

Research Update:

Region of Pays de la Loire 'AA/A-1+' Ratings Affirmed; Outlook Stable

December 10, 2021

Overview

- Capital spending above historical trends will lead to wider deficits and higher borrowing for the Region of Pays de la Loire in 2021-2023.
- However, increasing tax revenue and prudent financial targets will help limit debt accumulation.
- We affirmed our 'AA' long-term and 'A-1+' short-term issuer credit ratings on Pays de la Loire. The outlook remains stable.

Rating Action

On Dec. 10, 2021, S&P Global Ratings affirmed its 'AA' long-term and 'A-1+' short-term issuer credit ratings on the French Region of Pays de la Loire. The outlook remains stable.

At the same time, we affirmed our 'AA' long-term issue rating on the region's €2 billion euro medium-term note (EMTN) program and our 'A-1+' short-term issue rating on its €200 million French commercial paper (NEU CP) program.

Outlook

The stable outlook reflects our expectation that increasing tax revenue and cautious financial management will facilitate Pays de la Loire's elevated capital spending in 2021-2023, limiting debt accumulation. We also anticipate that the region will sustain its cash buffers, preserving its strong liquidity position.

Downside scenario

If we lower our ratings on France (unsolicited AA/Stable/A-1+) or revise the outlook to negative, we would take a similar action on Pays de la Loire. Moreover, we might also consider a negative rating action if the region loosens its financial discipline, posting after-capital deficits above 10% of total

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revenue or causing a structural deterioration in its liquidity position.

Upside scenario

We might consider an upgrade if we take a similar action on France and the region posts stronger budgetary performance metrics, leading to a declining debt ratio.

Rationale

The COVID-19 pandemic has significantly affected the budgetary performance of the Pays de la Loire region. Tax revenue was much lower in 2020 as the economy contracted, and the region launched sizable emergency and recovery stimulus packages worth €375 million. These will add to existing investment needs in high schools and transportation and pressure the region's budgetary performance, necessitating increased debt issuance in 2021-2023. Nevertheless, we believe that Pays de la Loire's track record of prudent fiscal management as well as the cautious financial targets that it set for the 2021-2027 regional mandate will lead to gradually narrowing deficits.

Strong financial management practices will continue to support Pays de la Loire's creditworthiness as the economy recovers

Pays de la Loire, France's eighth most populated region with over 3.8 million inhabitants, benefits from a diversified economy, which includes strong industrial companies (aeronautics, naval shipyards, and agroindustry) and an expanding services sector. The region's GDP per capita, which we estimate at \$39,000 in 2021, is high by international standards, although it is about 11% below that of France as a whole. The regional economy appears to be recovering from the COVID-19 recession; employment was up 3.6% in the year to June 2021, across all sectors apart from industry. Moreover, the unemployment rate, at 6.7%, remained stable and below the national average of 7.8%.

The region's creditworthiness is supported by its effective financial governance. Regional elections were held in June 2021, leading to the re-election of the center-right coalition, which won 57 out of 93 seats in the regional council. The executive confirmed that it intends to invest more in the first three years of its mandate, to support the local economy as the effects of the pandemic ease, and will not be bound by its previous €450 million ceiling for regional capital expenditure (capex). Nevertheless, the region also committed to strengthening budgetary performance metrics over the duration of the new mandate, including operating balances structurally above €250 million. We also take comfort in the debt-to-operating-surplus target of 7x by 2027, which the region defined in its latest multi-year budgetary trajectory, and view this as a commitment to curb capex and stabilize debt levels after 2024. The region established a track record of fiscal discipline in 2016-2019 and continues to benefit from strong financial planning. In addition, it exhibits sound debt and liquidity management practices. Pays de la Loire is the only French local and regional government to have its accounts certified by an external auditor, which supports our assessment of the region's financial management as very strong.

Moreover, Pays de la Loire benefits from the institutional framework for French regions, which we consider to be very predictable and well-balanced. Successive reforms have incrementally strengthened the role of regions, but additional tasks have been accompanied by proportionate funding, ensuring good adequacy of revenue to cover expenditure needs.

Increasing tax revenue will foster operating surpluses, but higher capex will widen deficits and create additional borrowing needs over our rating horizon

We expect Pays de la Loire to post gradually widening operating surpluses over our forecast horizon, averaging 16.6% of operating revenue in 2021-2023. As part of the fiscal reform included in the central government's (CG) 2021 budget act, regions now receive a second share of national value-added tax (VAT) in lieu of corporate value added tax (CVAE), with the two shares of VAT representing over 50% of Pays de la Loire's operating revenue. In our view, strong VAT receipts will contribute to healthy operating revenue growth rates in the coming years. However, we also expect operating expenditure to increase in 2021 compared with 2020, as economic reopening prompts the region to spend more on transportation services and its vocational training programs. However, we anticipate that spending growth will slow significantly in 2022 and 2023, since the executive should implement cost-containment measures and adjust the scope of some of its policies. It is also likely that CG-mandated operating expense growth caps will resume in some form by then, after being suspended last year.

In 2020, Pays de la Loire decided to launch an ambitious emergency and recovery package, aimed at mitigating the impacts of the pandemic on its economy, in large part through higher capex. In late September 2021, the region had effectively disbursed about one-third of this €375 million envelope, and the remaining credits will contribute to still-elevated economic development subsidies in 2022. Moreover, the region will seek to respond to expanding investment needs for high schools and regional trains, while implementing projects financed by the EU structural funds and the Recovery Assistance for Cohesion and the Territories of Europe (REACT-EU) facility. Overall, we anticipate the region's investments will exceed €600 million per year in 2021-2023, leading to budgetary deficits equivalent to 8.6% of total revenue. Nevertheless, we believe that capex will start receding after 2023, allowing Pays de la Loire to post lower after-capital shortfalls. Thereafter, the region's capacity to invest, without further pressuring its budgetary performance, will depend on tax-revenue dynamics and its ability to contain operating spending.

We forecast that Pays de la Loire's tax-supported debt (TSD) will increase over our forecast horizon, reaching €2.3 billion, or 162% of consolidated operating revenue in 2023, compared with 143% in 2020. The TSD ratio's rising trajectory is exacerbated by the expected roll-back of CG-funded vocational training scheme Pacte in 2023-2024. Although neutral in terms of operating balance, the phase-out will diminish operating revenue, subtracting from the TSD ratio's denominator. In our view, interest charges will only expand moderately, to about 2.8% of operating revenue in 2023, versus 2.5% in 2020. This evolution, driven by anticipated debt growth, will be mitigated by a decline in the average cost of debt through 2023. Notably, the region will seek to increase the maturity of new bond issuances, to lock in low interest rates.

We consider Pays de la Loire's liquidity position strong. The region currently has liquidity lines and revolving loans totaling €230 million. The total available facilities, in addition to our estimate of the region's average cash, will cover more than 120% of its debt service over the next 12 months. We expect higher capex will leave the ratio lower than previously but still above the 120% threshold. We also consider the region's access to external liquidity strong. This reflects large and regularly renewed contracted liquidity facilities and a diversified pool of investors, which include institutional lenders such as the European Investment Bank, as well as domestic commercial banks. Pays de la Loire also taps financial markets through its EMTN and NEU CP programs. In addition, the region has issued €255 million of bonds this year, including two sustainable bonds totaling €150 million in fourth-quarter 2021.

Key Statistics

Table 1

Region of Pays de la Loire--Selected Indicators

(Mil. €)	2018	2019	2020	2021bc	2022bc	2023bc
Operating revenues	1,356	1,471	1,296	1,346	1,425	1,437
Operating expenditures	1,076	1,127	1,078	1,134	1,195	1,180
Operating balance	281	345	218	213	230	257
Operating balance (% of operating revenues)	20.7	23.4	16.8	15.8	16.1	17.9
Capital revenues	138	137	155	183	270	236
Capital expenditures	467	479	515	534	645	628
Balance after capital accounts	(48)	2	(142)	(139)	(145)	(135)
Balance after capital accounts (% of total revenues)	(3.2)	0.1	(9.8)	(9.1)	(8.6)	(8.1)
Debt repaid	140	127	106	113	125	121
Gross borrowings	172	125	295	300	270	255
Balance after borrowings	(22)	(1)	16	48	0	0
Direct debt (outstanding at year-end)	1,668	1,666	1,854	2,042	2,187	2,321
Direct debt (% of operating revenues)	123.0	113.2	143.1	151.6	153.4	161.6
Tax-supported debt (outstanding at year-end)	1,668	1,666	1,854	2,042	2,187	2,321
Tax-supported debt (% of consolidated operating revenues)	123.0	113.2	143.1	151.6	153.4	161.6
Interest (% of operating revenues)	2.2	1.9	2.1	2.1	2.2	2.3
Local GDP per capita (single units)	30,946	32,150	30,114	32,191	33,859	34,912
National GDP per capita (single units)	35,199	36,226	34,115	36,840	38,749	40,174

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful.

Ratings Score Snapshot

Table 2

Region of Pays de la Loire--Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	1
Financial management	1
Budgetary performance	3

Table 2

Region of Pays de la Loire--Ratings Score Snapshot (cont.)

Key rating factors	Scores
Liquidity	1
Debt burden	4
Stand-alone credit profile	aa
Issuer credit rating	AA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Sovereign Risk Indicators, Oct. 12, 2021. An interactive version is available at <http://www.spratratings.com/sri>

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Governments | International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign, Dec. 15, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 20, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Public Finance System Overview: French Regions, Aug. 4, 2020.
- French LRGs Start The COVID Recovery On Solid Footing, Sept. 6, 2021
- Local Government Debt 2021: French LRG Debt Could Surpass €155 Billion Within A Year, March 25, 2021
- Public Finance System Overview: French Cities, Intercities, And Municipal Syndicates, Aug. 4, 2020

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the

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appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed

Region of Pays de la Loire

Issuer Credit Rating	AA/Stable/A-1+
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Senior Unsecured	AA
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Commercial Paper	A-1+
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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