

# Norwegian municipal finances weakened by high interest rates and inflation

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High interest rates and cost inflation had a negative impact on Norwegian municipal budgets, debt and cash balances in 2023, according to recently published data. Operating margins fell across the sector, and high interest costs weighed on cash balances. Gross debt levels remained under control, but rising costs and significant cash outflows resulted in material increases in nearly all municipal net debt burdens. In this report, we look at the implications for the country's 35 largest municipalities.

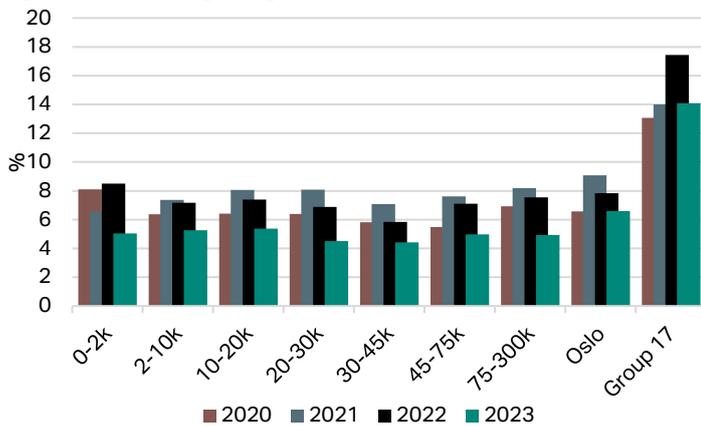
Earlier this month, the central bank decided to maintain its key policy rate at 4.5%, and indicated that it is likely to remain at that level for some time. The decision reflects ongoing efforts to reduce inflation to the bank's 2% annual target. We believe that this will force municipalities to focus on spending priorities and take a cautious approach to debt-financed investment in the remainder of 2024.

### OPERATING MARGINS SUFFER FROM HIGH OPERATING COSTS

Rising costs weighed heavily on all municipal operating performances in 2023, when the average operating margin in the sector fell to 5.3% from 7.6% in the two previous years, according to publicly available data. Our analysis takes into account consolidated operating margins (excluding depreciation) and focuses on cash flows.

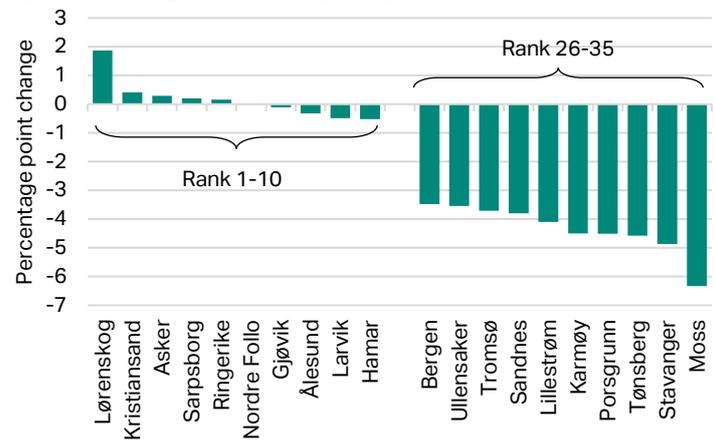
The impact of rising costs was most pronounced among the smallest municipalities (populations under 2,000). However, municipalities of all sizes (as defined by the KOSTRA system, through which municipalities and counties submit financial information to Statistics Norway) ended 2023 with material declines in operating margins. Among the 35 largest municipalities (populations over 30,000), operating expenses rose by 7.7%, outpacing average income, which rose by only 5.5%. As a result, the average operating margin fell by 2pp to 5.2%. Oslo, which operates as both a municipality and a county, had the smallest year-on-year margin decline of 1.2pp.

Figure 1. Operating margin by municipal population, 2020-2023



Source: Statistics Norway (SSB) and NCR. Group 17: The eight municipalities with the highest tax revenues/person.

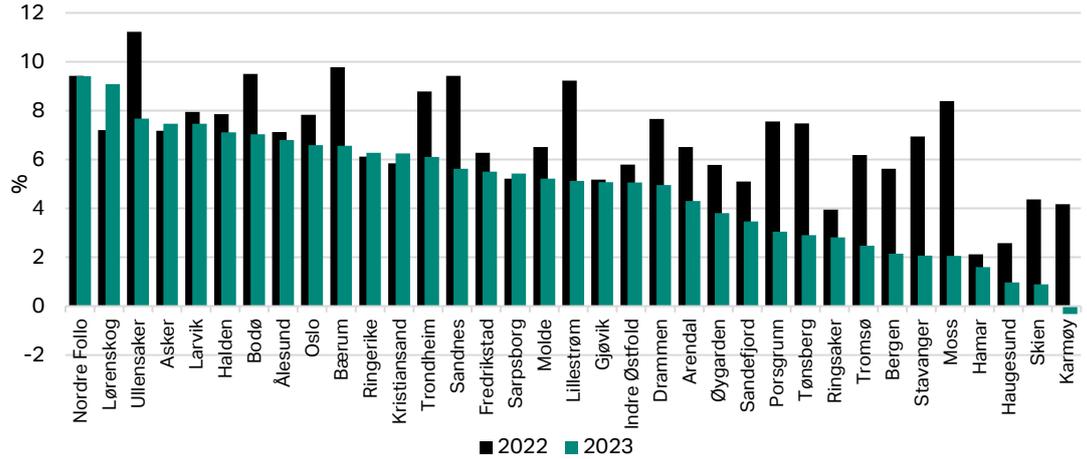
Figure 2. Change in operating margin\*, 2023 vs 2022



Source: SSB and NCR. \*Municipalities with a population over 30,000 according to KOSTRA.

All but five of the largest municipalities reported weaker operating margins in 2023 than in 2022, with an average decline of 2pp across the sample. The most notable outliers reversed recent trends. Lørenskog in Akershus county was the only municipality with a significant improvement in operating margin during 2023, partly reversing a 3.9pp decline in 2022. Conversely, an increase in operating expenses in Moss in Østfold county resulted in a 6.3pp decline in operating margin in 2023 after steady improvements in recent years. Karmøy in Rogaland county also reported a material deterioration in operating margin and was the only municipality to report a negative operating margin in 2023.

Figure 3. Operating margins of the 35 largest Norwegian municipalities, 2022-2023



Source: SSB and NCR.

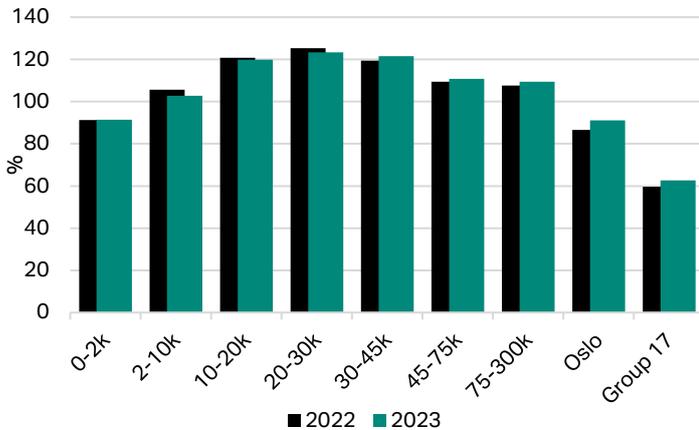
Municipal operating margins in Akershus county are among the strongest in Norway. Nordre Follo, Lørenskog, Ullensaker (including Oslo airport) and Asker municipalities lie within a comfortable commuting distance from Oslo city centre. Two other municipalities in Akershus, Bærum and Lillestrøm, had among the leading operating margins in 2023, though well below their 2022 levels. With the exception of Sandnes, the largest municipalities in Rogaland county, namely Stavanger, Haugesund and Karmøy, had among the weakest operating margins in 2023. The Rogaland municipalities were also among those with the largest year-on-year decline in operating margin in 2023.

**NET DEBT BURDENS INCREASE DUE TO CASH OUTFLOWS**

Among all municipalities, the average gross debt burden (gross debt as a proportion of operating revenues) fell to 105.6% at end-2023 from 106.3% a year earlier. However, the decline was primarily among small municipalities with populations under 30,000. Among the 35 largest municipalities, the average gross debt burden increased by 1.9pp. In addition, net debt burdens increased by an average 3.9pp among all municipalities and by 5.1pp among the largest 35.

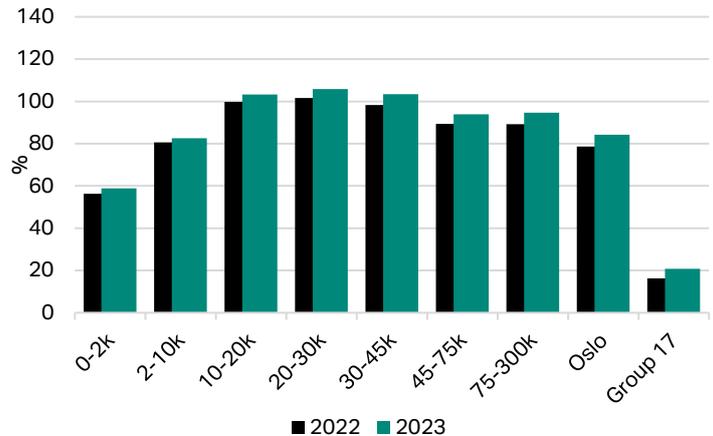
We interpret the relatively small changes in gross debt as an indication that municipalities were focused on maintaining debt levels at a time of rising operational and financial costs. However, this was from a starting point of relatively high debt levels due to investment to meet policy goals and strong population growth.

Figure 4. Gross debt burden by population size, 2022-2023



Source: SSB and NCR. Group 17: the eight municipalities with the highest tax revenues/person.

Figure 5. Net debt burden by population size, 2022-2023

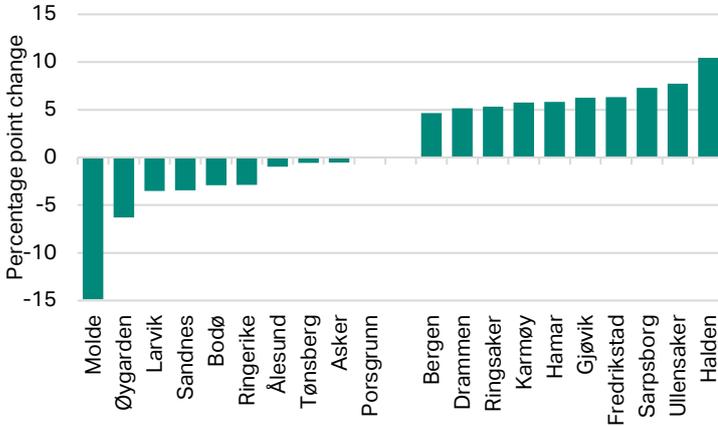


Source: SSB and NCR.

Despite a 5.5% increase in operating revenues, the largest municipalities' gross debt burdens increased to an average 114% of operating revenue in 2023 (from 112% in 2022). Among our sample, total gross debt increased by 8% in 2023 and net debt by 12%. The disparity in gross and net debt burdens is

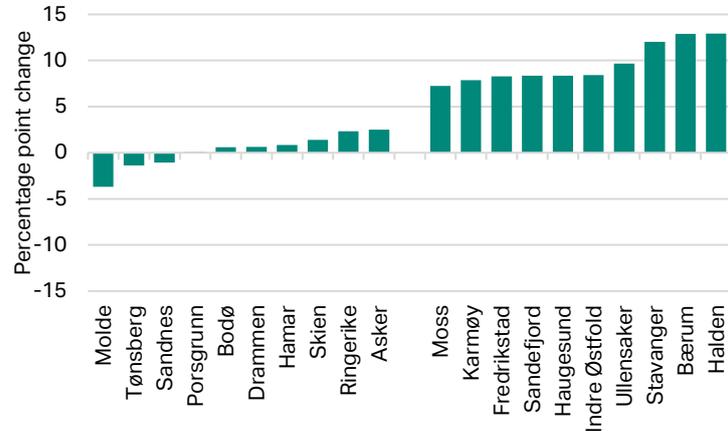
explained by a 14% reduction in cash balances due to higher spending. Many municipalities are also using financial reserves and reducing costs and investments where possible without affecting service levels. Among the largest municipalities, only 10 increased financial reserves as a proportion of operational revenues in 2023. Among the sample, average financial reserves fell 0.9pp to 12.1% of revenues in the course of the year.

Figure 6. Change in gross debt burden\*, 2023 vs 2022



Source: SSB and NCR. \*Municipalities with a population over 30,000.

Figure 7. Change in net debt burden\*, 2023 vs 2022

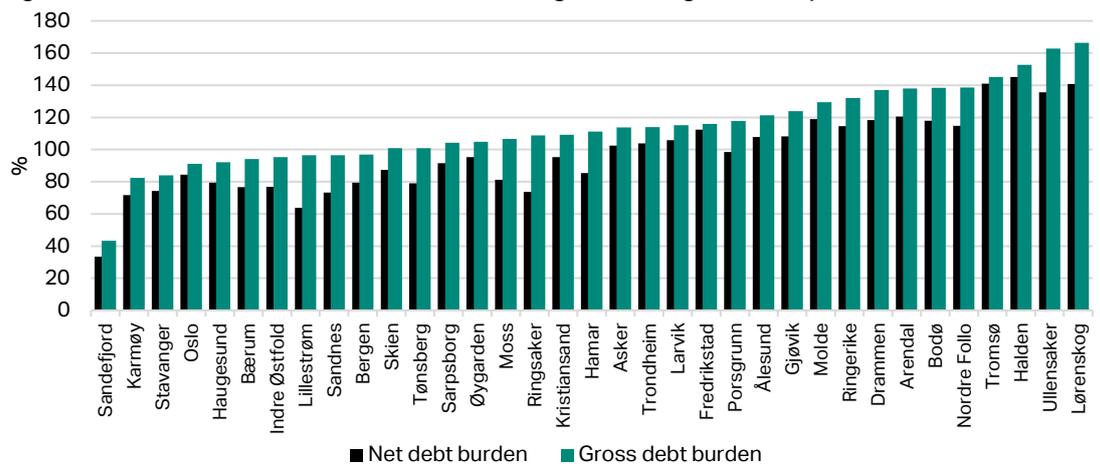


Source: SSB and NCR. \*Municipalities with a population over 30,000.

Norwegian municipalities are not allowed to take on debt to support operational performance. This was borne out by a relative lack of debt growth in 2023. In addition, rising interest costs reduce the attractiveness of debt-financed investments for municipalities and their subsidiaries. Nearly a third of the largest municipalities reduced their gross debt burden in 2023. Due to the impact of reduced cash balances, only three municipalities also reduced their net debt burden.

Molde municipality in Møre og Romsdal county saw the largest reduction in debt burden in its peer group in 2023. The city's improved operating revenues were more than offset by higher expenses, but still outpaced the increase in gross debt and reduced its gross debt burden to 129% from 144% a year earlier. Halden municipality in Østfold county saw its gross debt burden increase to 153% from 142%, leaving it with the third highest gross debt burden in our sample behind only Lørenskog and Ullensaker in Akershus county. Halden's 145% net debt burden placed it atop our sample as of end-2023.

Figure 8. Gross and net debt burden for the 35 largest Norwegian municipalities, 2023



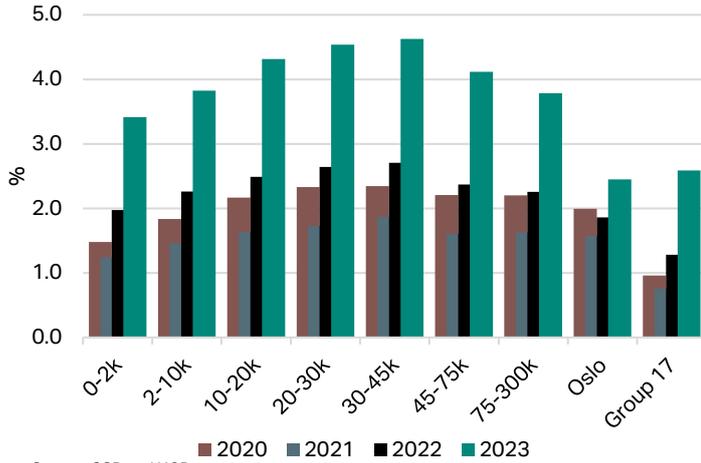
Source: SSB and NCR.

Municipal cash balances vary in the size. Ringsaker in Innlandet county and Lillestrøm in Akershus county each have cash balances of over 30% of operating revenues, nearly twice the 16% average of our sample. Conversely, Fredrikstad in Østfold county and Tromsø in Troms county had cash balances of less than 5% of revenues as of end-2023.

### INTEREST BURDENS INCREASE AS PROPORTION OF OPERATING REVENUES

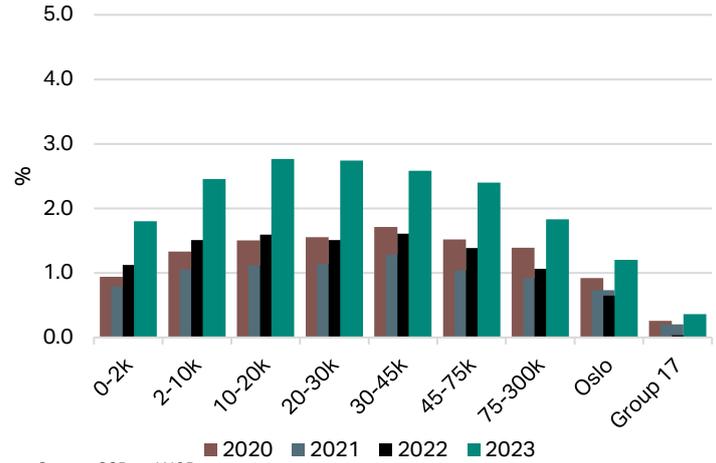
As a result of a sharp rise in interest rates in recent years, growing interest burdens present a challenge to all municipalities. The proportion of interest costs to operating revenues increased among municipalities by an average of about 70% in 2020-2023 (see Figure 9). The average interest burden across all municipalities increased to 3.9% at end-2023 from 2.3% a year earlier and only 1.5% in 2021. Municipalities and their subsidiaries have offset some of the rise in interest costs by earning interest income on their financial holdings and relatively large cash balances. As a result, the net interest burden increased to 2.3% of operating margins, a somewhat less dramatic increase from 1.4% in 2022 and only 1% in 2021.

Figure 9. Gross interest burden by population size, 2020-2023



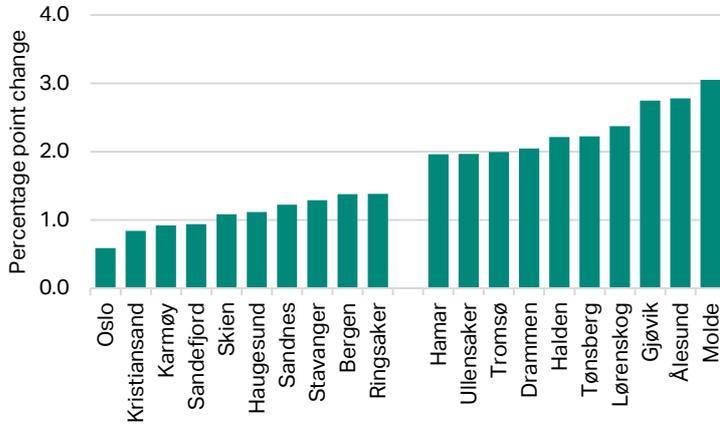
Source: SSB and NCR.

Figure 10. Net interest burden by population size, 2020-2023



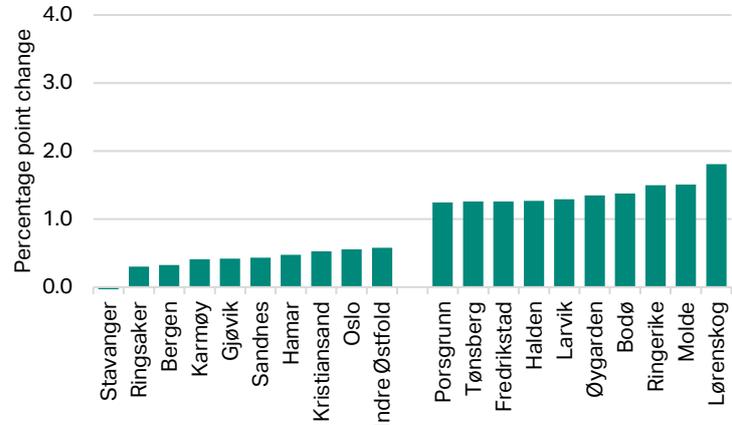
Source: SSB and NCR.

Figure 11. Change in gross interest burden\*, 2023 vs 2022



Source: SSB and NCR. \*Municipalities with a population over 30,000.

Figure 12. Change in net interest burden\*, 2023 vs 2022



Source: SSB, NCR. \*Municipalities with a population over 30,000.

Oslo reported the lowest increase in gross interest burden in 2023. The city also reported the second-lowest interest burden in 2023, behind Sandefjord in Vestfold county. We assume that Oslo benefits from interest rate hedging and more advanced financial management than other municipalities, given the size and complexity of its finances. Stavanger maintained a steady net interest burden in 2023, despite a below-average cash position at the end of the year.

Molde, which reported the largest reduction in gross debt, also reported the largest increase in interest burden in 2023. The city's gross interest burden of 7.9% in 2023 (4.9% in 2022) was the highest among the largest municipalities. Only Ålesund in Møre og Romsdal county (6.3%), had a gross interest burden of over 6% in 2023.

## NCR-RATED NORWEGIAN LOCAL AND REGIONAL GOVERNMENTS

The following table summarises NCR's ratings on Norwegian local and regional governments as of 16 May 2024.

Figure 13. NCR ratings on Norwegian local and regional governments

	Agder Fylkeskommune
Long-term issuer rating	AAA
Outlook	Stable
<b>Subfactors:</b>	
Sovereign creditworthiness	aaa
Local and regional government institutions	Strong
Entity-specific assessment	Strong
Other adjustments	n/a

See NCR [rating reports](#) for details.

## RELEVANT RESEARCH

- (i) [Norwegian counties face financial strain amid rising costs](#), 15 Feb. 2024.
- (ii) [Nordic Credit Rating publishes its final methodology for local and regional governments](#), 14 Feb. 2024.

## RECENT RATING ACTIONS

- (i) [Norway's Agder county assigned 'AAA' long-term issuer rating; Outlook stable](#), 5 Apr. 2024.

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