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Research Update:

French Bank BPCE 'A/A-1' Ratings Affirmed Despite Higher Industry Risks; Outlook Remains Negative

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Overview

- We think France's banking sector is facing increased industry risks, including pressure on revenues from the slowing economy and recent reforms that have constrained the environment for banks.
- Groupe BPCE's capital position has improved in recent quarters and we expect it to continue to strengthen its capital ratios.
- We are consequently affirming our 'A/A-1' ratings on BPCE.
- The negative outlook reflects that on France and the possibility that progress in the strengthening of Groupe BPCE's balance sheet and financial position could be hindered by the protracted economic recession in France and the difficult operating environment for European banks.

Rating Action

On June 20, 2013, Standard & Poor's Ratings Services affirmed its 'A/A-1' long- and short-term counterparty credit ratings on French bank BPCE and its core subsidiaries, Natixis S.A. and BRED - Banque Populaire. In a related rating action, we affirmed our 'A' long-term counterparty credit rating on core subsidiary Compagnie Europeenne de Garanties et Cautions. The outlook remains negative.

BPCE is the main funding bank and the central institution of the French cooperative banking group, Groupe BPCE. The ratings on BPCE reflect its core membership in Groupe BPCE.

Rationale

The affirmation reflects our expectation that Groupe BPCE's stronger capital position acts as a buffer against the increasing risks we see in the French operating environment. We are therefore maintaining BPCE's stand-alone credit profile (SACP) at 'a-'.

We believe French banks face increasing industry risks. Low economic growth prospects, historically low interest rates and recent reforms that create a more constraining environment for banks are, in our view, reducing financial institutions' ability to generate earnings. As a result, we have modified the anchor for banks operating predominantly in France, including BPCE, to 'bbb+' from 'a-'.

Groupe BPCE's capital position has nevertheless improved in recent quarters, in our view. We see its adequate risk-adjusted profits, more limited dividend payout ratios than peers', and new sales of cooperative shares as its major sources of capital formation. Under our base-case scenario, we expect further strengthening of the group's capitalization. This has led us to revise our assessment of BPCE's capital and earnings to "adequate" from "moderate," as our criteria define the terms. This is commensurate with our projected risk-adjusted capital (RAC) ratio before diversification for the group increasing to a range between 7% and 7.5% in the next 18 to 24 months from 6.7% as of Dec. 31, 2012. We take the view that BPCE's retained earnings in 2013 and 2014 should be adequate, but below its underlying capabilities. We believe that 2013 and 2014 will be challenging years for retail banking in France and for BPCE. BPCE's revenues are unlikely to grow much, compelling the bank to rein in costs further. We expect Groupe BPCE's prospective total cost of credit risk to moderately increase from 2012 levels, but to trend below domestic peers.

Groupe BPCE's funding is "average" and its liquidity "adequate," in our opinion. The group relies on a large and stable deposit base but also on confidence-sensitive wholesale funding to fund its sizable balance sheet. The group is therefore sensitive to prolonged disruption in capital markets. We believe that in the past 18 months BPCE has been rebalancing its funding profile toward longer-term liabilities and on-balance sheet savings while reinforcing its liquidity management and reserves. Under our base-case scenario, we expect the group's transition toward stronger funding and liquidity to continue.

We continue to assess Groupe BPCE's business position as "strong" and its risk position as "adequate." The ratings also reflect our view of Groupe BPCE's "high" systemic importance in France, which we assess as "supportive" toward its banking system.

Outlook

The negative outlook reflects the possibility that a protracted economic recession in France and difficult operating environment for banks could hinder progress in the strengthening of BPCE's balance sheet, capital, and funding. If this happened and if we were to lower our long-term sovereign rating on France (unsolicited AA+/Negative/A-1+) by one notch, we would downgrade BPCE.

We note that all other things being equal, we would not downgrade BPCE if we were to lower the long-term rating on France. In accordance with our methodology, we would continue to factor one notch of uplift into the ratings from our assessment of BPCE's stand-alone credit profile to reflect government support.

We might revise the outlook to stable if, all other factors remaining equal, we believed that the group's ongoing transition toward a stronger balance

sheet and enhanced financial position would be confirmed.

Ratings Score Snapshot

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

Related Criteria And Research

- Various Rating Actions Taken On French Banks Due To Rising Industry Risks, June 20, 2013
- Group Rating Methodology, May 7, 2013
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Bank Hybrid Capital Methodology And Assumptions, Nov. 1, 2011
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

BPCE

Counterparty Credit Rating A/Negative/A-1

Natixis S.A.

Counterparty Credit Rating A/Negative/A-1

BRED - Banque Populaire

Counterparty Credit Rating A/Negative/A-1

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Compagnie Europeenne de Garanties et Cautions
Counterparty Credit Rating A/Negative/--

N.B. This list does not include all ratings affected.

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