



RATING ACTION COMMENTARY

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

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Fitch Ratings - Paris - 10 Jun 2022: 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.

The affirmation reflects Fitch's expectations that Ile-de-France's payback ratio will remain between 5x and 6x under our rating case.

KEY RATING DRIVERS

Risk Profile: 'High Midrange'

Ile-de-France's 'High Midrange' risk profile reflects a mix of 'Stronger' and 'Midrange' attributes on its 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 with its operating balance will weaken unexpectedly over the forecast horizon (2022-2026), either because of lower-than-expected revenue or higher-than-expected expenditure, or because of an unanticipated rise in liabilities or debt-service requirements.

Revenue Robustness: 'Stronger'

Ile-de-France benefits from highly stable revenue sources and solid long-term revenue growth prospects. Operating revenue is mostly made up of growing and predictable tax items and stable transfers from the central government with low counterparty risk. The

latter include transfers from the state and fuel tax proceeds, mostly guaranteed by the state 37% of operating revenue in 2021).

Around half of operating revenue is linked to the economic cycle. VAT proceeds, collected at the national level, represented 42% of the region's operating revenue in 2021. We view the risk of declining VAT proceeds on a sustained basis as very low, and expect this tax item to grow in the coming years at a rate close to that of national GDP.

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.

French law does not provide any ceiling on vehicle registration fees. Assuming a normal increase to EUR60, Ile-de-France could have increased its total revenue by a modest 2% in 2021, which would fully cover what we would expect of a reasonable revenue decline (estimated at close to 2%) during an economic downturn.

Expenditure Sustainability: 'Stronger'

Ile-de-France has tight control over its expenditure. In 2016-2021, operating expenditure (opex) declined on average 0.8% a year (including the transfer of the apprenticeship responsibility) while operating revenue increased on average 0.5%. In 2021, we estimate opex would have increased by less than 1% excluding exceptional items. We expect high inflation to lead to an increase in spending in 2022, but this will likely be offset by an increase in VAT proceeds.

Ile-de-France's expenditure is mainly non-cyclical and unlikely to grow in an economic downturn (planned investments, transportation and secondary education), which drives our 'Stronger' assessment of this rating factor.

Expenditure Adjustability: 'Midrange'

Ile-de-France's operating expenditure is mainly made up of mandatory transfers related to transport (32% of operating spending in 2021), 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 opex in recent years.

The region retains flexibility to scale back capex in case of need given its high level of capex (46% of total spending in 2021, and above 40% expected in 2022-2026), mostly dedicated to transportation and high-schools. The latter could be postponed or scaled back if needed but is offset by the region's high capex needs. 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-2021, debt was 97% fixed-rate and 100% was deemed risk-free by national regulation (Gissler Charter). Debt service is structurally well-covered by the region's operating balance (2021: 3.7x). Short-term debt accounted for 17% of direct debt at end-2021, but corresponded to a commercial paper issue at negative interest rates.

The region's 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% seats on the company's board of directors. However, this entity is financially autonomous and the region is not legally liable for its debt. It was also supported directly 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 transfer of tax proceeds in advance from the French state, in case of 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 benefits also from a EUR587 million revolving line with an 'A+' rated bank, which will mature at end-2022.

Debt Sustainability: 'aa category'

Ile-de-France's debt sustainability is assessed at the upper end of the 'aa' category. Our rating case expects the payback ratio (net adjusted debt/operating balance) to be close to 5.5x-6x in 2025-2026; the coverage ratio (Fitch's synthetic calculation) at 2x-2.5x; and the fiscal debt burden at close to 180%.

Ile-de-France's payback ratio deteriorated to 5.3x in 2021 (2020: 4.6x) but remained sound. Its operating balance was stable at close to EUR1,060 million. Under our rating case, we expect the region's operating balance to vary between EUR1.1 billion and EUR1.2 billion in the coming four years. This will in particular depend on the national economic recovery, which will drive the region's VAT proceeds, and the impact of inflation on opex, such as staff costs, or mandatory transfers.

Ile-de-France's net adjusted debt increased to EUR5.6 billion in 2021, from EUR5 billion at end-2020, driven by high capex (EUR2.2billion). We expect net adjusted debt to rise to EUR7.2 billion at end-2026 as the region implements a large capex programme on average of more than EUR2 billion a year in 2022-2026.

DERIVATION SUMMARY

Ile-de-France's Standalone Credit Profile (SCP) is 'aa+', and reflects the combination of a 'High Midrange' risk profile and debt sustainability at the upper end of the 'aa' category, especially its payback ratio of 5x- 6x. The IDR is capped by that of France (AA/Negative) and the Negative Outlook reflects that of the sovereign.

KEY ASSUMPTIONS

Qualitative assumptions:

Risk Profile: 'High Midrange'

Revenue Robustness: 'Stronger'

Revenue Adjustability: 'Midrange'

Expenditure Sustainability: 'Stronger'

Expenditure Adjustability: 'Midrange'

Liabilities and Liquidity Robustness: 'Stronger'

Liabilities and Liquidity Flexibility: 'Stronger'**Debt sustainability: 'aa'****Support (Budget Loans): 'N/A'****Support (Ad Hoc): 'N/A'****Asymmetric Risk: 'N/A'****Sovereign Cap:****Sovereign Floor:****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 2017-2021 figures. The key assumptions for the scenario include for 2022-2026:

- Operating revenue growth on average at 2% a year
- Opex growth on average at 1.8% a year
- Negative net capital balance on average at EUR1.3 billion a year
- Average 1.8% cost of debt

Liquidity and Debt Structure

Fitch-adjusted debt includes the region's short-term debt (EUR1.2 billion at end-2021) and long-term debt (EUR6.1 billion). Net Fitch-adjusted debt corresponds to the difference between Fitch-adjusted debt and the cash at the end of the year deemed unrestricted by Fitch (EUR1.7 billion).

Summary of Financial Adjustments

Fitch considers the transfers by the region to offset the amount of VAT proceeds it receives as pass-through revenue (EUR2,237 million in total in 2021). These transfers include a transfer made to the state for the other regions ("fonds national de garantie individuelle des ressources"; the equalisation funds, and the transfer to the Ile-de-France departments

to compensate for the doubling of corporate-value-added tax regional share proceeds as of 2017.

Fitch believes these restatements allow a meaningful comparison with other LRGs. They are neutral to Ile-de-France's operating balance, and hence also for the payback and coverage assessment. However, they reduce the level of operating revenue and are negative on the fiscal debt burden assessment (net adjusted debt/operating revenue).

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 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 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

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PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

Ile-de-France' ratings are capped by France's IDRs (AA/Negative).

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.

RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡			PRIOR ⚡
Ile-de-France, Region of	LT IDR	AA Rating Outlook Negative		AA Rating Outlook Negative
	Affirmed			
	ST IDR	F1+	Affirmed	F1+
	LC LT IDR	AA Rating Outlook Negative		AA Rating Outlook Negative
	Affirmed			
	LC ST IDR	F1+	Affirmed	F1+
senior unsecured	LT	AA	Affirmed	AA

senior unsecured

ST

F1+

Affirmed

F1+

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APPLICABLE CRITERIA

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

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Ile-de-France, Region of

EU Issued, UK Endorsed

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