



## Fitch: Liquidity for Spain Regions Positive, More Detail Needed

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20 Jan 2012 Fitch Ratings-London-20 January 2012: Measures outlined by the Spanish government to ease liquidity tensions affecting autonomous regions will be positive for them, although Fitch Ratings needs to see more detailed implementation plans before making a full assessment.

Cristobal Montoro, Minister for the Treasury and Public Administration Services, Tuesday said that Spain's central government and the country's 17 regions had agreed on the need for new legislation to establish penalties if they miss budget targets. In exchange, the government has announced that it is willing to provide the regions with more liquidity for debt repayment and with a credit line from Instituto de Credito Oficial (ICO). This credit line could also cover some trade creditors, although neither its size nor the conditions for subscribing to it were specified.

Controlling regional expenditure remains critical to having the autonomous regions hit their deficit targets, but structural reforms are also needed if they are to achieve medium-term financial sustainability. This will demand a coordinated effort by the central government and the regions.

We have previously noted in October, when we downgraded Spain to 'AA-', that the Spanish regions pose the largest risk to fiscal consolidation in the country. But we also acknowledge that they have recently announced a series of measures to rein in expenditure. These should also be positive although it is too soon to assess their impact, and our negative outlook on the sector reflects implementation risk. Structural reforms to healthcare and education funding are needed if substantial savings are to be made.

New legislation would potentially give the central government more effective control over regional finances than the current veto on long-term debt issuance, which can weaken an autonomous region's debt profile by making it too reliant on short-term funding. The victory of the Partido Popular, which governs many regions, in last year's national elections should also make it easier for regional and central government to work together and for central government to take a leading role in driving regional structural reforms forward.

The failure by the autonomous regions to hit their deficit targets was identified as a key reason that Spain's public deficit for 2011 has been estimated at over 8% of GDP, well above the 6% target. This raises doubts over whether Spain will meet its budget deficit targets in 2012 and 2013.

Considering that structural reforms have not yet been passed and operating revenue growth at regional level has been relatively flat, the deficit target for the autonomous regions of 1.3% of GDP was already seen as ambitious.

Fitch has Spain's 'AA-' rating on Rating Watch Negative, alongside those of five other eurozone sovereigns. The review was initiated on 16 December - before it became clear that Spain would miss its 2011 deficit target - to reflect the lack of a comprehensive solution to the eurozone debt crisis. We expect to complete the review by the end of January. The outcome will also incorporate our assessment of Spain's economic and credit fundamentals and recent policy measures.

As a direct result, we put the ratings of five autonomous communities - Andalusia, Asturias, Canary Islands, Cantabria, and Madrid, on RWN in December. We also placed Castile-La Mancha's, Murcia's and Catalonia's ratings on RWN, reflecting concerns about their increasingly difficult operating environment, and refinancing risk due to difficulties in accessing liquidity.

Providing liquidity support to the regions could increase the central government's financing requirement. However, the importance of the sub-national sector, which accounts for a third of total expenditure, means that general government debt, which incorporates both central and regional debt, is a more important measure for the sovereign rating assessment. General government debt should be unaffected by the transfer of financing requirements from regional governments to the central government.

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**Applicable Criteria and Related Research:**

Spanish Regions Third-Quarter Results 2011  
Spain

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