Crédit Foncier de France Issuer Rating Report

STABLE

AA-

Overview

Scope assigns an Issuer Rating of AA- to Crédit Foncier de France ('CFF') with a Stable Outlook, and an identical rating and outlook to its key issuing subsidiary, Compagnie de Financement Foncier ('CoFF'). Both mirror those of CFF's parent, BPCE SA ('BPCE').

Both ratings were affirmed on 2nd July 2018, after the announcement of upcoming changes within the Group, to occur in 2019. CoFF will continue to refinance the Group's public-sector financing activities. CFF's existing assets will not change, however, new lending will flow through other Group entities. Group solidarity mechanisms will be unchanged.

Note: This report refers to the entire CFF group, including Compagnie de Financement Foncier

Highlights

- CFF is a wholly owned subsidiary of BPCE, the central body of the two large French banking groups, the Banque Populaire (BP) – cooperative banks – and Caisses d'Epargne (CdE) – savings banks. CFF's subsidiary CoFF's sole purpose is to act as a covered bond issuer financing the mortgage and public-sector lending of both CFF and the whole BPCE group, with covered bonds (obligations foncières).
- In June 2018 it was announced that from early 2019 new lending that now flows through CFF will be conducted by other entities within Groupe BPCE, to create efficiency savings. CFF will continue to manage its existing loans, and CoFF will continue to refinance the Group's public-sector financing activities. From 2019 CFF's balance sheet is expected to shrink gradually as existing loans roll off.
- Crucially, CFF and CoFF will still carry the status of affiliates within the Group, and CoFF, the issuer of covered bonds, will remain as a strategic subsidiary. Affiliate legal status supports equalisation of both Issuer Ratings with those of BPCE SA.
- CFF and CoFF both benefit from an internal guarantee and solidarity within Groupe BPCE. BPCE SA must guarantee the liquidity and solvency of all its affiliates. As a shareholder BPCE is obliged to draw on its own capital resources. Beyond this it would use its own mutual guarantee fund, and subsequently could draw upon the BP and CdE networks' guarantee funds. The three funds have nearly EUR 1.3bn of funds available for immediate distribution (as of 31 December 2017). If all these sources were to be exhausted, additional sums would be requested from all member banks of the BP and CdE networks. Groupe BPCE's aggregated Tier 1 capital may be used to cover financial failings of any affiliate.

Rating drivers (summary)

The rating drivers, in decreasing order of importance in the rating assignment, are:

- CFF and CoFF will continue to benefit from the strong internal solidarity system within Groupe BPCE. A rating or outlook change for BPCE would entail a similar action for CFF and CoFF.
- CFF and CoFF's ongoing positions within Groupe BPCE. CFF's role will reduce over time as its assets run off from 2019 onwards. CoFF will remain a strategically important issuer of covered bonds for the whole Group.
- Risk management is strongly aligned to that of Groupe BPCE, and bondholders benefit from the group's strong risk control culture.

Ratings & Outlook

Crédit Foncier de France

Issuer Rating	AA-
Outlook	Stable

The ratings are not applicable to debt issued by unguaranteed subsidiaries of the rated parent.

Compagnie de Financement Foncier (CoFF)

Issuer Rating	AA-
Outlook	Stable

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Rating change drivers

Given the close integration of CFF and CoFF within the BPCE group and the direct linkage of their ratings to BPCE's, ability to improve ratings on a standalone basis is currently limited. However, at Groupe BPCE level, restructuring aimed at reducing excess capacity and lowering costs (as will be the case with respect to both companies' roles from 2019 onwards) eventually could help to drive ratings upwards. Groupe BPCE's 2018-2020 strategic plan sets out several objectives including greater efficiency and broad digital transformation.

The rating is based on the positions of CFF and CoFF as affiliates of Groupe BPCE, and thus the benefit of the strong internal guarantee and solidarity system within the Group. Should the Group's commitment to its associates become weaker, the alignment of the issuer ratings with those of the parent could change.

Overview

Groupe BPCE, of which **BPCE SA** is the central institution, is France's second largest banking group by assets. BPCE SA was established in 2009 as the central body of the two large French banking groups – the fourteen Banque Populaire banks (BP) and the sixteen Caisses d'Epargne (CdE), each with co-operative shareholders.

In addition to CFF and CoFF, the main subsidiaries of the BPCE group consist of Natixis, Banque Palatine and BPCE International.

Crédit Foncier de France is a wholly owned subsidiary of BPCE SA (BPCE).

CFF is a bank organised as a société anonyme, subject to French commercial law. However, as a credit institution that is officially approved as a specialist financial institution, CFF is also subject to the provisions of the French Monetary and Financial Code. CFF's roots date back to 1852. It was taken over by CdE in 1999. Within the BPCE Group, CFF has over recent years been operating as a leading specialist in property financing and services, as well as in financing public entities.

Compagnie de Financement Foncier is wholly owned by CFF and licensed as a specialised credit institution and société de credit foncier. CoFF was established in 1999, the result of a new legal framework (the French Savings and Financial Security Act) being put in place for covered bond issuance in the wake of CdE's acquisition of CFF. Prior to this, only CFF or Crédit Foncier et Communal d'Alsace et de Lorraine were permitted to issue obligations foncières or covered bonds. The purpose of a société de crédit foncier is defined in Article L. 513-2 of the French Monetary and Financial Code: as the granting or acquiring of guaranteed loans i.e. loans backed by first-rank mortgages or real property collateral conferring at least an equivalent guarantee, or exposures to public-sector entities, and financing them by issuing obligations foncières.

Thus, CoFF's role is to fund mortgage and public-sector lending on behalf of Groupe BPCE and, at present, its parent. It is one of the largest covered bond issuers in the world.

Rating drivers (details)

CFF and CoFF both benefit and will continue to benefit from a strong internal solidarity system within Groupe BPCE, firstly through direct support from the central body BPCE SA (BPCE) using its own capital resources as a shareholder. The entities are further backed by the guarantee funds within the Group and ultimately the ability to tap into the resources of its member banks. A rating or outlook change for BPCE would entail a similar action for CFF and CoFF.

All credit institutions affiliated with Groupe BPCE, including CFF and CoFF, are covered by its guarantee and solidarity mechanism. This was set up pursuant to Article L. 512-107-6 of the French Monetary and Financial Code (Code monetaire et financier). BPCE, as the Group's central institution, is tasked with taking all necessary measures to guarantee the liquidity and capital adequacy of the group and of each network. This includes defining the principles covering intragroup cash flows and investments, as necessary for managing liquidity. It also covers any internal financing mechanisms designed to ensure the solvency of the Group, which includes the establishment and administration of a mutual guarantee fund shared by the BP and CdE networks. BPCE also manages the BP Network Fund and the CdE Network Fund. The amount of deposits made to BPCE for the three funds may not be less than 0.15% nor greater than 0.3% of Group risk-weighted assets.

Although CFF's role will be changing, the operation of the solidarity mechanism will remain unchanged. CFF and CoFF will continue to carry the status of affiliates within the Group. This legal status continues to support the equalisation of their Issuer Ratings with those of BPCE SA.

If CFF or CoFF were to encounter financial difficulty, BPCE would proceed as follows:

(i) BPCE as the Group's central body would be the first port of call for support, using its own capital (EUR 16.2 bn as at 31 Dec 2017) in accordance with its duty as a shareholder;

(ii) Should this prove insufficient, it would use the mutual guarantee fund created and controlled by BPCE, which at December 31, 2017 totaled €362.6 million in assets provided jointly by the BP and CdE networks, and which is increased through an annual contribution (subject to the amounts which would be used in the event of a call for funds);

(iii) If BPCE's capital and this mutual guarantee fund should prove insufficient, BPCE would call on (in equal proportions) both the BP and CdE networks' own guarantee funds of €900 million in total and; finally

(iv) If calls on BPCE's capital and these three guarantee funds should prove insufficient, additional sums would be requested from all member banks of the BP and CdE networks.

It should be noted that the guarantee funds referred to above consist of a Groupe BPCE internal guarantee mechanism activated at the initiative of the BPCE Executive Board or the French banking regulator, which may request that it be used if deemed necessary.

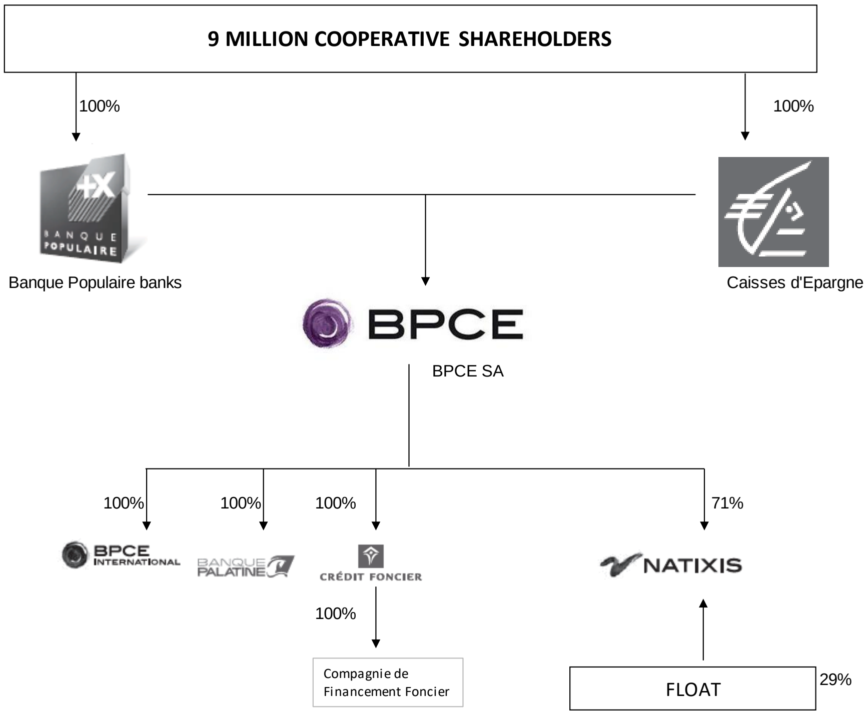
The group's aggregated Tier 1 capital may be used to cover any financial failings of any affiliate. As of 31 December 2017, the consolidated 1 capital of the BPCE group (99% comprising Common Equity Tier 1 capital) stood at EUR 59.4bn (YE16: EUR 56.6 bn).

As affiliates, CFF and CoFF do not contribute to the guarantee mechanism of Groupe BPCE and will not be called upon in the event of a BP or a CdE default.

Groupe BPCE has previously shown strong commitment to supporting various entities. For example, it guaranteed a large portion of the net value of a segregated workout credit portfolio for its investment banking arm, Natixis, in 2009. We also note that CFF benefited from a EUR 1.5bn capital increase in late 2011. CFF's securitisation portfolio was transferred to BPCE in September 2014, and BPCE's risk management division conducted the monitoring of this. In addition, a disposal plan was established and coordinated by the group finance division.

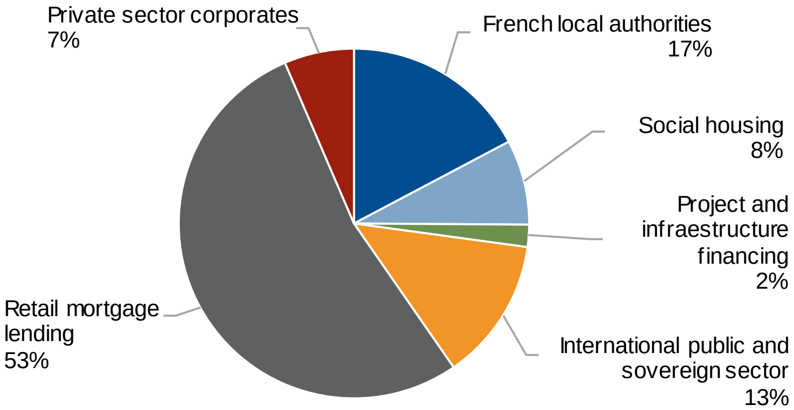
Groupe BPCE also implemented action plans in 2015, specifically to ensure the capital adequacy of its networks and subsidiaries. For example, BPCE may grant redeemable subordinated loans, or subscribe for perpetual, deeply subordinated notes as in the case of Crédit Foncier (EUR 550m).

Continuing position within Groupe BPCE, France's second largest banking group by assets, albeit CFF's role will reduce over time as assets run off from 2019 onwards. CoFF will continue as a strategically important subsidiary issuing covered bonds for the Group and has achieved deep and diversified market access for its covered bond offerings – which should continue to be the case.



CFF's clients comprise individuals, investors and real estate professionals, and public sector entities. It has been acting through multiple channels, including 218 branches in France, around 7,000 business partners in the real estate sector, and an internet platform. Over half of the loan book consists of retail mortgages (see Figure 1).

Figure 1: CFF Loan Book Split, YE17



Source: Company data, Scope Ratings

CFF's results have been affected by the low interest rate environment, exacerbated by the impact of early repayments. CFF's net banking income for 2017 was EUR 555m, 30.4% lower compared to the same period in 2016 (EUR 797m). The lower result was mainly due to a decline in net interest income (EUR 150m decrease YoY), losses on financial instruments held for trading and designated at fair value through profit or loss and lower net fee and commission income commissions. The 2017 cost-income ratio was about 85%.

To create greater efficiencies for Groupe BPCE going forward, it was announced on 26th June 2018 that from early 2019, CFF's role will change. Its wholly owned subsidiary Crédit Foncier Immobilier, which provides real estate services such as consultancy, valuation and property management, will be owned directly by BPCE SA. New loan production currently flowing through CFF's branches and internet portal will pass to other entities within Groupe BPCE, and many of CFF's staff will be offered roles elsewhere within the wider Group. CFF will continue to manage its existing loan outstandings, and will also continue to manage its largest subsidiary, CoFF.

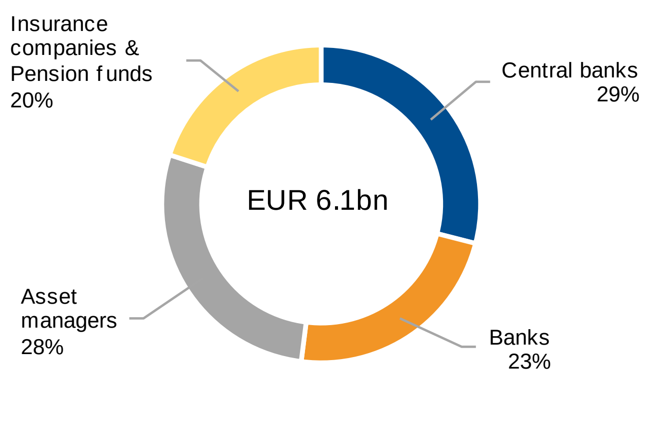
As of year-end 2017, CFF had a balance sheet size of around EUR 114bn (of which CoFF accounted for EUR 78.4 bn). Within this, around EUR 45.7bn of loans were outstanding to individuals, EUR 5.5bn to investors and real estate professionals, and EUR 34.6bn were public sector loans (which include those supporting infrastructure projects and social housing). Given the long term of many of its existing loans, it is expected that the size of the balance sheet will reduce gradually after new loan production ceases.

As CFF's primary funding vehicle, CoFF currently refinances both residential mortgages and loans granted by CFF and Groupe BPCE's other networks. CoFF's loans selection process is in two stages – CFF originates the loans, and CoFF applies risk filters to screen the loans originated (as would also be the case for loans acquired from elsewhere in the Group).

In the short term it will continue to refinance loans granted by CFF. From early 2019 its role is expected to be refocused, mainly to refinance the public sector and similar assets generated by Groupe BPCE as a whole.

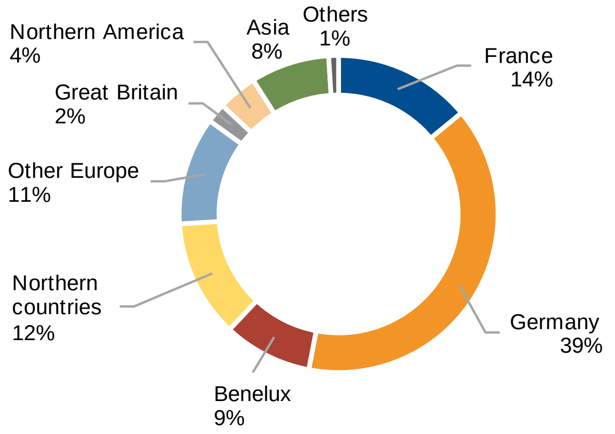
CoFF currently issues between EUR 6bn and EUR 7bn in covered bonds per year. Total issuance for 2017 was EUR 6.1bn, which included major benchmark issues and private placements. Outstanding obligations foncières stood at €63.4bn at December 31, 2017, (related payables included), versus €67.4bn one year previously. As one of the world's largest covered bond issuers CoFF has developed a deep and diverse international investor base for its covered bond offerings, and Scope expects that this will continue to be the case. Investors in the EUR6.1 bn raised in 2017 broke down as demonstrated in Figure 2 below:

Figure 2: 2017 Breakdown of issuances by investor type



Source: Company data, Scope Ratings

Figure 3: 2017 Breakdown of issuances by region



Source: Company data, Scope Ratings

Risk management is already strongly aligned to that of Groupe BPCE. Bondholders should continue to benefit from the group's strong risk control culture.

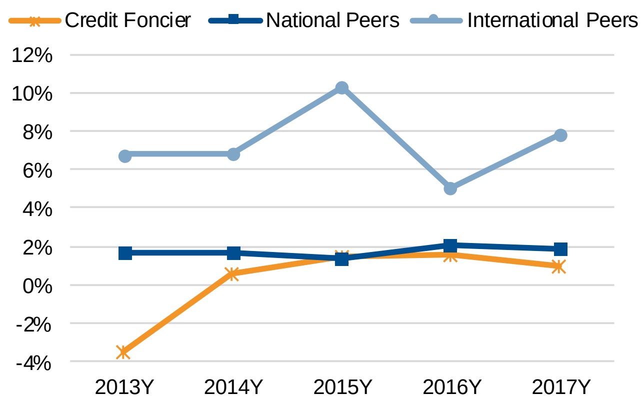
While CFF's executive management is responsible for implementing internal controls, the French Monetary and Financial Code makes BPCE SA responsible for defining the internal control system of Groupe BPCE and its networks, controlling the financial position of affiliated institutions, and defining Group risk management policies, procedures and limits. Thus, CFF's control systems incorporate the standards set by BPCE. Periodically internal audits are carried out by members of BPCE's General Inspection department.

From a risk management perspective, CFF has its own risk department and board level risk management committee. However, CFF's exposures are regularly reviewed in risk management committee meetings at group level.

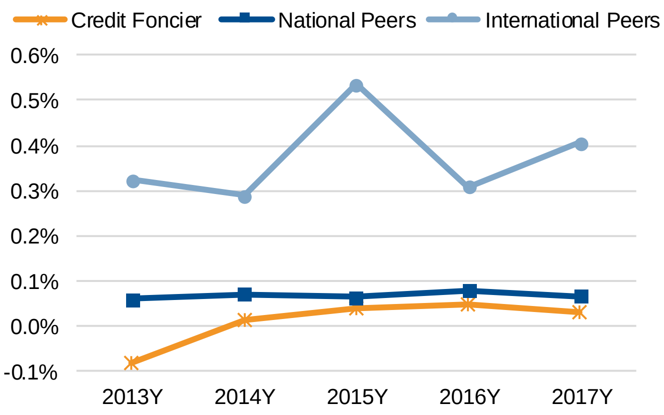
CFF's Risk and Compliance functions are responsible for internal control and compliance for CoFF.

I. Appendix: Peer comparison

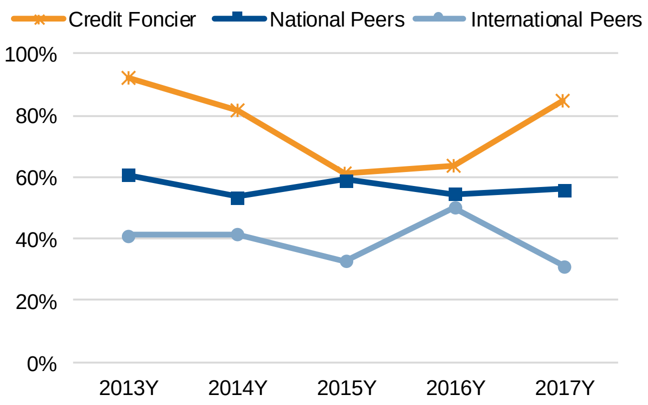
Return on average equity (%)



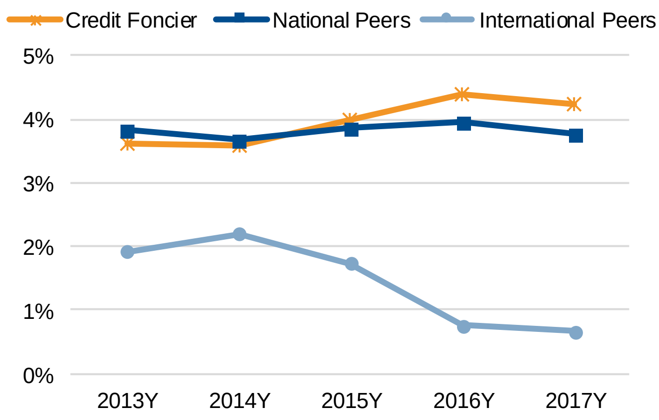
Return on average assets (%)



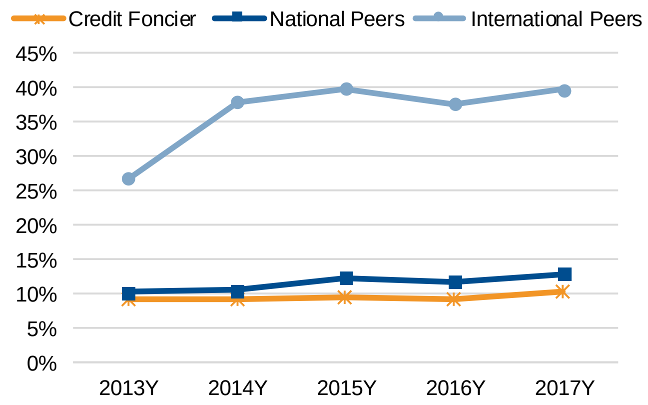
Cost-to-income ratio (%)



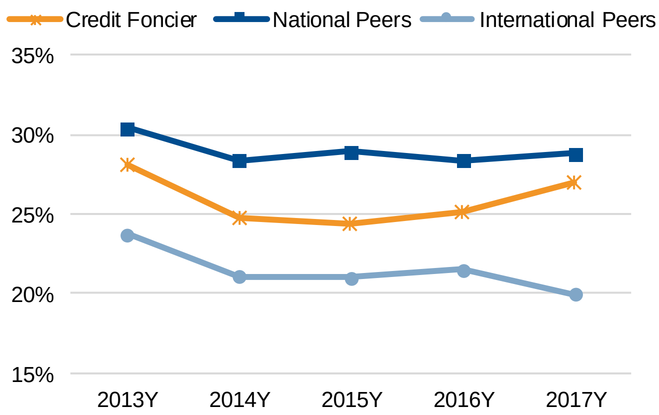
NPLs/Net Loans (%)



CET 1 Ratio (Phase-in, %)



Risk-weighted Assets/Assets (%)



Source: SNL, Scope Ratings

*National peers: BNP Paribas Home loan SFH, Societe Generale SFH, Credit Agricole Home Loan SFH, Groupe BPCE, Credit Mutuel Home Loan SFH, La Banque Postale Home Loan SFH, Credit Foncier

International peers: Hypo Burgenland, Hypo Oberoesterreich, Realkredit Danmark, Nordea mortgage bank, Sp mortgage bank, Op mortgage bank, Nordea Hypothek, Swedbank mortgage bank, Stadshypotek, Dusseldorfer Hypotheken, Munchener Hypotheken, DNB Boligkreditt, Coventry Building Society, Yorkshire Building Society, Credit Foncier.

II. Appendix: Selected financial information – Crédit Foncier de France

	2013Y	2014Y	2015Y	2016Y	2017Y
Balance sheet summary (EUR m)					
Assets					
Cash and interbank assets	22,618	14,532	17,577	14,551	12,106
Total securities	14,296	20,375	17,141	17,043	13,093
of which, derivatives	11,022	16,774	14,454	14,504	10,718
Net loans to customers	104,516	96,420	91,055	86,406	81,157
Other assets	6,530	9,743	8,699	8,731	7,963
Total assets	**147,960**	**141,070**	**134,472**	**126,731**	**114,319**
Liabilities					
Interbank liabilities	44,070	34,601	33,301	30,028	28,002
Senior debt	86,027	83,854	78,199	76,169	69,295
Derivatives	7,026	12,232	10,676	11,421	8,616
Deposits from customers	268	346	1,365	528	587
Subordinated debt	789	581	427	291	291
Other liabilities	6,091	6,457	6,801	4,681	3,772
Total liabilities	**144,271**	**138,071**	**130,769**	**123,118**	**110,563**
Ordinary equity	3,590	2,900	3,056	2,991	3,132
Equity hybrids	0	0	549	526	527
Minority interests	99	99	98	96	97
Total liabilities and equity	**147,960**	**141,070**	**134,472**	**126,731**	**114,319**
Core tier 1/Common equity tier 1 capital	3,748	3,139	3,124	2,911	3,181
Income statement summary (EUR m)					
Net interest income	482	526	584	472	322
Net fee & commission income	207	208	291	232	225
Net trading income	-191	-775	-96	16	-111
Other income	96	710	81	84	122
Operating income	**594**	**669**	**860**	**804**	**558**
Operating expense	549	547	528	511	473
Pre-provision income	**45**	**122**	**332**	**293**	**85**
Credit and other financial impairments	253	111	237	120	81
Other impairments	0	0	0	0	0
Non-recurring items	0	0	0	0	NA
Pre-tax profit	**-208**	**11**	**95**	**173**	**-19**
Discontinued operations	0	0	0	0	0
Other after-tax Items	0	0	0	0	0
Income tax expense	-80	-7	45	115	-54
Net profit attributable to minority interests	2	3	2	1	2
Net profit attributable to parent	**-130**	**15**	**48**	**57**	**33**

Source: SNL, Scope Ratings

III. Appendix: Ratios – Crédit Foncier de France

	2013Y	2014Y	2015Y	2016Y	2017Y
Funding and liquidity					
Net loans/deposits (%)	NM	NM	NM	NM	NM
Liquidity coverage ratio (%)	NA	NA	173.0%	110.0%	110.0%
Net stable funding ratio (%)	NA	NA	NA	NA	NA
Asset mix, quality and growth					
Net loans/assets (%)	70.6%	68.3%	67.7%	68.2%	71.0%
NPLs/Net Loans (%)	3.6%	3.6%	4.0%	4.4%	4.2%
Loan-loss reserves/NPLs (%)	27.6%	27.8%	28.0%	27.2%	25.7%
Net loan growth (%)	-6.3%	-7.7%	-5.6%	-5.1%	-6.1%
NPLs/Tangible Equity and Reserves (%)	79.0%	86.3%	75.7%	80.6%	73.3%
Asset growth (%)	-9.4%	-4.7%	-4.7%	-5.8%	-9.8%
Earnings and profitability					
Net interest margin (%)	0.3%	0.4%	0.5%	0.4%	0.3%
Net interest income/average RWAs (%)	1.1%	1.4%	1.7%	1.5%	1.0%
Net interest income/operating income (%)	81.1%	78.6%	67.9%	58.7%	57.7%
Net fees & commissions/operating income (%)	34.8%	31.1%	33.8%	28.9%	40.3%
Cost/income ratio (%)	92.4%	81.8%	61.4%	63.6%	84.8%
Operating expenses/average RWAs (%)	1.3%	1.4%	1.6%	1.6%	1.5%
Pre-impairment operating profit/average RWAs (%)	0.1%	0.3%	1.0%	0.9%	0.3%
Impairment on financial assets /pre-impairment income (%)	562.2%	91.0%	71.4%	41.0%	95.3%
Loan-loss provision charges/net loans (%)	0.2%	0.1%	0.3%	0.1%	0.1%
Pre-tax profit/average RWAs (%)	-0.5%	0.0%	0.3%	0.5%	-0.1%
Return on average assets (%)	-0.1%	0.0%	0.0%	0.0%	0.0%
Return on average RWAs (%)	-0.3%	0.0%	0.1%	0.2%	0.1%
Return on average equity (%)	-3.5%	0.5%	1.5%	1.6%	0.9%
Capital and risk protection					
Common equity tier 1 ratio (%, fully loaded)	9.0%	NA	NA	NA	NA
Common equity tier 1 ratio (%, transitional)	9.0%	9.0%	9.5%	9.2%	10.3%
Tier 1 capital ratio (%, transitional)	9.7%	9.6%	11.8%	11.4%	12.6%
Total capital ratio (%, transitional)	9.9%	10.3%	12.0%	11.4%	12.6%
Leverage ratio (%)	NA	NA	2.8%	3.4%	3.9%
Asset risk intensity (RWAs/total assets, %)	28.1%	24.7%	24.4%	25.1%	27.0%
Market indicators					
Price/book (x)	NA	NA	NA	NA	NA
Price/tangible book (x)	NA	NA	NA	NA	NA
Dividend payout ratio (%)	NA	NA	NA	NA	NA

Source: SNL, Scope Ratings

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