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Research Update:

France-Based BPCE 'A/A-1' Ratings Affirmed On Strengthened Capital And Funding Profiles; Outlook Remains Negative

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Overview

- BPCE's funding and liquidity profiles continue to improve in line with our expectations, on the back of a lengthened funding profile and reducing funding gap.
- Its capital position has also materially strengthened, which we believe is due to its sound retained earnings and the continued issuance of cooperative shares.
- We are affirming our 'A/A-1' ratings on BPCE.
- The negative outlook now solely reflects the possible removal of government support from the rating by the end of 2015, unless offset by another factor such as additional loss-absorbing capacity if we deem by then the resolution regime in France to be effective.

Rating Action

On July 13, 2015, Standard & Poor's Ratings Services affirmed its 'A/A-1' long- and short-term counterparty credit ratings on France-based bank BPCE and related entities (see Ratings List below). The outlook remains negative.

Rationale

The affirmation reflects our view that BPCE has continued consolidating its funding profile in 2014 and in the year-to-date, in line with our expectations. We do not see risks of this positive trend reversing, although we note that our ratios at end-2014 still compared slightly weaker than those of peers. We therefore no longer view funding as a material potential downside for the ratings.

The group relies on a large and stable deposit base and on confidence-sensitive wholesale funding to support its sizable balance sheet. We believe that Groupe BPCE has been rebalancing its funding profile toward longer-term liabilities and on-balance-sheet savings over the past three years, while reinforcing its liquidity management under stress test scenarios. On Dec. 31, 2014, the group's stable funding ratio was 88.4%, while its broad liquid assets to short-term wholesale funding ratio reached 91%. Based on strong deposit gathering and long-term debt issuance, we expect that the ratios increased in the first quarter of 2015. These ratios are materially above end-2011 levels of 84% and 0.84x, respectively. We adjust all our

funding and liquidity metrics above to exclude the portion of regulated deposits (including "Livret A") centralized at state institution, Caisse des Dépôts et Consignations. Of note, we consider all refinancing by the European Central Bank (ECB) to be short term, regardless of actual maturity, including the Targeted Longer-Term Refinancing Operations, which constrained our metrics in 2014. We believe that BPCE's access to ECB funding is opportunistic, however.

We expect further moderate improvements in these ratios in the next couple of years. Indeed, the group's main action plan focuses on efforts to continue increasing customer deposits, pursue improvement in its loan-to-deposit ratio, reinforce Natixis' originate-to-distribute model, and continue improving the diversification of its funding tools. We also see stricter regulatory requirements as supportive of this expectation. Of note, Groupe BPCE is the second-largest deposit taker in France.

Our "adequate" assessment of Groupe BPCE's capital and earnings is based on our view that the group's projected risk-adjusted capital (RAC) ratio before diversification will continue to increase to a range of 8.5%-9% by mid-2017. Groupe BPCE's RAC ratio increased materially to 7.8% at end-2014, up from 6.9% a year earlier, reflecting among other things retained earnings and limited growth in risk exposures. Of note, the group's capital position also benefitted from the sale of around €6 billion cooperative shares to its member-customers over 2012-2014. Our RAC projection for the next two years reflects our view that the group will continue to improve its capital ratios on the back of broadly stable profitability, further issuances of cooperative shares (albeit smaller than in the past three years), a modest dividend payout (reflecting its mutual status), and moderate growth in Standard & Poor's risk-weighted assets. We expect BPCE to maintain a low cost of risk, supported by the gradual recovery in the French economy.

Outlook

The negative outlook indicates that we may remove the one notch of uplift that we factor into our ratings if we believe that the potential for extraordinary support has become too unpredictable for French banks.

If we categorize France as "support uncertain," we would remove the notch of support we currently include in the ratings on BPCE. However, if we remove this systemic support notch, we may include instead a notch of support for additional loss-absorbing capacity (ALAC) if we deem the resolution regime in France to be effective and if we expect BPCE's subordinated buffers to meet a required threshold over a two-year horizon, or potentially longer.

We could revise the outlook to stable if our view of government support remains unchanged or if the removal of the notch of systemic support is offset by a notch for ALAC uplift.

We see relatively limited downside or upside risk for BPCE's stand-alone credit profile (SACP) at this juncture. A weakening in the maturity profile of BPCE's funding could weigh on the SACP, while, conversely, a material strengthening in its capitalization, with our prospective RAC ratio exceeding 10%, could exert upward pressure.

Ratings Score Snapshot

Issuer Credit Rating	A/Negative/A-1
SACP	a-
Anchor	bbb+
Business Position	Strong (+1)
Capital and Earnings	Adequate (0)
Risk Position	Adequate (0)
Funding and Liquidity	Average and Adequate (0)
Support	+1
GRE Support	0
Group Support	0
Sovereign Support	+1
Additional Factors	0

Related Criteria And Research

Related Criteria

- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises - December 19, 2014
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity - April 27, 2015
- Criteria - Financial Institutions - Banks: Assessing Bank Branch Creditworthiness - October 14, 2013
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework - June 22, 2012
- General Criteria: National And Regional Scale Credit Ratings - September 22, 2014
- General Criteria: Standard & Poor's National And Regional Scale Mapping Tables - September 30, 2014
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions - January 29, 2015
- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17, 2013
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions - November 09, 2011

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