



Moody's Investors Service Ltd

Autonomous Province of Trento

(Aa1/Stable Outlook)

Credit Strengths

Credit strengths of the Autonomous Province of Trento are:

- Long-established special status, which ensures greater legislative and financial autonomy and offers protection from interference by the Italian government
- Recently reinforced political stability, which has boosted the pace of government efforts and driven the implementation of new strategies
- Strong financial management, with excellent planning capacity
- Well above-average wealth levels, but a degree of economic reliance on tourism-related activities and public support
- Good overall fiscal flexibility and very strong operating margins
- Absence of direct financial debt, and low indirect risk
- Sound liquidity position, recently strengthened

Credit Challenges

Credit challenges of the Autonomous Province of Trento are:

- Although the special status protects continuity of tax revenue cash flows, these are mostly regulated by the national government, which also collects the taxes
- Capacity to change the tax base and tax rates is limited, mitigated by the province's ability to levy new local taxes
- Debt may rise following planned acquisition of hydroelectric power stations

Rating Rationale

The Autonomous Province of Trento's Aa1 issuer rating is based on its well-established special legal status, wealthy economy and sound financial fundamentals, reflected in a consistently strong budgetary performance, a good liquidity position and lack of direct debt. It also factors the administration's intention to acquire several hydroelectric power stations within the province, which may lead to debt funding. The rating additionally reflects Trento's limited direct leeway to modify tax revenue and the State's control over cash inflows.

Trento enjoys good wealth levels, with GDP per capita exceeding national and EU15 averages by 22% and 12%, respectively. The province's economy accounts for around 1% of Italy's GDP and is largely focused on services, with tourism-related activities particularly prominent. The local manufacturing system is based on small-sized companies, with no significant specialisations and relatively limited internationalisation. The construction sector performed well in recent years, boosted also by strong public spending.

According to official statistics, during 2000-2003 Trento's real GDP annual growth rate averaged 0.4%, below that for Italy overall (1.4%). However, provincial GDP growth seems to have accelerated recently, underpinned by a positive tertiary sector performance and dynamic construction activities. The province's economic buoyancy is mirrored in a low unemployment rate, which is in the range of 3%.

Given its constitutionally recognised special status, Trento enjoys a diversified revenue structure and retains nearly all locally generated and collected tax revenues. However, it is constrained by limited revenue flexibility, as the base and rates on these taxes can only be adjusted by the central government, which also collects the taxes – a constraint mitigated by the province's ability to levy new local taxes. The province also enjoys good expenditure flexibility, reflected in a well-diversified operating expenditure structure and a significant discretionary component of capital spending. Unlike normal-status regions, Trento records a much lower weight of healthcare expenditures in its budget and has historically run its hospitals efficiently without incurring healthcare deficits. In addition, under its special status, the central government cannot impose changes in its budgetary position without the province's consent.

Trento's budgetary performance has consistently recorded very robust operating margins - on both an accrual and cash basis - thanks to steady growth in operating revenues supported by the wealthy local economy and various administration initiatives aimed at increasing tax revenue streams. The province's good overall budgetary flexibility, the good level of predictability of its revenue streams, and strict cost controls should ensure that budgetary performance remains sound in the medium term.

Trento's consistent track record of self-financing and conservative financial management is reflected in a lack of direct indebtedness, which is almost unique by national and international standards. However, its intention to purchase several hydroelectric power stations within the province may lead to direct and/or indirect debt funding. Nevertheless, these acquisitions are likely to generate steady profits, with the returns being used to repay debt. In addition, Trento mainly executes services and public works through public and private law entities, which currently represent a low risk for the province.

Rating Outlook

Trento's stable rating outlook reflects its good degree of financial autonomy, strong financial position and sound liquidity.

What Could Change the Rating - UP

The province remains exposed to State decisions over its cash inflows and local economic cycles. Any devolution of true tax autonomy powers from the central government to the province, together with the confirmation of the province's good financial track record, could have additional positive credit implications.

What Could Change the Rating - DOWN

Trento's special status and strong credit fundamentals are key factors supporting its rating. Although highly unlikely given the support of the constitutional framework, any

alterations in the fundamental structure of the province's special status could prompt a negative rating change.