

08 OCT 2021

Fitch Affirms Ile-de-France at 'AA'; Outlook Negative

Fitch Ratings - Paris - 08 Oct 2021: Fitch Ratings has affirmed the Region of Ile-de-France's Long-Term Foreign-and-Local-Currency Issuer Default Ratings (IDRs) at 'AA' with Negative Outlook. A full list of rating actions is below.

We have revised Ile-de-France's Standalone Credit Profile (SCP) to 'aa+' from 'aa', following an improvement of the region's debt-sustainability ratios in our rating case, especially a forecast debt payback ratio of around 5x in 2024-2025 (close to 6x previously). Ile-de-France's IDR, however, remains the same as it is now capped by the French state's (AA/Negative). The Negative Outlook also reflects that of the sovereign.

KEY RATING DRIVERS

Risk Profile: 'High Midrange'

Ile-de-France's 'High Midrange' risk profile reflects a mix of 'Stronger' and 'Midrange' attributes on six key risk factors. The assessment reflects Fitch's view of a low risk compared with international peers' that the region's ability to cover debt service by the operating balance may weaken unexpectedly over the forecast horizon (2021-2025), either because of lower-than-expected revenue or expenditure overshooting expectations, or because of an unanticipated rise in liabilities or debt-service requirements.

Revenue Robustness: 'Stronger'

Ile-de-France's operating revenue is mostly made up of predictable and growing tax items. VAT proceeds, collected at the national level, so far in 2021 represent more than 40% of the region's operating revenue (Fitch-adjusted). We expect VAT proceeds to grow in the coming years at a rate close to that of national GDP.

We expect state transfers and the fuel tax, whose proceeds are mostly guaranteed by the French state, to represent more than 30% of the region's operating revenue in 2021-2025. Counterparty risk is low due to the high sovereign rating. Vehicle registration fees (10% of operating revenue in 2020) are a less robust revenue source as they are solely linked to vehicle purchases.

As with other French regions, Ile-de-France benefits from the replacement of its corporate value-added tax (CVAE) proceeds by a new share of VAT as of 2021. It insulates the region from an expected drop in CVAE proceeds in 2021-2022 (as CVAE proceeds are based on value-added in the previous one or two years), and reduces significantly the impact of the Covid-19 pandemic on the region's revenue. In 2020,

the region's operating revenue declined 3% (excluding one-off effects), mainly driven by a 6% decrease in VAT proceeds.

Revenue Adjustability: 'Midrange'

As with other French metropolitan regions, Ile-de-France's rate-setting power is limited to vehicle-registration fees. The region's current rate is EUR46.15, close to the French median of metropolitan regions (the rate varies from EUR33 in the former region of Picardie to EUR51.2 in Provence-Alpes-Cote-d'Azur (AA-/Stable)). French law does not provide any ceiling on this tax rate, but assuming a normal increase to EUR60, Ile-de-France could have increased its operating revenue by a moderate 3% in 2020, fully covering what we would reasonably expect of a revenue decline (estimated at close to 3%) during an economic downturn.

Expenditure Sustainability: 'Stronger'

Ile-de-France has tight control of expenditure, as reflected by a continuous decline in operating expenditure in the last five years. Operating spending decreased on average 2.3% a year in 2015-2019, while operating revenue growth was on average 2.6% a year during this period. In 2020, operating spending declined 0.6% (including the transfer of apprenticeship responsibility).

The region's expenditure is mainly non-cyclical but unlikely to grow in an economic downturn. During the pandemic, the region participated in national measures to support businesses, given its responsibilities for economic development, which translated into a high EUR2.1 billion capex in 2020, above its 2016-2019 average of EUR1.6 billion.

Expenditure Adjustability: 'Midrange'

Ile-de-France's operating expenditure is mainly made up of mandatory transfers related to transport (32% of operating spending in 2020), vocational training (24%) and secondary education (12%). Staff costs (18%) are also a rigid spending item as most of the region's employees have the status of civil servants. However, cost-cutting measures may still be implemented, as indicated by cuts to the region's operating spending in recent years.

The region has large capex, expected at close to 45% of total expenditure in 2021-2025, which could be postponed or scaled down, if needed. However, this flexibility is offset by the economic impact of the pandemic, which will increase the need for support measures, and by the region's high capex needs, especially in transportation and high-school infrastructure. Overall, we estimate the share of inflexible expenditure at 70%-80%.

Liabilities & Liquidity Robustness: 'Stronger'

Ile-de-France's liabilities carry little risk. At end-2020, debt was 95% fixed-rate and 100% was considered risk-free under national regulation (Gissler Charter). Debt service is structurally well-covered by the region's operating balance (2020: 2x). The share of short-term debt is moderate (12%), solely represented by a commercial-paper issue. Its debt amortisation schedule has some bullet repayments in 2025-2027 (around EUR750 million in 2025 and around EUR700 million in 2026-2027).

However, the risk of bullet repayments is mitigated, in Fitch's view, by the modest amount of these maturities in absolute terms and as a proportion of the region's operating balance.

Off-balance-sheet liabilities are mostly related to Ile-de-France Mobilites, a public-sector entity in charge of public transport in the region. The region has 51% of the seats on its board of directors. However, this entity is financially autonomous and the region is not legally liable for this entity's debt. It has also been supported by the French state since the beginning of the pandemic, without any impact on the region's finances.

Liabilities & Liquidity Flexibility: 'Stronger'

Fitch views the framework for emergency-liquidity support from the French state as strong. This is evident in cash pooling between French local and regional governments (LRGs) and the French state, with liquidity from LRGs deposited at the national Treasury. French LRGs may benefit from the transfers of tax proceeds in advance from the French state in a liquidity shortfall. Counterparty risk is low due to the high sovereign rating.

Ile-de-France has strong access to liquidity in various forms. It has access to institutional lenders such as Caisse des Depots et Consignations (AA/Negative), as with all other French LRGs. It also benefits from a EUR587 million revolving line with an 'A+' rated bank.

Debt Sustainability: 'aa category'

Ile-de-France's debt sustainability is assessed in the upper-end of the 'aa' category. Our rating case expects a debt payback ratio (net adjusted debt/operating balance) at close to 5x in 2024-2025; a coverage ratio (Fitch's synthetic calculation) at 2.5x-3x, and a fiscal debt burden at close to 160%.

Ile-de-France's debt payback remained sound at 4.6x in 2020 (2019: 3.8x), despite the impact of the pandemic. Its operating balance declined to EUR1.1 billion in 2020, from EUR1.38 billion in 2019. Under our rating case, we expect the region's operating balance to vary between EUR1 billion and EUR1.25 billion in the coming years, depending on the national economic recovery, which will drive the region's VAT proceeds.

Ile-de-France's net adjusted debt declined slightly to EUR5.1 billion at end-2020, from EUR5.2 billion at end-2019, despite high capex (EUR2.1 billion). This is due to the resilience of the region's operating balance in 2020 and proceeds from a one-off EUR190 million asset sale (former headquarters in the center of Paris). We expect net adjusted debt to rise to EUR6.2 billion at end-2025 as the region implements a large capex programme of close to EUR2 billion a year on average in 2021-2025.

Derivation Summary

Ile-de-France's final IDRs are derived from the region's SCP and capped by the sovereign's IDRs. No other rating factors affect the IDRs. The Negative Outlook mirrors that of the sovereign.

Key Assumptions

Qualitative assumptions:

Risk Profile: 'High Midrange, Unchanged'

Revenue Robustness: 'Stronger, Unchanged'

Revenue Adjustability: 'Midrange, Unchanged'

Expenditure Sustainability: 'Stronger, Unchanged'

Expenditure Adjustability: 'Midrange, Unchanged'

Liabilities and Liquidity Robustness: 'Stronger, Unchanged'

Liabilities and Liquidity Flexibility: 'Stronger, Unchanged'

Debt sustainability: 'aa, Improved'

Support (Budget Loans): 'N/A, Unchanged'

Support (Ad Hoc): 'N/A, Unchanged'

Asymmetric Risk: 'N/A, Unchanged'

Sovereign Cap: 'AA, Unchanged'

Sovereign Floor: 'N/A, Unchanged'

Quantitative assumptions - Issuer Specific

Fitch's rating case is a "through-the-cycle" scenario, which incorporates a combination of revenue, cost and financial risk stresses. It is based on 2016-2020 figures and 2021-2025 projected ratios. The key assumptions for the scenario include:

- Operating revenue growth on average at 2% a year;
- Operating expenditure growth on average at 1.6% a year;
- Negative net capital balance on average at EUR1.35 billion a year; and
- Cost of debt on average at 1.3%.

Summary of Financial Adjustments

Fitch treats the transfers by the region to offset the amount of CVAE proceeds it receives as pass-through revenue. These transfers include a transfer made to the state for the other regions ("fonds national de garantie individuelle des ressources"; EUR675 million in 2020), equalisation funds (EUR160 million); and transfers to Ile-de-France departments to compensate for the doubling of CVAE regional share proceeds as of 2017 (EUR1,372 million).

Issuer Profile

Ile-de France is France's main political and economic centre and one of the EU's wealthiest regions. With a population of 12.2 million, it represents 18% of the national population and more than 30% of national GDP.

Rating Sensitivities

Factors that could, individually or collectively, lead to negative rating action/downgrade:

Deterioration of the debt payback ratio to 7.5x on a sustained basis in our rating case could lead to a downgrade, which Fitch views as unlikely. A downgrade of the sovereign would also be reflected in the region's ratings.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

The Outlook would be revised back to Stable if the Outlook on the sovereign is revised to Stable, all else being equal.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

References for Substantially Material Source Cited as Key Driver Rating

The principal sources of information used in the analysis are described in the Applicable Criteria.

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Ile-de-France, Region of	LT IDR	AA	Affirmed	AA
	ST IDR	F1+	Affirmed	F1+
	LC LT IDR	AA	Affirmed	AA
	LC ST IDR	F1+	New Rating	
• senior unsecured	LT	AA	Affirmed	AA
• senior	ST	F1+	Affirmed	F1+

ENTITY/DEBT	RATING	RECOVERY	PRIOR
	unsecured		

RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◊
NEGATIVE	⊖	◊
EVOLVING	◊	◆
STABLE	⊙	

Applicable Criteria

[International Local and Regional Governments Rating Criteria \(pub.03 Sep 2021\) \(including rating assumption sensitivity\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

Ile-de-France, Region of EU Issued, UK Endorsed

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