FitchRatings

02 Jul 2019 | Affirmation

Fitch Upgrades SNCF Mobilites' Short-Term IDR to 'F1+'

Fitch Ratings-Paris-02 July 2019:

Fitch Ratings has upgraded SNCF Mobilites' Short-Term Issuer Default Ratings (IDR), and the short-term ratings on the company's EUR12 billion EMTN, EUR3,048 million NeuMTN and EUR2 billion NeuCP programmes to 'F1+' from 'F1'. The ratings have been removed them from Under Criteria Observation. All long-term ratings have been affirmed.

The upgrade follows the publication of our 'Short-Term Ratings Criteria' on 2 May 2019 and reflects the application of the higher short-term rating of two options mapping to a Long-Term IDR of 'A+' using a top-down approach.

Fitch classifies SNCF Mobilites as a government-related entity (GRE) of the French state (AA/Stable/F1+) under its GRE Rating Criteria, and rates it two notches below the sovereign. In Fitch's view, SNCF Mobilites remains strongly linked to the French state, but its large share of activities exposed to competition could limit the state's incentive to provide timely support in case of need.

On 7 June 2019 the railway group unveiled its new organisation structure, and notably its future financing mechanism. SNCF Mobilites' debt will move to SNCF Holding and all new borrowings (including for SNCF Reseau (AA/Stable/F1+)) will be incurred by SNCF Holding from 1 July 2020. Fitch assesses that SNCF Holding's GRE score and ratings will be the same as SNCF Mobilites'.

Key Rating Drivers

The assessment of the following four rating factors under Fitch's GRE Rating Criteria translates into an overall support score of 30, out of a maximum possible score of 60, and the application of a 'top-down minus two' approach:

Status, Ownership and Control (Very Strong)

The railway reform triggered by the law dated 28 June 2018 creates a unified railway group. On 1 January 2020 SNCF Mobilites, SNCF Reseau and SNCF Holding will lose their EPIC status and be transformed into limited liability companies. SNCF Reseau and Mobilites will be 100% owned by SNCF Holding, which in turn will be 100% owned by the French state. The law states that the capital of the three companies is non-transferable.

On 1 January 2020, SNCF Mobilites will merge with SNCF Holding, relocating its debt to the holding level, and all operational activities will be relocated into subsidiaries (passengers, freight etc.). All new borrowings will be incurred by SNCF Holding.

The state, as the sole shareholder, will remain closely involved in the management of the subsidiaries' activities, notably through the State Participation Agency.

Support Track Record and Expectations (Strong)

Fitch expects SNCF Mobilites to continue benefiting from ongoing support from the state and the public sector in general, although the extent of extraordinary support for competitive activities may be challenged by European regulation regarding state aid.

As France's main passenger and freight rail transport operator, SNCF Mobilites receives tangible ongoing support from the public sector. Public service orders contracted with the state, French regions and SNCF Reseau, amounted to EUR5.5 billion in 2018 (17% of SNCF Mobilites' consolidated turnover). SNCF Mobilites is also compensated by French regions to operate loss-making lines. Furthermore, it receives operating grants and investment support in the form of third-party financing from regional transport authorities, mostly for rolling stock (EUR1.8 billion of public transfers received in 2018 for this purpose).

SNCF Mobilites also benefits from financial receivables from the state, SNCF Holding and SNCF Reseau (totaling EUR2.4 billion at end-2018), which it uses to repay part of its financial debt.

Socio-Political Implications of Default (Moderate)

As a railway operator with moderate and stable debt, Fitch does not believe a default on financial obligations would have a large and immediate impact on SNCF Mobilites' operations, such as activity standstill, as its day-to-day activity is not dependent on access to debt capital markets.

Fitch believes the opening up of the domestic rail passenger market to competition from 2020 for regional trains and from 2021 for long-distance trains will reduce, in the medium term, the state' incentive to prevent a default as substituting the incumbent will be easier, or at least legally feasible.

Fitch, however, notes that competition will only materialise gradually as some multi-year contracts with regions for regional trains run until 2025 and also because barriers to entry on long-distance trains may remain high, as shown by the example of Deutsche Bahn, which remains to this day the sole provider on domestic long-distance routes.

Financial Implications of Default (Strong)

SNCF Mobilites is a large issuer on capital markets through its EUR12 billion EMTN programme, its EUR2 billion ECP programme and its EUR3 billion NeuCP programme. A default on financial obligations would therefore have a direct impact on its cost of financing as market debt constitutes most of SNCF Mobilites' debt.

Fitch believes that a default by SNCF Mobilites on its financial obligations could have contagion effect on the cost of financing for other public companies, first among them being SNCF Reseau, which shares the same shareholder and economic sector and belonging to the same public group SNCF, even though the two companies have currently completely distinct and separate debt programmes. Fitch believes the state will remain committed to fully supporting SNCF Reseau, which will retain its monopoly over the French railway infrastructure network. Therefore Fitch believes that this contagion risk reinforces the incentive for the state to prevent SNCF Mobilites from defaulting on its financial obligations.

Standalone credit profile assessed at 'bbb'

SNCF Mobilites' current debt will be transferred to SNCF Holding as of 1 January 2020. From 2H20, SNCF Holding will centralise all new borrowings of the railway group, including those of SNCF Reseau. EU regulation prevents the infrastructure manager to cross-finance activities exposed to competition (currently housed in SNCF Mobilites). Fitch therefore believes that during financial stress, SNCF Holding will rely on two non-fungible streams of cash flows (one from the infrastructure manager and one from competitive activities). If either of these streams dries up, notably from competitive activities, SNCF Holding could be facing difficulties to repay its debt. Hence, Fitch has assessed SNCF Holding's SCP at the lower of SNCF Reseau - (recently assessed at bbb+) and that of entities that will comprise competitive activities (SNCF Holding's consolidated perimeter excluding SNCF Reseau).

SNCF Mobilites' 'bbb' SCP reflects:

-'Midrange' revenue defensibility driven by strong and sustained demand for railway services both for passengers and freight. SNCF Mobilites also benefits from a strong presence overseas (30% of its turnover in 2018), which can offset the mature state of its home market. The 'Midrange' attribute also reflects the gradual liberalisation of the market starting in 2020 and current intermodal competition, which constrain SNCF Mobilites' pricing ability.

-'Midrange' operating risks as SNCF Mobilites does not depend on any rare or volatile resource. The main cost item for SNCF Mobilites are staff costs (38% of operating expenses in 2018), which are broadly contained.

-SNCF Mobilites' net adjusted leverage is expected to slightly increase to 5x in Fitch's rating case from 4x at end-2018. This is driven by prudent macroeconomic assumptions driving transportation revenue and a slight decline in EBITDAR margin to below 10% in the medium term from 11% at end-2018.

RATING SENSITIVITIES

A change in France's sovereign ratings would be mirrored in SNCF Mobilites' ratings. An improvement of the leverage to below 4x could lead to an upgrade of the ratings.

A downgrade could result from a weakening of the state's support through significantly weaker assessment of strength of linkage or incentive to support factors, which we see as unlikely in the medium term.

SNCF Mobilites; Long Term Issuer Default Rating; Affirmed; A+; RO:Sta
----; Short Term Issuer Default Rating; Upgrade; F1+
----senior unsecured; Long Term Rating; Affirmed; A+
----senior unsecured; Short Term Rating; Upgrade; F1+

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Additional information is available on www.fitchratings.com

Applicable Criteria

Government-Related Entities Rating Criteria (pub. 25 Oct 2018)
Public Sector, Revenue-Supported Entities Rating Criteria (pub. 28 May 2019)
Short-Term Ratings Criteria (pub. 02 May 2019)

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