

# Credit Analysis

## Moody's International Public Finance Government-Related Issuers

October 2009

### UNEDIC

Paris, France

### Summary Rating Rationale

UNEDIC's<sup>1</sup> Aaa long-term issuer rating and its Prime-1 short-term issuer rating reflect the entity's crucial role in France's social welfare system. Since its creation in 1958, UNEDIC has been the manager of France's Unemployment Insurance Regime (UIR). UNEDIC provides a public service mission and operates under a highly regulated framework. In its strategic role, UNEDIC manages the cash flow of the regime and is in charge of providing unemployment insurance benefits and collecting employers' and employees' contributions. The ratings also take into account the high sensitivity of UNEDIC's financial position to the level of unemployment in France, which can be partly compensated by a powerful fiscal levy that UNEDIC benefits from. Finally, the ratings are also based on UNEDIC's good cash flow management.

As a reflection of the application of Moody's Joint Default Analysis methodology for Government-Related Issuers (GRIs), UNEDIC's ratings are composed of two principal inputs: (i) a Baseline Credit Assessment (BCA) of 3 (on a scale of 1 to 21, where 1 represents the lowest credit risk); and (ii) Moody's assessment of a high likelihood of extraordinary support by France (Aaa, stable) to prevent a default by UNEDIC.

The high likelihood of extraordinary support reflects: (i) the state's commitment to providing unemployment insurance in France; (ii) the political and social implications that would ensue from a failure/discontinuity in providing unemployment compensation; (iii) the reputation risk for the state (should UNEDIC default, this would inevitably raise doubts about the state's support for public entities and possibly about its own commitment to its debt obligations); and (iv) the track record of financial support provided by the state to UNEDIC – through the provision of debt guarantees or direct subsidies – as a consequence of which Moody's considers the probability that the state would allow the entity to default on both its mission and its debt as extremely remote.

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<sup>1</sup> *Union Nationale pour l'Emploi dans l'Industrie et le Commerce* (National Union for Employment in Industry and Trade).

This Credit Analysis provides an in-depth discussion of credit rating(s) for UNEDIC and should be read in conjunction with Moody's most recent Credit Opinion and rating information available on Moody's website. [Click here to link.](#)



## UNEDIC

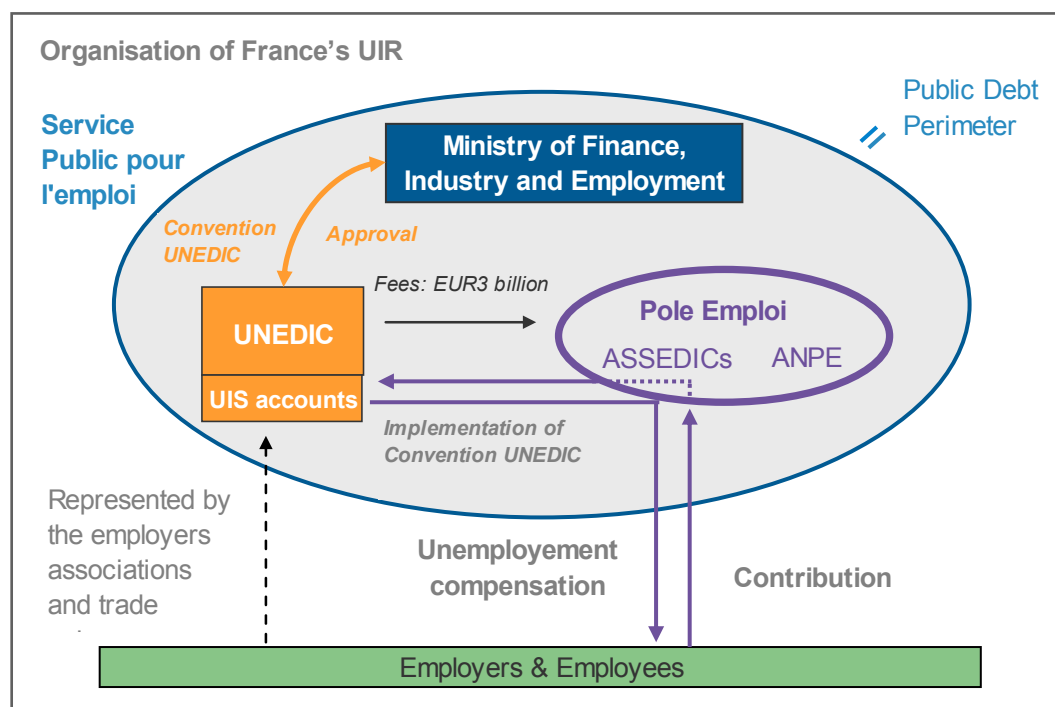
## Rating Outlook

A material change to UNEDIC's institutional and financial framework and to its short-term funding/backing policy could be considered a negative credit factor.

## Issuer Overview

UNEDIC is a not-for-profit entity created under France's "1901 association law" in 1958. Since then, it has fulfilled its mission of managing France's UIR. UNEDIC is jointly and privately managed by the main unions representing employers<sup>2</sup> and employees<sup>3</sup>; each group (employers and employees) is entitled to five seats on UNEDIC's board. The board of UNEDIC determines the UIR contributions to be paid by the employers and employees; the amounts are based on salary levels, as well the level and the lengths of unemployment benefits (the unemployment compensation rules), which affect UNEDIC's financial position. The resolutions relating to contributions are enshrined in a multiyear agreements (together, "the Convention") covering all funding and allowance mechanisms; however, before the agreements apply to all employers and employees in France, the agreements must be approved by the state. Thus, in practice, the Convention is the result of a discussion between the employers associations, the trade unions and the state. The UNEDIC Convention was last renewed and officially approved by the state in February 2009; it applies from 1 April 2009 through 31 March 2011.

**Figure 1:**



Recently, following the state's initiative, the operational arm of UNEDIC, (the ASSEDICs' network<sup>4</sup>), which is in charge of the distribution of unemployment benefit allowances and the collection of the employer and employee contributions throughout France, was merged with the ANPE<sup>5</sup>, the state agency in charge of job searches and placements. The new entity resulting from this merger, *Pole Emploi*, has been entrusted with the former missions of both the ASSEDICs' network and the ANPE by means of an agreement between *Pole Emploi* and UNEDIC. The reform has had only a limited impact on UNEDIC's role: UNEDIC remains the entity

<sup>2</sup> MEDEF, CGPME, UPA.

<sup>3</sup> CFDT, CFE-CGC, CFTC, CGT, CGT-FO.

<sup>4</sup> *Association pour l'emploi dans l'industrie et le commerce* (Association for Employment in Industry and Trade).

<sup>5</sup> *Agence Nationale pour l'Emploi* (National Agency for Employment).

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in charge of funding the unemployment benefit allowances and is the decision maker in this field; UNEDIC's existing and future debt obligations continue to be repaid by UNEDIC. However, UNEDIC no longer has to fulfill the distribution of compensations and collection of contributions; rather, it now pays a fee to *Pole Emploi* for the costs incurred in performing these duties, fixed by law for the year N at 10% of the contributions collected during the year N-2.

In addition, UNEDIC is entrusted with various additional programmes on behalf of the state, which account for a small part of UNEDIC's budget (less than 5%).

## Key Rating Considerations

### Institutional Framework

#### UNEDIC's status and role is very unlikely to be challenged

Unemployment insurance is a state responsibility<sup>6</sup> in France; therefore, the management and the organisation of the UIR are considered to be in the interest of the general public. UNEDIC was entrusted with the management of the UIR by the state in 1958, when UNEDIC was created. In more than 45 years, UNEDIC's role has been confirmed by various agreements. In fact, UNEDIC's key role in providing a public service mission was reconfirmed in a 2005 law that created a *Service Public de l'Emploi* ("SPE", or public employment service). Under this law, three entities – UNEDIC, the state and the ANPE – were entrusted with the SPE and UNEDIC's exclusive role as the insurer against unemployment was confirmed. Additionally, although UNEDIC is not subject to a regular audit carried out by France's court of audit (*Cour des comptes*), a state representative (*Contrôleur d'Etat*) is in charge of controlling UNEDIC and attends all of UNEDIC's board meetings as a non-voting member.

#### As a public service provider, UNEDIC has a strictly regulated framework under which it must balance the UIR

The unemployment compensation rules to be enforced by all employers and employees located in France are defined in the Convention, which must be approved by the state before becoming compulsory. Moreover, the law (*Code du travail*) requires that these compensation rules guarantee UIR's financial balance. In an event of a lack of agreement between the employers associations and the trade unions, the law stipulates that the state could take over UNEDIC and ultimately entrusts the UIR's management to a public entity with EPA status (*Etablissement Public à caractère administrative*, or public administrative status). Consequently, if the economic environment deteriorates and the terms of the incumbent agreement no longer ensures the financial balance of the system, or if the state were to judge that there were a discrepancy between the agreement and the law, UNEDIC is obliged to redefine the agreement. If UNEDIC were to fail to redefine a convention with which the state agrees, this later could refuse to grant or could withdraw its approval; alternatively, as in 1982-83 and 2000, the state could temporarily take over the regime and rule it by decree.

Generally, given that UNEDIC's debt is consolidated within France's general government debt, the state is very concerned that the unions' and employers' representatives do not adopt costly measures, which could lead to significant budget imbalances for UNEDIC, and in turn for itself.

#### Strong, ongoing support by the state is evidenced by the extra funding and debt guarantee that the state granted UNEDIC

UNEDIC does not enjoy any automatic or *a priori* support from the state. However, on numerous occasions over the past 20 years, the state has indicated its strong commitment to supply additional funding – through annual subsidies, as in 1994 – or its explicit guarantee to debt issued by UNEDIC (in 2003 and 2005). Usually, these types of arrangements are part of the discussions that take place every time the Convention is negotiated between the state – which generally has strong views on how the unemployment allocation system

<sup>6</sup> France has signed all European and international agreements that acknowledge the unemployment insurance system as a compulsory "social security" responsibility.

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should work – and the unions. In the past, the debt guarantee has been granted to compensate for some costly measures requested by the state.

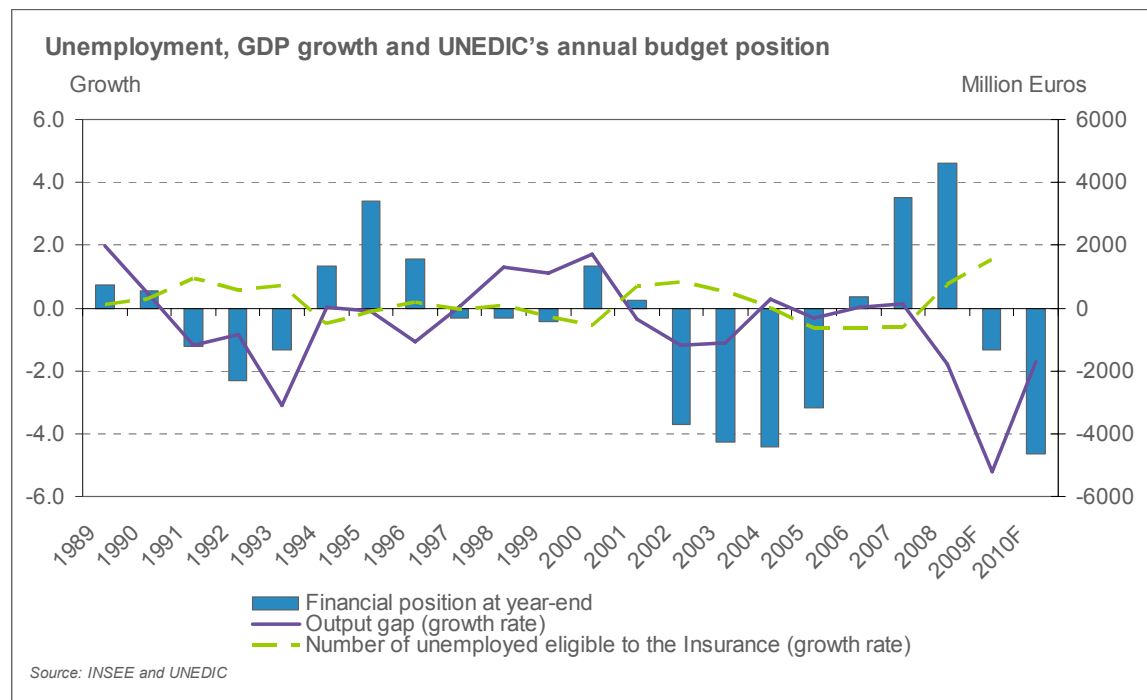
## Financial Position and Performance

### A budget position highly sensitive to the macro-economic trend and structurally difficult to balance

UNEDIC's financial position is closely linked to the level of unemployment and, more generally, to the country's economic performance through the GDP growth rate. Therefore, the regime's sensitivity to the evolution of macroeconomic indicators is predictable. The recently introduced two-year lag between a potential drop in the collected contributions and the subsequent decrease in the fee to be paid by UNEDIC to *Pole Emploi* further increases the sensitivity of UNEDIC's budget position to the level of unemployment.

Moreover, UNEDIC's budget position tends to be structurally imbalanced. Indeed, the gap between the benefit allowances and the contributions is a function of (i) the unemployment compensation rules, (ii) the wages paid in total (*masse salariale*), and (iii) the number of unemployed people. Given that, in the long term, the unemployment level is asymmetrically rigid downward to movements in the output gap (measured as the difference between the real GDP growth rate and the potential GDP growth rate)<sup>7</sup>, the surpluses generated during periods of economic expansion can not compensate for the surpluses generated during periods of economic downturn (assuming that everything is equal).

**Figure 2:**



<sup>7</sup> Over the 1985-2008 period, assuming a potential GDP growth rate of 2.2%, in expansion period (i.e. when the output gap is positive), the decrease pace of unemployment's level (source UNEDIC) is three times less than the increase in GDP, and in recession period (i.e. when the output gap is negative), the increase pace of unemployment level is two times more than the decrease in GDP.

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**Despite a significant fiscal levy, UNEDIC's responsiveness is constrained, as any actions to be taken need a consensus between the state, the unions and the employers' representative**

In theory, the fiscal levy that UNEDIC benefits from is significant. Indeed, as the subscription to the UIR is compulsory for all employers and employees located in France, the fiscal base (salary levels) under which the contributions are raised is wide. At year-end 2008, 16.5 million employees paid contributions to UNEDIC. However, every change in the unemployment compensation rules that would help to balance UNEDIC's budget position needs to be amended in a new agreement that requires approval by all the players. This political nature of UNEDIC's decision-making process can hinder the timeliness of major decisions, such as an increase in the employees' and employers' contributions. As a result, UNEDIC has often had to finance a significant annual deficit, between EUR0.3 billion (1998) and EUR4.4 billion (2004), reaching a maximum of EUR13.5 billion on an accumulated basis in 2005. At year-end 2008, UNEDIC managed to release a surplus of EUR4.6 billion, leading to an accumulated deficit of EUR5 billion.

**In the current context of rising unemployment, deficits will occur, increasing financing needs going forward**

In its regular publication (*Equilibre financier de l'Assurance Chômage*), dated 26 May 2009, UNEDIC officially forecast deficits for 2009 and 2010 based exclusively on macroeconomic assumptions. UNEDIC expects deficits to reach EUR1.3 billion in 2009 and EUR4.9 billion in 2010, leading to an accumulated deficit of EUR10.9 billion at year-end 2010. While these deficits will oblige UNEDIC to increase its debt to a considerable amount (EUR10.9 billion at year-end 2010), this level still compares well with UNEDIC's past track record (debt stock peaked at EUR13.2 billion in 2005).

Beyond 2010, as the trend is unlikely to abruptly reverse, Moody's believes that some modifications in the unemployment compensation rules are likely to be submitted by the employers' and employees' unions for the approval by the state to restore UNEDIC's fiscal position. Indeed, these players are likely to take action to curb the expected deteriorating trend, because: (i) the new Convention will be negotiated as of Q4 2010 so that an agreement is reached by February 2011; and (ii) UNEDIC is not used to having a persistent deficit, as it must balance the UIR's financial position under law.

**Debt & Liquidity****To avoid heavily relying on short-term funding, UNEDIC will resort to medium- to long-term funding**

Historically, UNEDIC has relied heavily on its CP programme (*Billet de Trésorerie*) for funding needs. Indeed, in normal business conditions, UNEDIC has mainly faced a structural negative monthly net working capital (BFR), as a lag exists between the unemployment compensation payments made by UNEDIC and the receipt of the contributions from employers and employees. Indeed, UNEDIC pays two-thirds of its contributions in the first five days of the month, while it only receives around 15% of contributions during this period. In 2009, the BFR reached, on average, -EUR1.2 billion, and represents -EUR1.6 billion (April 2009) – the highest attained in a month. The threshold of its CP programme is currently sized at EUR3 billion, which is 100% covered by dedicated and committed back-up lines. UNEDIC is now projecting to increase its ECP programme up to EUR6 billion to respond in the most efficient way to the more adverse economic conditions.

As the deficits are expected to persist in the medium term, UNEDIC expects that it will refinance long-term an important part of its short-term debt via an EMTN programme, planned to be sized at EUR12 billion, in line with UNEDIC's forecasts.

**Loss of market access is very unlikely...**

Moody's does not expect UNEDIC to face restricted access to the market. Indeed, over the past few decades, French banks have consistently supported UNEDIC by bridging short-term gaps; thus, it has never been short of cash. Loss of market access has never been an issue given the banking community's understanding of

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UNEDIC's highly cyclical position and confidence that UNEDIC's financial balance will ultimately be restored with or without central government support.

### **UNEDIC enjoys a predictable cash position with secured external short-term funding**

UNEDIC's cash position is predictable in the short term; it mainly changes in line with:

- The monthly receipt of the contributions that represent more than 95% of the total revenues received by UNEDIC. Their evolution is related to the development of unemployment in France, as well as the evolution of wages.
- The monthly compensation payments, which are also linked to the unemployment rate.
- The payment of subsidies to *Pole Emploi*, which are, by law, set at a fixed rate of 10% of the contributions received by UNEDIC.

Over the past 18 months, UNEDIC recorded maximum daily short-term funding needs of EUR4.3 billion in April 2009. During this period, the institution secured sufficient access to credit facilities to cover these short-term financing needs in the form of (i) a EUR3 billion CP programme, 100% backed by dedicated lines, and (ii) an agreed overdraft of up to EUR1.5 billion (but uncommitted).

The forecast short-term financing needs of UNEDIC are matched by the external funds available. Indeed, over the next two years, UNEDIC expects to reach a maximum short-term funding need of EUR5.5 billion. To cover these liquidity requirements, UNEDIC intends to increase its CP programme to EUR6 billion. In the meantime, it is planning to realise a conservative investment portfolio of approximately EUR1 billion in September 2009 (before then, the forecast maximum short-term funding need is expected to materialise), which should allow UNEDIC access to funds in case of need for its CP redemptions. With this portfolio, the liquidity facilities previously cited (EUR3 billion of back-up lines and EUR1.5 billion of overdraft facilities) will increase to EUR5.5 billion.

### **Governance and Management Factors**

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UNEDIC is jointly and privately managed by the main unions representing employers and employees, with each group entitled to five seats on UNEDIC's board. These unions' representatives constitute the legislative body of UNEDIC, and decisions need a majority vote by each group (the employers associations and the trade unions). Moreover, UNEDIC is overseen by a state representative (*Contrôleur d'Etat*), who attends all board meetings as a non-voting member.



## UNEDIC

<b>UNEDIC</b>							
€ 000,000's	31/12/2008	31/12/2007	31/12/2006	31/12/2005	31/12/2004	31/12/2003	31/12/2002
<b>Income Statement</b>							
<b>TECHNICAL SECTION</b>							
<b>TOTAL REVENUES</b>	30,636.30	29,843.24	28,733.90	27,229.72	26,282.01	25,733.09	23,270.01
Contributions	30,339.36	29,536.29	28,351.10	26,708.42	25,678.67	24,870.91	21,805.21
Use of reserves	33.47	27.34	27.00	88.40	273.99	628.57	1,190.22
Other	263.47	279.60	355.80	432.90	329.36	233.61	274.58
<b>TOTAL EXPENDITURES</b>	24,342.44	24,301.85	25,893.70	28,046.74	29,014.87	28,163.53	25,363.29
Allocation unique degressive	N/A	N/A	N/A	8.18	648.28	1,351.21	2,188.89
Allocation retour a l'emploi	19,582.37	19,639.12	20,969.50	23,102.03	22,835.48	20,792.65	15,971.76
Autres allocations	N/A	N/A	N/A	1,791.71	2,245.35	2,896.30	3,764.23
Aides du fonds							
Aides PARE	822.27	761.96	428.20	395.30	428.65	357.91	306.73
Validation des points de retraite	1,447.31	1,240.29	1,622.40	1,620.05	1,679.69	1,524.29	2,026.12
Other	979.89	1,076.16	1,117.60	1,123.76	1,172.23	1,236.42	1,104.20
Provision for depreciation	3.09	37.77	34.80	5.71	5.21	4.75	1.36
<b>TECHNICAL SECTION BALANCE</b>	<b>6,293.86</b>	<b>5,541.39</b>	<b>2,840.20</b>	<b>-817.01</b>	<b>-2,732.86</b>	<b>-2,430.44</b>	<b>-2,093.29</b>
<b>ADMINISTRATIVE SECTION</b>							
<b>TOTAL REVENUES</b>	424.37	192.08	196.60	203.86	196.90	178.01	207.61
Provision of services	232.30	180.64	186.30	186.99	182.94	160.26	171.91
Use of reserves	185.26	5.53	N/A	4.29	0.62	3.61	7.26
Other	6.80	5.90	N/A	12.57	13.34	14.15	28.43
<b>TOTAL EXPENDITURES</b>	1,483.07	1,582.73	1,546.80	1,519.45	1,498.05	1,443.48	1,453.72
Personal expenditure	757.73	848.40	825.30	808.81	776.61	753.37	738.23
External services	543.61	528.41	499.60	496.21	479.86	471.72	495.43
Other	102.27	113.31	109.90	106.25	107.04	104.92	104.38
Provision for depreciation	79.45	92.61	112.00	108.19	134.55	113.47	115.68
<b>ADMINISTRATIVE SECTION BALANCE</b>	<b>-1,058.70</b>	<b>-1,390.65</b>	<b>-1,350.20</b>	<b>-1,315.60</b>	<b>-1,301.16</b>	<b>-1,265.46</b>	<b>-1,246.12</b>

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€ 000,000's	31/12/2008	31/12/2007	31/12/2006	31/12/2005	31/12/2004	31/12/2003	31/12/2002
<b>FINANCIAL &amp; EXCEPTIONAL SECTION</b>							
<b>FINANCIAL SURPLUS / DEFICIT</b>	-264.37	-424.02	-417.20	-346.31	-236.46	-112.49	143.36
Financial revenues	13.51	0.00	0.00	0.01	0.17	9.24	247.32
Interest charges	275.09	419.08	N/A	341.48	233.28	120.76	102.46
Provisions	2.79	4.94	N/A	4.84	3.35	0.96	1.51
<b>EXCEPTIONAL SURPLUS / DEFICIT</b>	3.62	1.62	452.80	4.12	1.70	-1,272.75	-12.36
Exceptional revenues	8.19	8.68	N/A	30.80	17.99	41.56	35.57
Exceptional expenditures	4.58	7.06	N/A	26.69	16.29	1,314.30	47.93
<b>COMPANIES TAXE</b>	0.04	0.04	N/A	0.03	0.01	0.02	0.00
<b>GENERAL BALANCE</b>	<b>4,974.37</b>	<b>3,728.30</b>	<b>1,525.60</b>	<b>-2,474.84</b>	<b>-4,268.79</b>	<b>-5,081.16</b>	<b>-3,208.41</b>

UNEDIC

## Moody's Related Research

### Analyses:

- France, Government of, February 2008 (107421)

### Rating Methodology:

- The Application of Joint Default Analysis to Government Related Issuers, April 2005 (92432)

*To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.*

Report Number: 119607

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