S&P Global Ratings

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Swisscom AG

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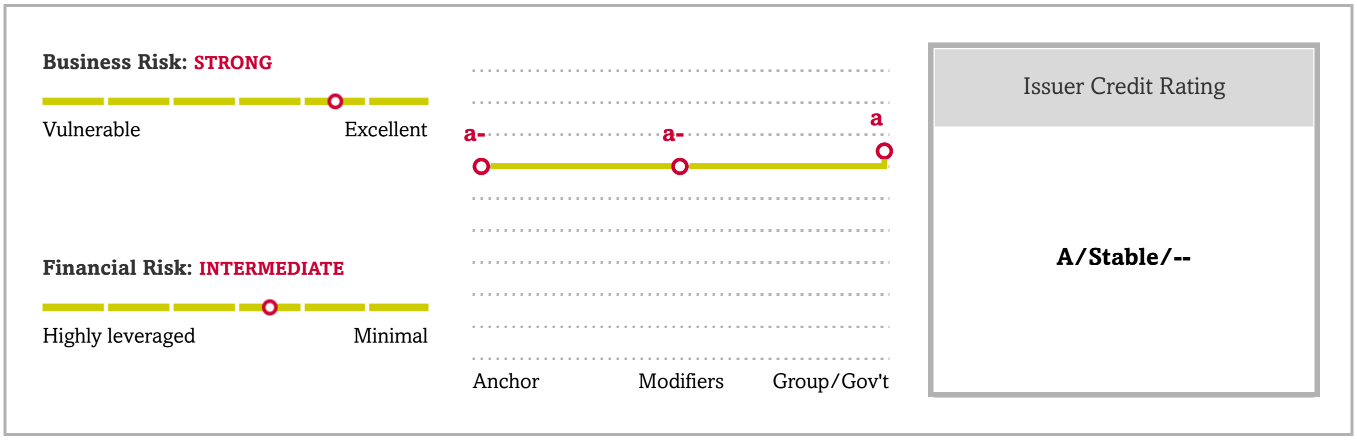


Credit Highlights

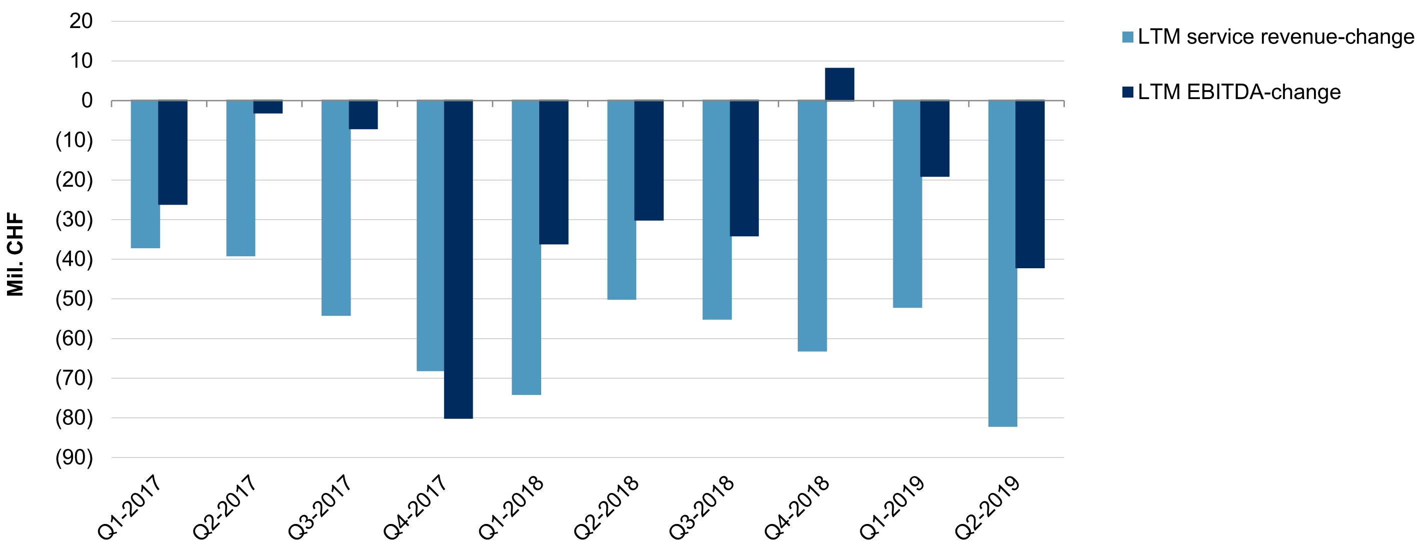
Overview

Key Strengths	Key Risks
Leading position in fixed and mobile markets in Switzerland, a wealthy, quality-focused service area, with a 51% retail market share in fixed broadband, and about 58% in mobile postpaid.	Intense competition in the saturated domestic fixed and mobile markets, steadily eroding Swisscom's telecom service revenues.
High-quality fixed and mobile networks, with about 30% fiber-to-the-home (FTTH) and 99% fourth-generation (4G), as well as expanding fifth-generation (5G) mobile population coverage, supporting premium market positioning, and pricing.	Pending Sunrise-UPC merger could further increase competition based on fixed-mobile convergence products between Swisscom, Sunrise-UPC, and Salt.
Favorable regulation that does not mandate regulated access to Swisscom's next generation networks, giving the company flexibility to set wholesale access prices on commercial terms.	High capital expenditure (capex) of Swiss franc (CHF) 2.2 billion–CHF2.3 billion annually and Fastweb's limited cash flow generation constrain free operating cash flow (FOCF) to 13%-15% of adjusted debt (before spectrum payments).
Conservative and predictable financial policy, supporting S&P Global Ratings-adjusted debt to EBITDA of maximum 2.5x and funds from operations (FFO) to debt of at least 35% in our forecast for 2019-2021.	FTTH network expansion by Swiss utilities to more than two million homes may reinforce competition between network infrastructures and pose certain risks to Swisscom's wholesale revenues in the long term.
Predictable, albeit somewhat inflexible, dividend policy, targeting stable pay-outs of about CHF1.1 billion annually.	

Although steady pressure on domestic service revenues could affect the ratings further out, the impact has been offset by continuous cost-cutting so far. We generally view conditions in the Swiss telecom market as more benign than in other European markets. This is because Switzerland houses a wealthy customer base with a strong focus on quality, supporting favorable pricing. However, with a fixed broadband penetration rate of about 47% of the population, the highest in the OECD and a mobile phone penetration of about 132% (data from end-December 2018), we regard the Swiss telecom market as highly saturated. This, alongside increasing competition and the structural decline in fixed voice, has contributed to declines of 2%-5% in Swisscom's domestic telecom service revenues over the past few years. So far, Swisscom has succeeded in containing a significant part of associated EBITDA drag with cost-efficiency programs (see chart 1). The company is targeting additional savings of at least CHF200 million in 2019–2020, after successful cumulative cost reductions of CHF233 million over 2016–2018. In our view, streamlining costs is likely to become more difficult over time, indicating that credit metrics could come under pressure over the longer term if service revenue losses continue at this pace or accelerate over a prolonged time period. However, given our forecast of annual revenue declines of 1.5%-4.0% in Switzerland, we do not believe this scenario will materialize over the next two years.

Chart 1

Swisscom's Cost-Cutting Reduces Service Revenue Loss Impact On EBITDA
Change in LTM service revenue and EBITDA

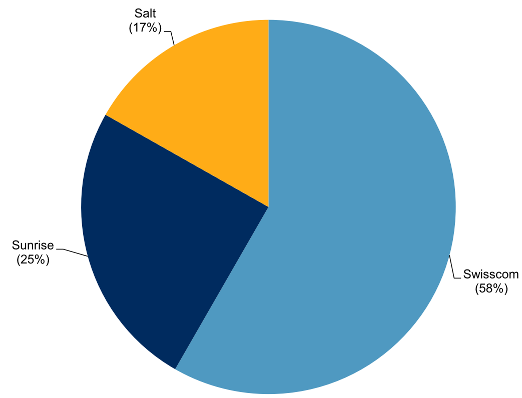


EBITDA after leases used for Q1 and Q2 2019. LTM--Last 12 months. CHF--Swiss franc. Source: S&P Global Ratings.

Heightening competition in Switzerland is unlikely to threaten Swisscom's dominant position but will exert steady pressure on pricing. Swisscom enjoys strong market positions across both residential and business customer segments in the Swiss telecom market. At year-end 2018, the company held a 58% mobile subscriber market share and a 51% share of the retail fixed broadband market (data by national regulator ComCom). This is well ahead of competitors Sunrise, UPC, and Salt, and materially higher than the average market shares of European incumbent telecom operators (see charts 2 and 3).

Chart 2

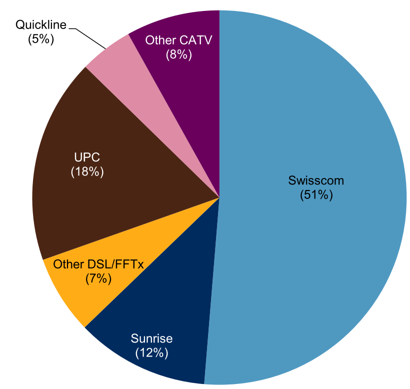
Mobile Subscriber Market Shares In Switzerland (Dec. 2018)



Source: ComCom, S&P Global Ratings.

Chart 3

Broadband Subscriber Market Shares In Switzerland (December 2018)

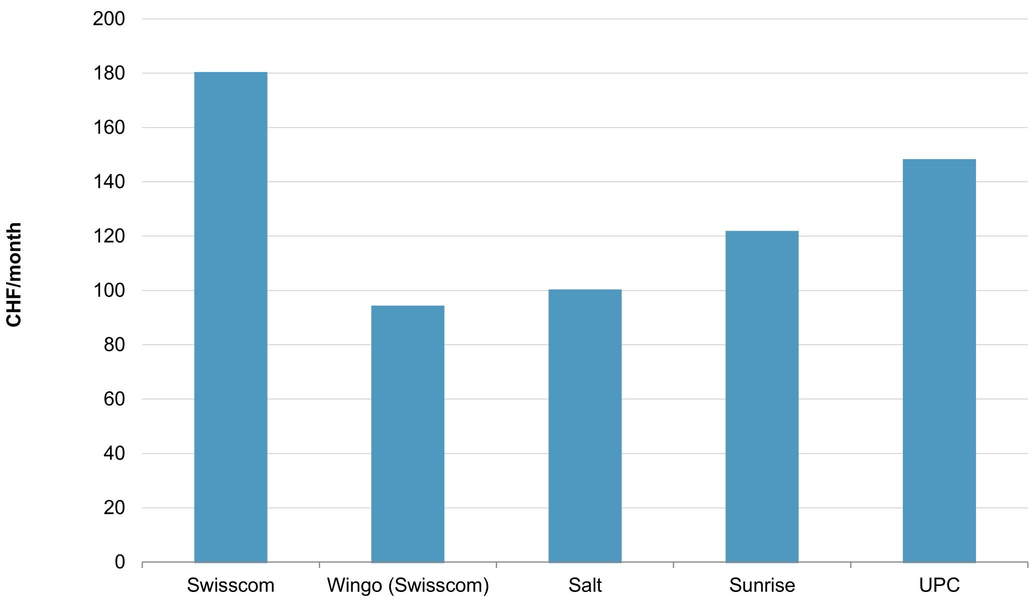


Source: ComCom, S&P Global Ratings.

However, we have observed an uptick in competition over the past few years in mobile, broadband, and TV services. Since the launch of Salt's fixed broadband and TV offer in the first half of 2018, all four major players now provide the full range of services, and competition is increasingly centered on fixed-mobile bundles (triple or quadruple-play offers). Other players' products are often priced at marked discounts to Swisscom (see chart 4), and we expect attractively priced bundles will continue to constrain pricing in the overall market and force Swisscom to offer greater discounts or serve more customers through no frills brands such as Wingo.

Chart 4

Prices For Comparable 4P Bundles Per Operator



Note: 4P Offers include following minimum services: (1) Unlimited mobile voice and highspeed broadband in Switzerland; (2) 200 Mbit broadband; (3) 150 TV channels and replay/recording function; (4) unlimited domestic fixed-voice calls. Wingo offer excludes unlimited fixed-voice calls becauuse this product is not available. Wingo includes 2GB of mobile data. CHF--Swiss franc Source: Companies' websites.

The pending merger between no. 2 mobile operator Sunrise and cable TV and no. 2 broadband operator UPC (expected to close in fourth-quarter 2019) could further reinforce competitive headwinds for Swisscom, in our view, since it would provide the combined entity with enhanced cross-selling opportunities across the two customer bases. However, up to this point, competition has done little to challenge Swisscom's market shares, which are down about 1 percentage point in broadband and nearly unchanged in mobile since 2014, according to the company data. We forecast Swisscom to cede some incremental market share in the next three years, but we think its position will be somewhat protected based on our expectation that price sensitivity in Switzerland will remain lower than in other markets, its strong brand, focus on the premium segment, and fostering retention with bundled offers. As of June 30, 2019, about 43% of Swisscom's retail broadband customers subscribed to one of its fixed-mobile bundles--four percentage points higher than a year ago.

Swisscom's conservative financial policy implies very low re-leveraging risk. We continue to view Swisscom's financial policy as conducive to protecting the company's strong credit metrics. Swisscom targets a net debt-to-EBITDA ratio of about 1.9x, as per the group's definition (excludes the effects of the new lease accounting standard), with an actual ratio of 1.75x at end-2018. Similarly, we perceive Swisscom's dividend policy as very predictable, underpinned by a track record of constant payouts of about CHF1.1 billion per year since 2011. That said, we consider that the group's declared objective to pursue stable dividends may somewhat limit its willingness to reduce distributions, if necessary. The company has not engaged in major acquisitions since the purchase of Fastweb in 2007, and we consider

M&A-related event risk as very low. These policies will likely continue to keep its S&P Global Ratings-adjusted debt to EBITDA at or below 2.5x and adjusted FFO to debt of at least 35% in the next three years. However, we forecast Swisscom's high annual capex of CHF2.2 billion–CHF2.3 billion (excluding spectrum) will cap adjusted FOCF to debt at 15% over this period. Considering dividends of more than 80% of free cash flow, in our base case we assume the company's organic de-leveraging capacity through discretionary cash flow after lease payments will be limited to about CHF100 million–CHF300 million annually.

Outlook: Stable

The stable outlook reflects our view that, despite increasing competition, Swisscom will be able to avert a significant erosion of its market position in Switzerland and domestic service revenue declines materially exceeding our expectations. We also expect Swisscom will continue to partly cushion the ongoing pressure on service revenues with cost-savings. We think this will allow Swisscom to maintain an S&P Global Ratings-adjusted debt to EBITDA at no higher than 2.5x and adjusted FFO to debt of at least 35% over 2019-2020. In addition, we expect the Swiss government will retain its majority ownership of Swisscom over the long term.

Downside scenario

We could lower the rating if more intense competition, combined with diminishing opportunities for cost-savings, led to stronger pressure on service revenues and EBITDA than we currently expect, causing a lasting deterioration of our adjusted debt to EBITDA to above 2.5x and FFO to debt below 35%. Such a scenario could result from increasing competition with fixed-mobile convergence products and heightened price pressure in both the business-to-consumer (B2C) and business-to-business (B2B) segments, compounded by the structural decline of landline voice services and difficulties achieving growth in Swisscom's IT solutions business. Alternatively, the privatization of the company could lead to a one-notch downgrade to align the rating with its stand-alone credit profile, but we think the risk of this occurring is slim.

Upside scenario

We could raise our rating on Swisscom if stable competitive conditions supported sustainable improvements in the trajectory of revenues and EBITDA, enabling Swisscom to strengthen its adjusted debt-to-EBITDA ratio to below 2x on a sustainable basis. This improvement would also require the group to revise its financial policy to be even more conservative, which we think is unlikely at this stage.

Our Base-Case Scenario

Assumptions

- Swiss real GDP growth slowing to 1.3% in 2019 from 2.6% in 2018, and 1.4% in 2020, accompanied by consistently low unemployment rates of 2.6%-2.8% during this period. We believe the slowdown in growth is unlikely to affect revenue prospects with retail customers, but it may add somewhat to topline pressure with business customers.
- For the Swiss telecoms market overall, we project flattish mobile subscription numbers (excluding M2M SIM cards) in 2019 and 2020, and we expect the remaining very modest increases in total fixed broadband lines to flatten out over this period. Moreover, we expect Swisscom to cede some incremental subscriber market share to competitors in both segments.
- An annual average €/CHF exchange rate of about 1.13 in 2019 and 1.16 in 2020, compared with 1.16 in 2018.
- Payments of CHF196 million for spectrum acquired in Switzerland in 2019, after CHF71 million spectrum purchases in Italy in 2018.
- Cash outflows of CHF240 million for the acquisition of the 31% minority stake in Swisscom Directories and CHF90 million earn-out payments in connection with the acquisition of Tiscali assets in Italy in 2019.
- Stable dividend payouts of CHF22 per share in 2019 and 2020, as targeted by Swisscom, at the same level as in 2018, resulting in total annual distributions of CHF1.14 billion.

Key Metrics

	2018A	2019E	2020E
Revenues (bil. CHF)	11.7	11.4–11.5	11.3–11.5
EBITDA margin (%)	37.6	38-39	37-39
Capex/sales (%)*	19.9	19.5–20.5	19.5–20.5
Debt/EBITDA	2.2	2.3–2.5	2.3–2.5
FFO/debt (%)	39.6	36-38	35-38
FOCF/debt (%)	14.6	12-14	13-15
FOCF/debt (%)*	15.3	13-15	13-15

All data adjusted by S&P Global Ratings, except capex to sales. FFO--Funds from operations. FOCF--Free operating cash flow, defined as cash flow from operations after investments in property, plant, and equipment, and intangible assets. *Excluding spectrum. CHF--Swiss franc. A--Actual. E--Estimate.

Base-case projections

We foresee continued revenue decline in Switzerland, driven by lower retail and enterprise service revenue. We project declines in domestic revenue of 2.5%-4.0% in 2019 and 1.5%-3.0% in 2020, after a 2.7% contraction in 2018, owing to price pressure for connectivity services in the enterprise segment, price discounts for convergence products, and some small-scale customer attrition in the retail segment, and the structural decline in fixed voice lines. The improvement in 2020 is mainly linked to our expectation of a stabilization in Swisscom's IT solutions business with enterprise customers.

We think Fastweb will help stabilize the group's topline from 2020. We forecast between 0.0% and 1.0% revenue growth at Fastweb in 2019, down from 8% in 2018, but rebounding to 5%-7% growth in 2020. The temporary dip in growth in 2019 mainly owes to some one-time revenue in 2018. In our base case, this will support about flat group revenues in 2020, after our estimate of decline of 2.0%-3.0% in 2019 and 0.4% growth in 2018. In our view, underlying growth at Fastweb will mainly be fueled by ICT solutions in the B2B segment, some subscriber growth in consumer mobile and broadband, and marketing Fastweb's fiber network to other fixed and mobile players in Italy, for example for fiber base station backhaul.

Service revenue pressure is set to weigh on EBITDA margins in the medium-term, but we expect decreasing capex to counter the free cash flow impact. In 2019, we foresee that successful cost reductions, paired with a small effect from the implementation of the new lease accounting standards, will support an increase in our adjusted EBITDA margins to 38%–39% from 37.6% in 2018. Over time, however, we think it will become more difficult for Swisscom to offset declining service revenues in Switzerland with cost-cutting. Combined with margin dilution from the increasing share of lower-margin information and communications technology (ICT) solutions, this is captured in our projection of adjusted EBITDA margins beginning to gradually deteriorate within the 37%-39% range from 2020 onwards. At the same time, we expect capex to stay high at around 20% of sales in 2019 and 2020, excluding spectrum, but to gradually decrease on an absolute basis as Swisscom realizes certain efficiencies in its network investments at home. This should support relatively constant reported FOCF after leases of CHF1.3 billion–CHF1.4 billion.

Company Description

Swisscom AG is the leading telecommunications operator in Switzerland, offering fixed and mobile telephony, broadband and TV services for residential and business customers, as well as ICT solutions for businesses. Swisscom also owns 100% of Italian telecom operator Fastweb. As of June 2019, Swisscom served about 6.4 million mobile, 2.0 million retail broadband, and 1.5 million TV subscribers in Switzerland, as well as 2.6 million broadband and 1.6 million mobile subscribers in Italy. The largest shareholder, with a 51% stake, is the federal government of the Swiss Confederation.

Business Risk: Strong

High-quality networks support market position but require high capex. In our view, Swisscom's market position is supported by its high-quality fixed-line and mobile networks. By the second quarter of 2019, Swisscom was able to offer broadband download speeds of at least 80 megabits per second (Mbps) to about 68% of all Swiss residential and business premises, and download speeds of at least 200 Mbps to 40% of premises. By 2021, the group aims to cover 75% of homes and businesses with 200 Mbps, and 90% with 80 Mbps. Also, although Swisscom employs a mix of network technologies, it covers about 30% of premises with FTTH, currently the fastest fixed-line technology. However, Swisscom's network competes with two major other infrastructures for high-speed fixed broadband, namely the network of cable TV operator UPC (about 60% household coverage as by Sunrise) and the network of Swiss Fiber Network (SFN), a joint-venture of Swiss utility companies. In second-quarter 2019, SFN signed an agreement with Sunrise and Salt to expand FTTH coverage to more than two million households over the next five to 10 years (greater 54% household coverage by our estimate). Increased utilization of UPC's and SFN's networks by Sunrise and Salt could pose a risk to Swisscom's high-margin wholesale access revenues (CHF282 million in 2018) over time, in our view.

In mobile, Swisscom covers 99% of the Swiss population with 4G mobile networks, and 95% have access to 4.5G with speeds of up to 300 Mbps. However, Swisscom's competitors have reached similar coverage levels, with virtually

100% 4G population coverage reported by Sunrise and 97% by Salt. All operators are preparing or already launching 5G services with a view to enhancing their respective networks' positioning.

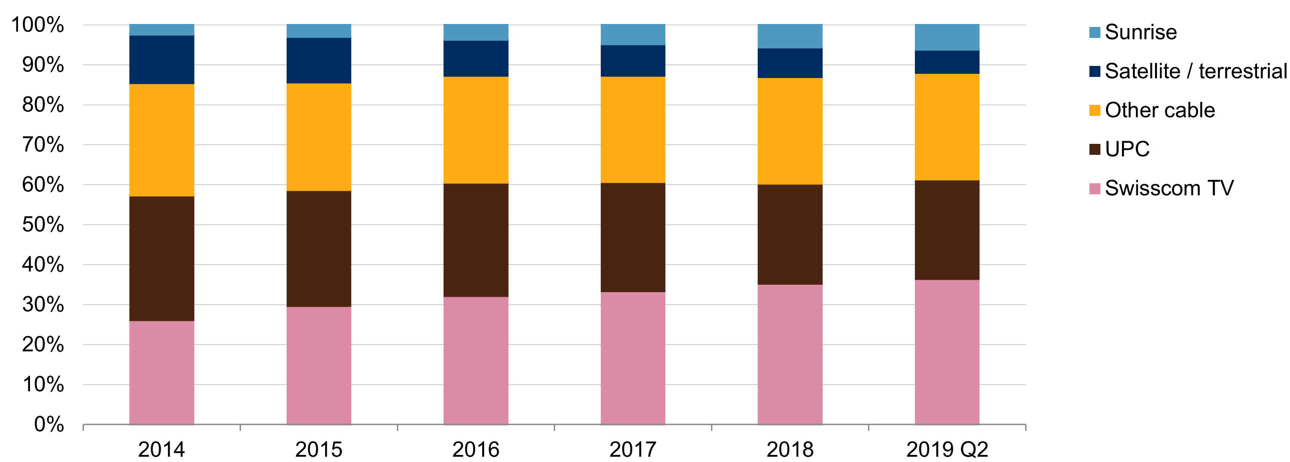
Swisscom's fixed and mobile network upgrade plans require continued substantial investments, resulting in capex of about 19%-21% of 2015-2018 revenues, and we expect annual capex to remain close to this level for the next three years.

Favorable regulation in Switzerland. We expect the regulatory environment in Switzerland to remain relatively benign compared with other European markets. For example, unlike incumbent operators in EU countries, Swisscom is not subject to access and price regulation for its high-speed broadband network. Although lawmakers deliberated a potential change to this as part of an ongoing review of Swiss telecom legislation, the proposal was rejected, and we do not anticipate any other significant tightening of regulatory oversight.

Leading position in TV, but rapid drop in legacy fixed voice. Swisscom has successfully used its Internet-protocol-TV (IPTV) offering to increase its market share in TV services in the past few years to about 36% by mid-2019, according to group estimates, at the expense of UPC (25%), other cable operators (27%), and terrestrial and satellite TV.

Chart 5

TV Market Shares In Switzerland



Source: Swisscom, S&P Global Ratings.

At the same time, Swisscom faces strong revenue pressure in fixed voice. This stems from a more rapid structural decline of this segment than in other European countries. As of June 30, 2019, Swisscom operated about 1.7 million fixed telephony lines, down by more than 35% compared with four years ago.

Fastweb continues to grow in a competitive Italian market, but cash contribution still limited. We continue to view operating trends at Swisscom's Italian subsidiary Fastweb as robust. Fastweb benefits from ongoing investments in its fiber network, the lack of competition from cable operators, and some, albeit decelerating, growth in Italy's fixed broadband penetration. It has therefore been able to expand its broadband subscriber base by more than 3.5% each year since 2014, and held a broadband subscriber market share of approximately 15% as of the first quarter of 2019, well behind leader Telecom Italia (43%), but similar to Vodafone (16%) and Wind Tre with 14% (data according to national regulator AGCOM). However, Fastweb is currently the leader for fast broadband lines with 100 Mbps or more, with a market share of about 39% (first-quarter 2019), followed by Vodafone (34%). By end-2018, Fastweb provided about 29% of Italian households and business sites (8 million premises) with download speeds of at least 200 Mbps based on its own FTTH and fiber-to-the street network (including coverage through its joint venture with Telecom Italia). In addition, Fastweb covers another 14% of premises through the fixed-wireless-access (FWA) network acquired from Tiscali in 2018, and intends to double FWA coverage by 2024. In 2017, Fastweb entered the Italian mobile market with an MVNO offering, and has since gained about 1.6 million mobile subscribers (equivalent to about 2% market share), with a longer term target of 4%-5%.

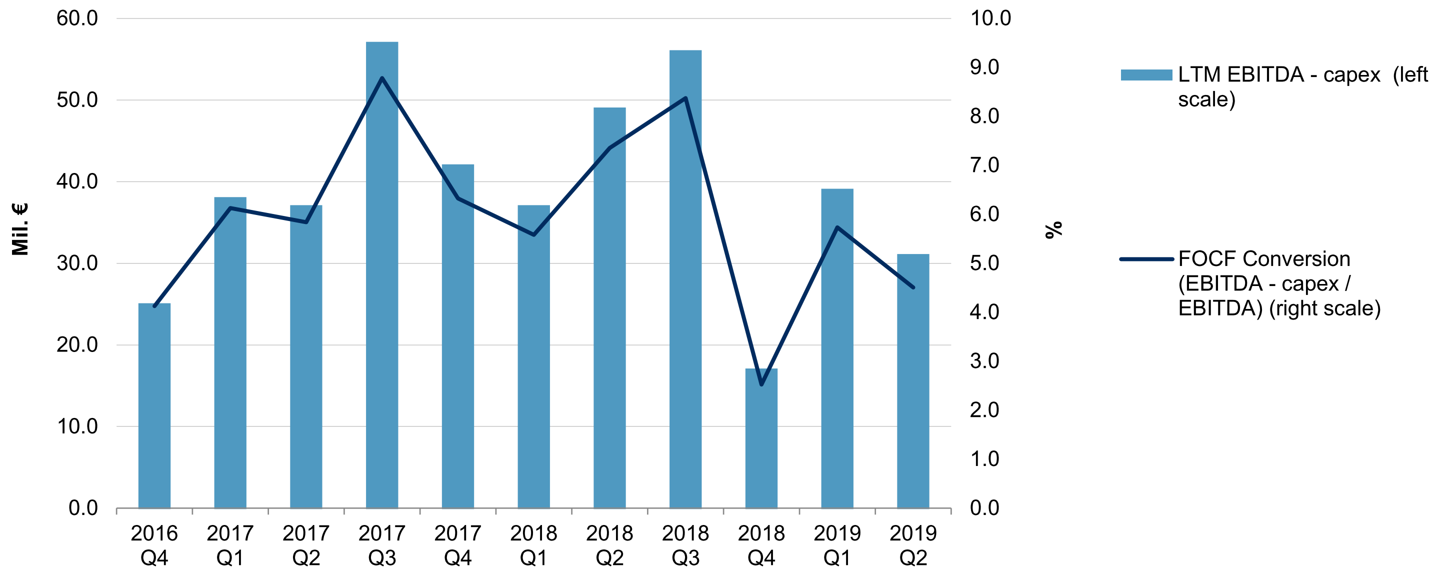
We assess economic and market conditions in Italy as rockier than those in Switzerland. Competition in mobile is very intense in our view, and has been reinforced by the market entry of Iliad, which has used aggressive pricing to take about 4% market share in about one year (AGCOM, first-quarter 2019, excluding M2M). In fixed broadband, four major and some smaller operators vie for retail customers, and pay TV provider Sky is also expected to enter the market with its own broadband product. Moreover, we think ongoing FTTH investments by investment joint venture Open Fiber, which is backed by Italian utility Enel SpA and Cassa Depositi e Prestiti Group, could further spur competition at the retail and wholesale level. Open Fiber plans to cover 270 Italian cities with FTTH over the next six years, compared with about 2.4 million homes at the end of 2017 (by Swisscom's estimate).

In our view, Fastweb enjoys a fairly entrenched position in the market for ICT solutions for B2B clients, in particular with mid-size and larger corporates. This segment has a duopolistic structure, with 31% market share for Fastweb and 53% for Telecom Italia (Fastweb's estimates for 2018).

Despite Fastweb's commercial success and solid organic EBITDA growth of 5%-10% over the past three years, its significant capex (31%-33% of sales in 2016–2018) continues to constrain its cash contribution to the overall Swisscom group (see chart 6). In June 2019, Fastweb teamed up with Wind Tre to co-invest in the build-out a shared 5G network, targeting 90% population coverage by 2026. Although this requires incremental wireless capex, we think the agreement could become cash flow accretive from 2020 thanks to savings of MVNO costs and additional revenue from stronger subscriber growth in mobile and fixed-mobile convergence products, as well as from wholesale service revenues with Wind for fiber base station backhaul and last-mile broadband access.

Chart 6

Italian Subsidiary Fastweb's LTM FOCF Contribution And Conversion



EBITDA after leases used for Q1 and Q2 2019. Source: S&P Global Ratings.

Peer comparison

We view Swisscom's business risk profile as substantially stronger than that of Sunrise, based on Swisscom's ownership of its high-quality nationwide fixed network, significantly higher market shares in fixed-line and mobile, and its stronger brand perception that enables the company to charge premium prices. We also consider Swisscom's business risk stronger than that of Proximus due to Swisscom's more dominant domestic market position, its less price-sensitive and quality-focused service area, and lighter regulation. Swisscom's and Telenor's respective domestic positions are about on par, in our view, somewhat stronger in TV for Telenor, somewhat stronger in fixed broadband for Swisscom, and similar in mobile. While Telenor is significantly more diversified geographically, we think this is offset by its substantial exposure to country and currency risks and a lower cash circulation owing to a number of only partly owned subsidiaries in emerging markets.

Table 1

Swisscom AG -- Peer Comparison

Industry Sector: Diversified Telecom

	Swisscom AG	**Sunrise Communications Holdings S.A.**	**Telia Company AB**	**Proximus S.A.**	**Telenor ASA**
Ratings as of Aug. 28, 2019	A/Stable/--	BBB-/Negative/--	BBB+/Stable/A-2	A/Stable/A-1	A/Watch Neg/A-1
	--Fiscal year ended Dec. 31, 2018--				

Table 1

Swisscom AG -- Peer Comparison (cont.)

Industry Sector: Diversified Telecom

	Swisscom AG	Sunrise Communications Holdings S.A.	Telia Company AB	Proximus S.A.	Telenor ASA
(Mil. CHF)					
Revenue	11,714.0	1,876.5	9,251.9	6,566.8	12,529.9
EBITDA	4,407.0	691.8	3,142.1	2,120.2	5,468.6
Funds from operations (FFO)	3,891.8	556.4	2,615.7	1,747.3	4,348.9
Interest expense	218.2	85.5	328.1	83.4	369.4
Cash interest paid	221.2	85.4	388.9	92.4	370.6
Cash flow from operations	3,835.8	498.8	3,056.0	1,817.1	4,397.1
Capital expenditure	2,400.0	295.3	1,623.0	1,238.1	2,385.5
Free operating cash flow (FOCF)	1,435.8	203.5	1,433.1	579.0	2,011.6
Discretionary cash flow (DCF)	294.8	23.2	(138.9)	2.2	(1,086.2)
Cash and short-term investments	556.0	420.9	2,077.6	387.5	2,055.3
Debt	9,838.2	1,975.5	7,426.1	3,368.0	9,310.2
Equity	8,208.0	1,481.2	12,207.9	3,551.0	6,182.5
Adjusted ratios					
EBITDA margin (%)	37.6	36.9	34.0	32.3	43.6
Return on capital (%)	12.2	6.6	7.9	13.6	18.6
EBITDA interest coverage (x)	20.2	8.1	9.6	25.4	14.8
FFO cash interest coverage (x)	18.6	7.5	7.7	19.9	12.7
Debt/EBITDA (x)	2.2	2.9	2.4	1.6	1.7
FFO/debt (%)	39.6	28.2	35.2	51.9	46.7
Cash flow from operations/debt (%)	39.0	25.3	41.2	54.0	47.2
FOCF/debt (%)	14.6	10.3	19.3	17.2	21.6
DCF/debt (%)	3.0	1.2	(1.9)	0.1	(11.7)

Financial Risk: Intermediate

Our adjusted leverage is currently 0.4x–0.5x higher than Swisscom's reported leverage predominantly due to the inclusion of lease liabilities of CHF1.8 billion and unfunded postretirement obligations of currently about CHF1.2 billion. We note that, after the adoption of the new lease accounting standards from 2019, both items are subject to changes in discount rates, which may lead to somewhat higher volatility in our calculation of Swisscom's credit metrics.

Financial summary

Table 2

Swisscom AG -- Financial Summary					
Industry Sector: Diversified Telecom					
	--Fiscal year ended Dec. 31--				
	2018	**2017**	**2016**	**2015**	**2014**
(Mil. CHF)					
Revenue	11,714.0	11,662.0	11,643.0	11,678.0	11,703.0
EBITDA	4,407.0	4,368.0	4,406.0	4,462.5	4,580.5
Funds from operations (FFO)	3,891.8	3,841.9	3,838.8	3,852.6	3,894.1
Interest expense	218.2	235.1	304.2	284.9	307.4
Cash interest paid	221.2	237.1	239.2	259.9	300.4
Cash flow from operations	3,835.8	4,102.9	3,948.8	3,793.6	3,638.1
Capital expenditure	2,400.0	2,373.0	2,410.0	2,419.0	2,448.0
Free operating cash flow (FOCF)	1,435.8	1,729.9	1,538.8	1,374.6	1,190.1
Discretionary cash flow (DCF)	294.8	581.9	386.8	225.6	29.1
Cash and short-term investments	556.0	603.0	506.0	409.0	342.0
Gross available cash	689.0	738.0	576.0	551.0	342.0
Debt	9,838.2	9,595.1	10,468.6	11,824.2	11,406.0
Equity	8,208.0	7,645.0	6,522.0	5,242.0	5,457.0
Adjusted ratios					
EBITDA margin (%)	37.6	37.5	37.8	38.2	39.1
Return on capital (%)	12.2	12.1	12.7	13.5	14.8
EBITDA interest coverage (x)	20.2	18.6	14.5	15.7	14.9
FFO cash interest coverage (x)	18.6	17.2	17.0	15.8	14.0
Debt/EBITDA (x)	2.2	2.2	2.4	2.6	2.5
FFO/debt (%)	39.6	40.0	36.7	32.6	34.1
Cash flow from operations/debt (%)	39.0	42.8	37.7	32.1	31.9
FOCF/debt (%)	14.6	18.0	14.7	11.6	10.4
DCF/debt (%)	3.0	6.1	3.7	1.9	0.3

Liquidity: Adequate

We assess Swisscom's liquidity as adequate because we expect that liquidity sources will cover uses by at least 1.2x over the 12 months from July 1, 2019. We also think that the company has sound relationships with banks, evidenced by an extensive network of Swiss and international banks that have worked with Swisscom for many years, and a high standing in the credit markets, as demonstrated by a long track record of issuance using a variety of instruments and in different currencies.

Below, our estimates of Swisscom's principal liquidity sources and uses for the 12 months started July 1, 2019.

Principal Liquidity Sources	Principal Liquidity Uses
• About CHF350 million in cash balances and short-term financial investments. • Two undrawn committed unsecured revolving credit facilities of CHF1 billion each, due March 2022 and April 2024, respectively. • Annual FFO of about CHF3.7 billion-CHF 3.9 billion.	• Capex of about CHF2.2 billion-CHF2.3 billion. • Maturities of debt and lease liabilities of about CHF1.5 billion. • About CHF1.14 billion in dividends.

Debt maturities

As of July 1, 2019*:

- 2019: CHF311 million
- 2020: CHF831 million
- 2021: CHF556 million
- 2022: CHF500 million
- 2023: CHF250 million
- Thereafter: CHF4,011 million

*Includes bank loans, bonds, and private placements.

Covenant Analysis

Change-of-control clauses exist in Swisscom's bank loans, bonds, and private placements. The bank loans would be due for immediate repayment if the stake of the Swiss government in Swisscom were to fall below one-third, or if another shareholder were to take control of the group. Bondholders would be entitled to sell the bonds if another shareholder gained a majority share in Swisscom and at the same time, the long-term issuer credit rating on the group fell below 'BBB-'. Under one of its credit agreements, Swisscom is subject to a maintenance covenant relating to net debt to EBITDA. We forecast ample headroom of more than 40% under this covenant over the next two years.

Environmental, Social, And Governance

Environmental factors play a limited role for Swisscom's credit rating at this point. Switzerland has enacted particularly strict electromagnetic fields (EMF) radiation limits for mobile base stations that are 10 times more demanding than similar rules in other countries. We think this could prove an impediment to achieving broad 5G coverage quickly, because, all other things equal, it may force the company to deploy more antennas, increasing the cost of 5G roll-out.

Swisscom is a major consumer of energy, particularly through the operation of networks and data centers. This creates some exposure to energy cost inflation, but these costs still remain a small fraction of the overall cost base, and Swisscom has devised a comprehensive set of measures to achieve its target of improving energy efficiency by 35% over 2016-2020. Key measures include the use of more energy-efficient hardware for mobile antennas, more cost-effective cooling systems, greater virtualization of data centers, and more energy-efficient buildings. Total 2018 energy consumption of 558 GWh was about 4% higher than in 2016, but it would have increased 24% over this timeframe without the aforementioned initiatives. After considering the purchase of emission certificates, Swisscom used 100% renewable electricity in 2018, higher than other European operators such as Telefonica with 58% or Deutsche Telekom with 52%.

We currently do not see any material governance concerns arising from the Swiss federal government's controlling stake in Swisscom. In our view, the government does not interfere with the day-to-day management, nor do we believe it would exert undue influence on important commercial or strategic decisions such as cost reduction programs or network investments.

Unionization plays an important role in Swisscom's employee base, with 82% of the total workforce covered by collective employment agreements in 2018. We think this could somewhat complicate the realization of cost savings from headcount reductions longer-term. Wage inflation has been muted in recent years, as annual negotiations for salary adjustments have only yielded increases commensurate to the change in the overall consumer price index.

Government Influence

Our rating on Swisscom incorporates one notch of uplift reflecting our view of likely timely support from the Swiss government in the event of financial distress. The Swiss government has control of Swisscom through its 51% ownership stake, and we believe it values Swisscom's role as the most important provider of connectivity services for the Swiss economy. We therefore think that it has a meaningful propensity to extend support to avoid major disruptions to Swisscom's operations, as well as potential repercussions for its own reputation, emanating from financial distress at the company.

Issue Ratings - Subordination Risk Analysis

We rate Swisscom's senior unsecured debt at the same level as the issuer credit rating. This is because, out of about CHF8.6 billion of reported financial debt for the group (excluding leases) on June 30, 2019, secured debt and unsecured third-party liabilities at Swisscom's subsidiaries accounted for less than 5% of total debt. Therefore, we assess that subordination risk for group-level creditors is limited.

Reconciliation

Our adjustments to Swisscom's 2018 financials mainly relate to our standard adjustments for operating leases, unfunded defined-benefit postretirement obligations, asset retirement obligations, share-based compensation expense, gains/losses on disposals of property, plant, and equipment, and capitalized interest. In calculating surplus cash, we add to CHF474 million of cash and cash equivalents CHF215 million of current and noncurrent deposits and debt securities which we consider sufficiently liquid.

From 2019, we discontinue our adjustment for operating leases as it is superseded by the application of the new International Financial Reporting Standard (IFRS) for leases (IFRS 16). Under the new standard, Swisscom reports total lease liabilities of about CHF1.8 billion, whereas the reclassification of operating lease expense to interest and depreciation improves reported EBITDA by about CHF 200 million. Compared with our operating lease adjustment, this would have increased our 2018 adjusted debt to EBITDA by about 0.15x.

Table 3

Reconciliation Of Swisscom AG Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. CHF)

	--Fiscal year ended Dec. 31, 2018--							
Swisscom AG reported amounts								
	Debt	**Shareholders' equity**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**	**Capital expenditure**
	8,167	8,223	4,213	2,069	138	4,407	3,720	2,404
S&P Global Ratings' adjustments								
Cash taxes paid	--	--	--	--	--	(294.0)	--	--
Cash taxes paid: Other	--	--	--	--	--	--	--	--
Cash interest paid	--	--	--	--	--	(157.0)	--	--
Operating leases	952.6	--	180.0	60.2	60.2	(60.2)	119.8	--
Postretirement benefit obligations/deferred compensation	980	--	5	5	6	--	--	--
Accessible cash and liquid investments	(689)	--	--	--	--	--	--	--
Capitalized interest	--	--	--	--	4	(4)	(4)	(4)
Share-based compensation expense	--	--	1	--	--	--	--	--

Table 3

Reconciliation Of Swisscom AG Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. CHF) (cont.)								
Dividends received from equity investments	--	--	18	--	--	--	--	--
Asset retirement obligations	481.6	--	--	--	10.0	--	--	--
Nonoperating income (expense)	--	--	--	23	--	--	--	--
Noncontrolling interest/minority interest	--	(15)	--	--	--	--	--	--
Debt: Derivatives	(54)	--	--	--	--	--	--	--
EBITDA: Gain/(loss) on disposals of PP&E	--	--	(10)	(10)	--	--	--	--
Total adjustments	1,671.2	(15.0)	194.0	78.2	80.2	(515.2)	115.8	(4.0)
S&P Global Ratings' adjusted amounts								
	Debt	**Equity**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Capital expenditure**
	9,838.2	8,208.0	4,407.0	2,147.2	218.2	3,891.8	3,835.8	2,400.0

Ratings Score Snapshot

Issuer Credit Rating

A/Stable/--

Business risk: Strong

- **Country risk:** Very low
- **Industry risk:** Intermediate
- **Competitive position:** Strong

Financial risk: Intermediate

- **Cash flow/Leverage:** Intermediate

Anchor: a-

Modifiers

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Strong (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile : a-

- **Related government rating:** AAA
- **Likelihood of government support:** Moderate (+1 notch from SACP)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Telecommunications And Cable Industry, June 22, 2014
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	Modest	**Intermediate**	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	**a-/bbb+**	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of August 28, 2019)*

Swisscom AG	
Issuer Credit Rating	A/Stable/--
Senior Unsecured	A
Issuer Credit Ratings History	
30-Jun-2009	A/Stable/--
12-Mar-2007	A-/Stable/--

Ratings Detail (As Of August 28, 2019)*(cont.)

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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