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Credit Opinion: SNCF Mobilités

Global Credit Research - 31 Mar 2016

Paris, France

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating	Aa3
Senior Unsecured	Aa3
Commercial Paper -Dom Curr	P-1
Other Short Term -Dom Curr	(P)P-1

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Key Indicators

[1]**SNCF Mobilités**	12/31/2015	12/31/2014	12/31/2013	12/31/2012	12/31/2011
Revenue ($ Billion)	**$32.5**	**$36.2**	**$35.9**	**$41.4**	**$45.4**
EBITA Margin	**3.0%**	**3.2%**	**3.5%**	**4.7%**	**4.6%**
EBITA / Avg. Assets	**2.1%**	**2.0%**	**2.2%**	**3.4%**	**3.3%**
Debt / Book Capitalisation	**66.8%**	**65.4%**	**67.2%**	**63.4%**	**60.9%**
Debt / EBITDA	**5.6x**	**6.1x**	**5.5x**	**4.7x**	**4.7x**
FCF / Debt	**-0.8%**	**0.5%**	**-0.9%**	**-3.2%**	**-0.5%**
RCF / Net Debt	**17.7%**	**19.9%**	**21.4%**	**17.7%**	**18.7%**
(FFO + Interest) / Interest	**7.9x**	**8.0x**	**11.3x**	**7.6x**	**7.9x**

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Weak margins remain the main credit concern

- Stable leverage supports the BCA

- SNCF Mobilités' exposure to domestic railway competition is limited, and market opening will be slow

- Probability of support is very high, and default dependence is very high

Corporate Profile

SNCF Mobilités (formerly SNCF) is the national railway operator in France and one of the world leaders in transport services and logistics, with operating activities in 120 countries and a workforce of 200,000 people. SNCF Mobilités is a French public entity with autonomous management, established under the special status of an `Etablissement Public à Caractère Industriel et Commercial' (EPIC). SNCF Mobilités is fully owned by the holding company SNCF, which is also the parent company of the French railway network SNCF Reseau (Aa2 stable), and which in turn is fully controlled by the French state (Aa2 stable). At the end of December 2015, SNCF Mobilités reported consolidated revenues of EUR29.4 billion (EUR27.2 billion in 2014) and an EBITDA of EUR2.6 billion (EUR2.4 billion in 2014).

Rating Rationale

In accordance with our government-related issuer rating methodology, SNCF Mobilités' Aa3 issuer rating reflects the combination of the following inputs:

1) A baseline credit assessment (BCA), which is a measure of the group's standalone financial strength without the assumed benefit of government support, of baa1;

2) The Aa2 local-currency rating of the French government;

3) Very high probability of support; and;

4) Very high default dependence.

SNCF Mobilités' BCA is constrained by the company's weak profitability. SNCF Mobilités' EBITA margin (as adjusted by Moody's) further slightly deteriorated in financial year (FY) 2015 to 3.0%, from 3.2% in 2014, owing mainly to the poor operating performance of some TGV (high-speed trains) lines and the Intercity services. We expect that profitability will remain stable in the next 24 months at 3.0-3.2%, a level that is weak for the current BCA, representing a major rating constraint. More positively, the BCA is supported by our expectation that leverage will remain at around 5.5x in the next 24 months (5.6x in FY 2015), a level that we deem compatible with a BCA in the baa category.

SNCF Mobilités' baa1 BCA reflects its solid business profile, underpinned by (1) its large scale, with a degree of international diversification, with approximately 30% of revenues generated outside France; (2) its role as a quasi-monopolist in the domestic passenger railway segment; and (3) its large share of revenue derived from French government-related authorities (approximately 27%, including under public service remit mass transit activities for French regional and local authorities), which provides some stability and visibility of top-line.

DETAILED RATING CONSIDERATIONS

WEAK MARGINS REMAIN THE MAIN CREDIT CONCERN

We expect that SNCF Mobilités' profitability will remain under pressure in the next 24 months, with its EBITA margin (as adjusted by Moody) remaining between 3.0%-3.2. SNCF Mobilités is implementing a number of cost-saving and efficiency measures that should bring some benefits. Also the renegotiation of the service contract with the State for some long-distance trains, the Trains d'Équilibre du Territoire service agreement, could potentially improve the group's profitability from 2017 onwards.

On the other hand, the company's services will remain exposed to increasing competition from alternative transportation means, such as long-distance buses, car sharing or low-cost flights, which could exert pressure on prices and/or erode volumes. The large impairment of EUR11.8 billion posted by the SNCF group (of which EUR9.6 billion for the infrastructure manager SNCF Reseau and EUR2.2 billion for SNCF Mobilités) related to the TGV assets confirms the muted economic prospects for this business. As such, it will be difficult for SNCF Mobilités' profitability to recover to pre-crisis levels, i.e., with an EBITA margin close to 5% in 2012.

However, the long term sustainability of the current French railway system structure remains in our view uncertain, in light of the high and increasing debt of SNCF Reseau which in the long-run could add pressure to SNCF Mobilités, via a change in the current track access fee system or dividend requirements from SNCF holding. This would add further pressure on SNCF Mobilités' profitability.

STABLE LEVERAGE SUPPORTS THE BCA

In FY 2015, the company's leverage (measured as Moody's-adjusted debt/EBITDA) improved to 5.6x, from 6.1x in 2014. We expect that it will remain substantially stable at around 5.5x in the next 24 months. We forecast that the company's stable operating cash flow of some EUR1.8 billion per annum in the next two years will cover for the expected net capex of a similar amount.

Despite margin pressure, SNCF Mobilités' operating performance remained relatively stable in the last two years. Reported EBITDA at EUR2.6 billion in FY 2015 (excluding the impact of the non-recurring items such as an antitrust fine in the freight business), was an improvement from the EUR2.4 billion of FY 2014. However, the FY 2014 results were impacted by a 15-day strike that caused the loss of some EUR172 million of EBITDA. Reported net debt marginally deteriorated to EUR7.7 billion from EUR7.4 billion in FY 2014.

SNCF MOBILITES' EXPOSURE TO DOMESTIC RAILWAY COMPETITION IS LIMITED, AND MARKET OPENING WILL BE SLOW

We expect that SNCF Mobilités' dominant market positioning in France will not be challenged in the near future. SNCF Mobilités is the main rail company in its domestic market and operates in a particularly favourable operating environment, mainly because the group has a de-facto monopoly in both domestic long-distance and regional transportation passenger rail services, in one of the most developed passenger rail markets in the world.

In our view, the French railway market will be very slow to open, and will be driven by changes in the European regulation. In this respect, the European Parliament and Council drastically changed the original proposal of the European Commission for new legislation aimed at opening domestic rail passenger services to competition. Although the new legislation remains under discussion, the liberalisation of national railway markets will likely take significantly longer than previously expected, with tender bids for public service contracts to become mandatory only in the long term and with several exceptions allowed.

PROBABILITY OF SUPPORT IS VERY HIGH, AND DEFAULT DEPENDENCE IS VERY HIGH

Our assessment of a very high probability of extraordinary financial support from the French government reflects (1) SNCF Mobilités' strategic role as the current dominant provider of public railway services in France, which are central to the core missions of the state; (2) SNCF Mobilités' legal status as an EPIC and its 100% ownership by the French State; and (3) the strong financial support provided by the government in the past when needed, as evidenced by the 2009 transfer of unfunded pension commitments to a third independent entity, which relieved the group of a significant financial burden.

SNCF Mobilités' very high default dependence on the French government reflects (1) that the large share of SNCF Mobilités' business derived from France; (2) the high level of group revenues that is derived from French government-related entities, at approximately 27%, including under public service remit mass transit activities for French regional and local authorities; and (3) the importance of the group's rail passenger and freight transportation network to the French economy.

Liquidity Profile

We consider SNCF Mobilités' liquidity profile to be good. As of the end of December 2015, SNCF Mobilités had available cash of approximately EUR4 billion, and we expect that it will generate operational cash flow of around EUR1.8 billion within the next 12 months. In addition to its self-generated liquidity, SNCF Mobilité has access to committed credit lines amounting to EUR780 million at the parent company level at the end of December 2015 and for 2016.

SNCF Mobilités' main cash requirements for the next 12 months will be (1) the group's intensive gross investment programme, which we expect will amount to approximately EUR2.1 billion; and (2) approximately EUR2 billion in debt maturities. Our debt calculation excludes approximately EUR3.0 billion that are backed by financial credits towards SNCF, SNCF Reseau and the French State and includes EUR2.3 billion of Moody's standard adjustments for operating leases and pension liabilities.

Rating Outlook

The outlook on SNCF Mobilités' rating is stable, reflecting the stable outlook on the sovereign rating.

What Could Change the Rating - Up

We would consider upgrading SNCF' Mobilités' rating only if there were an increase in the rating of the sovereign rating. We could raise SNCF Mobilités' BCA if the group's EBITA margin were to increase to above 5%, provided that its debt/EBITDA ratio remains at least stable, at around 5.5x, and its retained cash flow/net debt ratio remains in the mid to high teens in percentage terms.

What Could Change the Rating - Down

Government support of SNCF Mobilités is currently at a very high level, and we expect that this will remain the case as long as the group's current ownership and legal structure do not change. However, any reduction in the expected level of available support would most likely have a negative impact on the rating. In addition, a downgrade of the sovereign rating would also drive a downgrade of SNCF Mobilités' rating, with the one-notch differential likely to be maintained.

The BCA could come under pressure if, inter alia, (1) SNCF Mobilités' EBITA margin decreases below 2.5%; (2) its debt/EBITDA ratio rises above 7.0x; and (3) its retained cash flow/net debt ratio falls below 10%. Any significant deterioration in SNCF Mobilités' BCA and/or liquidity could potentially affect the group's final rating.

Other Considerations

SNCF Mobilités' BCA of baa1 is one notch above the indication received from the application of our "Global Passenger Railways" rating methodology grid, owing mainly to the weak profitability. This is partially offset by the company's solid business profile and market positioning.

Rating Factors

SNCF Mobilités

Passenger Railway Industry Grid [1][2]	**Current FY 12/31/2015**		[3]**Moody's 12-18 Month Forward ViewAs of 3/24/2016**	
Factor 1 : SIZE (15%)	**Measure**	**Score**	**Measure**	**Score**
a) Revenue ($ Billion)	$32.5	Aa	$33.5 - $34.5	Aa
b) Number of Passenger Transported (PKM billion)	Aa	Aa	Aa	Aa
Factor 2 : MARKET POSITION (40%)				
a) Stability of Operating Environment	Baa	Baa	Baa	Baa
b) Market Characteristics	Aaa	Aaa	Aaa	Aaa
c) Competitive Environment	Aaa	Aaa	Aaa	Aaa
Factor 3 : COST POSITION AND PROFITABILITY (15%)				
a) EBITA Margin	3.0%	B	3% - 3.3%	B
b) EBITA / Avg. Assets	2.1%	B	2.4% - 2.7%	B
Factor 4 : CAPITAL STRUCTURE (15%)				
a) Debt / Book Capitalisation	66.8%	A	65% - 67%	A
b) Debt / EBITDA	5.6x	Ba	5x - 5.4x	Ba
Factor 5 : CASH FLOW AND INTEREST COVERAGE (15%)				
a) FCF / Debt	-0.8%	Ba	-3% - -2%	Ba
b) RCF / Net Debt	17.7%	Baa	18% - 20%	Baa
c) (FFO + Interest) / Interest	7.9x	Aa	9x - 9.4x	Aa
Rating:				
a) Indicated Rating from Grid		A3		A3
b) Actual Rating Assigned				Aa3

Government-Related Issuer	**Factor**
a) Baseline Credit Assessment	baa1
b) Government Local Currency Rating	Aa2/Stable
c) Default Dependence	Very High

d) Support	Very High
e) Final Rating Outcome	Aa3/Stable

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 12/31/2015; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

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