Research Update:

French Strategic Oil Reserves Manager SAGESS Affirmed At 'AA/A-1+'; Outlook Stable

September 27, 2019

PRIMARY CREDIT ANALYST

Christophe Dore
Paris
(33) 1-4420-6665
christophe.dore
@spglobal.com

SECONDARY CONTACT

Mehdi Fadli
Paris
(33) 1-4420-6706
mehdi.fadli
@spglobal.com

ADDITIONAL CONTACT

Industrial Ratings Europe
Corporate_Admin_London
@spglobal.com

Overview

- We continue to view Société Anonyme de Gestion de Stocks de Sécurité (SAGESS) as a government-related entity (GRE), and believe there is an almost certain likelihood that the French government would provide SAGESS with timely and sufficient extraordinary support in the event of financial distress.
- We do not consider that SAGESS' role for or link with the state has changed following the French government's decision to prohibit certain GREs, including SAGESS, from issuing long-term debt.
- We therefore equalize our ratings on SAGESS with those on France and are affirming our 'AA/A-1+' issuer credit ratings on SAGESS.
- The stable outlook mirrors that on France.

Rating Action

On Sept. 27, 2019, S&P Global Ratings affirmed its 'AA/A-1+' long- and short-term issuer credit ratings on France-based Société Anonyme de Gestion de Stocks de Sécurité (SAGESS). The outlook remains stable.

We also affirmed our 'AA' long-term issue rating on SAGESS' outstanding bonds, and our 'A-1+' short-term issue rating on its €1.4 billion French commercial paper (CP) program.

Rationale

We continue to equalize our ratings on SAGESS with those on France (unsolicited; AA/Stable/A-1+). In our view, there is an almost certain likelihood that the French government would provide timely and sufficient extraordinary support to SAGESS in the event of financial distress. Furthermore, we consider that the French government's limited level of contingent liabilities does not constrain its capacity and willingness to support SAGESS in a timely manner if needed. We do not consider the government's general propensity to support its

government-related entity (GRE) sector to be doubtful.

We factor into our assessment of SAGESS our view of the agency's:

- Critical role for France--which has a high dependence on imported oil--in supporting the country's energy security and fulfilling its legal obligation to stockpile strategic oil reserves, according to International Energy Agency and EU requirements. SAGESS was recognized by a 2012 state decree as France's sole central stockholding entity under the 2009 EU directive on oil stockpiling obligations. In our opinion, SAGESS' strategic mission of maintaining national energy security and independence ensures it receives strong state support; and
- Integral link with France. SAGESS is integrated into the government's energy and defense policy and, through its agreement with Comité Professionnel des Stocks Stratégiques Pétroliers (CPSSP; not rated), subject to state supervision and control. It benefits from a special legal status, including specific tax privileges, full cost coverage, and legal restrictions over its shareholding. Furthermore, SAGESS' debt is consolidated into the central government's debt.

In August 2016, the state included SAGESS on a list of GREs whose debt is consolidated with the central government's debt and are prohibited from issuing long-term debt from August 2017, and it confirmed this in an updated list in mid-August 2017. SAGESS contested the government's decision, but Paris' administrative court rejected its claims in January 2019. SAGESS appealed the court decision in May 2019, and we understand the appeal court may reach a decision over the coming months. The government's decision to place SAGESS on this list confirms the agency's integral link with the French government, in our view, even if SAGESS has contested the decision.

If the appeal court confirms the state's decision regarding long-term debt issuance, we understand SAGESS could start progressively disposing of its oil reserves to pay down its debt, and would progressively enter a run-off mode. Alternatively, SAGESS could receive funding directly from the French government to pay down its debt. If the appeal court overturns the decision, or if the government decides to remove SAGESS from the list or allows it to take long-term debt, SAGESS, in line with its funding strategy until August 2017, would likely issue long-term debt to meet its debt repayment schedule and oil stock purchases.

SAGESS' role remains intertwined with that of CPSSP. SAGESS' role is to stockpile oil and carry out related operating, administrative, and financial tasks on behalf of CPSSP, under an agreement with CPSSP that the French government approved. In accordance with the EU's 2009 directive, oil operators in the EU countries must ensure a supply of strategic oil reserves equivalent to 29.5% of inland oil consumption in the previous calendar year. Oil operators in France can delegate this obligation to CPSSP which, in turn, uses SAGESS to manage the obligation.

Since 2000, oil consumption in France has generally tended to decline, due to improved energy efficiency and the rising use of alternative energy sources. However, oil operators have increasingly delegated to SAGESS the management of their strategic oil stocks over the past 10 years. As a result, the level of stock managed by SAGESS has tripled over the past 20 years--SAGESS accounted for about 76% of France's total strategic oil stocks as of end-July 2019, compared with 23% in 1995. After peaking in 2014, the oil stocks managed by SAGESS started to decrease in 2015, as confirmed by a 2.15% reduction in oil consumption in 2018. Based on continued reduction in oil consumption, we expect SAGESS will be in a position to sell part of its oil stocks from 2020.

Reflecting its mission, SAGESS' net income has been marginally positive for the past decade, with some peaks in 2015 and 2017 (when it sold oil stocks) and in 2018, when SAGESS sold an oil repository and a pipeline, recording a large €77 million profit, and paid a €20 million dividend to its shareholders. We expect that over the longer term, SAGESS may use proceeds from oil reserves

sales to partly redeem its debt, rather than transferring large dividends to shareholders. Therefore, we expect SAGESS' future funding needs will mostly stem from debt refinancing.

Ongoing government support of SAGESS remains very strong, in our view. CPSSP charges fees to oil operators for SAGESS' services, which are SAGESS' sole recurrent revenue source. SAGESS' legal framework ensures full cost recovery, because CPSSP reimburses all SAGESS' charges--operating, financing, and exceptional--as stated by decree.

This was tested in 2012-2013 when SAGESS had to settle a one-time tax on oil stocks, although it is exempt from corporate income tax, according to French law. SAGESS funded the tax from an increase in fees paid by oil operators to CPSSP. Moreover, CPSSP will compensate SAGESS for any potential losses related to the sale of oil stocks in the event of a persistent drop in oil prices. More generally, we consider that CPSSP could impose fee increases to mitigate any risks to SAGESS arising from interest rates or significant drops in oil prices, if needed.

Liquidity

Most of SAGESS' cash outflows (which are chiefly oil stock storage costs, debt service, and oil stock purchases) and inflows (monthly repayments from CPSSP, proceeds from CP, and oil stock sales) are highly predictable.

We expect SAGESS will use its €1.4 billion CP program to issue around €1 billion from October 2019, when it is to redeem its maturing €700 million bond. We understand that, under its financial policies, SAGESS has committed to continuing to demonstrate 100% coverage of its outstanding CP at any time through its committed €900 million multiyear syndicated revolving credit facility (fully available until June 2021) and its €100 million liquidity line (fully available until November 2019 and for which SAGESS is negotiating a 12-month extension until November 2020). However, if the appeal court overturned the state's decision to prohibit SAGESS from taking on long-term debt from August 2017, or if the state removed SAGESS from the list of GREs affected, we would expect CP issuances to be lower, because we understand SAGESS would likely take on long-term debt to cover parts of its funding needs, as it has done over the past decade.

If a period of severe financial market disruption created refinancing risks for SAGESS on either its outstanding bonds or its CP, we also understand that the state and CPSSP could authorize SAGESS to sell up to 10% of its stocks, if it needed the liquidity. This 10% was worth about €600 million at market prices, as of Dec. 31, 2018. We would expect such authorization to occur within a day, because adequate mechanisms and procedures are already in place, though these have never been tested.

If necessary, SAGESS could also access emergency funding from the French treasury ("Agence France Trésor"). The treasury could use its public debt fund ("Caisse de la Dette Publique") to buy SAGESS' bonds or CP issues. This would enable the state to offer prompt and ample support to SAGESS in the event of financial distress.

Outlook

The stable outlook mirrors that on France. We expect that SAGESS will retain its critical role for and integral link with France, and we therefore expect the ratings on SAGESS to move in line with those on the sovereign.

We could lower the ratings on SAGESS if we revised down our assessment of the likelihood of support from almost certain. We consider this as very unlikely, however. It could occur if we observe a weakening in the French government's commitment to international rules regarding oil

stock management, or if there were changes in the regulatory framework, such as the one guaranteeing full cost coverage.

We could raise the ratings if we raised those on France and the likelihood of support for SAGESS remained almost certain.

Related Criteria

- 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
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- France, April 5, 2019

Ratings List

Ratings Affirmed	
Societe Anonyme de Gestion de Stocks de Securite	
Issuer Credit Rating	AA/Stable/A-1+
Senior Unsecured	AA
Commercial Paper	A-1+