

Rating Action: Moody's Changes Outlook On BPCE's Long-term Debt And Deposit Ratings To Positive, From Stable

Global Credit Research - 26 Jul 2017

Long-term deposit and senior unsecured debt ratings of A2 affirmed

London, 26 July 2017 -- Moody's Investors Service, ("Moody's") affirmed BPCE's and affiliated subsidiaries' (Natixis, Crédit Foncier de France and Banque Palatine) long-term senior unsecured debt and/or deposit ratings of A2 and changed the outlooks on these ratings to positive, from stable. The rating agency also affirmed BPCE's and Crédit Foncier de France (CFF)'s standalone baseline credit assessments (BCA) of ba2 and b1, respectively. Moody's upgraded Natixis's BCA to ba1, from ba2, and downgraded Banque Palatine's BCA to ba1, from baa3. Finally, the agency affirmed all entities' adjusted BCAs of baa2, as well as their short term ratings and long- and short-term Counterparty Risk (CR) assessments of Prime-1 and A1(cr)/P-1(cr), respectively.

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_196618 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

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- Principal Methodology

Today's rating action follows the improvement of Groupe BPCE's asset risk, capitalization and funding profile over the last few years. The group's cost of risk has decreased to a historically low level of 22 basis points (bps) of gross loans, in the first quarter of 2017, thanks to the improving macroeconomic environment in France, where most of the group's activities take place. Groupe BPCE increased its total capital ratio to 18.7% of its risk-weighted assets (RWAs) at the end of Q1-2017, meeting its 2018 target ahead of schedule. Groupe BPCE's capitalization benefits from its ability to retain a large share of its annual profits, as do other French mutualist groups, while it endeavors to restrict RWA growth. The group's funding profile has also been strengthened in recent years. Its use of confidence-sensitive wholesale funding decreased to 39% of its tangible banking assets in 2016, from 46% in 2014; it has also lengthened the average maturity of its funding, through the issuance of long-term covered bonds, and finally it has diversified its funding sources, expanding its non-European investor base.

Nevertheless Groupe BPCE's creditworthiness is constrained by its relatively low, but stable, profitability and weak cost-efficiency. The group's net interest margin has declined recently as a result of the low interest rate environment. Meanwhile, all things being equal, Moody's does not expect the revenues generated by the more dynamic insurance, asset management and capital market business lines to be sufficient to offset both the continuous erosion of net interest income and additional costs generated by the digitalization and restructuring of the retail franchise. The group will disclose a new strategic plan in November 2017, which is expected to deliver a roadmap towards a more cost-efficient business model.

The upgrade in Natixis's BCA primarily reflects its improved standalone capitalization, which results from the successful implementation of a new business model focusing on the development of asset management and retail activities (insurance activities, consumer finance, payment systems, etc.) which benefit from the distribution channel of the two networks. While Natixis still aims to develop its wholesale banking activities (large corporate and asset-based finance), it strives to restrict RWA growth through the distribution of new loans to third parties.

Furthermore, Banque Palatine's BCA was downgraded as a result of its relatively low standalone capitalization given its exposures to corporates and SMEs, which makes the bank more sensitive to material one-off losses.

As a French mutualist group, Groupe BPCE is required by law to maintain an internal solidarity mechanism,

which ensures that all affiliated entities would benefit from capital and liquidity support from other group members in case of need. The strong support from the group is reflected in the baa2 adjusted BCA that Moody's assigns to each affiliate.

BPCE's and affiliated entities' long-term deposit and senior debt ratings also benefit from very low loss-given failure and a moderate likelihood of government support, which translate respectively into a two-notch and one-notch uplift from their adjusted BCA.

WHAT COULD CHANGE THE RATING UP/DOWN

The outlook on BPCE's deposit and senior unsecured debt ratings is positive, reflecting Moody's expectation that the group's revised strategy will provide further detail on its plans (i) to achieve balanced profitability, with increased focus on non-interest income; (ii) to materially reduce its cost base while maintaining a low risk profile; and (iii) to further increase capitalization through a clear common equity Tier 1 (CET 1) target.

The adjusted BCA of Groupe BPCE's affiliated entities could be upgraded as a result of increased profitability, which amongst other things could result from a reduction of the bank's cost structure. A higher CET1 capital would also be beneficial to the group's creditworthiness, while Moody's expects Groupe BPCE to maintain its current risk profile. An increase in the adjusted BCA would likely result in an upgrade of all group ratings. BPCE's deposit and senior unsecured debt ratings could also be upgraded as a result of a lower than expected loss-given-failure stemming from the additional issuance of material amounts of junior senior and/or subordinated debt.

Conversely, the adjusted BCA of Groupe BPCE's affiliated entities could be downgraded as a result of an unexpected erosion of its profitability or a sudden increase of asset risk. A decrease in the adjusted BCA would likely result in a downgrade of all group ratings. BPCE's deposit and senior unsecured debt ratings could also be downgraded as a result of a higher than expected loss-given-failure stemming chiefly from an unexpected decrease of the senior debt outstanding amount. Each affiliated entity's own ratings could also be downgraded if the agency were to assume, on a case-by-case basis, a weaker probability of group support.

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