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Research Update:

France-Based BPCE Upgraded To 'A+/A-1' On Strengthened Balance Sheet; Outlook Stable

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Overview

- Over the past five years, BPCE has demonstrated continuous improvement in its capitalization, which we now see as a rating strength.
- We expect that management will continue building up capital, and will tap the senior nonpreferred market to strengthen significantly its total loss-absorbing capacity.
- Therefore, we are raising our long-term ratings on BPCE and all its core group members to 'A+' from 'A'.
- At the same time, we are raising to 'A/A-1' from 'A-/A-2' our long- and short-term ratings on BPCE's highly strategic subsidiary Crédit Foncier de France (CFF).
- The stable outlook reflects our expectation that the group will maintain a solid balance sheet and achieve business development in line with its strategic plan, but will have difficulty translating its business position into stronger earnings that are commensurate with those of comparable peers globally.

Rating Action

On Oct. 19, 2018, S&P Global Ratings raised to 'A+' from 'A' its long-term issuer credit ratings on French bank BPCE and its core group members, including Natixis. We also raised by one notch all the long-term ratings on these entities' debt, including hybrid capital instruments and senior nonpreferred notes.

At the same time, we raised our long- and short-term issuer credit ratings on BPCE's highly strategic subsidiary Crédit Foncier de France (CFF) to 'A/A-1' from 'A-/A-2'.

The outlook on all entities is stable.

We raised our resolution counterparty credit rating (RCR) on BPCE S.A., Natixis S.A. and its New-York branch, and BRED Banque Populaire to 'AA-/A-1+' from 'A+/A-1', and our RCR on CFF to 'A+/A-1' from 'A/A-1'.

Rationale

Following the strong improvement in capital and loss-absorbing capacity that BPCE achieved in 2017, we expect that the group will sustain a risk-adjusted capital (RAC) ratio above 10%, while further strengthening its bail-in-able debt buffer and additional loss-absorbing capacity (ALAC). We expect the strengthening of the balance-sheet to be supported by the group's stable earnings, its low pay-out ratio along with its cooperative structure, recurring sales of cooperative shares, and by low-single-digit annual growth in S&P Global Ratings' risk-weighted assets (RWA) over 2018-2020. We forecast that our measure of ALAC will increase into the 6.0%-6.5% range in 2019-2020, hence exceeding our 5.00% threshold for one notch of ALAC support for BPCE. Our expectations reflect our belief that BPCE will raise its total loss-absorbing capacity (TLAC), based on planned issuance of €4 billion to €5 billion annually in senior nonpreferred notes up to 2020. Therefore, we have revised our assessment of BPCE's unsupported group credit profile (UGCP) to 'a' from 'a-', while we continue to factor into our long-term rating one notch of extraordinary support for additional loss-absorbing capacity (ALAC).

Our ratings on BPCE are supported by the group's prominent and longstanding franchise in domestic retail banking and asset management, as well as its growing insurance activities, by its predictable earnings, and by its conservative management and financial policy. We believe that BPCE has successfully completed most of its transition toward a reduced risk profile, and the winding-down of its legacy assets. However, we view the group's growth potential in the mature French domestic banking market as moderate, its profitability and efficiency as not on par with those of market leaders in other countries, and its funding and liquidity position as comparatively unfavorable.

BPCE is a universal banking group with a dominant focus on retail banking in France, where it ranks No. 2, with 7,800 branches. The group's leading and stable domestic retail franchise is the primary driver of our assessment of its business position. We consider business diversification to be average, and, by geography, limited in comparison with other national champions in Europe. BPCE is not a global player in corporate and investment banking, but has strong expertise in certain types of business, while asset and wealth management, and specialized financial services (SFS) complement its business set-up. We see growth in insurance and asset-gathering activities as a key component to the group's strategy.

We consider the group's earnings generation to be stable and predictable, albeit reflective of limited cost-efficiency. Notably, we see BPCE's profitability as structurally constrained by the fact that its business model entails sizable concentration on the lower margin domestic mortgage activity. We expect a low-single-digit increase in revenues in 2018, still pressured by the current low-interest-rate environment, since more than half of the group's revenues come from its French retail activities. This is mitigated though by the dynamic growth in BPCE's loans and deposits volumes in French retail, and by the sizable and recurring contribution to net profit generated by other businesses like corporate and investment banking and asset management, which are incorporated under Natixis. We also expect that profitability will be further supported by low new loan loss provisions, as a result of careful underwriting and a moderate recovery in France, where the bulk of BPCE's exposure is concentrated.

Over the past five years, BPCE has steadily strengthened its capitalization, which we now see as a rating strength. Under our base-case scenario, we expect that the group's RAC ratio will improve into the range 10.5%-11.0% in 2019-2020, from 10.1% achieved at year-end 2017. Our forecast reflects our view that BPCE will continue to adhere to its conservative financial policy and improve its capital ratios on the back of stable profitability. We expect issuance of cooperative shares to remain dynamic (following €10 billion in new cooperative shares issued to member-customers over 2012-2017), still modest dividend pay-outs (reflecting the cooperative status), and low-single-digit growth in S&P Global rating's RWA--although higher than the 1% increase achieved in 2017. Our forecast does not include any issuance of additional Tier 1 (AT1) instruments as we understand that the group's strategy is to strengthen its common equity ratio through retained earnings, while issuance of loss-absorbing debt is expected to be primarily under the form of senior nonpreferred debt. Quality of capital is also a supportive factor of our assessment, as total adjusted capital (TAC) included hardly any contribution from hybrid capital instruments at year-end 2017.

Considering the announced plan to sell to parent entity BPCE S.A. the retail banking activities currently hosted by Natixis under its SFS division, we factor in our expectation of a €0.5 billion cut in TAC as a result of the special dividend that Natixis would consecutively distribute for a total planned amount of €1.5 billion, and 29% of which would be paid out of the group to Natixis' minority shareholders. In parallel, Natixis is to accelerate its development and could invest up to €2.5 billion, primarily in the asset management business, compared with previous planned investment of up to €1.0 billion. Our forecasts reflect our view that this could put additional weight on BPCE's capital position by 2020, although we believe that the impact should remain limited. In addition, we expect the group's reorganization projects will induce costs, which could weigh on earnings beyond the €0.1 billion already incurred in first-half 2018. We also factor in a €1.6 billion negative impact on TAC from the first-time application of International Financial Reporting Standard 9 on Jan. 1, 2018.

We view BPCE's risk-management capabilities as adequate compared with peers' and the group's risk policy as conservative. We consider that BPCE has successfully completed most of its transition toward a reduced risk profile, and the winding down of its legacy assets.

Our central scenario factors in that the group will slightly improve its funding and liquidity position. We see the current level as somewhat below domestic peers', mainly because we adjust our metrics for the retail deposits that BPCE collects from regulated saving plans (mostly Livret A) and centralizes at the Caisse des Dépôts et Consignations; we do not consider these deposits as available for refinancing of BPCE's assets. Nevertheless, we do not see the group's funding and liquidity as a distinctive factor, and we consider it as neutral for the ratings. We see BPCE's access to European Central Bank funding as opportunistic.

Our long-term rating on BPCE is one notch higher than the UGCP, as we continue to incorporate one notch of ALAC uplift. We understand that BPCE plans to further increase its bail-in-able buffer, notably by issuing sizable amounts of senior nonpreferred debt. We expect this trend to be also supported by the increase in TAC along with the RAC improvement in excess of 10%, and by low-single-digit annual growth in S&P Global Ratings' RWA.

We forecast that our ALAC ratio will increase into a 6.0%-6.5% range, above the 5.00% threshold for one notch of ALAC uplift. At year-end 2017, with our capital and earnings assessment still at adequate at that time, our ALAC ratio for BPCE was 6.96% of our RWA measure, compared with 5.69% at year-end 2016. The revision of our assessment of capital and earnings to strong has a 300-basis-point (bps) negative impact on the ALAC ratio, as excess TAC is reduced. Therefore the pro forma ALAC ratio at year-end 2017 was 3.96%. We expect the group to increase its ALAC to about 5.0% in 2018, stemming largely from issuance of close to €7.3 billion of new senior nonpreferred debt--this volume has already been executed over the first nine months of 2018.

The upgrade of CFF hinges on our view of its highly strategic importance to the group, and factors in BPCE's announcement in June 2018, that it plans a reorganization that will integrate CFF's expertise and employees into the group's other companies. Since 2017, sizable early repayments and renegotiation of fixed-rate loans have weighed increasingly on the subsidiary's already low profitability prospects. The plan is to transfer new loan generation to the Caisses d'Epargne and Banque Populaires networks (financing for individuals, corporate financing for social housing), and to Natixis (financing for project and infrastructure), while real-estate specialized subsidiaries Socfim and Crédit Foncier Immobilier would become subsidiaries of BPCE S.A. As a result, CFF would concentrate on refinancing the group via its covered bond issuer, Compagnie de Financement Foncier (CFiF), and on managing the existing portfolio of loans until their maturity. BPCE said that the project remains subject to an information and consultation process involving the works councils. We believe that this initiative can address historic profitability concerns that we had identified at CFF, hence helping to improve the group's profitability.

We rate BPCE's hybrid capital instruments and senior subordinated (that is senior nonpreferred) notes by notching down from our 'a' assessment of its stand-alone credit profile (SACP).

Outlook

Our stable outlook on BPCE and all its core and highly strategic subsidiaries reflects our expectation that the group will maintain a solid balance sheet and achieve business development in line with its strategic plan. We balance this against our view that BPCE will have difficulties translating its business position into stronger earnings that are commensurate with those of comparable peers globally.

We could lower the ratings if the group was not able to achieve business development and improve efficiency in line with its strategic plan to 2020. Sizable acquisitions could also put pressure on our ratings if they affected our capital assumptions or increased managerial risks, in our view. A negative rating action could also result if the group was not able to sustain its capital position and improve its loss-absorbing capacity in line with our expectations. This could be the case, for instance, if there was a strong increase in new business volumes that inflated S&P Global Ratings' RWA, or if BPCE did not continue to issue sufficient ALAC-eligible debt in the coming years, or as a result of subdued retained earnings prospects.

We consider an upgrade scenario as remote.

Ratings Score Snapshot

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

Related Criteria

- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Criteria - Financial Institutions - General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 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, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Financial Institutions - Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Risk-Adjusted Capital (RAC) Ratios For The Top 50 Western European Banks, Oct. 17, 2018
- Top 100 Banks: Banks Are On Track To Withstand A Credit Cycle Turn, Oct. 1, 2018
- Banking Industry Country Risk Assessment: France, July 11, 2018
- S&P Global Ratings' National And Regional Scale Mapping Specifications, June 25, 2018

- Resolution Counterparty Ratings Jurisdiction Assessment For France Completed, June 11, 2018
- The Resolution Story For Europe's Banks: The Clock Is Ticking, April 25, 2018
- Proposed Backstop For The Eurozone Bank Resolution Fund Is Potentially Ratings-Positive, April 24, 2018
- The Adoption Of IFRS 9 And Bank Ratings, Feb. 19, 2018
- On This Year's Menu For French Banks: Digitalization And Efficiency Gains, Feb. 13, 2018
- Creditor Insurance Policies: The End Of Easy Money For French Bancassurers , Jan. 22, 2018
- Does French Banks' Capital Buildup Stop Here?, Jan. 18, 2018
- Bulletin: French Bank BPCE's Removal From G-SIB List Has No Effect On Ratings And Outlook, Nov. 2017, 22
- French Bank BPCE Outlook Revised To Positive On The Balance Sheet's Strengthening Trend; 'A/A-1' Ratings Affirmed, Oct. 20, 2017

Ratings List

Upgraded; Ratings Affirmed

	To	From
BPCE		
Natixis S.A.		
Natixis Financial Products LLC		
Natixis Australia Pty Ltd.		
Natixis (New York Branch)		
BRED - Banque Populaire		
Issuer Credit Rating	A+/Stable/A-1	A/Positive/A-1

Upgraded

	To	From
BPCE		
Natixis S.A.		
Natixis (New York Branch)		
BRED - Banque Populaire		
Resolution Counterparty Rating	AA-/--/A-1+	A+/--/A-1
Compagnie Europeenne de Garanties et Cautions		
Issuer Credit Rating		
Local Currency	A+/Stable/--	A/Positive/--
Financial Strength Rating		
Local Currency	A+/Stable/--	A/Positive/--
Parnasse Garanties		

Issuer Credit Rating	A+/Stable/--	A/Positive/--
Credit Foncier de France		
Issuer Credit Rating	A/Stable/A-1	A-/Positive/A-2

Upgraded; Ratings Affirmed

	To	From
Credit Foncier de France		
Resolution Counterparty Rating	A+/--/A-1	A/--/A-1
Natixis S.A.		
BRED - Banque Populaire		
Certificate Of Deposit	A+/A-1	A/A-1

Upgraded

	To	From
BPCE		
Senior Unsecured	A+	A
Senior Unsecured	A+p	Ap
Senior Subordinated	A-	BBB+
Subordinated	BBB+	BBB
Junior Subordinated	BBB-	BB+
Natixis S.A.		
Senior Unsecured	A+	A
Senior Unsecured	A+p	Ap
Subordinated	BBB+	BBB
Junior Subordinated	BBB-	BB+
Natixis Structured Products Ltd.		
Senior Unsecured	A+	A
Natixis US Medium-Term Note Program LLC		
Senior Unsecured	A+	A
Senior Unsecured	A+p	Ap
Credit Foncier de France		
Certificate Of Deposit	A/A-1	A-/A-2

Ratings Affirmed

BPCE	
Certificate Of Deposit	A-1
BPCE	
BRED - Banque Populaire	
Natixis (New York Branch)	

Natixis S.A.	
Commercial Paper	A-1