



Rating Action: Moody's assigns Aa3 rating to the City of Bellinzona; stable outlook

17 Oct 2023

Paris, October 17, 2023 – Moody's Investors Service (Moody's) has today assigned Aa3 long-term local currency issuer rating to the City of Bellinzona. Concurrently, Moody's has assigned a aa3 Baseline Credit Assessment (BCA). The outlook is stable.

RATINGS RATIONALE

The Aa3 long term issuer rating and aa3 BCA reflect the city's sound operating performance, solid economic base – despite small in size -, robust institutional framework, and good governance and management. The rating also factors in the municipality's high investment needs that will weigh on its already high debt burden and debt service.

Bellinzona is the capital of the southern Switzerland Republic and Canton of Ticino (Aa2 stable) and the headquarter of its public administration. It is the second most populated urban area in Ticino, with over 40,000 inhabitants, after the City of Lugano (Aa3 stable), and a relevant economic center in the Canton. The local government of Bellinzona, as we know it today, was created in 2017 after the merger of 13 neighboring municipalities and became operative in 2018.

Since 2018 – first financial year of the new entity - Bellinzona has recorded a sound operating performance, even though somewhat volatile due to the merger and the COVID pandemic. Over the last five years the gross operating balance (GOB) averaged 6.8% of operating revenue. Steady personal and corporate tax receipts, underpinned by a solid economic base, which includes an important presence of public administration and health care sectors, support the city's operating performance. Moreover, the city benefits from a mature and stable institutional framework, which through a robust equalization system and a legal requirement in terms of financial equilibrium, contributes to the municipality's solid financial results. Moody's expects Bellinzona to continue to record sound GOB levels above 4% of operating revenue over 2023-24. This expectation is underpinned by the favorable economic prospects coupled with the city's commitment to expenditure control and financial equilibrium.

The governance and management of Bellinzona is good, as demonstrated by the successful implementation of the merger, prudent financial planning and strong stance towards expenditure control. The municipality is committed to further streamline municipal processes, procedures and organization. This efficiency-gain target will contribute to the spending review launched by the city, also to offset the revenue decrease expected from 2024 onwards (due, in particular, to the end of cantonal merger-related transfers and the cantonal corporate tax rate reduction). Another key goal of the local government is to increase the attractiveness of its territory, which has the potential to reinforce the municipality's tax revenue. The city's economic strategy is focused on promoting innovation and attracting new businesses, notably in sectors like life science and high-tech, which could lead to an increased diversification of the small-sized local economy compared to international peers.

Bellinzona has defined an ambitious investment plan to meet infrastructure needs stemming from the enlarged urban area and investments aiming to increase the attractiveness of the territory. The local government plans to achieve CHF 25 million (over 11% of 2022 operating revenue) of net investments per year until 2026. According to Moody's estimation, Bellinzona's self-financing ratio will range between 45% and 50%, meaning that around a half of these expenses will be funded by internal resources, while the remaining part will be financed through new borrowing.

Among the city's credit constraints Moody's highlights its high debt burden compared to national and international peers. Net direct and indirect debt (NDID) to operating revenue was 175% in 2022. Moody's expects Bellinzona's

NDID-to-operating revenue to increase to over 180% in 2024, to fund the high investment requirements and refinancing needs. Nevertheless, the very low average interest rate, at 0.8% at year-end 2022, and its simple debt profile make the municipality's debt burden manageable.

Similarly, Bellinzona posts an elevated debt service, owing to its high debt stock with a relatively short maturity and mainly composed by bullet loans. Between 2019 and 2022, debt service as a percentage of operating revenue averaged a very high 46%. Moody's expects some peaks on debt repayments over the next three years also due to the coincidence of maturities of merged municipalities' debt. However, Bellinzona's good access to liquidity and careful treasury management mitigate risks associated with a high debt service. The management expertise tempers risks stemming from the absence of clear guidelines or thresholds on debt burden and annual repayment levels.

Bellinzona's credit profile incorporates a low exposure to contingent liabilities, representing 7.4% of operating revenue. Contingent liabilities comprise the financial debt of Azienda Multiservizi Bellinzona (AMB), the city's multi-service utility. Exposure to pension liabilities is not material.

Bellinzona's Aa3 rating incorporates a Baseline Credit Assessment (BCA) of aa3 and Moody's assessment of a moderate likelihood of extraordinary support from the Republic and Canton of Ticino (Aa2 stable).

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook reflects the city's capacity to manage potential revenue pressure and maintain control over expenditures, which will preserve a sound operating performance over the next two years. The financial debt will gradually increase, given the high investment requirements, but debt burden will remain manageable and consistent with the current rating level.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Collectively, environmental, social and governance considerations do not have a material impact on the Aa3 rating assigned to Bellinzona, as captured by Moody's assignment of a CIS-2 ESG Credit Impact Score.

The city's environmental issuer profile score (IPS) is E-2, reflecting some, albeit limited, exposure to physical climate risk, owing to increasingly volatile weather conditions and a growing number of heat stress episodes. This climate change-related environmental trend may cause losses in productivity, weigh on investment and exert pressure on the city's revenue base, although the economy is only moderately sensitive to weather conditions.

The S-2 social IPS assigned to Bellinzona reflects the absence of material social risks. Residents benefit of good access to basic services, water management and health and safety. Bellinzona's service-based economy is solid, despite being small in size. The city has a moderate exposure to demographic risks, notably population ageing, with budgetary pressure that can emerge from increased social spending.

Bellinzona's governance IPS of G-2 also reflects the absence of material risks. Bellinzona's management and governance practices are good, and the city benefits from a mature and stable institutional framework, which ensures financial equilibrium.

ECONOMIC DATA

The specific economic indicators, as required by EU regulation, are not available for the City of Bellinzona. The following national economic indicators are relevant to the sovereign rating, which was used as an input to this credit rating action.

Sovereign Issuer: Switzerland, Government of

GDP per capita (PPP basis, US\$): 84,661 (2022) (also known as Per Capita Income)

Real GDP growth (% change): 2.7% (2022) (also known as GDP Growth)

Inflation Rate (CPI, % change Dec/Dec): 2.8% (2022)

Gen. Gov. Financial Balance/GDP: 1% (2022) (also known as Fiscal Balance)

Current Account Balance/GDP: 10.2% (2022) (also known as External Balance)

External debt/GDP: 282.2% (2022)

Economic resiliency: aaa

Default history: No default events (on bonds or loans) have been recorded since 1983.

SUMMARY OF MINUTES FROM RATING COMMITTEE

On 24 August 2023, a rating committee was called to discuss the rating of the City of Bellinzona. The main points raised during the discussion were: The issuer's economic fundamentals, including its economic strength. The issuer's institutions and governance strength. The issuer's governance and/or management. The issuer's fiscal or financial strength, including its debt profile. The systemic risk in which the issuer operates. An analysis of this issuer, relative to its peers.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

A combination of the following could have positive rating implications: a meaningful and structural increase of its gross operating balance; and a sustained material reduction in leverage. An improvement in the credit strength of the Republic and Canton of Ticino could also result in an upgrade of Bellinzona's rating.

Negative pressure on the rating could be exerted by one or a combination of the following: a significant deterioration in the city's operating performance sustained over time; a substantially higher-than-expected NDID-to-operating revenue ratio; and a sustained weakening of liquidity metrics. The weakening of the credit strength of the Canton or, although not likely, a sovereign downgrade could also exert downgrade pressure on Bellinzona's rating.

The principal methodology used in these ratings was Regional and Local Governments published in January 2018 and available at <https://ratings.moodys.com/rmc-documents/66129>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

This rating action concerns a new rating for an issuer not previously publicly rated by us at the time that the EU sovereign release calendar was published, and is therefore being released on a date not listed in that publication.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/research/doc-PBC_1355824.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

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Emanuela Colzani
Analyst
Sub-Sovereign Group
Moody's France SAS
96 Boulevard Haussmann
Paris, 75008
France
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Sebastien Hay
Associate Managing Director
Sub-Sovereign Group
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Releasing Office:
Moody's France SAS
96 Boulevard Haussmann
Paris, 75008
France
JOURNALISTS: 44 20 7772 5456

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