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Research Update:

French Postal Operator La Poste Outlook Revised To Positive; 'A/A-1' Ratings Affirmed

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Overview

- The French government recently announced a major project to combine insurance company CNP Assurances with La Poste's banking subsidiary La Banque Postale by 2020, with Caisse des Dépôts et Consignations (AA/Stable/A-1+) becoming La Poste's majority shareholder. The French government would become La Poste's sole minority shareholder.
- If the transaction materializes as announced, La Poste's stand-alone credit profile could improve, reflecting LBP's improving credit metrics and more diversified revenues. La Poste would also retain its very high likelihood of extraordinary support from the French government in times of need.
- We are therefore revising our outlook on La Poste to positive from stable.
- We are also affirming our 'A/A-1' long- and short-term ratings on La Poste.

Rating Action

On Oct. 30, 2018, S&P Global Ratings revised its outlook on La Poste to positive from stable. We also affirmed the 'A' long-term and 'A-1' short-term issuer credit ratings on La Poste.

Rationale

The outlook revision reflects our view that La Poste could benefit structurally from La Banque Postale's (LBP) partial takeover of French insurance company CNP Assurances by 2020. This would likely strengthen La Poste's stand-alone credit profile (SACP), which we currently assess at 'bbb-', boosting the importance of its bank and insurance services within the group. These have historically displayed stronger credit metrics than La Poste's traditional commercial and industrial activities. LBP would also display stronger credit metrics and more diversified revenues stemming from its majority shareholding in CNP Assurances.

The French government, alongside Caisse des Dépôts et Consignations (CDC) and La Poste, recently presented a major project to create a large French financial public hub by 2020. This includes LBP's partial, majority takeover of CNP Assurances, with CDC becoming La Poste's majority shareholder. In this transaction, CDC would transfer its current 41% stake in CNP Assurances to La

Poste (under a capital increase), and La Poste would in turn transfer this stake to its banking subsidiary, LBP. LBP would become the majority shareholder of CNP Assurances, with a stake of more than 61% under the project's current terms. In return for its CNP Assurances shares, CDC would become La Poste's majority shareholder (from its current 26.32% stake), with the French government becoming the sole minority shareholder (from its current 73.68% stake).

If the project is implemented as announced, we understand La Poste could retain its very high likelihood of timely and sufficient extraordinary support from France (unsolicited ratings; AA/Stable/A-1+) in the event of financial distress. We understand La Poste would remain fully publicly owned by the French government and by CDC, with strong monitoring and controls from the French government. La Poste's activities and public operations would likely remain strategically important to the government.

However, we are still uncertain about the project's calendar, technicalities and practicalities for implied changes, and some potential regulatory obstacles--including a potential requirement of a formal share buyback of CNP Assurances' minority shareholders. These factors could cause the project to change and depart from the terms and conditions that were publicly announced.

We continue to regard La Poste as a government-related entity (GRE). In accordance with our GRE criteria, we think there is a very high likelihood that France would support La Poste if needed. This reflects La Poste's:

- Very important role for the French government, due to the economic, political, and social importance of La Poste's four public policy mandates entrenched in the 2010 postal law: i) the universal postal service provision; ii) the maintenance of an extensive network; iii) the provision of almost free, basic banking services and the distribution of state-subsidized savings accounts ("Livret A"); and iv) the distribution of press at discounted prices. The state partly compensates three of these policy mandates. La Poste is France's second-largest employer after the state, and a large portion of its workforce comprises civil servants. Acting through its core subsidiary LBP, the group has been increasingly active in the funding of French local and regional governments since 2013, at the French government's request. LBP was the largest lender to French local governments in 2017, accounting for one-fourth of all loans extended.
- Very strong link with the French state. The 2010 postal law mandates that the state retain full ownership--direct, or indirect through CDC--of La Poste. The government could modify this law by early 2019 to allow the CDC to become La Poste's majority shareholder. Such a scenario, with the French state remaining the sole minority shareholder, would not affect our opinion that there is a very high likelihood that the French government would support La Poste if needed. Overall, we expect La Poste will remain fully state-owned (directly or through the CDC) in the foreseeable future. The state monitors La Poste on a regular basis, including its financial situation, business plan, and strategy, as

reflected in the multiyear contracts between the state and La Poste (the most recent of which covers 2018-2022). Following its status change in March 2010 to a limited company (from its previous public agency status), La Poste received a €2.7 billion capital increase spread over 2011-2013 (€1.2 billion from the state and €1.5 billion from its financial arm, CDC). In our view, this capital injection highlights the government's track record of strong, ongoing support to La Poste, as it enabled the group to pursue sizable capital expenditures, mitigate downside risk related to the structural decline in the core mail business, and accelerate La Poste's deleveraging.

Our 'bbb-' assessment of La Poste's SACP reflects our view of the company's satisfactory business risk profile and significant financial risk profile. Our assessment of La Poste's business risk profile continues to reflect its very strong market position in mail and parcels in France, where its extensive distribution network creates significant barriers to entry. La Poste receives support from its subsidiary, Geopost, which has a solid position and growth prospects in the European parcels delivery market. This subsidiary provides La Poste with significant business and geographic diversification benefits.

Our business risk profile assessment also incorporates LBP's sound and sustainable contribution to profits through dividend distribution. Like its peers in the mail delivery sector, La Poste is exposed to structurally declining mail volumes. However, revenue has grown consistently, at a compound annual growth rate of 3.4% between 2013 and 2017. This suggests the group has so far been able to deal with volume decline through a balance of negotiated price increases and growing revenues from parcel delivery, in France and abroad.

That said, the low profitability of La Poste's mail activities--with limited room for improvement, given its high and predominantly fixed cost base--constrains La Poste's business risk profile assessment. La Poste is also subject to more stringent public service obligations than most of its European peers are (including regional development and press delivery missions). We expect the group's overall profitability, as measured by S&P Global Ratings-adjusted EBITDA margins, will decline marginally to about 9.5% in 2018 from 10% in 2017. This is due to cost pressure in the express and logistics business--in part caused by the shortage of truck drivers in Europe--and a further decrease in mail volumes (down 7% during the first half of 2018 compared with the first half of 2017). Margins should then stabilize at about 9.5%-10% in 2019 and beyond, provided La Poste executes its cost-improvement measures and the group continues to enjoy substantial dividends from LBP.

La Poste still enjoys significant headroom under its current financial risk profile category, given our expectation of funds from operations (FFO) to debt of 25%-27% in 2018 and 2019 under our base case, well above the 23% minimum we require for the current rating. We view La Poste's financial policy as supportive, as demonstrated by the group's moderate dividend policy, with shareholder returns sustainably maintained between €150 million and €200 million per year since 2012.

Liquidity

The short-term issuer credit rating is 'A-1'. We assess La Poste's liquidity as exceptional, and expect that sources of liquidity will exceed uses by more than 2.0x over the 24 months from end-June 2018. In our view, the group also has high standing in credit markets, given its state ownership, and as demonstrated by the successful recent hybrid issuance and the favorable rates at which it issues debt.

For the 12-month period ending June 30, 2019, we estimate the following principal liquidity sources:

- About €2.0 billion of cash and liquid investments;
- €1.0 billion as a committed undrawn syndicated facility that matures in 2023 (we do not include in our liquidity assessment €400 million bilateral line provided by LBP);
- €1.87 billion of cash FFO; and
- €297 million of proceeds from tax credit ("CICE") securitization.

For the same period, we estimate the following principal liquidity uses:

- €30 million in short-term liabilities;
- Capital spending of about €1.4 billion;
- €150 million of working capital outflows; and
- No contracted acquisitions.

We also note that La Poste pays €190 million-€200 million of dividends to shareholders each year, but we assume that La Poste could cut these payments under stress, given the high likelihood of support that we expect from the French state.

Outlook

The positive outlook reflects our view that, if the transaction materializes as announced, La Poste's SACP could improve. This would reflect LBP's improving credit metrics, more diversified revenues, larger importance within the group's activities and financials, and the continued very high likelihood of extraordinary support from the French government in times of need.

Upside scenario

The abovementioned scenario would lead us to take a positive rating action within the next two years.

Downside scenario

We could revise the outlook to stable in the next two years if the integration of CNP Assurances within LBP were to fail, if the project were to be formalized under adverse terms and conditions for La Poste, or if La Poste's role for or link with the French government weakened. We could also revise the outlook to stable if La Poste's operating and financial performance proved substantially weaker than we currently envisage. This could occur, for example, if mail volumes declined more sharply than expected, or if a surge of competition in the express business dampened profitability in this segment.

Ratings Score Snapshot

Issuer Credit Rating: A/Positive/A-1

Business risk: Satisfactory

- Country risk: Low
- Industry risk: Low
- Competitive position: Satisfactory

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bbb-

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Exceptional (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb-

- Sovereign rating: AA/Stable/A-1+
- Likelihood of government support: Very high (+4 notches)

Related Criteria

- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology And Assumptions: Assigning Equity Content To Hybrid Capital Instruments Issued By Corporate Entities And Other

Issuers Not Subject To Prudential Regulation, Jan. 16, 2018

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Railroad And Package Express Industry, Aug. 12, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Insurance - General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Related Research

- Credit FAQ: What Could Potential Ownership Changes Mean For The Creditworthiness Of CNP Assurances, La Poste, La Banque Postale, And CDC? Aug. 6, 2018

Ratings List

Ratings Affirmed; Outlook Action

La Poste

	To	From
Issuer Credit Rating	A/Positive/A-1	A/Stable/A-1
Senior Unsecured	A	A
Junior Subordinated	BB	BB
Commercial Paper	A-1	A-1

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