CREDIT OPINION

30 May 2024

Update

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RATINGS

Ceske drahy, a.s.

Domicile	Czech Republic
Long Term Rating	Baa2
Type	LT Issuer Rating - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Ceske drahy, a.s.

Update to credit analysis

Summary

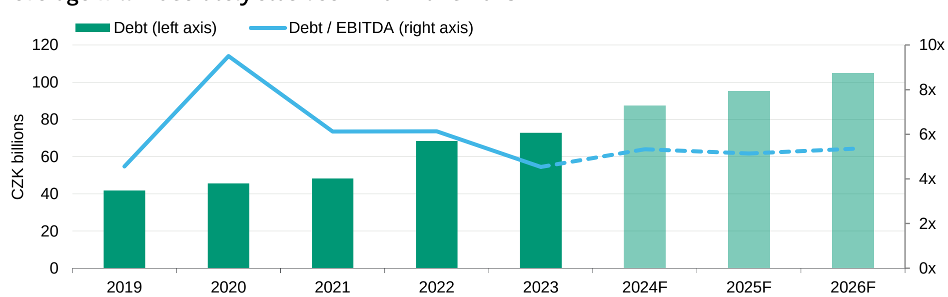
Ceske drahy, a.s.'s (CD) Baa2 long-term issuer rating factors in its ba2 Baseline Credit Assessment (BCA); our expectation of high support from the Government of Czech Republic (Aa3 stable) in times of need; and our assessment of a very high default dependence between the company and the government. This assessment results in a three-notch uplift from the ba2 BCA, in accordance with our Government-Related Issuers Methodology. The uplift reflects the continued strong relationship between CD and its sole shareholder, the Czech Republic.

CD's ba2 BCA is underpinned by the company's solid market position in the Czech Republic and high revenue visibility because of its contracts with the government and the country's 14 municipalities for the passenger railway operations.

The BCA is constrained by CD's slow approach to liquidity management although the company is taking steps to remedy this. In addition, CD will continue to face high capital spending needs, which drive negative free cash flow (FCF) and higher leverage. Capital spending will be mainly allocated to the continued modernisation of the passenger and freight rolling stock, which is key to remaining competitive.

Exhibit 1

Leverage will moderately stabilise in 2024 and 2025



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Sources: Moody's Financial Metrics™ and Moody's Ratings forecasts

Credit strengths

» High probability of extraordinary support from the Czech government

» Solid operating performance, illustrated by growth in traffic and EBITDA

» Strong market position in the domestic passenger rail market

» Good revenue visibility because of long-term service contracts with central and local authorities

Credit challenges

» Persistent negative FCF driven by high capital spending

» Liquidity management has been sluggish but the company has taken steps to remedy this for the short and medium term.

» High leverage but we expect it to reduce to around 5.5x in the next 12-18 months

» Modest reduction in market share in light of the ongoing liberalisation of the railway market

Rating outlook

The stable outlook is in line with the stable outlook on the Czech Republic's rating, and reflects our expectation that CD's strategic importance to the country and strong support from the government, if and when needed, will remain intact over the foreseeable future. The stable outlook also reflects our expectation that the company's leverage, although likely to increase due to capital spending investments, will not exceed 5.5x in the next 12-18 months.

Factors that could lead to an upgrade

» The rating could be upgraded if CD's BCA is upgraded as a result of a sustainable improvement in the company's operating performance; and its EBIT margin remains in the mid-single-digit percentages, Moody's-adjusted debt/EBITDA decreases to around 4.5x and FCF remains positive, all on a sustained basis.

» While we consider the company's links with the sovereign strong and an upgrade of the Czech Republic's rating would be credit positive for CD, it is unlikely to result in an upgrade of CD's rating, which is constrained by the ba2 BCA.

Factors that could lead to a downgrade

» Downward pressure on the rating could result if the company does not perform according to our expectations and maintains leverage above 6x in the next 12-18 months, then we could downgrade the BCA to ba3 from ba2. The BCA could also come under pressure if the company's FCF remains negative for a prolonged period or its liquidity deteriorates.

» A downgrade of CD's rating could also be triggered by a downgrade of the sovereign rating, or a weakening of the close links between the company and its sole shareholder, or both.

Key indicators

Exhibit 2
Ceske drahy, a.s.

(in CZK billions)	2019	2020	2021	2022	2023	2024F	2025F	2026F
Revenue	40.7	35.9	38.5	44.2	49.1	52.7	56.6	59.7
EBIT Margin %	4.9%	-8.2%	-0.9%	4.4%	13.1%	10.6%	11.0%	11.9%
Debt / EBITDA	4.6x	9.5x	6.1x	6.1x	4.5x	5.3x	5.1x	5.4x
FCF / Debt	-7.3%	-11.0%	-11.8%	-22.3%	-6.2%	-24.4%	-10.6%	-10.0%
RCF / Net Debt	22.2%	14.4%	17.1%	13.8%	16.3%	12.4%	14.5%	14.3%
(FFO + Interest Expense) / Interest Expense	7.3x	6.3x	7.5x	5.0x	4.7x	4.7x	5.4x	5.3x
EBITDA Margin %	22.6%	13.3%	20.5%	25.2%	32.6%	31.1%	32.7%	32.8%
EBITA / Interest Expense	1.9x	-2.4x	-0.1x	1.1x	2.4x	2.1x	2.2x	2.2x

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Sources: Moody's Financial Metrics™ and Moody's Ratings forecasts

Profile

Ceske drahy, a.s. (CD) is the national railway operator in the Czech Republic. The company is mainly engaged in passenger and freight transportation and associated activities.

CD was formed in 2002 when the state-owned company, Czech Railways, split into two separate companies: Ceske drahy, a joint-stock company, and the Railway Infrastructure Administration (Sprava zeleznicni dopravni cesty), a state-owned company. CD is 100% controlled by the Czech Republic, which exercises its shareholding rights through a steering committee. This committee has three representatives from the Czech Ministry of Transportation, and one representative each from the ministries of finance, defence, industry and trade, and regional development.

In 2023, CD recorded total revenue from principal operations of CZK49.1 billion (€2.0 billion), of which around 68% (including other income) was from passenger transportation and around 32% was from freight transportation. The company had around 21,823 employees as of 31 December 2023 and is one of the largest employers in the Czech Republic.

Detailed credit considerations

Strong revenue performance in passenger and cargo to continue in 2024-25

In 2023, CD's overall revenue improved 11% from that in 2022, driven mainly by higher ticket sales (volumes were up 4.6%), and higher compensations received from the Ministry of Transport and regions, reflecting the regular rise in inflation and extra compensation from traction cost inflation.

Revenue from cargo was up by 7.2% from the level in 2022 because of the continuing expansion abroad and an increase in prices, despite lower volumes in the overall market.

Company-reported EBITDA grew by 45% to CZK16,140 million and the margin grew to 32.8% from 25.1% in 2022 due to lower prices of purchased consumables and services, and lower traction electricity and diesel costs. The positive impact of this decline in costs was somewhat offset by the decline in rent on land under the tracks, and the extraordinary inflation benefits negotiated with unions had a negative impact on employee benefit costs.

We expect Moody's-adjusted EBITDA to remain stable at around CZK16 billion in 2024 despite an increase in revenue because of higher expected service costs, and to increase to around CZK18 billion in 2025.

Assuming EBITDA will grow at the above levels and debt will increase due to capital spending, we expect leverage of around 5.3x for 2024 and 5.1x in 2025.

CD's business profile is underpinned by its solid market position and revenue visibility

CD's BCA reflects its limited size, with annual revenue of around €1.9 billion, which is smaller than that of its major European peers. However, the ba2 BCA also positively reflects CD's role as the dominant provider of rail transportation in the Czech Republic and the high visibility into its revenue from its passenger transportation activities, in light of the company's contracts with the government and the country's 14 municipalities. We expect to see a gradual increase in the proportion of revenue from public entities as regions gradually switch to availability-based contracts (Brutto contracts) from contracts with revenue risk from the sale of tickets for CD (Netto contracts). We also expect to see higher pricing in contracts to compensate for increasing energy costs.

Tenders will continue, but we expect CD to retain a market share of more than 80%

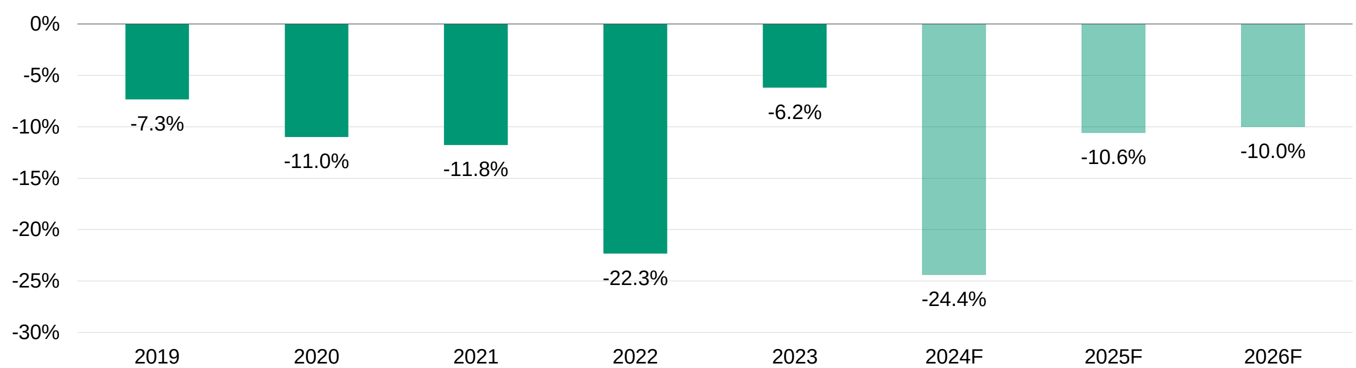
The company has service contracts with the state for 21 national long-distance services and with 14 local authorities for regional services. CD remains exposed to the risk of loss of market share from the tender of contracts maturing soon. The expiry of both long-distance and regional contracts is phased, such that less than 10% of the total passenger railway market will be up for renewal each year. We expect CD to continue to win a large portion of the contracts tendered because of its position as the incumbent operator, boosted by its ongoing efforts to improve its service and modernise its fleet. For example, in 2022, the company deployed 10 new five-wagon non-traction units on the R15 and Ex6 routes, significantly improving the quality and attractiveness of the services for passengers. CD has won 86% of the contracts tendered since 2019.

CD's market share remained broadly stable in 2023, with 81% of the long-distance passenger market, 86.8% of the regional passenger market and 55% of the cargo market. In 2023, of the four contracts that expired, CD lost one contract and was awarded extensions on the remaining three. We expect CD's market share to remain stable at well above 80% for at least the next 18-24 months.

Higher debt levels and negative FCF because of capital spending and lower earnings

We expect high levels of capital spending to continue because of CD's need to renew its train fleet, which will be key to ensuring that the company remains competitive. Capital spending needs are likely to peak in 2024-25 and decrease from 2026. We expect the company to generate around CZK10 billion from land disposals to the Czech railway infrastructure owner, which will boost cash flow from operations. Even with the disposals, the increase in capital spending will strain FCF, which will remain negative at least until 2026 because internal cash flow generation will not be sufficient to fund future capital spending needs.

Exhibit 3
Negative FCF driven by capital spending requirements
Moody's-adjusted FCF/debt



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Sources: Moody's Financial Metrics™ and Moody's Ratings forecasts

We expect the company to continue to borrow to fund its capital spending needs; however, the pressure on financial metrics, particularly leverage, will be significantly offset by growth in EBITDA and cash from asset sales.

High probability of government support

As the national railway operator in the Czech Republic, CD is 100% owned by the Czech government and, therefore, we have applied our Government-Related Issuers rating methodology. In accordance with this methodology, the Baa2 rating of CD reflects the combination of the following inputs:

» the BCA of ba2

» the Aa3 local-currency rating of the Czech government with a stable outlook

» our assessment of a high probability of government support

» a very high default dependence between the company and the government

The high probability of support reflects the company's 100% state ownership and significant control by the Czech government. The Czech government does not explicitly guarantee CD's obligations, but we expect that it would likely provide extraordinary support to the company in case of financial stress.

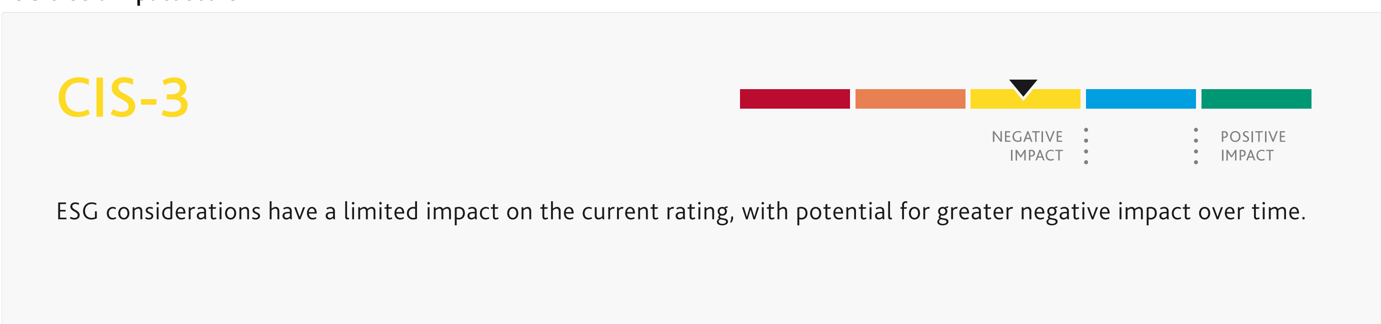
In 2022, the government provided extraordinary support in the form of a subsidy of around CZK380 million to partly compensate CD for the renewable energy surcharge it pays because of its internal combustion engine vehicles.

The very high default dependence currently assigned to CD reflects the high level of operational and financial links between CD and its sole shareholder because around 60% of the company's passenger transport revenue was received directly by the state and the regions(38% of the company's total revenue). It also reflects the very high degree of overlap between the revenue bases of CD and its sole shareholder because both entities generate most of their income in the Czech Republic.

ESG considerations

Ceske drahy, a.s.'s ESG credit impact score is CIS-3

Exhibit 4
ESG credit impact score



Source: Moody's Ratings

Ceske Drahy's ESG Credit Impact Score (**CIS-3**) reflects CD's government ownership and high level of government support which partially offset the ESG risks identified for CD in the IPS scores. As a standalone entity without government support CD's credit rating would be more impacted by ESG risks.

Exhibit 5
ESG issuer profile scores

Source: Moody's Ratings

Environmental

CD's Environmental Issuer Profile Score (IPS) reflects the company's moderate exposure to natural capital, in light of the company's rail freight segment which represents around one third of revenues in and relies on the transport of natural resources such as coal and metals.

Social

CD's exposure to social risks (**CIS-4**) is mainly driven by the company's high fixed cost base related to employees which is difficult to reduce or restructure in line with revenue trends due to the government ownership. Human Capital risk also includes the risk of industrial action, strikes and pressure to increase salaries. CD is moderately exposed to Health and Safety, and well as customer relations because managing sensitive consumer information creates data privacy risks.

Governance

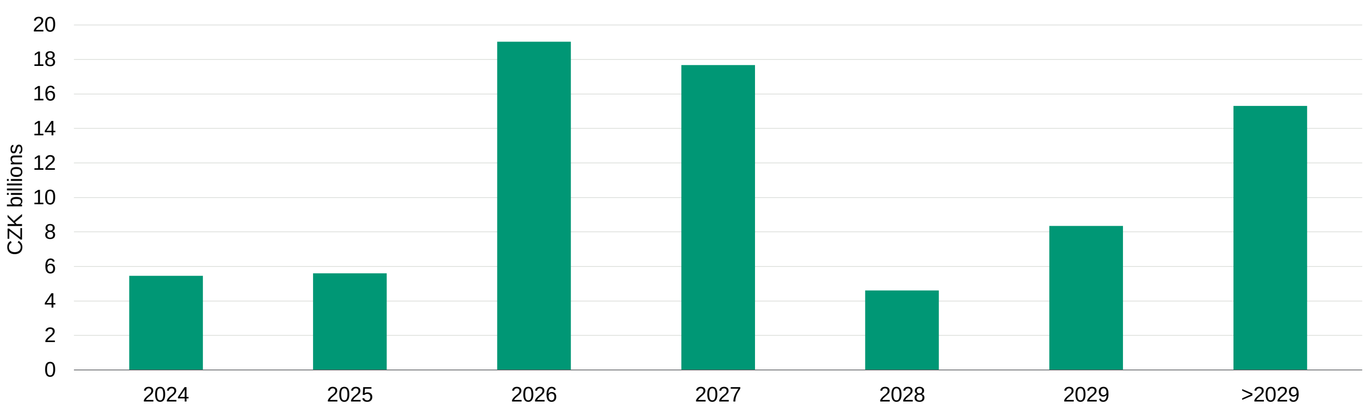
CD's governance risk (**G-3**) is linked primarily to high levels of senior management turnover and concentrated ownership. The company's governance risks are supported by the sovereign governance score; for the Czech Republic this is positive (G-1).

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Liquidity analysis

CD has adequate liquidity, however the approach has been slow and we are assuming that certain facilities under negotiation will be signed in the next few months. The company has access to at least CZK53 billion of liquidity, including CZK7.5 billion unrestricted cash on its balance sheet as of the end of December 2023, CZK10.9 billion availability under committed facilities (with maturities >12 months), a Eurofima loan of CZK4.2 billion, EIB loans of CZK 2.3 billion, new CZK6.4 billion EIB loan and new CZK9.8 billion Eurofima loan which should be signed shortly, subsidies of CZK1.5 billion and operating cash flow, which we estimate at CZK10.4 billion. This available liquidity will comfortably cover the expected capital spending of close to CZK33.8 billion (post-IFRS 16) and debt repayments of CZK5.5 billion in 2024.

Exhibit 6
CD has upcoming refinancing needs in 2024



Source: Company data

Methodology and scorecard

To provide an overall indication of CD's credit quality on a standalone basis (that is, the BCA), we have applied our Passenger Railways and Bus Companies Methodology. The BCA is three notches lower than the 2023 scorecard-indicated outcome of Baa2, and two notches below the forward-looking grid outcome of Baa3, reflecting the company's slow approach to liquidity management and its increasing capital spending needs.

Exhibit 7
Rating factors
Ceske drahy a.s.

Passenger Railways and Bus Companies Industry Scorecard	Current FY Dec-23		Moody's 12-18 month forward view	
Factor 1 : Scale (15%)	**Measure**	**Score**	**Measure**	**Score**
a) Revenue (% billions)	2.2	B	2.3 - 2.5	B
Factor 2 : Business Profile (25%)				
a) Stability of Operating Environment	Baa	Baa	Baa	Baa
b) Market Characteristics	Baa	Baa	Baa	Baa
c) Competitive Environment	A	A	A	A
Factor 3 : Profitability and Efficiency (10%)				
a) EBIT Margin %	13.1%	A	10.6% - 11%	A
Factor 4 : Leverage and Coverage (35%)				
a) Debt / EBITDA	4.5x	Ba	5.1x - 5.3x	Ba
b) RCF / Net Debt	16.3%	Baa	12.4% - 14.5%	Ba
c) (FFO + Interest) / Interest	4.7x	A	4.7x - 5.4x	A
Factor 5 : Financial Policy (15%)				
a) Financial Policy	Baa	Baa	Baa	Baa
Rating:				
a) Scorecard-Indicated Outcome		Baa2		Baa3
b) Actual Rating Assigned				Baa2
Government-Related Issuer	**Factor**			
a) Baseline Credit Assessment	ba2			
b) Government Local Currency Rating	Aa3/Negative			
c) Default Dependence	Very High			
d) Support	High			
e) Actual Rating Assigned	Baa2/Stable			

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Appendix

Exhibit 8
Peer comparison
Ceske drahy a.s.

	Ceske drahy, a.s. Baa2 Stable			Deutsche Bahn AG Aa1 Stable			SNCF S.A. Aa3 Stable		
(in $ millions)	FY Dec-21	FY Dec-22	FY Dec-23	FY Dec-21	FY Dec-22	FY Dec-23	FY Dec-21	FY Dec-22	FY Dec-23
Revenue	1,778	1,898	2,215	55,697	54,894	48,869	41,117	43,684	45,159
EBITDA	364	479	723	3,490	5,319	2,687	6,585	8,188	8,293
EBIT Margin %	-0.9%	4.4%	13.1%	-1.6%	2.0%	-2.7%	4.9%	8.7%	8.6%
(FFO + Interest Expense) / Interest Expense	7.5x	5.0x	4.7x	9.6x	9.7x	6.4x	2.4x	4.1x	4.1x
Debt / EBITDA	6.1x	6.1x	4.5x	13.9x	7.9x	17.3x	14.6x	9.8x	9.4x
FCF / Debt	-11.8%	-22.3%	-6.2%	-6.3%	-2.3%	-13.2%	-1.7%	0.6%	2.0%
RCF / Net Debt	17.1%	13.8%	16.3%	14.7%	16.3%	9.5%	6.6%	17.7%	15.2%

All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. LTM = Last 12 months.
Source: Moody's Financial Metrics™

Exhibit 9
Moody's-adjusted debt reconciliation
Ceske drahy, a.s.

(in CZK millions)	2019	2020	2021	2022	2023
As reported debt	**41,837.0**	**45,548.0**	**48,299.0**	**68,405.0**	**72,760.0**
Non-Standard Adjustments	2.0	-	-	-	-
Moody's-adjusted debt	**41,839.0**	**45,548.0**	**48,299.0**	**68,405.0**	**72,760.0**

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Source: Moody's Financial Metrics™

Exhibit 10
Moody's-adjusted EBITDA reconciliation
Ceske drahy, a.s.

(in CZK millions)	2019	2020	2021	2022	2023
As reported EBITDA	**9,991.0**	**4,533.0**	**8,587.0**	**11,469.0**	**16,038.0**
Unusual Items	(813.0)	260.0	(705.0)	(309.0)	-
Moody's-adjusted EBITDA	**9,178.0**	**4,793.0**	**7,882.0**	**11,160.0**	**16,038.0**

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Source: Moody's Financial Metrics™

Exhibit 11

Overview of selected historical and forecast Moody's-adjusted financial data

Ceske drahy a.s.

(in CZK millions)	2019	2020	2021	2022	2023	2024F	2025F	2026F
INCOME STATEMENT								
Revenue	40,656	35,915	38,534	44,222	49,148	52,710	56,638	59,700
EBITDA	9,178	4,793	7,882	11,160	16,038	16,405	18,510	19,600
EBIT	1,987	(2,955)	(359)	1,966	6,433	5,599	6,247	7,089
Interest Expense	1,186	1,091	1,191	2,041	2,836	2,834	3,056	3,382
BALANCE SHEET								
Cash & Cash Equivalents	8,436	5,751	3,434	8,761	8,119	2,942	2,125	2,462
Total Debt	41,839	45,548	48,299	68,405	72,760	87,419	95,140	104,878
Net Debt	33,403	39,797	44,865	59,644	64,641	84,477	93,015	102,416
CASH FLOW								
Funds from Operations (FFO)	7,441	5,731	7,687	8,253	10,516	10,442	13,483	14,618
Cash Flow From Operations (CFO)	7,682	3,736	6,421	6,457	11,209	11,002	13,483	14,618
Capital Expenditures	(10,742)	(8,725)	(12,101)	(21,740)	15,715	32,327	23,540	25,112
Dividends	12	12	-	-	-	-	-	-
Retained Cash Flow (RCF)	7,429	5,719	7,687	8,253	10,516	10,442	13,483	14,618
RCF / Debt	17.8%	12.6%	15.9%	12.1%	14.5%	11.9%	14.2%	13.9%
RCF / Net Debt	22.2%	14.4%	17.1%	13.8%	16.3%	12.4%	14.5%	14.3%
Free Cash Flow (FCF)	(3,072)	(5,001)	(5,680)	(15,283)	(4,506)	(21,325)	(10,057)	(10,494)
FCF / Debt	-7.3%	-11.0%	-11.8%	-22.3%	-6.2%	-24.4%	-10.6%	-10.0%
PROFITABILITY								
% Change in Sales (YoY)	4.0%	-11.7%	7.3%	14.8%	11.1%	7.2%	7.5%	5.4%
EBIT Margin %	4.9%	-8.2%	-0.9%	4.4%	13.1%	10.6%	11.0%	11.9%
EBITDA Margin %	22.6%	13.3%	20.5%	25.2%	32.6%	31.1%	32.7%	32.8%
INTEREST COVERAGE								
(FFO + Interest Expense) / Interest Expense	7.3x	6.3x	7.5x	5.0x	4.7x	4.7x	5.4x	5.3x
(EBITDA - CAPEX) / Interest Expense	-1.3x	-3.6x	-3.5x	-5.2x	0.1x	-5.6x	-1.6x	-1.6x
EBIT / Interest Expense	1.7x	-2.7x	-0.3x	1.0x	2.3x	2.0x	2.0x	2.1x
EBITDA / Interest Expense	7.7x	4.4x	6.6x	5.5x	5.7x	5.8x	6.1x	5.8x
LEVERAGE								
Debt / EBITDA	4.6x	9.5x	6.1x	6.1x	4.5x	5.3x	5.1x	5.4x
Net Debt / EBITDA	3.7x	8.3x	5.7x	5.3x	4.0x	5.1x	5.0x	5.2x

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Ratings

Exhibit 12

Category	Moody's Rating
CESKE DRAHY, A.S.	
Outlook	Stable
Issuer Rating	Baa2
Senior Unsecured	Baa2

Source: Moody's Ratings

REPORT NUMBER 1404681