Compagnie de Financement Foncier French Covered Bonds – Performance Update

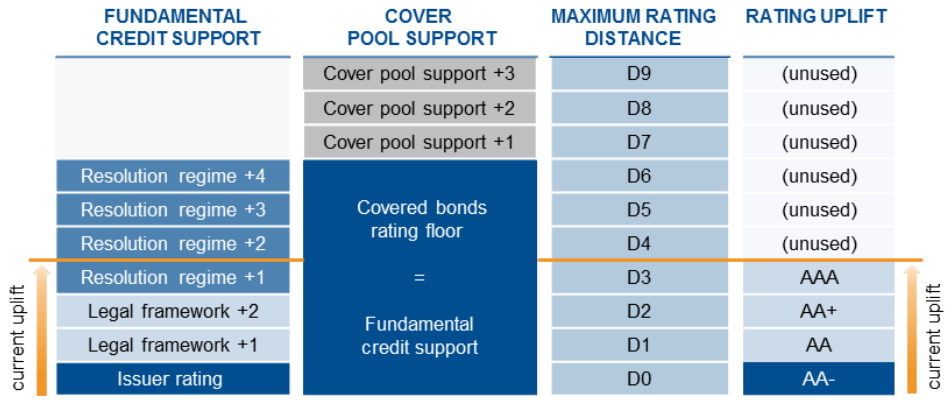
The AAA ratings with a Stable Outlook on the obligations foncières (OF) issued by Compagnie de Financement Foncier S.A. (CoFF) are based on the bank's issuer rating of AA- enhanced by fundamental credit support of up to six notches.

Cut-off date	Cover pool	Cover asset type	Covered bonds	Rating/Outlook
31 Dec 2019	EUR 70.0bn	Mixed	EUR 59.9bn	AAA/Stable

CoFF, wholly owned by Crédit Foncier (CFF), is an integral member of BPCE Group (all AA-/Stable). As the group's largest covered bond issuer, CoFF is dedicated to providing secured funding for the group's financing activities, typically on the public-sector. Our issuer rating on CoFF reflects its role as a strategic subsidiary and its inclusion in the group's internal guarantee and solidarity system.

Fundamental credit support factors from the French legal and resolution framework provide a six-notch uplift above the bank's rating. In addition, the cover pool can support a credit uplift of up to nine notches to the issuer rating, providing further rating stability.

The programme also benefits from a buffer of six notches against an issuer downgrade. The maximum uplift is nine notches, as opposed to the three notches currently used to achieve the highest covered bonds rating.



Stable Outlook

The Stable Outlook on the covered bond rating reflects our expectation of: i) CoFF's stable credit performance; and ii) unchanged fundamental support given our view that European covered bond harmonisation will not negatively impact the fundamental support factors relevant for the issuer and French covered bonds in general.

Highlights since last performance update

Although we cannot determine the impact of the Covid-19 outbreak on the credit risk of the bank or the cover pool, our analysis shows that CoFF's covered bond rating could withstand even a severe increase in default risk for mortgage and public sector obligors.

Over the medium term, CoFF's mixed cover pool will become more strongly focused on domestic sub-sovereign and lower-tier public sector exposures. Following strategic changes within BPCE Group, mortgage loan types previously underwritten by CFF and refinanced by CoFF are now underwritten, managed and refinanced by other BPCE entities. We also expect the cover pool's size to decrease further through a reduction in international public finance exposures.

Ratings & Outlook

Issuer rating	**AA-**
Outlook	Stable
Last rating action	Affirmation
Last rating action date	02.07.18
Covered bond rating	**AAA**
Outlook	Stable
Rating action	Affirmation
Last rating action date	09.04.20

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Related Research

Scope affirms Compagnie de Financement Foncier's French covered bonds at AAA/Stable
April 2020

New Analysis on Crédit Foncier de France SA ('CFF')
January 2020

Covered bond outlook 2020
November 2019

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Bloomberg: SCOP

The issuer

Dedicated covered bond issuer within BPCE Group

CoFF, wholly owned by CFF, is an integral member of BPCE Group (AA-/Stable) and the group's largest covered bond issuer.

Both CFF and CoFF are rated AA-/Stable based on our credit view of the ultimate parent, BPCE. As an affiliated French regulated credit institution (FRCI) within BPCE Group, CoFF benefits from an internal guarantee and solidarity system. As such, BPCE is legally obliged to guarantee the liquidity and solvency of its FRCI affiliates.

BPCE has a leading position in France

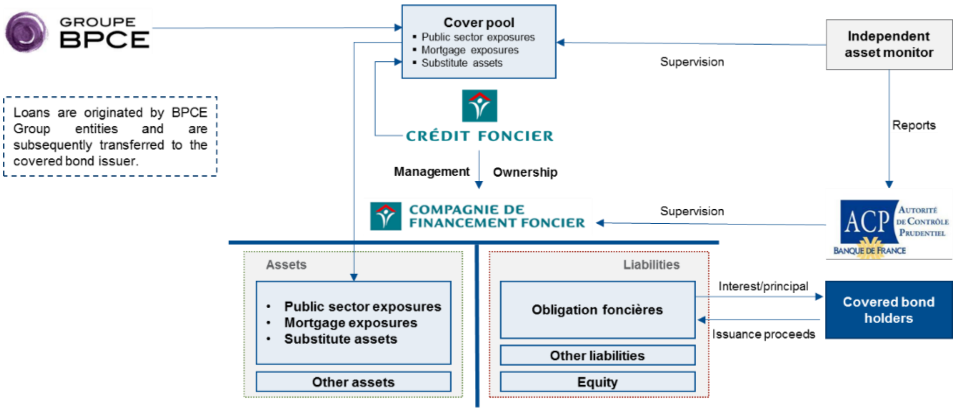
Our credit view reflects the stable and generally predictable financial fundamentals of BPCE Group, as well as its low-risk business model, anchored mostly in domestic retail banking and financial services. BPCE holds a leading position in France's domestic-banking and financial services market.

Further details on our credit assessment of CoFF are available at www.scoperatings.com.

Programme structure

CoFF is an OF issuer operating as a société de crédit foncier. The French covered bond framework permits issuers to operate as specialist banks. Most of CoFF's operations are provided by its parent, CFF, and these activities are governed by service-level agreements. The issuer needs to independently maintain its compliance with regulatory requirements and is independently supervised.

Issuance structure



Source: Scope Ratings

Fundamental credit support analysis

Fundamental credit support factors enhance the covered bond rating by six notches above CoFF's issuer rating. Only three notches are needed to maintain the AAA rating. This is based on our view of: i) France's strong legal covered bond framework; and ii) the benefits of the resolution regime and systemic importance of CoFF's covered bonds.

Two notches of uplift based on legal framework analysis…

The current French covered bond framework meets all the relevant criteria in our rating methodology, allowing up to two notches of rating differentiation. The upcoming European covered bond harmonisation does not impact this assessment.

… plus four notches of uplift reflecting resolution regime

CoFF's covered bonds benefit from an additional credit differentiation of four notches. This is based on our positive assessment of the resolution regime for OFs, our view of the issuer's resolvability, the systemic importance of French covered bonds, and CoFF's high visibility as one of the largest covered bond issuers worldwide. Coupled with an active stakeholder community, we believe these factors could help to avoid negative credit implications for the covered bonds should the issuer fall into distress. For more information, see our related research.

Cover pool analysis

CoFF's cover pool can support at least the same rating uplift as the fundamental credit support factors. The current overcollateralisation (OC) is well above the rating-supporting level, providing the ratings with very high stability. The cover pool supports an uplift of up to nine notches above the issuer rating, of which only three would be needed for the rating in the absence of fundamental credit support factors.

Since our last review in 2019, the minimum supporting OC needed to achieve the highest rating, in the absence of fundamental support factors, has remained unchanged at 6.0% reflecting only small changes in the cover pool composition and stable cash flow risks.

Cover pool characteristics

Reporting date	Dec 2019	Dec 2018
Balance (EUR bn)	70.0	74.7
Residential (%)	54.1	53.1
Commercial (%)	1.1	0.9
Public sector (%)	35.2	37.1
Substitute (%)*	9.5	8.8

*as classified by the issuer

General info – mortgages

Reporting date	Dec 2019	Dec 2018
No. of exposures	483,804	517,058
Avg. size (EUR '000)	80.0	78.6
Top 10	0.3%	0.3%
Remaining life (y)	20	21
WA (indexed) LTV	71.3%	72.3%

Collateral type (%)

Reporting date	Dec 2019	Dec 2018
Owner occupied	72.7	73.6
Buy-to-let	24.3	23.4
Other	3.1	3.0

Repayment type (%)

Reporting date	Dec 2019	Dec 2018
Amortising	98.3	98.4
Bullet	1.7	1.6

Interest type (%)

Reporting date	Dec 2019	Dec 2018
Fixed	91.1	89.2
Floating	8.9	10.8

Collateral ranking (%)

Reporting date	Dec 2019	Dec 2018
1st lien	82.4	84.3
Guaranteed	17.6	15.6

Cover pool composition

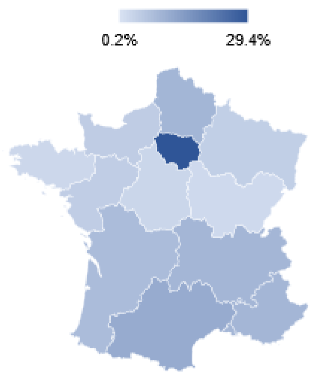
CoFF's covered bond programme is secured by a mixed cover pool comprising public-sector loans (35.2%), mortgage exposures (55.2%) – of which 54.1% are residential and 1.1% commercial – and 9.5% substitute assets. The asset composition has remained broadly stable within the respective sub-pools.

Mortgage pool: composition and credit risk analysis

The mortgage pool is highly granular with around 500,000 loans which are well diversified across France. We have not applied stresses for geographic concentrations and there were no credit-relevant aspects that would warrant a different analytical treatment for non-domestic mortgages (around 2% of the sub-pool). Owner-occupied properties make up around three-quarters of the mortgage asset sub-pool with the remainder mainly comprising buy-to-let mortgages.

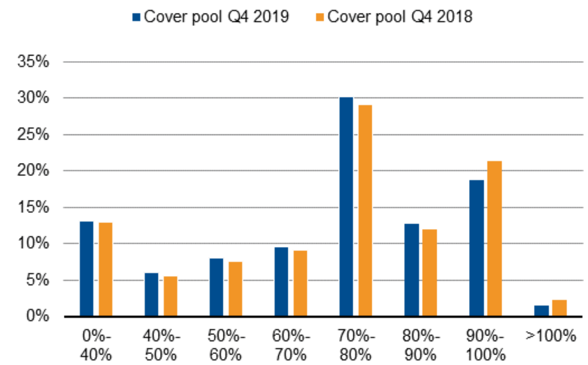
The portfolio has a high share of mortgage loans with a loan/value (LTV) greater than 80%. However, this is not credit-negative as their presence generally reflects additional state guarantees that allow the financing of an LTV of up to 100%.

Regional distribution



Source: Scope Ratings, CoFF.

LTV distribution (indexed)



Source: Scope Ratings, CoFF.

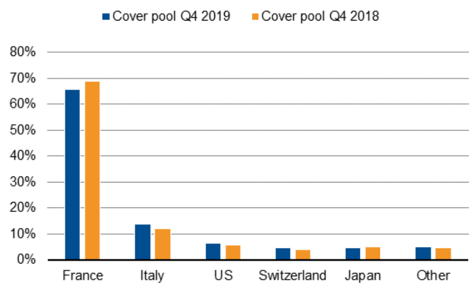
The credit quality of the cover pool remains strong. Our mortgage credit risk analysis takes into account default and recovery vintage data provided by the issuer. The analysed data provides information on the credit performance of annual origination vintages between 2000 and 2016, a timeframe which contains several periods of economic stress.

We assumed an unchanged annual average default probability of 40bps, a stable coefficient of variation of 24% and also maintained the weighted average recovery rate of 95.0% under a base case scenario and 57.0% under the most stressful scenario.

Public sector pool: composition and credit risk analysis

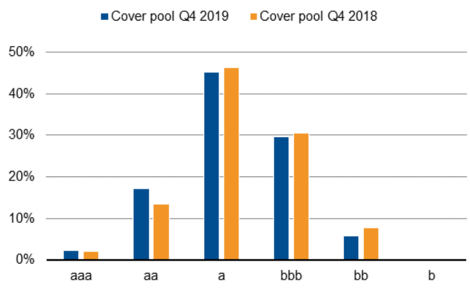
The public sector pool mainly comprises self-originated domestic sub-sovereign and lower-tier public sector exposures. Following the strategic changes mentioned before, we expect the relative share of the public sector sub-pool and its domestic focus to increase over the medium term. International exposures, currently about a third of the sub-pool, will amortise but not be replenished upon their maturity. The weighted average credit quality remained stable at an 'a-' equivalent rating

Geographical distribution



Source: Scope Ratings, CoFF.

Credit quality



Source: Scope Ratings, CoFF.

For the public sector pool, we derived a default distribution by using name-by-name credit assessments and consolidating the exposures into 'risk-representing entities'. We also used a correlation framework to incorporate the impact of geographical and issuer concentrations. The annual average default probability has decreased slightly to 18bps, down from 20 bps in our previous analysis, reflecting a lower share of below-investment-grade exposures. The coefficient of variation has increased to 100% from 97.6% given the portfolio's increased concentration.

For each exposure, we applied stressed recovery rate assumptions ranging between 40% and 75% based on obligor type. This led to an unchanged weighted average recovery rate of 100% under a base case scenario and 65.5% under the most stressful scenario.

General info – public sector

Reporting date	Dec 2019	Dec 2018
No. of exposures	8,191	10,308
Avg. size (EUR '000)	2,823	2,642
Top 10*	27.3%	26.2%
Remaining life (y)	13	14

*per Scope aggregated borrower

Debtor type (%)

Reporting date	Dec 2019	Dec 2018
Sovereigns	16.3	14.7
Regions	32.0	31.2
Municipalities	29.3	30.6
Other	22.4	23.5

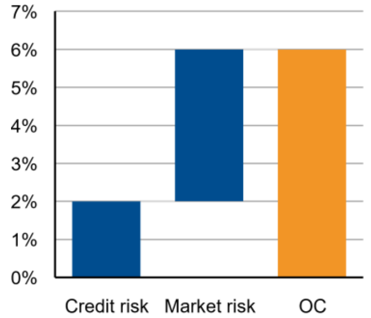
Repayment type (%)

Reporting date	Dec 2019	Dec 2018
Amortising	70.7	70.2
Bullet	29.3	29.8

Interest type (%)

Reporting date	Dec 2019	Dec 2018
Fixed	68.3	69.7
Floating	29.9	28.6
Other	1.8	1.7

Supporting OC breakdown



Source: Scope Ratings

Asset-liability mismatches

	Assets	Liabilities
EUR*	100%	100%
Fixed**	82.4%	90.7%
Floating**	17.6%	9.3%
WAL (years)	8.9	7.1

*post-hedge
**pre-hedge

Cash flow risk analysis

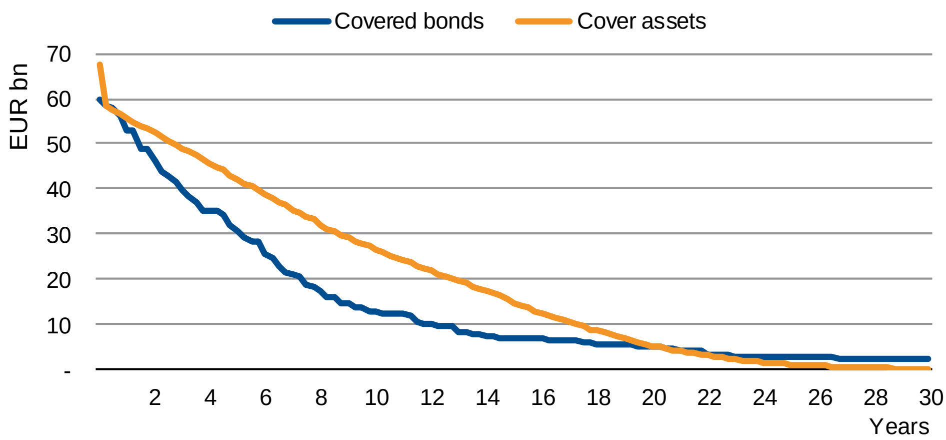
The programme's cash flow risk profile has remained stable, resulting in an unchanged rating-supporting OC level. In the absence of fundamental support factors, i.e. based on the cover pool's credit strength alone, a 6.0% OC would be sufficient to support the AAA rating.

The stability of the rating-supporting OC reflects the issuer's prudent strategy to mitigate market risk (i.e. interest and foreign exchange risks). Residual interest rate risk is low. Maturity mismatch is also limited, reflecting the issuer's focus on matching cash flows, particularly in the short term, and its provision of immediate liquidity for the first 180 days via highly liquid collateral registered in the cover pool.

The rating-supporting OC mainly reflects the programme's sensitivity to low prepayments in combination with increasing and non-reverting interest rates. In a scenario in which asset sales are needed to repay interest or principal, we calculated the net present value of remaining cash flows using a discount curve, adding asset-specific liquidity premiums that reflect the composition of the sub-pools. We used liquidity premiums of 300bps for mortgage assets and 290bps for public sector assets. Market risk in total accounted for an (unchanged) 4pp of the supporting OC of 6.0%.

Credit risk only accounts for an (unchanged) 2pp of the supporting OC. This is low, reflecting the portfolio lifetime mean default rate of 6.8%, a coefficient of variation of 34.4% and a stressed recovery rate of 58.1%.

Amortisation profile



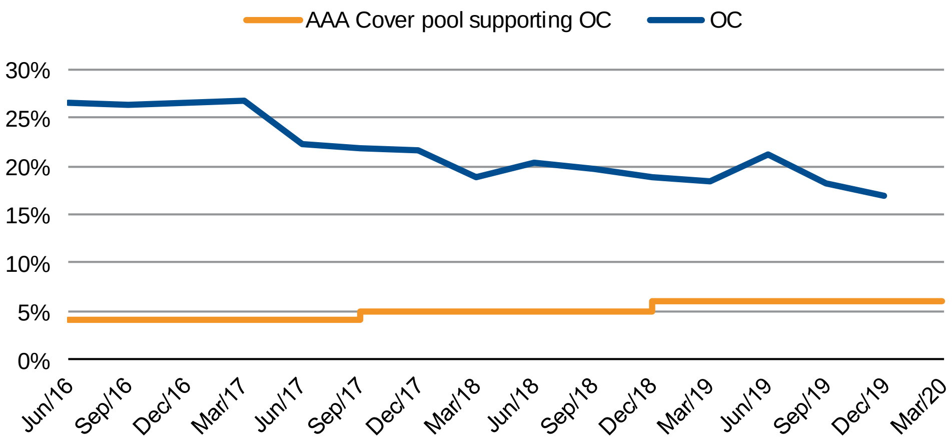
Source: Scope Ratings, CoFF

Availability of overcollateralisation

OC well above legal minimum

CoFF typically provides much higher levels of OC than the minimum stipulated by the legal framework (currently 5%), demonstrating the issuer's willingness and ability to support the covered bond programme's strong credit quality. We also view positively the internal OC guidance as it is not static but rather a function of the portfolio's composition and risk profile. We are not aware of plans that would significantly change the risk profile or reduce available OC.

Available overcollateralisation vs cover pool rating-supporting level



Source: Scope Ratings, CoFF

Other risk considerations

Derivative counterparties generally have high credit quality

CoFF actively uses derivatives to limit or eliminate market risk. We take comfort from the fact that the derivative counterparties generally have high credit quality, benefit from the BRRD, and are resolvable. Further, most derivatives entered into by CoFF have additional mechanisms to mitigate counterparty risk, i.e. collateralisation upon a counterparty's negative credit migration, including its replacement with counterparties of stronger credit quality. Most of the derivatives are market-standard micro and macro hedges, and the diversity of counterparties should also facilitate their replacement.

Sovereign risk does not affect the ratings

Scope currently rates the French sovereign at AA/Stable. Sovereign risk does not limit the ratings of the OFs. The risks of an institutional framework meltdown, legal insecurity or currency-convertibility problems are immaterial at present.

No impact from ESG

We have not directly included ESG aspects in our rating of the covered bonds issued by CoFF. The issuer has no specific ESG underwriting guidelines which provide for positive/negative adjustments to the terms and conditions of a mortgage or public sector loan if minimum ESG conditions are met/not met. We were therefore unable to differentiate between ESG and non ESG compliant assets in our credit risk analysis.

Sensitivity analysis

Three-notch buffer from fundamental support …

The issuer rating of AA- in combination with the fundamental credit support uplift of up to six notches allows the AAA ratings to be maintained without additional credit support from the cover pool, even upon an issuer downgrade of up to three notches.

… plus additional three notches from cover pool support

The covered bond ratings could even withstand an issuer downgrade of up to six notches considering the possible three notches of uplift provided by the cover pool. However, such drastic changes to the issuer rating would require a major adverse shock to the French economic and banking environment or significant, idiosyncratic credit-negative developments affecting either the issuer or BPCE Group. Such events are likely to result in corresponding changes to the cover pool's asset quality and risk structure and would thus require the constant monitoring of the programme's credit quality.

Assuming the issuer's willingness to support the highest ratings as well as a stable covered bond programme risk profile, a one-notch downgrade would increase the cover pool supporting OC, in the absence of fundamental support factors, to 8.0%.

Reporting date	31 Dec 2019	31 Dec 2018[1]
Issuer name	Compagnie de Financement Foncier S.A.	
Country	France	
Covered bond name	Obligations foncières (French covered bonds)	
Covered bond legal framework	French legal covered bond framework	
Cover pool type	Mixed assets	
Composition	Residential = 54.1%	Residential = 53.1%
	Commercial = 1.1%	Commercial = 0.9%
	Public sector = 35.2%	Public sector = 37.1%
	Substitute assets = 9.5%	Substitute assets = 8.8%
Issuer rating	AA-/Stable	AA-/Stable
Current covered bond rating	AAA/Stable	AAA/Stable
Covered bond maturity type	Hard bullet	Hard bullet
Cover pool currencies	EUR (100% hedged)	EUR (100% hedged)
Covered bond currencies	EUR (100% hedged)	EUR (100% hedged)
Fundamental cover pool support	6	6
Maximum achievable covered bond uplift	9	9
Potential covered bond rating buffer	6	6
Cover pool (EUR bn)	70.0	74.7
thereof, substitute assets and deposits (EUR bn)	6.7	6.7
Covered bonds (EUR bn)	59.9	62.8
Overcollateralisation: current / legal minimum	17.0% / 5.0%	19.0% / 5.0%
Overcollateralisation to support current rating	0.0%	0.0%
Overcollateralisation upon a one-notch issuer downgrade	0.0%	0.0%
Weighted average life of assets	8.9 years	9.3 years
Weighted average life of liabilities	7.1 years	7.2 years
Number of exposures (public sector / mortgages)	8,191 / 483,804	10,308 / 517,058
Average loan size (public sector / mortgages, in EUR '000s)	2,823 / 80.0	2,642 / 78.6
Top-10 exposures (public sector / mortgages)	27.3% / 0.3%	26.2% / 0.3%
Interest rate type – assets (before hedge)	Fixed 82.4%	Fixed 81.2%
	Floating 17.6%	Floating 18.8%
Interest rate type – liabilities (before hedge)	Fixed 90.7%	Fixed 90.1%
	Floating 9.3%	Floating 9.9%
Weighted average LTV (indexed)	71.3%	72.3%
Geographic split (top 3) Public Sector	France (65.7%)	France (69.0%)
	Italy (13.9%)	Italy (12.0%)
	US (6.5%)	US (5.5%)
Default measure (public sector / mortgages)	Non parametric / Inverse Gaussian	Non parametric / Inverse Gaussian
Mean default rate (public sector / mortgages)	2.8% / 9.0%	3.0% / 9.0%
Coefficient of variation (public sector / mortgages)	100.0% / 24.0%	97.6% / 24.0%
Weighted average recovery assumption (D0/D9) (public sector)	100.0% / 65.5%	100.0% / 65.5%
Weighted average recovery assumption (D0/D9) (mortgage)	95.0% / 57.0%	95.0% / 57.0%
Interest rate stresses (max./min.; currency-dependent)	-1 to 10%	-1 to 10%
Max liquidity premium (public sector / mortgages)	290bps / 300bps	293bps / 300bps
Servicing fee (public sector / mortgages)	10bps/ 25bps	10bps/ 25bps

D0 and D9 denote the stresses commensurate with the rating distance from the minimum and maximum achievable covered bond uplift

[1] Scope analysed the covered bonds based on detailed performance information provided by the bank. We reconciled this data with publicly available HTT information. Data presented in this report refers to the publicly available information unless noted.

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