

A brighter future for Italian water utilities

The establishment of a national water regulator was a key turning point for the Italian water sector, according to a new report. The sector's fragmented nature and political ownership structure still make it hard to invest.

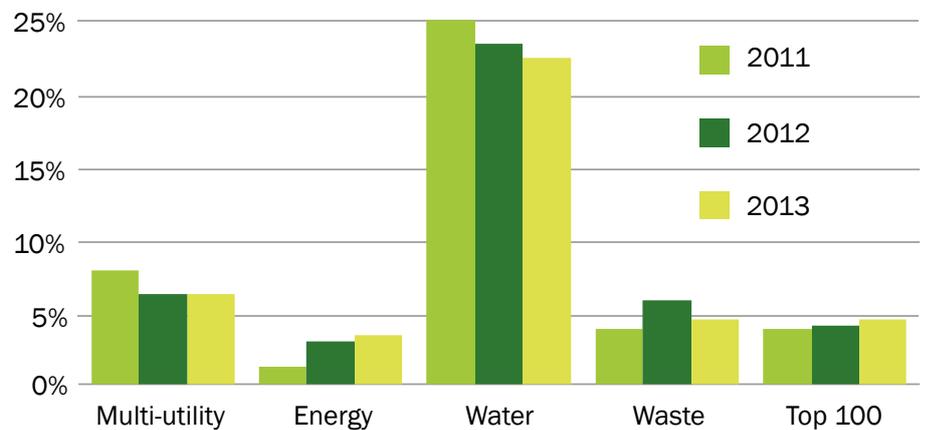
Operators are now better equipped to deal with the challenges of the Italian water and wastewater sector following the introduction of a national regulator, according to a new study of Italy's top 100 utilities carried out by consultancy Althesys.

The Top Utility report, released on 4th February, found that although Italian water utilities generated average EBITDA margins in excess of 20% between 2011 and 2013 (considerably higher than their peers in the energy, solid waste and multi-utility sectors), they also had the highest debt to EBITDA ratios, partly as a result of the need to invest more capital (see chart, right).

According to the document, the 27 water and wastewater utilities which achieved a top 100 ranking by turnover supplied 66% of the water used in Italy in 2013. The sector continues to be fragmented relative to other utility segments, however (see chart below). This situation is bound to change, according to report author and Althesys CEO Alessandro Marangoni. He argues that the consolidation trend is likely to intensify in the coming years, given that larger companies are better able to attract investment and withstand the sector's complex challenges.

The report argues that the law which established a national water regulator in 2012 was a clear turning point for the Italian water sector. "Previously tariffs were semi-regulated at the national level, but ultimately set by each ATO [ambito territoriale ottimale, a local body in charge of water and wastewater services], which in effect left the operators in charge of regulating themselves," said Marangoni. "The national regulator provides homogenous criteria for calculating tariffs, and thus ensures more uniformity across the board."

Investments as a percentage of revenues for Italian utilities (2011-2013)



Source: Top Utility/Althesys

The introduction of a national regulator had a demonstrably positive effect on the performance of utilities in other sectors in Italy. For example, electricity blackouts were reduced dramatically once a regulator was up and running in the energy sector. "We expect similar improvement in the delivery of water and wastewater services," says Marangoni, although he points out that any changes are likely to take a long time to materialise.

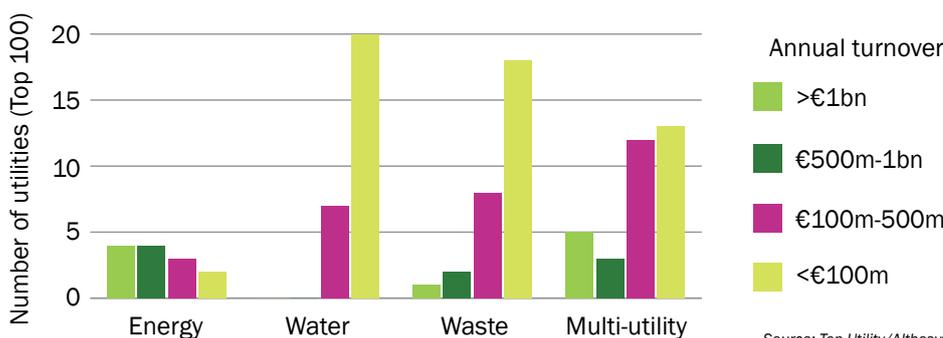
According to Marangoni, the Italian water regulator is likely to tread cautiously because of the continued regulatory and political uncertainty in the sector. Legal challenges are still ongoing on the back of the referendum in 2011 which revoked legislation allowing water operators to make a profit – and which sanctioned the principle of water as a "public good". In addition, infrastructure upgrades tend to be long-term projects requiring huge investment, added to which returns on investment tend to be lower in water than in the energy sector.

While a much-improved regulatory environment and the need for investment appear to provide the ideal backdrop for large international companies to enter the Italian water and wastewater sector, Marangoni is cautious. "In my opinion, the large-scale involvement of foreign players is unlikely, because 95% of water operators are local utilities that are either solely or largely publicly owned," he told GWI. The events of a few years ago, when foreign players including Thames Water and Saur attempted to enter the Italian market only to become embroiled in never-ending political, regulatory and legal wrangles, still acts as a major deterrent, he argues. "The Italian water and wastewater sector remains a complex market, and I don't think many foreign companies will wish to get involved," he told GWI.

Several Italian cities continue to be in breach of EU rules on wastewater treatment. The situation is improving slowly, but is hampered both by a chronic lack of investment capital, and by the protracted nature of the infrastructure build-out. "In the past, the threat of the referendum, coupled with uncertainty over tariffs, made for a powerful deterrent for would-be investors," laments Marangoni.

He is more optimistic about the future. The likelihood of multi-million-Euro EU fines, combined with a consolidation trend which could result in larger operators with greater economies of scale, a clearer regulatory environment, and a more stable long-term policy approach should, he argues, provide a more attractive market for investors.

Fragmentation in the Italian water industry



Source: Top Utility/Althesys