	2.4	3.6	2.0
Equity/biggest individual loan	8.7	8.0	7.9	7.1	6.5	6.3	19.3

Table 3

Municipal Guarantee Board--Profit And Loss Statement Statistics							
	--Year ended Dec. 31--						
('000 €)	2015	2014	2013	2012	2011	2010	2009
Profitability							
Guarantee fee	2,300	2,300	2,300	2,000	2,000	1,500	1,500
Net interest income	425	273	307	280	347	373	233
Total revenues	2,832	2,667	2,607	2,280	2,347	1,873	1,733
Personnel expenses	600	566	582	547	468	446	395
Other general and administrative expense	1,044	924	824	739	707	735	591
Depreciation and amortization-other	27	33	26	28	25	21	9
Noninterest expenses	1,670	1,523	1,432	1,314	1,200	1,203	995
Earnings (before transfer to capital fund)	1,055	1,049	1,175	966	1,147	670	738

Related Criteria And Research

Related Criteria

- General Criteria: Methodology And Assumptions For Rating Jointly Supported Financial Obligations - May 23, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Criteria - Governments - International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign - December 15, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And

Assumptions - November 19, 2013

- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers - May 07, 2013
- General Criteria: Principles Of Credit Ratings - February 16, 2011
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Research Update: Finland Outlook Revised To Stable On Gradual Economic Recovery; Ratings Affirmed At 'AA+/A-1+' - September 16, 2016

Ratings Detail (As Of December 22, 2016)

Municipal Guarantee Board

Issuer Credit Rating AA+/Stable/A-1+

Issuer Credit Ratings History

30-Sep-2016	AA+/Stable/A-1+
13-Oct-2015	AA+/Negative/A-1+
14-Oct-2014	AA+/Stable/A-1+
15-Apr-2014	AAA/Negative/A-1+
16-Jan-2013	AAA/Stable/A-1+
20-Jan-2012	AAA/Negative/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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