FitchRatings

RATING ACTION COMMENTARY

Fitch Assigns EUROFIMA 'AA' Long-Term IDR; Outlook Stable

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Feedback

Fitch Ratings - Paris - 07 Jul 2021: Fitch Ratings has assigned EUROFIMA European Company for the Financing of Railroad Rolling Stock (EUROFIMA) a Long-Term Issuer Default Rating (IDR) of 'AA' with a Stable Outlook and Short-Term IDR of 'F1+'.

KEY RATING DRIVERS

EUROFIMA's ratings are driven by its Standalone Credit Profile (SCP) of 'aa', based on a 'aa-' solvency assessment, 'aa+' liquidity assessment and a one-notch uplift over the lower of solvency and liquidity (aa-) to reflect EUROFIMA's 'low' risk business environment. Fitch's assessment of extraordinary support from shareholders is 'a' and does not lead to any uplift to the rating. Fitch assesses EUROFIMA's ratings based on the multilateral development bank (MDB) approach as per its Supranationals Criteria.

EUROFIMA's public mission is to support the development of public service passenger rail transportation by providing railway companies with loans to renew and modernise their railway equipment. The institution can only extend loans to its 26 shareholders or to a railway company in one of its member countries that benefits from a guarantee from one of its shareholders. Loans to shareholders benefit from an explicit guarantee by the shareholder's respective sovereign.

EUROFIMA's 'aa-' solvency reflects 'strong' capitalisation and 'low' risk assessments.

EUROFIMA's strong capitalisation is primarily based on its 'excellent' Fitch risk-weighted asset (FRA) ratio, at 56% as of end-2020. This in turn reflects the high credit quality of the institution's assets and callable capital (73% of which is guaranteed by sovereigns rated in the 'AAA' and 'AA' categories). The 'excellent' FRA ratio is balanced against a 'moderate' equity-to-assets ratio of 9.3% as of end-2020, the lowest across Fitch-rated MDBs, reflecting EUROFIMA's high leverage (the institution has no leverage limit). Fitch expects the two ratios to remain in the same ranges in the medium term, although the FRA ratio could be affected by increased exposure to non-investment grade borrowers, as per EUROFIMA's medium-term plan.

The 'low' risk assessment is primarily driven by a 'very low' assessment of credit risk. The average rating of loans was 'A+' as of end-2020, based on the sovereign guarantors' ratings. Although 20% of the loans are guaranteed by sovereigns that currently have a Negative Outlook (19% to Belgium, 1% to France), a downgrade of these sovereigns would not affect the average rating of loans. Fitch assesses EUROFIMA's preferred creditor status (PCS) as 'excellent', leading to a three-notch uplift above the average rating of loans to 'AA+'. The PCS assessment reflects the institution's 100% exposure to sovereigns and the record of loan performance, with no non-performing exposure since operations started in 1956.

Loan book concentration is the main weakness in EUROFIMA's risk profile. The five largest borrowers accounted for 91% of total loans as of end-2020. The concentration limits are based on risk-weighted measures that support high exposures towards highly rated borrowers. To reduce concentration, EUROFIMA has introduced a premium in the pricing of loans to borrowers with the largest exposures. Fitch expects loan book concentration to remain very high in the medium term.

The risk profile also reflects a 'strong' risk management framework. The very high credit quality of the loan portfolio (with all loans guaranteed by an entity with a minimum rating of 'BBB-', except for a limited portion of non-investment grade exposure accounting for 1.5% of total loans in 2020) somewhat mitigates the very high concentration. EUROFIMA match-funds its loans and passes through funding costs to its borrowers. Residual currency and interest rate risks are fully hedged through interest rate and currency swaps.

Fitch assesses EUROFIMA's business environment as 'low' risk, leading to a one-notch uplift over the weaker of its solvency and liquidity assessments. The 'low' risk business environment reflects a 'medium' risk business profile and a 'low' risk operating environment.

The 'medium' risk business profile is supported by the sovereign guarantees on the loan book and EUROFIMA's 'low' governance risk. Although the national railway companies are both borrowers and shareholders, the most important decisions at board level require the consent of the sovereign member states. The 'medium' risk assessment of the strategy reflects the deleveraging and de-risking trend in the last decade, as well as the potential increase in exposures to non-sovereign and non-IG borrowers in the medium term.

The assessment also factors in our expectation that EUROFIMA's stated objective to diversify the loan book may only result in limited improvement in concentration metrics. Our assessment of EUROFIMA's policy importance is affected by its 'moderate' size (the loan book was EUR11 billion as of end-2020) and the limited role of the supranational organisation for its shareholders overall, with only half of them borrowing from it.

The 'low' risk operating environment reflects the strong creditworthiness and high income per capita of EUROFIMA's 25 countries of operations (19 are high-income countries, six are upper-middle income). World Bank Governance indicators of the countries of operations are also strong relative to those of MDB rated peers. EUROFIMA's headquarters are in Switzerland (AAA/Stable).

Fitch assesses EUROFIMA's liquidity at 'aa+'. Liquid assets accounted for 121% of short-term debt as of end-2020 and Fitch expects it will remain in the 'strong' range in the medium term. EUROFIMA must hold at least 12-months coverage of net disbursements (after accounting for a haircut on securities). 59% of treasury assets were rated 'AAA'/'AA' as of end-2020 and 98% were investment grade. EUROFIMA is a regular bond issuer in various currencies, primarily euros (49% of funding), Swiss francs (20%) and US dollars (15%). EUROFIMA is not eligible for the European Central Bank's bond buying programmes.

Fitch assesses extraordinary support from shareholders at 'a'. The shareholders' capacity to support is based on the average rating of key shareholders (the national railway companies from Germany, France and Italy), assessed at 'AA-' after accounting for the guarantee of callable capital by their respective sovereigns. Fitch applies a two-notch negative adjustment to the capacity to support, to 'a', to reflect a 'weak' propensity of shareholders to support. The 'weak' propensity accounts for callable capital not fully covering net debt and the termination of the cross-shareholders joint and several guarantee in 2018. The assessment also takes into account that EUROFIMA has paid dividends to its shareholders in recent years, which is unusual for a supranational institution.

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RATING SENSITIVITIES

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

Business Environment (business profile): A strengthening in our assessment of EUROFIMA's policy importance. This could be the case if the gradual liberalisation of railway markets in Europe supported demand for EUROFIMA financing from a more diversified pool of borrowers.

Solvency (risk): Success of EUROFIMA's strategy to achieve stronger diversification of its loan book, evidenced by a significant fall in the share of loans to the five largest borrowers.

Solvency (capitalisation): Stronger capitalisation driven by significant reduction in EUROFIMA's leverage, bringing the equity-to-assets ratio towards the 15% threshold for 'strong'.

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

Solvency (capitalisation): A deterioration in our assessment of capitalisation, for example, if the equity-to-assets ratio fell below the 8% threshold for a 'moderate' assessment.

Solvency (credit risk): Deterioration in our assessment of credit risk due to a decline in the average rating of loans and/or a breach in EUROFIMA's PCS if an exposure covered by a sovereign guarantee became non-performing.

Business Environment (Business Profile): Deterioration in EUROFIMA's business profile driven by a weakening of our assessment of its policy importance. This could stem from lower demand for EUROFIMA financing by its shareholders and/or failure to diversify its pool of borrowers.

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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.

KEY ASSUMPTIONS

-The global economy will develop in line with Fitch's Global Economic Outlook published on 15 June 2021, including marked improvement in GDP growth in 2021 as economies adapt to social distancing and vaccination programmes gather momentum.

-EUROFIMA's shareholders' respective sovereigns, which ultimately guarantee the institution's loan book, will preserve EUROFIMA's PCS, even if experiencing severe difficulties,.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

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

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ESG CONSIDERATIONS

EUROFIMA has an ESG Relevance Score of '4[+]' for Policy Status and Mandate Effectiveness. All loans extended by EUROFIMA to its shareholders are guaranteed by the shareholders' respective sovereigns, as per EUROFIMA's status. The sovereign guarantee also applies to the callable capital subscribed by shareholders. This has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

EUROFIMA has an ESG Relevance Score of '4' for Rule of Law, Institutional & Regulatory Quality. All supranationals attract a score of '4'. Supranationals are neither subject to bank regulation nor supervised by an external authority. Instead, supranationals comply with their own set of rules. Fitch pays particular attention to internal prudential policies, including compliance with these policies. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

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

RATING ACTIONS

ENTITY/DEBT	RATING		
Eurofima European Company for the Financing of Railroad Rolling Stock	LT IDR	AA Rating Outlook Stable	New Rating
•	ST IDR	F1+	New Rating

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Supranationals Rating Criteria (pub. 20 May 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

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Eurofima European Company for the Financing of Railroad Rolling Stock -

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