FitchRatings

RATING ACTION COMMENTARY

Fitch Downgrades Autonomous Region of Valle d'Aosta to 'BBB+' on Sovereign Rating Action

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Link to Fitch Ratings' Report(s):
Autonomous Region of Valle d'Aosta - Rating Action Report

Fitch Ratings - Milan - 08 May 2020: Fitch Ratings has downgraded the Autonomous Region of Valle d'Aosta's (VdA) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) to 'BBB+' from 'A-'. The Outlooks are Stable. A full list of rating action is below.

The downgrade reflects the recent downgrade of the Italian sovereign (BBB-Stable) as VdA's ratings are constrained at two notches above the sovereign. The Outlooks mirror that on the sovereign.

VdA's Standalone Credit Profile (SCP) remains 'aa', reflecting the region's operating revenue resiliency amid expectations of tax revenue declining by -5% to -10% in

2020 under a rating scenario of a contracting economy after the coronavirus outbreak.

While Italian LRGs' most recently available issuer data may not have indicated performance impairment, material changes in revenue and cost profiles are occurring across the sector and likely to worsen in the coming weeks and months as economic activity suffers and some form of government restrictions are maintained or broadened. Fitch's ratings are forward-looking in nature, and we will monitor developments in the sector for their severity and duration, and incorporate revised base- and rating-case qualitative and quantitative inputs based on performance expectations and assessment of key risks.

KEY RATING DRIVERS

HIGH

Sovereign Cap

VdA's IDRs are constrained at two notches above the sovereign's rating, reflecting the risk of possible interferences by the state in case of macroeconomic or financial stress of sovereign finances and the subsequent risk of weakening predictability of intergovernmental relations. This is balanced by VdA's financial autonomy and budgetary flexibility with room to partly absorb rising spending, while contributions to national consolidation efforts are subject to bilateral agreement.

MEDIUM

Debt sustainability: 'aaa'

Under its conservative scenario of a contracting economy, Fitch expects that the operating balance will halve to EUR150 million in 2020 compared with 2019. Coupled with debt at EUR600 million by 2024 (when including regional financial company Finaosta's debt), this leads to a payback of around four years from the current 0.5. Even with this sharp deterioration of the payback under stressed circumstances, VdA's debt sustainability remains in the 'aaa' category.

VdA is classified by Fitch as a type B LRG, as it covers debt service from cash flow on an annual basis. VdA is a special-statute region located in the north-west of Italy, with a diversified set of responsibilities funded with a fixed share of major national taxes (100% of almost all national taxes) as set in the Italian constitution. VdA maintains a high degree of financial and fiscal autonomy (including taxation power, funding, ability to borrow and expenditure responsibilities), and bilateral consent is required on changes to funding and responsibilities. This protects the region from unilateral interferences by Italy's central government.

LOW

Risk Profile: 'Midrange'

Fitch has assessed VdA's risk profile at 'Midrange', reflecting a majority of 'Midrange' attributes on the six key risk factors, with one 'Stronger' for debt and liquidity. The Midrange risk profile stems from Fitch's assessment of VdA's cash flow generation capacity, which combines the region's revenue and expenditure structure and flexibility. It also considers VdA's sustainable debt profile and moderate access to liquidity sources, translating into relatively low risk that the region's capacity for payments of financial commitments weakens over Fitch's 2020-2024 rating scenario.

For detailed key rating drivers see therating action commentary published on 3 April 2020 at www.fitchratings.com.

DERIVATION SUMMARY

The combination of VdA's 'Midrange' risk profile with a debt payback ratio of four years leads to its SCP being assessed in the 'aa' category. A high debt-service coverage ratio above 3x, debt-to revenue ratio below 50% and peer comparison with other European regions lead to a 'aa' notch-specific SCP.

VdA's IDR is constrained at two notches above the sovereign's rating, reflecting the region's special autonomous status while also considering potential intervention by the state in case of sovereign stress, such as a moderate increase in the contribution to state's budget of around EUR20 million.

VdA's Short-Term IDR is assessed at the higher possible level of 'F1' amid a short-term liquidity coverage ratio (Fitch unrestricted cash and operating balance/debt service) estimated above 3x on average in 2020-2022, debt robustness assessed as Stronger and debt flexibility assessed as Midrange.

KEY ASSUMPTIONS

Qualitative Assumptions and assessments and their respective change since the last review on 3 April 2020 and weight in the rating decision:

Risk Profile: Midrange, unchanged with low weight

Revenue Robustness: Midrange, unchanged with low weight

Revenue Adjustability: Midrange, unchanged with low weight

Expenditure Sustainability: Midrange, unchanged with low weight

Expenditure Adjustability: Midrange, unchanged with low weight

Liabilities and Liquidity Robustness: Stronger, unchanged with low weight

Liabilities and Liquidity Flexibility: Midrange, unchanged with low weight

Debt sustainability: 'aaa' category, unchanged with medium weight

Support: n/a

Asymmetric Risk: n/a

Sovereign Cap or Floor: Yes, lowered with high weight

Quantitative assumptions - issuer specific

Fitch's rating case scenario is a "through-the-cycle" scenario, which incorporates a combination of revenue, cost and financial risk stresses. It is based on the 2015-2018 figures, 2019 preliminary figures and 2020-2024 projected ratios. The key assumptions for the scenario include:

- around 1% decrease in operating revenue on average in 2020-2024 in rating case, while average operating revenue remains substantially flat in the same period;

- about 1% increase in operating spending on average in 2020-2024 in our rating scenario versus roughly 2% in base case;

- Adjusted debt at EUR600 million in rating scenario versus around EUR450 in base scenario.

Quantitative assumptions - sovereign related (note that no weights are included as none of these assumptions was material to the rating action)

Figures as per Fitch's sovereign estimates for 2019 and forecast for 2021, respectively:

- GDP per capita (US dollar, market exchange rate): 32,979; 31,362

- Real GDP growth (%): 0.3%; 3.7%

- Consumer prices (annual average % change): 0.6%; 0.5%

- General government balance (% of GDP): -1.6%; -6.6%

- General government debt (% of GDP): 134.8%; 157.4%

- Current account balance plus net FDI (% of GDP): 2.1%; 1.1%

- Net external debt (% of GDP): 48.9%; 51.6%

- IMF Development Classification: DM

- CDS Market Implied Rating: BB+

RATING SENSITIVITIES

Factors That Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade:

Negative rating action on the sovereign will lead to similar action on VdA's IDRs.

Deterioration in the region's debt sustainability with a payback ratio towards five years together with a weaker debt service coverage ratio would lead to a downward revision of the region's SCP.

Further deterioration with a payback ratio above five years leading to a three-notch downgrade of the SCP would narrow the rating differential between VdA and the sovereign to one notch and consequently lead to a downgrade of the region's IDR to 'BBB+'.

Factors That Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade:

VdA's IDRs are partly constrained by the Italian sovereign ratings and hence will mirror rating action on the sovereign.

COMMITTEE MINUTE SUMMARY

Committee date: 6 May 2020

There was an appropriate quorum at the committee and the members confirmed that they were free from recusal. It was agreed that the data was sufficiently robust relative to its materiality. During the committee no material issues were raised that were not in the original committee package. The main rating factors under the relevant criteria were discussed by the committee members. The rating decision as discussed in this rating action commentary reflects the committee discussion.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Public Finance issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING		
Valle d'Aosta,Autonomous Region of	LT IDR	BBB+	Downgrade
•	ST IDR	F1	Affirmed
•	LC LT IDR	BBB+	Downgrade
• senior unsecured	LT	BBB+	Downgrade

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Rating Criteria for International Local and Regional Governments (pub. 13 Sep 2019) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Valle d'Aosta,Autonomous Region of	EU Issued

ADDITIONAL DISCLOSURES FOR UNSOLICITED CREDIT RATINGS

Valle d'Aosta,Autonomous Region of (Unsolicited)

With Rated Entity or Related Third Party Participation	Yes
With Access to Internal Documents	Yes
With Access to Management	Yes

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UNSOLICITED ISSUERS

ENTITY/SECURITY	ISIN/CUSIP/COUPON RATE	RATING TYPE	SC ST
Valle d'Aosta,Autonomous Region of	-	Long Term Issuer Default Rating	Ur
Valle d'Aosta,Autonomous Region of	-	Short Term Issuer Default Rating	Ur
Valle d'Aosta,Autonomous Region of	-	Local Currency Long Term Issuer Default Rating	Ur
Valle d'Aosta,Autonomous Region of	-	Stand-Alone Credit Profile	Ur

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