Autonomous Community of Madrid

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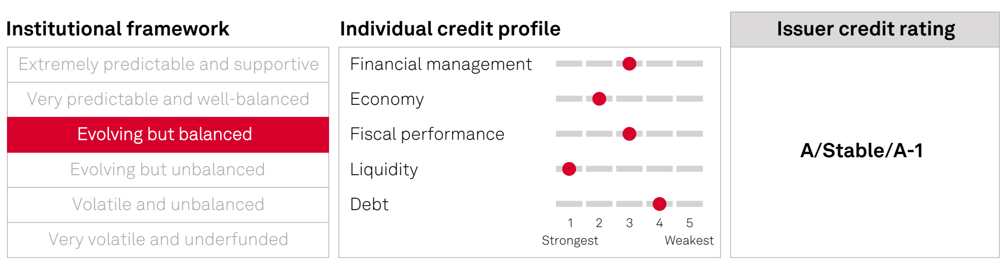
This report does not constitute a rating action.

Ratings Score Snapshot



Credit Highlights

Overview

Credit context and assumptions	Base-case expectations
We believe that in 2024, Madrid will benefit from large resources from the regional financing system, which we estimate could increase about 12.7%.	We expect the region not to have complied with the reference budget deficit target in 2023. We estimate an operating deficit of 2.3% of operating revenue in 2023, down from 2022's 4.1%.
We expect the region's economy to remain resilient, and the large availability of EU funds should support its economic growth and competitiveness.	We think the reinstatement of fiscal rules in 2024, prudent management policies, high revenue, and

Overview

Credit context and assumptions	Base-case expectations
	moderating expenditure growth will allow Madrid to return to operating surpluses.
Madrid's liquidity remains exceptional and supported by its strong access to capital markets even in period of market volatility, owing to a strong established track record and access to a wide investor base.	Debt remains high in an international context, although related metrics will continue to improve, supported by higher operating revenue.

S&P Global Ratings thinks the Autonomous Community of Madrid's operating performance will improve over 2024-2026, mainly due to increased revenue from the financing system. Despite a slightly weaker budgetary performance in 2023 than in our previous review, we continue to forecast an improvement in the region's operating budgetary performance over 2024-2026. This is supported by our expectation that revenue will remain high, while management will limit expenditure growth and comply with the reinstated fiscal rules from 2024 onwards.

We expect Madrid to accelerate investment related to the Recovery and Resilience Fund (RRF) over the forecast period, particularly in 2024. We estimate the region has spent about 46% of the funds received as of October 2023. Accelerating investment related to the RRF might create temporary budget deficits after capital accounts. Nevertheless, the availability of EU funds should support the region's economic growth in the next couple of years.

Madrid will maintain a strong liquidity position over the next two years. Supporting this will be its strong access to external liquidity sources, particularly through capital markets. The region remains the most active regional issuer in Spain, with a strong track record of accessing capital markets even during market volatility. Also, Madrid has €1.82 billion of credit lines, a €1 billion commercial paper program, and access to European Investment Bank (EIB) funding. Expected higher operating revenue over the next two years will allow the region to slightly improve its tax-supported debt ratio, which we forecast to decline to 132% of operating revenue by 2026 from 151% in 2023.

Outlook

The stable outlook reflects our expectation that Madrid will improve its budgetary performance over our forecast period, thanks to increased revenue from the financing system, which will offset cost pressures. The outlook also reflects our view that the region's financial management will remain committed to budgetary and fiscal consolidation while maintaining the solid liquidity position.

Downside scenario

We could lower our ratings on Madrid if we downgraded Spain. We could also downgrade the region if we saw loosened controls over budgetary spending, which would likely result in materially weaker budgetary performance than what we project. In this context, we would also expect liquidity to deteriorate.

Upside scenario

Any upgrade to Madrid would depend on an upgrade to Spain, because we do not think the region meets our requirements to be rated above the sovereign. However, should this condition be met, we could upgrade Madrid if the region's budgetary performance materially improves compared with our base-case scenario. For this, we would expect a stronger deleveraging path than forecast.

Rationale

Sound economic performance, high revenue from the regional financing system, and tight expenditure control will support financials

Madrid's economy continues to be a credit strength, in our view. It is the wealthiest among Spanish regions, with per capita GDP at 137% of the national average, according to the most recent public data available from the National Statistics Institute. Moreover, unemployment is below the national average (at 10.5% versus 11.8% for Spain as of September 2023). Given its wealthy economy, Madrid is also a net contributor to the Spanish regional equalization system, although this prevents it from retaining part of its wealth. We expect the regional economy to perform in line with Spain's over the forecast period. Madrid will continue to benefit from EU grants, particularly those from the Next Generation EU program, which should accelerate investments in 2024 and positively contribute to the region's competitiveness and economic growth if spent effectively.

In December 2023, the central government announced that Spanish regions will continue to benefit from significant revenue from the regional financing system in 2024. While figures for individual regions have not been announced, the central government stated that advances will rise 8.3% on average, while the settlement of 2022, which takes effect in 2024, will reach about €20.7 billion for the overall sector. We estimate that Madrid's revenue from the financing system, which represent about 78% of operating revenue, could increase 12.7% in 2024. Spanish regions had to revise their 2024 budgets under the challenging condition of not having visibility on this revenue nor on the deficit targets set by the central government for 2024. Given this, the region approved its 2024 budget under the assumption of a balanced budget target and, in our view, prudent estimates of revenue from the financing system.

The central government raised the possibility for Spanish normal status regions to benefit from a debt write-off over the next years. On Nov. 2, 2023, the Socialist Party announced an agreement with ERC, the party that holds the regional presidency of Catalonia, to absorb €15 billion of debt that the region owes to the central government (or 17.3% of Catalonia's debt as of June 2023). The central government has decided to extend this to all normal-status regions and for all type of debt, including debt to third parties. For Madrid, which does not owe debt to the central government, this means it would be entitled to this debt write-off.

Management will continue to implement its fiscal strategy over our forecast period. As announced in 2022, the region decreased several tranches of personal income taxes (PIT) and approved PIT deductions in 2023 related to birth rates. While these measures will reduce PIT collection, authorities expect part of the lost revenue will be offset by higher consumption and resulting collection of proceeds from as value-added or excise taxes.

Fiscal rules will return in 2024 after being suspended in 2020 due to the pandemic. The central government has announced that Spanish regions overall will have to comply with a deficit of 0.1% of GDP in 2024, and are expected to return to balanced budgets by 2025. We expect Madrid's management to maintain an effective control of its expenditure, which together with high revenue should allow the region to comply with the fiscal targets over the forecast period.

High revenue should contribute to Madrid's deleveraging and maintain exceptional liquidity

We expect Madrid to return to small operating budget surpluses in 2024, given that operating revenue will remain high and regional management will be able to maintain tight control on expenditure growth over the forecast period. Budget balances after capital accounts should also improve, as capital expenditure will decline after peaking in 2024.

We estimate Madrid's 2023 budgetary performance to have improved when compared to 2022, albeit with weaker results than what we had anticipated in our previous review (an operating deficit of 2.34% versus 0.81%). This followed lower operating revenue from a more pronounced drop in Madrid's real estate transaction tax collection than we had estimated, coupled with increased operating expenditure. Greater personnel costs and purchase of goods and services driven mostly by still-high inflation and a higher budget for Madrid's hospitals added pressure to budgetary performance in 2023.

Nevertheless, we forecast the region to return to positive operating budget balances in 2024 and maintain surpluses over the forecast period. It will benefit from a high increase in revenue from the financing system in 2024 and 2025. We expect settlements from the regional financing system for 2022 and 2023 to be large, owing to Spain's buoyant tax collection through 2022 and 2023, which takes effect two years later through the regional financing system settlement paid by the central government to Spanish regions. Also, we think the return of binding fiscal rules in 2024 will force Spanish regions, including Madrid, to slow expenditure growth. Furthermore, lower inflation should ease some budgetary pressure.

As of October 2023, the region has received about €2.4 billion of RRF financing from the EU and has already spent about 46% of these funds, while 72% of these funds have been allocated to specific projects. We expect Madrid's capital expenditure to peak in 2024, then gradually stabilize up to 2026. Over 2024 and 2025, the region is also set to receive funds from React EU to reimburse the related spending from previous years. We estimate this to reach about €600 million.

Madrid’s debt remains high in an international comparison and remains a constraint to its creditworthiness. Nevertheless, we expect the region to reduce its tax-supported debt ratios over the forecast period thanks to rising operating revenue. We forecast tax-supported debt ratio to reach 132% of consolidated operating revenue by 2026, down from 151% in 2023. About 60% of Madrid's debt consists of market issuance, whereas the remaining 40% are bank loans, including from multilateral institutions such as the EIB. As well, the region's debt is relatively shielded from volatility in interest rates because about 89% of its debt is fixed-rate.

Madrid uses capital markets to finance its needs and due to the rise of interest rates over the past year, interest payments now represent about 4% of its operating revenue. Nevertheless, by using market funding, the region manages well its debt maturity profile, getting longer maturities than if it were to finance itself through central government liquidity, for example.

Madrid displays an excellent liquidity position, supported by our view of its strong access to capital markets and thanks to the region's €1.8 billion in signed credit lines and €1 billion in commercial paper. We estimate Madrid’s financing needs for 2024 at about €3 billion, of which the region will likely use bonds, bank loans, and MLI funding. We assess the region's access to external liquidity as strong, given that it is the largest regional issuer in Spain and exposed to a wide investor base.

Autonomous Community of Madrid Selected Indicators

Mil. EUR	2021	2022	2023e	2024bc	2025bc	2026bc
Operating revenue	23,517	21,621	23,528	25,709	26,509	27,252
Operating expenditure	22,404	22,504	24,079	25,043	25,974	26,619
Operating balance	1,112	(884)	(552)	666	535	633
Operating balance (% of operating revenue)	4.7	(4.1)	(2.3)	2.6	2.0	2.3
Capital revenue	951	1,049	676	698	353	312
Capital expenditure	1,002	2,039	1,359	1,575	1,060	910
Balance after capital accounts	1,062	(1,873)	(1,235)	(212)	(171)	36
Balance after capital accounts (% of total revenue)	4.3	(8.3)	(5.1)	(0.8)	(0.6)	0.1
Debt repaid	2,622	2,926	2,680	2,960	2,826	2,965
Gross borrowings	2,622	3,773	3,743	3,017	3,150	3,050
Balance after borrowings	1,062	(1,026)	(172)	(155)	153	121
Direct debt (outstanding at year-end)	32,400	33,283	34,345	34,402	34,726	34,811
Direct debt (% of operating revenue)	137.8	153.9	146.0	133.8	131.0	127.7
Tax-supported debt (outstanding at year-end)	35,062	35,750	37,218	37,193	37,435	37,611
Tax-supported debt (% of consolidated operating revenue)	142.7	157.3	150.7	138.2	134.9	131.9
Interest (% of operating revenue)	3.0	3.0	3.2	3.9	4.2	4.3
Local GDP per capita	35,380	38,435	--	--	--	--
National GDP per capita	25,462	27,979	29,850	31,090	32,471	33,714

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. EUR--euro.

Autonomous Community of Madrid Rating Component Scores

Key rating factors	Scores
Institutional framework	3
Economy	2
Financial management	3
Budgetary performance	3
Liquidity	1
Debt burden	4
Stand-alone credit profile	a
Issuer credit rating	A

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, Dec. 11, 2023. An interactive version is available at http://www.spratings.com/sri

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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
- Criteria | Governments | International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign, Dec. 15, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Spanish Regions May Receive Debt Relief From State, Nov. 7, 2023
- SLIDES Published: Spanish Regions' Rising Revenues, Pressure On Expenditures, July 10, 2023
- Institutional Framework Assessment: Spanish Normal Status Regions , July 21, 2022

Ratings Detail (as of January 16, 2024)*

Madrid (Autonomous Community of)	
Issuer Credit Rating	A/Stable/A-1
Commercial Paper	
Local Currency	A-1
Senior Unsecured	A

Ratings Detail (as of January 16, 2024)*

Issuer Credit Ratings History

04-Nov-2022	A/Stable/A-1
06-May-2022	A-/Positive/A-2
23-Oct-2020	A-/Stable/A-2
08-Nov-2019	A-/Positive/A-2
10-May-2019	A-/Stable/A-2

*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.