

## **Fitch Affirms City of Oradea at 'BBB-'; Outlook Stable**

Fitch Ratings-London/Frankfurt/Milan-25 February 2008: Fitch Ratings has today affirmed the City of Oradea's (Oradea) Long-term foreign and local currency ratings at 'BBB-' (BBB minus) and Short-term foreign currency rating at 'F3'. The Outlooks for both Long-term ratings are Stable.

The ratings reflect the City of Oradea's sound financial performance, expected to be maintained also in the medium term despite the strong growth of the city's debt to fund local infrastructure investments, and good management practices. They also take into account Romania's developing institutional framework, which translates, among others, into modest budgetary flexibility for Romanian cities and significant support and control by the State.

A negative rating action could be prompted by a significant increase in debt and lower operating performance against current projections - potentially stemming from unfavourable state policies on tax-sharing agreements and spending drivers such as salaries - leading to deteriorating debt and debt service coverage ratios. Conversely, a positive rating action could be triggered by budgetary performance remaining in line with projections and by a favourable evolution of the Romanian institutional framework, which would provide more budgetary flexibility to local governments while maintaining important central government support.

The city reported a sound operating balance in 2006-2007 at about 20% of operating revenue, abundantly covering its debt servicing requirements. Fitch expects the city's operating performance to remain sound at about 15% in 2008-2010, mainly on projected strong growth of personal income tax (PIT) and the city's ability to control expenditure growth. This would help the city to maintain a robust debt service coverage ratio despite expected strong growth of the city's debt in the medium term to fund local infrastructure investments. Total spending on roads, public utilities and urban regeneration should total approximately RON340m during 2008-2010, of which 40% will be debt-financed.

The city's debt should reach about RON210m by 2010, up from RON58m in 2006. However, the debt/current balance ratio should remain strong for the rating at about five years in 2010. Refinancing and currency risks are limited (although the latter are set to increase after a euro-denominated loan is issued 2008), while debt is fully exposed to interest-rate fluctuations. The availability of EU funds should help limit pressure on leverage-financed investments, especially from 2010, keeping debt under control.

Financial rigidity is high, as the state controls the PIT tax base and rate, sets limits on local tax rates, and annually decides VAT transfers (which should account for 35% of the city's total projected current revenue in 2008). Furthermore, the local tax burden is relatively high compared with those of other Romanian cities, and the state controls main expenditure drivers (staff salaries) and sets quality standards for public services provided by the city. However, the highly centralised budgetary system ensures adequate support and control from the central government, as it supervises the city's accounts and finances including debt approval.

Oradea, in north-west Romania, is the capital and largest city of Bihor County with about 207,000 residents. The city's strategic location near the Hungarian border and comparatively wealthy economy by national standards underpin its budgetary revenue. Locally generated and collected PIT and local taxes account for most of the local budget (at about 60% of forecast operating revenue in 2008).

A full report on the City of Oradea will be soon available on the agency subscribers' website, [www.fitchresearch.com](http://www.fitchresearch.com)

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