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Bulletin:

Deutsche Bahn's Sale Of DB Schenker Signals Focus On Large Mobility Transition Investments

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PARIS (S&P Global Ratings) Dec. 21, 2022--S&P Global Ratings said today that effects on the credit quality of Deutsche Bahn AG (DB; AA-/Stable/A-1+) from the potential disposal of its logistics service subsidiary, DB Schenker, are not yet clear and that further progress on the disposal will clarify the size of the stake disposed and the amount of proceeds. In addition, we expect DB to focus on achieving its large investment plan and mobility transition, fostering and improving railway services to decarbonize transportation in Germany, which could be supported by the proceeds from the sale.

The timing for the concrete start of the sale remains uncertain and DB's management board has been mandated to examine and prepare the possible sale of up to 100% of DB Schenker. At the same time, it has been decided by the supervisory board that the related proceeds would remain entirely within DB to, among others, significantly reduce its leverage.

The potential disposal is in line with DB's strategy to focus on the core German passenger railway operations (both DB Regional and Long-Distance segments contributed about 36% of EBITDA in 2019), which we view as less cyclical and generating higher margin than the logistic operations (S&P Global Ratings-adjusted EBITDA margin of 15.8% for the long-distance segment in 2019 versus 6.3% for DB Schenker). That said, depending on the stake of the potential disposal, DB's absolute size and diversification could shrink, because DB Schenker's strong performance generated about 54% of total reported EBITDA in the first half of 2022 (€1.5 billion), from 21% in 2019. This was supported by continued constrained air freight capacity, and high rates, while long-distance rail traffic is still trending below pre-pandemic levels (with passenger volumes in long-distance at 82% of 2019 levels in the first half of 2022). At the same time, the transaction would reduce DB's geographic diversification, as most of DB Schenker's revenue derives from international activities.

The rail passenger transport operations are key for the German government to achieve its carbon reduction objectives, with DB targeting to reduce CO_2 emissions by 2030 (compared with 1990), resulting among others in a goal for the company of doubling the number of long-distance rail passengers by then. For further information on the implications of the mobility transition for European railways please see "European Rail Looks To Ride The Energy Transition," published Nov. 28, 2022, on RatingsDirect.

In this regard, the sale of DB Schenker could offer additional sources of funds to mitigate the impact of DB's large investment plan on the development of its financial leverage (€37.7 billion of S&P Global Ratings-adjusted debt on Dec. 31, 2021). The group is pursuing high modernization and capacity expansion investments in railway infrastructure (around €90 billion over 2022-2026), which will weigh on the group's leverage in the next several years, although state subsidies will cover more than 60% of total annual capital expenditure. In our current forecasts, which fully consolidate DB Schenker, we assume the group will post S&P Global Ratings-adjusted funds from operations to debt of about 11%-12% in 2022, followed by 8.5%-9.5% in 2023. The potential inflationary pressures on building materials pose some downside to our forecasts (see more details in "Deutsche Bahn AG Outlook Revised To Stable From Negative On Traffic Recovery And Strong State Support; 'AA-' Affirmed," published on July 29, 2022).

This report does not constitute a rating action.