MOODY'S
RATINGS

Rating Action: Moody's Ratings affirms Deutsche Bahn's Aa1 ratings following disposal of DB Schenker; outlook stable

15 Oct 2024

Paris, October 15, 2024 -- Moody's Ratings (Moody's) has today affirmed the Aa1 long-term issuer rating of Deutsche Bahn AG (DB or the company). We have also affirmed DB's (P)Aa1 senior unsecured MTN program rating, its (P)P-1 other short term rating, its P-1 commercial paper rating and its a3 Baseline Credit Assessment (BCA). Concurrently, we have affirmed the Baa1 rating on the backed Undated Subordinated Resettable Fixed Rate Notes (junior subordinated "Hybrid") issued by DB through its subsidiary Deutsche Bahn Finance GmbH. We have also affirmed Deutsche Bahn Finance GmbH's Aa1 senior unsecured rating, its Aa1 backed senior unsecured ratings, its (P)Aa1 backed senior unsecured MTN program ratings, its P-1 backed commercial paper rating and its (P)P-1 backed other short term rating. The outlook on both entities remains stable.

The rating action was prompted by DB's announcement on 2 October 2024 [1] that its Supervisory Board approved the sale of DB Schenker to the Danish transport and logistics group DSV A/S (A3 stable) for an enterprise value of €14.3 billion and an equity value of €11.3 billion. At the same time, the federal government granted the approval required for the transaction under the Federal Budget Code (BHO). The sale is expected to be completed during the course of 2025 once all regulatory approvals have been obtained.

"We have affirmed the rating at Aa1 because the sale of Schenker – despite making DB a smaller less diversified company, will allow DB to repay debt while the new DB will be more focused on core operations and on Germany, enabling a closer alignment and increased support from the German government," says Kristin Yeatman, a Moody's Ratings Vice President – Senior Analyst and lead analyst for DB.

RATINGS RATIONALE

The divestment of DB Schenker will reduce DB's revenue to about €26 billion compared with €45.2 billion in fiscal 2023. However, the increased focus on its core rail business will benefit DB's strategic focus on infrastructure renewal, rail operations and profitability over the next three years.

Post divestment, DB's revenue will be more concentrated in Germany, since DB Schenker had a global presence. The higher revenue concentration in Germany (around 95% of total revenues) will put even more importance and relevance on DB's core contribution to the transport and climate policy goals of the German government. The increase in common revenue base between DB and the Government has lead us to increase the level of default dependence to very high from high.

The German Government, which owns 100% of DB, has recently stepped up its on-going support for the rail infrastructure which is owned by DB, committing about €16.4 billion for 2024 and about €18.3 billion for 2025. The over €36 billion total contribution for the two years comprises €15.9 billion in equity increases (including €1.1 billion contribution for the climate action programme), about €16 billion investment and income grants, and a €3 billion low interest loan. In addition, the German Government supports rail freight transport and long-distance rail passenger transport with an total amount of about €1.5 billion in 2024 and 2025. DB will also benefit from these sector-wide measures. The Government is aiming to increase rail passenger traffic and railways' share of freight traffic above other modes of transport. As a result of the increased level of Government alignment and financial contributions, we have changed our assessment of Government support to very high from high. This assessment is based on the German Government's willingness (given the constitutional mandate to provide railway services via DB) and very strong ability to provide support to DB, given the sovereign's ample financial reserves, as reflected in its Aaa rating.

The sale proceeds from DB Schenker will remain entirely within the DB group and will be used to significantly reduce its debt, according to DB. Despite earmarking the bulk of sale proceeds for debt repayment, the deconsolidation will lead to a reduction in EBIT and cash flow such that the transaction in and of itself without the planned restructuring of the core business is unlikely to result in a material improvement in financial metrics. However, the company expects its restructuring plans to support its goal of achieving an EBIT of €2 billion (negative €2 billion in 2023 excluding DB Schenker) and a 12% increase in operating cash flow to adjusted net debt by 2027.

DB's a3 BCA is weakly positioned owing to the company's high leverage. The company's Moody's adjusted gross debt remained at around €43 billion in 2023 compared with the pre-pandemic amount of around €36 billion in 2019. We expect debt to reduce to around €30 billion in 2025 mainly as a result of the DB Schenker divestment, and we expect gross leverage to reduce to around 6.8x in 2025 from 9.9x expected in 2024. From 2026 onward, we expect leverage to reduce toward 6x. However, we note that this is dependent on the success of the new restructuring and cost savings plan. We do not expect free cash flow (FCF) to turn positive during the current investment period which is expected to continue for at least the next 5 years.

The a3 BCA remains supported by (1) the company's large size and vertically integrated business model, including monopolistic railway infrastructure activities; and (2) solid business profile, supported by a predictable operating environment and significant subsidies.

Conversely, the BCA is constrained by (1) persistent pressure on profitability due to inefficiencies and infrastructure development, despite the cost-savings programmes underway; (2) negative free cash flow because of an intense capital spending programme; (3) high leverage, and (4) the execution risk associated with the divestment of DB Schenker.

DB's Aa1 long-term issuer rating combines: (1) its a3 BCA; (2) our assessment of a very high likelihood that the company will receive extraordinary support from the Government of Germany (Aaa stable) in times of need, and (3) our assessment of a very high default dependence between DB and the Government. Such an assessment results in a five-notch uplift to the company's a3 BCA for a final rating of Aa1.

LIQUIDITY

We expect DB to have excellent liquidity over the next 12 months, supported by its cash position of €5.8 billion (including cash and cash equivalents, highly liquid cash investments and financial receivables) as of 30 June 2024; its undrawn €2.1 billion committed credit lines as of 30 June 2024; its cash flow from operations, which we expect to be around €3.8 billion in 2024; and the planned government contributions of more than €36 billion for 2024 and 2025.

The major cash needs for DB are capital expenditure (net of grants from the German government), which we estimate at around €11 billion (including IFRS 16) in 2024 and debt repayments of around €4 billion (excluding hybrid) due in the next 18 months.

We expect DB to maintain its excellent access to the capital markets.

STRUCTURAL CONSIDERATIONS

The Baa1 rating of the Hybrid is one notch lower than DB's a3 BCA and six notches lower than the company's Aa1 long-term issuer rating. This reflects certain features of the security, which is perpetual, deeply subordinated and allows DB to opt for coupon deferrals on a cumulative basis. Because of these characteristics we believe that, in case of need, Government support may not be as strong, or as timely as it would be for senior unsecured debt.

RATIONALE FOR STABLE OUTLOOK

The stable outlook reflects our expectation that the company will successfully execute its restructuring plans to support its goal of achieving an EBIT of €2 billion and a 12% increase in operating cash flow to adjusted net financial debt by 2027. As a result, leverage will stabilize at below 7x in the next 18-24 months, a level commensurate with its a3 BCA.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade is unlikely given that DB's rating is one notch lower than the sovereign rating and we expect this gap to remain.

The BCA could be upgraded if DB's leverage, measured by Moody's-adjusted debt/EBITDA, decreases below 6.0x on a sustained basis, DB successfully executes its plan to materially improve operational efficiencies, operating performance improves as evidenced by a substantial and sustained increase in Moody's-adjusted EBIT margin to mid-single digits and the company achieves a sustainable, positive free cash flow.

A downgrade of Germany's sovereign rating could result in a downgrade of DB's ratings. In addition, we could downgrade DB's ratings if the likelihood of extraordinary support from the Government decreases and the BCA deteriorates further.

DB's BCA could be downgraded if the company fails to execute its new restructuring and cost-savings plan following the divestment of DB Schenker, and its Moody's-adjusted debt/EBITDA remains above 7x on a sustained basis, or DB's EBIT margin fails to improve to at least 3%. Negative rating action could also occur if the company's business profile weakens, for example as the result of a change in its integrated business model, with a separation of its railway operations from its infrastructure management activities.

PRINCIPAL METHODOLOGIES

The methodologies used in these ratings were Passenger Railways and Bus Companies published in August 2024 and available at https://ratings.moodys.com/rmc-documents/426543 , and Government-Related Issuers methodology published in January 2024 and available at https://ratings.moodys.com/rmc-documents/406502 . Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of these methodologies.

COMPANY PROFILE

Deutsche Bahn AG (DB) is a vertically integrated rail and logistics group that owns and operates the German national rail transportation network. In 2023, DB generated €45 billion of revenue and €2.8 billion of reported EBITDA. The company is fully owned by the German Government.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions .

For any affected securities or rated entities receiving direct credit support/credit substitution from another entity or entities subject to a credit rating action (the supporting entity), and whose ratings may change as a result of a credit rating action as to the supporting entity, the associated regulatory disclosures will relate to the supporting entity. Exceptions to this approach may be applicable in certain jurisdictions.

For ratings issued on a program, series, category/class of debt or security, certain regulatory disclosures applicable to each rating of a subsequently issued bond or note of the same series, category/class of debt, or security, or pursuant to a program for which the ratings are derived exclusively from existing ratings, in accordance with Moody's rating practices, can be found in the most recent Credit Rating Announcement related to the same class of Credit Rating.

For provisional ratings, the Credit Rating Announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating.

Moody's does not always publish a separate Credit Rating Announcement for each Credit Rating assigned in the Anticipated Ratings Process or Subsequent Ratings Process.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

The Global Scale Credit Rating(s) discussed in this Credit Rating Announcement was(were) issued by one of Moody's affiliates outside the UK and is(are) endorsed for use in the UK in accordance with the UK CRA Regulation.

REFERENCES/CITATIONS

[1] Deutsche Bahn press release 02-Oct-2024: https://www.deutschebahn.com/en/presse/press_releases/Supervisory-Board-of-Deutsche-Bahn-AG-approves-sale-of-logistics-subsidiary-DB-Schenker-to-DSV-13092854#

Please see https://ratings.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the issuer/deal page on https://ratings.moodys.com for additional regulatory disclosures for each credit rating.

Kristin Yeatman
Vice President - Senior Analyst
Corporate Finance Group
Moody's France SAS
21 Boulevard Haussmann
Paris, 75009
France
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Ivan Palacios
Associate Managing Director
Corporate Finance Group
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Releasing Office:
Moody's France SAS
21 Boulevard Haussmann
Paris, 75009
France
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

CONSIDERED A BENCHMARK.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the credit rating process or in preparing its Publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to: (a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY CREDIT RATING, ASSESSMENT, OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc. have, prior to assignment of any credit rating, agreed to pay to Moody's Investors Service, Inc. for credit ratings opinions and services rendered by it fees ranging from $1,000 to approximately $5,000,000. MCO and Moody's Investors Service also maintain policies and procedures to address the independence of Moody's Investors Service credit ratings and credit rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold credit ratings from Moody's Investors Service, Inc. and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moodys.com under the heading "Investor Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Additional terms for Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors.

Additional terms for Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJKK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJKK or MSFJ (as applicable) have, prior to assignment of any credit rating, agreed to pay to MJKK or MSFJ (as applicable) for credit ratings opinions and services rendered by it fees ranging from JPY100,000 to approximately JPY550,000,000.

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.