Fitch Affirms Italy's Region of Valle d'Aosta at 'A'; Outlook Negative

Ratings Endorsement Policy

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Fitch Ratings-Milan/Paris/London-14 March 2014: Fitch Ratings has affirmed the Region of Valle d'Aosta's (VdA) Long-term foreign and local currency Issuer Default Ratings (IDR) at 'A' and Short-term foreign currency IDR at 'F1'. The Outlooks on the Long-term IDRs are Negative, mirroring those on Italy's sovereign IDRs.

The agency has simultaneously affirmed the Long-term ratings of the region's EUR74m and EUR543m (bullet) bonds, maturing in 2026 and 2021, respectively, at 'A'.

KEY RATING DRIVERS

The 'A' rating reflects Fitch's expectation that the region will continue recording solid, albeit declining, operating performance, supported by satisfactory budgetary flexibility and a robust balance sheet. The ratings also consider the reduction of the fund balance surplus, which Fitch expects to be fully absorbed by 2014-2015 by investments, as well as the region's small size and tax base concentration. This is, nevertheless, mitigated by the sound finances of the region's core taxpayers, including fully controlled Compagnia Valdostana delle Acque (A/Stable).

Preliminary 2013 figures point to a 17% operating margin, down from 25% in 2012, mainly due to the region's contribution to the national budget consolidation. Fitch expects the margin to be 15% over the medium term (EUR150m). VdA's tax resilience and a mild GDP recovery (0.5%) expected for 2014 would only partially compensate for on-going governmental contributions to balance the national budget, which are expected to double to almost EUR200m in 2014-2015.

To maintain a balanced budget, and given the high quality of its socio-economic infrastructure, Fitch believes that VdA will downsize its cumulative direct investment to match available resources, or EUR200m a year over 2014-2016, down from EUR400m in 2010-2012. In Fitch's view, regional companies, primarily the development agency Finaosta, will however increase their share in public spending, playing a more active role in supporting the local economy.

In line with VdA's zero-borrowing policy, direct debt declined towards EUR275m at end-2013 (net of the EUR323m sinking fund for the bullet bond), or 20% of operating revenue, from EUR308m in 2012. Fitch believes that, even if VdA should eventually start borrowing again alongside an economic upturn, debt protection ratios would remain solid, with the current balance at almost 3x debt service and a payback ratio below two years. Fitch expects VdA's direct debt to further decline to EUR190m by 2016 ,or EUR550m when Finaosta's committed debt is taken into full consideration.

VdA's robust liquidity - EUR250m at end-2013 (based on preliminary figures) - is underpinned by strong tax compliance, despite a prolonged economic downturn (GRP -1.9% in 2013). Fitch expects liquidity to be at EUR150m-EUR200m over the medium term, almost matching the region's outstanding debt and more than 2x annual debt service. The fund balance surplus, which accounted for 25% (EUR400m) of operating revenue in 2008, is expected to have declined to EUR21m in 2013, following the region's decision to self-finance its investments.

VdA's ratings are above Italy's sovereign ratings, as budgetary flexibility allows the region to maintain a healthy budget while coping with external pressures, including contributions to national budget consolidation. Protection granted by its special autonomous status shields the region from the risk of unilateral interference from the state, including risks of annual budgetary appropriations.

RATING SENSITIVITIES

A downgrade of Italy, a prolonged economic downturn that weakened tax generation, or a structural decline of the margin below 10% could result in a downgrade of VdA's ratings.

Its ratings are two notches above the sovereign's, down from three notches, following Italy's latest downgrade in March 2013. The narrower rating differential reflects the risk that an intensification of economic stress weakens the predictability of inter-governmental relations.

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Applicable criteria 'Tax-Supported Rating Criteria' dated 14 August 2012, 'International Local and Regional Governments Rating Criteria' dated 9 April 2013 and 'Rating Subnationals Above the Sovereign - Outside US' dated 2 May 2012 are available at www.fitchratings.com.

Applicable Criteria and Related Research:
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Additional Disclosure
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