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Research Update:

Italian Province of Rome Affirmed At 'BBB' On Sound Budgetary Performance; Outlook Remains Negative

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Overview

- We anticipate that the Italian Province of Rome will maintain its strong budgetary performance, owing to strong and resilient tax bases, tight spending discipline, and positive financial management, despite depressed economic prospects for Italy.
- In addition, we forecast strong cash flows, decreasing payables, a very positive cash position, and the reduction of high tax-supported debt.
- We are affirming our 'BBB' rating on the province.
- The negative outlook mirrors that on Italy, reflecting the possibility that we could lower the rating on the province should we lower our ratings on Italy.

Rating Action

On Nov. 22, 2013, Standard & Poor's Ratings Services affirmed its 'BBB' long-term issuer credit rating on the Italian Province of Rome. The outlook is negative.

Rationale

The rating on the Province of Rome primarily reflects our long-term rating on Italy (unsolicited; BBB/Negative/A-2). We consider that the Province of Rome, like all other Italian local and regional governments (LRGs), does not meet all the criteria under which we could rate an LRG above the sovereign. In particular, in our view, the Province of Rome lacks sufficient financial autonomy to oppose negative intervention from the sovereign, such as a change in the local revenue structure. In addition, Italian law obliges the province to deposit the majority of its cash holdings at the Italian central bank.

In accordance with our criteria, we continue to assess the Province of Rome's indicative credit level (ICL) at 'aa-' (see "Methodology For Rating International Local And Regional Governments," published Sept. 20, 2010, on RatingsDirect). The ICL is not a rating but a means of assessing the intrinsic creditworthiness of an LRG, assuming no sovereign rating cap. The ICL results from the combination of our assessment of an LRG's individual credit profile and the benefits we see from the institutional framework in which it operates.

The 'aa-' ICL reflects the province's positive financial management, very strong budgetary performance, strong and resilient economy, very positive liquidity, very low contingent liabilities, and an institutional framework that we assess as "evolving but sound." The Province of Rome's still high, although rapidly declining, tax-supported debt and moderate financial flexibility partly offset these positives, because they decrease the province's leeway to raise taxes.

We believe that the institutional framework in which the Province of Rome operates is positive for the rating. Despite fiscal consolidation measures by the central government and dwindling tax bases owing to the economic crisis, the Italian LRG tier, in general, has not experienced a revenue-expenditure mismatch. In the case of the Province of Rome, it has posted improving budgetary performance since 2011, leading to fiscal surpluses and lower debt. This is also because the central government has gradually set up sounder fiscal rules and promoted spending austerity, which has in turn triggered cost rationalization at the provincial level.

The ICL is mainly supported by our assessment of financial management as "positive." In our view, managers' effective spending control will enable the province to maintain operating expenditure growth slightly below revenue increases, thereby consolidating its very strong budgetary performance in 2013-2015.

The ICL is also supported by a powerful economy that fuels the province's tax bases. Wealth levels in the province are more than 20% above the national average. In addition, the Province of Rome's 10% unemployment rate is lower than Italy's 10.7% average partly because the Province of Rome is where the central government has its headquarters and employs a large number of civil servants. The province's economy is undergoing Italy's current recession, however.

Our forecasts encompass a 1.8% contraction of Italy's real GDP this year and the country's maintaining structurally low growth after that. Nevertheless, we consider that the province's tax bases are fairly resistant to the economic downturn, which bolsters our view that budgetary performance will remain very strong during 2013-2015. In particular, operating revenues should increase by a notable 4.3% annually over this period, thanks to higher car-related tax receipts. These stem mainly from:

- Rental car fleet renewals and related acquisitions of second-hand cars, which pushed up car transactions in the provincial territory by 16% as of Oct. 31, 2013, year on year, versus a 2% decrease nationally;
- Amendments to the regulation on car registration tax in October 2012, which benefit the province because they mitigate the negative effect of fiscal competition based on different regulations among provinces on car registration tax; and
- Higher car insurance tax rates, which should generate about €50 million in 2013 (9% of our estimated operating revenue for the province).

In our view, the latest increase in car insurance tax in 2013 has whittled down the province's leeway to raise related revenues further, reducing its flexibility on the revenues side.

This is partly offset by what we see as the Province of Rome's still notable capacity to rein in spending if necessary, on which we partly base our forecast of the province's budgetary performance. We estimate operating expenditures will rise by only about 3.9% in total over 2013-2015. The province cut operating expenditures by a substantial 24% in 2011 and kept spending stable in 2012. During our forecast period (2013-2015), we anticipate that the Province of Rome will maintain its fiscal discipline on the back of administrative and personnel spending rationalization, given our positive assessment of its financial management. We anticipate robust and slightly improving operating margins at around 18%.

On the capital side, we expect healthy surpluses after capital expenditures of about 14%. In addition to robust operating margins, we see investments gradually dwindling to 5% of total expenditures in 2013-2015, from 15% in 2009-2011. The Province of Rome's consistent long-term planning is helping it to tailor new investments and ensure compliance with strategic long-term goals. Based on this conclusion, we believe that the province might use a portion of its abundant unreserved fund balance to increase investments above our forecasts in 2014-2015, without jeopardizing its sound budgetary performance in the medium term (2014-2015). And with such strong expected surpluses, the province is unlikely to take on new debt. Moreover, we anticipate that the Province of Rome's debt stock will decline more than the annual principal repayment in 2013, because the province will most likely redeem early its still undrawn loans contracted with Cassa Depositi and Prestiti, as it did in 2012. We regard this as an additional debt-reduction practice entailing no cash outflows.

We then expect tax-supported debt to decline more rapidly and fall to about 110% of operating revenues by 2015. The province's strong cash flow should also allow it to reduce payables without draining its cash balances.

We see low risk from the Province of Rome's non-self-supporting fully owned companies (Provincia Attiva and Capitale Lavoro, now merged) which posted an aggregate minor surplus in 2012 and are debt free. We therefore assess that the province does not carry material contingent liabilities.

In our downside scenario, our assessment of the Province of Rome's ICL could weaken to 'a+' if its financial performance deteriorated because of lower car tax proceeds than we expect, higher spending growth (+6% in our downside scenario), and much lower liquidity. In particular, less buoyant tax collection rates and delays in receiving transfers from the Region of Lazio, the latter totaling a significant 15% of the province's operating revenues, could strain liquidity.

Liquidity

According to our criteria, we assess the Province of Rome's liquidity position as "very positive," based on structurally high cash holdings and satisfactory access to external funding.

We estimate that the province's average cash (adjusted for the next 12 months' budgetary performance) should cover debt service requirements for the next 12 months by more than 3x, because we also expect debt service to stabilize at 12% of operating revenues in 2013-2015.

We acknowledge that the increasing arrears payments as of the midyear have not reduced the province's buoyant liquidity in 2013. Higher arrears payments stem from the central government's recent legislation to speed up the payment of LRGs' nonfinancial arrears. As part of the change, the central government has relaxed the Internal Stability Pact for LRGs in 2013. In the case of the Province of Rome, less stringent budgetary targets have meant that the province could pay all the arrears on executed investments of about €78 million in 2013. But despite the repayment of these arrears, the province's cash holdings still stood at €180 million as of Sept. 30, 2013, in effect a stable level compared with that in April 2013, when the central government enacted the decree (Law Decree 35) to speed up the repayment of such arrears.

In our view, the province manages to avoid weakening its cash holdings because it:

- Generates high operating cash surpluses, which we estimate at about 12% in 2013, despite high operating payment rates;
- Collects receivables on capital transfers from Lazio. This is in light of Lazio's use of central-government-sponsored liquidity facilities to pay arrears to local LRGs, including the Province of Rome, in 2013 and likely in 2014; and
- Draws on loans already contracted with Cassa Depositi e Prestiti.

In view of the province's medium-term zero-borrowing policy, our base case estimates that the Province of Rome will maintain high payment rates without depleting its cash holdings because it will continue to generate budgetary surpluses averaging 4% in cash terms in 2014-2015.

For these estimates, we factor in that the Province of Rome will maintain its annual cash holdings consistently higher than €100 million and reduce adjusted payables below a moderate 40% of operating revenues by 2015, from 96% in 2012.

Outlook

The negative outlook on the Province of Rome mirrors that on Italy. The outlook reflects the possibility that we could lower the rating on the province should we lower our ratings on Italy.

Apart from a sovereign downgrade, and in accordance with our criteria, we would lower the rating on the province if the ICL deteriorated to below the 'bbb' level. Given the currently strong 'aa-' ICL, however, such a scenario appears remote.

If we revised the outlook on Italy to stable and the province performed in line with our base-case scenario, we would likely take a similar action on the province.

Published Rating Factor Scores

Table 1

Province of Rome--Summary of Published Rating Factor Scores*

Rating factor	Score
Institutional framework	Evolving but sound
Financial management	Positive
Liquidity	Very positive

*Standard & Poor's ratings on local and regional governments are based on, among other things, a scoring system that covers eight main rating factors, as further explained in our criteria. We publish our scores for the three rating factors above.

Key Statistics

Table 2

Province of Rome--Financial Statistics

(Mil. €)	2008	2009	2010	2011	2012	2013bc	2014bc	2015bc	2013dc	2014dc	2015dc
Operating revenues	533	563	581	472	499	554	558	565	510	509	512
Operating expenditures	478	515	539	412	412	450	458	462	467	477	490
Operating balance	55	48	42	60	87	104	100	103	43	32	21
Operating balance (% of operating revenues)	10.31	8.55	7.30	12.68	17.37	18.74	17.89	18.27	8.50	6.32	4.20
Capital revenues	68	59	42	18	9	4	4	4	3	3	3
Capital expenditures	151	117	121	37	24	25	24	24	24	25	25
Balance after capital accounts	(28)	(9)	(36)	41	72	83	80	83	23	11	(1)
Balance after capital accounts (% of total revenues)	(4.60)	(1.47)	(5.85)	8.42	14.20	14.85	14.18	14.61	4.39	2.06	(0.12)
Debt repaid	42	55	43	37	69	39	40	41	39	40	41
Balance after debt repayment and onlending	(70)	(64)	(79)	4	3	44	40	43	(16)	(29)	(41)
Balance after debt repayment and onlending (% of total revenues)	(11.58)	(10.32)	(12.75)	0.83	0.69	7.93	7.11	7.48	(3.13)	(5.70)	(8.01)
Gross borrowings	50	19	0	0	0	0	0	0	0	0	0
Balance after borrowings	(20)	(45)	(79)	4	3	44	40	43	(16)	(29)	(41)
Operating revenue growth (%)	(4.55)	5.57	3.21	(18.81)	5.67	11.06	0.67	1.39	2.28	(0.21)	0.51
Operating expenditure growth (%)	(5.14)	7.65	4.62	(23.52)	(0.00)	9.22	1.72	0.92	13.25	2.17	2.79
Modifiable revenues (% of operating revenues)	58.21	50.38	47.95	65.59	67.09	71.32	71.95	72.26	72.02	72.74	73.60
Capital expenditures (% of total expenditures)	23.99	18.45	18.36	8.19	5.40	5.23	4.98	4.94	4.83	4.89	4.85

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Table 2

Province of Rome--Financial Statistics (cont.)											
Direct debt (outstanding at year-end)	958	922	879	841	773	715	676	635	715	676	635
Direct debt (% of operating revenues)	179.57	163.73	151.16	178.29	155.04	129.18	121.19	112.35	140.28	132.76	124.15
Tax-supported debt (% of consolidated operating revenues)	179.57	163.73	151.16	178.29	155.04	129.18	121.19	112.35	140.28	132.76	124.15
Interest (% of operating revenues)	7.61	6.57	5.85	6.99	6.22	5.07	4.84	4.55	5.50	5.30	5.02
Debt service (% of operating revenues)	15.49	16.36	13.25	14.88	19.98	12.04	11.96	11.72	13.07	13.11	12.95

bc--Base case: reflects Standard & Poor's expectations of the most likely scenario. dc--Downside case: represents some, but not all, aspects of Standard & Poor's scenarios that could be consistent with a downgrade.

Table 3

Province of Rome--Economic Statistics	2008	2009	2010	2011	2012	2013bc
Population	4,110,035	4,154,684	4,194,068	3,995,250	4,039,813	4,083,282
Population growth (%)	1.19	1.09	0.95	(4.74)	1.12	1.08
GDP per capita (€)	32,815	31,643	31,689	32,065*	31,521*	N/A
Unemployment rate (%)	7.00	8.10	9.09	8.53	10.04	N/A

bc--Base case: reflects Standard & Poor's expectations of the most likely scenario. *Standard & Poor's calculation using data from Istat and Unioncamere. N/A--Not available. Source: Istat.

Key Sovereign Statistics

For sovereign statistics, please click here:
S&PCORRECT: Long-Term Ratings On Italy Lowered To 'BBB'; Outlook Negative, July 10, 2013

Related Criteria And Research

- International Local And Regional Governments Default And Transition Study: 2012 Saw Defaults Spike, March 28, 2013
- Principles Of Credit Ratings, Feb. 16, 2011
- Methodology For Rating International Local And Regional Governments, Sept. 20, 2010
- Methodology: Rating A Regional Or Local Government Higher Than Its Sovereign, Sept. 9, 2009
- Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs, Oct. 15, 2009.

Ratings List

Ratings Affirmed

Rome (Province of)	
Issuer Credit Rating	BBB/Negative/--
Senior Unsecured	BBB

Additional Contact:
International Public Finance Ratings Europe; PublicFinanceEurope@standardandpoors.com

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.