

CREDIT OPINION

14 June 2018

✓ Rate this Research

RATINGS

Municipal Guarantee Board

Domicile	Finland
Long Term Rating	Aa1
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Municipal Guarantee Board (Finland)

Update to credit analysis

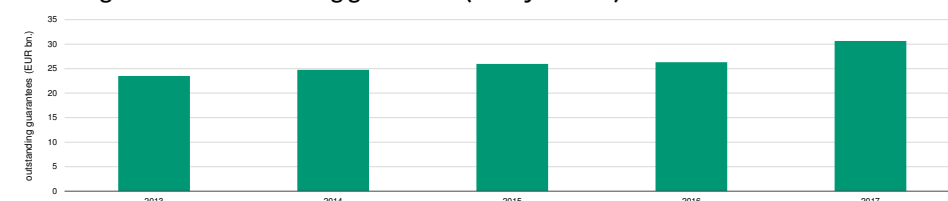
Summary

The credit profile of the [Municipal Guarantee Board \(MGB; Aa1 stable\)](#) reflects the strong cooperation and linkages between the [Government of Finland \(Aa1 stable\)](#) and MGB's member municipalities. The inter linkages, controls and importance of services provided by the local government sector would indicate that the absolute end supporter in the unlikely event of an acute liquidity stress would be the Government of Finland.

MGB was set up by the Finnish parliament in 1996 under a special law with the purpose of safeguarding and developing the joint funding of Finnish municipalities. MGB plays its role by guaranteeing all funding by credit institutions directly or indirectly owned by municipalities that will be used for lending to municipalities, entities under their control and government guaranteed social housing entities. These guarantees improve funding availability and assist the municipalities ability to deliver their public services in Finland as mandated by the central government.

Exhibit 1

Increasing volume of outstanding guarantees (as of year-end)



Source: MGB

Credit Strengths

- » Strong municipality ties with the central government
- » Joint guarantee issued by all municipalities on the Finnish mainland
- » MGB plays an important role in the Finnish local government funding system
- » Low likelihood of guarantee being triggered

Credit Challenges

- » Weak standalone liquidity in relation to total guarantee stock
- » Untested guarantee mechanism

Rating Outlook

The rating outlook is stable. This reflects the outlook of its support provider, the Government of Finland.

Factors that Could Lead to an Upgrade

An upgrade in Finland's sovereign rating could lead to an upgrade of MGB's rating.

Factors that Could Lead to a Downgrade

Negative pressure on the rating could result from one or a combination of the following: A downgrade in Finland's sovereign rating, a weakening of the ties between the local government sector and the sovereign or a weakening of the MGB Act and the joint guarantee and reduced importance of MGB.

Detailed Rating Considerations

The credit profile of Municipal Guarantee Board, as expressed in an Aa1 stable issuer rating, is reflecting the support from the central government.

In our view, it is not meaningful to distinguish between MGB and Government of Finland. The significance of MGB's public mandate and the members' close ties with the central government leads to an expectation of near certain likelihood of support from the central government (Aa1, stable) to provide liquidity in the unlikely event that the local government sector and MGB would require this support.

Strong Municipality ties with the central government

While Finnish municipality sector is characterized by a high level of devolved powers, there is also strong ties and dialogue between local government and central government. Local authorities have full autonomy to levy municipal income tax and property tax. Municipalities also have autonomy in matters of debt and this system has been working well as the debt of municipalities is low and stable, at around 25% of own revenues in 2017. The Finnish municipality sector is present at the highest level of parliament debates via the Finnish Local and Regional Authority, collaborating on all matters affecting their own sector. The creditworthiness of the municipality sector stems from a high level of revenue predictability, low levels of debt, a strong equalization system and most importantly the close government oversight, collaboration and ties. Approximately one fifth of the local government's revenue in Finland comes from the central government and this level has remained stable for many years. We note however, that [planned structural \(health and social care\) reforms could raise debt metrics of local government sector](#).

The central and local government have a strong cooperation procedure based on the close interplay through the Finnish Local and Regional Authority monitoring process. Local finances and services are accessed every year and should a municipality be flagged, the municipal council would immediately start a recovery plan to address any highlighted issues. The significance of MGB's public mandate and the members' close ties with the central government leads to an expectation of near certain likelihood of support from the central government (Aa1, stable) to provide liquidity in the unlikely event that the local government sector and MGB would require this support.

Joint guarantee issued by all municipalities on the Finnish mainland

In accordance with the MGB Act, MGB guarantees are strong because all municipalities located on the Finnish mainland are members. Consequently, MGB guarantees are backed by the entire nations' municipal tax base. If one municipality fails to meet its obligations to MGB, then all peers are required to cover the shortfall on a joint basis based on population size. The island of Åland, which represent 0.5% percent of the Finnish population, is not an MGB member due to their self-governance status. The payment obligation can be utilized without a court order and the MGB Act allows MGB to support government owned credit institutions even before the latter fails to make a payment to its creditors. Since MGB's inception, the only credit institution to meet the criteria set out in the Act was Municipality Finance Plc (MuniFin) (Aa1, Stable). So, MGB is anticipated to support MuniFin without going through complex procedures.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

MGB plays an important role in the Finnish local government funding system

MGB was established by law in 1996. The MGB Act allows it to extend guarantees to any credit institution that is (a) owned or controlled by municipalities; and (b) in the business of lending to municipalities and their associated entities and government guaranteed social housing companies. MGB, however, only guarantees MuniFin's debt (and payments from hedging counterparties to MuniFin) because MuniFin is the only credit institution owned by municipalities in Finland. In effect, MGB ensures that MuniFin meets its obligations and allows it to function as the debt management office for the Finnish local government sector.

Funds borrowed from MuniFin are used for investments in public services such as education, social housing and elderly care. The municipalities are in continuous dialogue with the central government related to the legislation concerning the services to be provided by the municipal sector.

The strong ties between MGB and the central government are also underlined by its governance. The Ministry of the Finance appoints MGB's council of 15 members at the recommendation of the Association of Finnish Local and Regional Authorities. Members serve four-year terms. The council appoints a board of seven members, and the board in turn appoints the managing director for MGB. MGB has its own auditor as well as one appointed by the Ministry of Finance.

Low likelihood of guarantee being triggered

MuniFin's underlying credit strengths makes the likelihood of MGB needing to action the guarantee very remote. MuniFin has a history of strong predictable financial performance, low risk appetite, important national and public mandate, diverse funding resources and a low risk appetite. In addition MuniFin's liquidity portfolio is of good quality and large in size. At year end-2017 the portfolio amounted to EUR 6.5 billion compared to total assets of EUR 34.7 billion. MuniFin also benefits from Central Bank access. MGB will thus only be required to exercise the guarantee in the remote and unlikely chance that MuniFin faces acute financial distress and a long term loss of access to whole sale funding.

Weak stand-alone liquidity in relation to total guarantee stock

MGB's has a standalone liquidity portfolio of EUR 17.8 million and also benefits from a committed credit line (EUR 150 million). This is considered small compared to its outstanding guarantee stock, which in year end 2017 amounted to EUR 30.6 billion. Moody's does not place much significance on MGB's standalone liquidity, but instead takes comfort in the sizeable reserves held by MuniFin and the Finnish local government sector. The Finnish local government sector holds around EUR 5.7 billion in cash reserves (at 31 December 2016) which MGB members could use to repay MuniFin's obligations (source: Ministry of Finance Finland). Projections from that Ministry suggest that the level of liquidity will decrease only slightly during the next four years.

Untested guarantee mechanism

The MGB guarantee has never been triggered, but practical procedures for delivering financial support to MuniFin has been documented. MGB can claim payment from its member-municipalities in order to support MuniFin without a court order.

A mitigating factor is the financial health of Finnish local government sector¹. MuniFin and MGB could take several early-steps to prevent triggering the MGB-guarantee mechanism. This view is based on the fact that:

1. MuniFin maintains liquid securities sufficient to cover obligations for a minimum of six months, assuming uninterrupted lending. MuniFin can also repo its municipal lending portfolio with the central bank.
2. The Finnish local government sector holds around EUR 5.7 billion in cash reserves
3. MGB has access to EUR 150 million in liquidity line with one counterparty as well as maintaining its own small (EUR 17.8 million) investment portfolio.

Rating Methodology

We use the methodology for Government Related Issuers, published August 2017.

The significance of the joint and pro-rata guarantee, involving all Finnish municipalities, ultimately leads to an expectation of near certain extraordinary support from the [Government of Finland](#) (Aa1 stable) in the unlikely event of financial distress.

Ratings

Exhibit 2

Category	Moody's Rating
MUNICIPAL GUARANTEE BOARD	
Outlook	Stable
Issuer Rating - Dom Curr	Aa1

Source: Moody's Investors Service

Endnotes

1 [Moody's: Nordic Local Governments' Credit Quality Boosted by Support Expectation and Inherent Strength, published 20th May 2016](#)

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