Credit Rating Announcement

10 November 2021

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

The issuer rating of A+ combined with fundamental credit support results in the highest achievable ratings for the covered bonds. The cover pool provides additional rating stability.

Rating action

Scope Ratings GmbH (Scope) has today affirmed its AAA ratings on the French covered bonds (obligations foncières) issued by Compagnie de Financement Foncier S.A. (CoFF), the fully owned subsidiary of Crédit Foncier de France, itself a wholly owned subsidiary of BPCE Group. The rating Outlook is Stable.

The rating action follows the downgrade of CoFF's issuer rating to A+/Stable, from AA-/Negative (see here).

Key rating drivers

Solid issuer rating (positive)[1]. The A+/Stable rating of the issuer and its parent reflects CoFF's close integration with BPCE Group, one of France's leading banking franchises.

Fundamental credit support (positive)[2]. Fundamental credit support is the primary rating driver. It provides the covered bonds with six notches of uplift above the issuer rating. As such, only four notches are needed to raise the covered bonds' ratings to the highest achievable level.

Cover pool support (positive)[3]. Scope's cover pool analysis provides additional rating stability. This is reflected by:

1. **Cover Pool Complexity Score (positive).** Scope has assigned the interplay between complexity and transparency a CPC Score of '1', allowing for a maximum additional uplift of up to three notches on top of the fundamental uplift

2. **Over-collateralisation (positive).** The 19.6% of over-collateralisation as of 30 June 2021 can shield the current AAA ratings against a potential issuer downgrade of up to five notches.

3. **Sound credit quality (positive).** The mixed cover pool comprising public-sector loans and seasoned mortgage exposures is of high credit quality, posing low credit risk.

4. **Market risks (positive).** Market risks are moderate reflecting the issuer's prudent hedging and cash flow matching strategy. However, the programme is exposed to rising interest rates given the relatively

long life of floating-rate liabilities.

Rating-change drivers

Scope's Stable Outlook on the covered bonds reflects a rating buffer of five notches, including three notches of potential cover pool support. The ratings may be downgraded upon: i) an issuer rating downgrade by more than five notches; ii) a deterioration in Scope's view on fundamental support factors relevant to the issuer and French covered bonds in general; or iii) an inability of the cover pool to provide uplift if the issuer rating is downgraded by more than two notches.

Quantitative analysis and assumptions

Scope performed a cover pool analysis in order to assess the cover pool's ability to provide additional support should the issuer be downgraded by more than two notches.

Scope's projections of default for CoFF's mortgage loans were made using an inverse Gaussian distribution. Based on credit performance data provided by the bank ('90 days past due' annual vintages between 2000 and 2018), Scope derived an effective lifetime mean default rate of 2.2% and a volatility of defaults (coefficient of variation) of 150.0%. Assumptions included an asset recovery rate of 95.0% in the base case and 67.0% in the most stressed scenario.

Base case recovery rates reflect recovery vintages provided by the issuer. For stressed recoveries, Scope applied rating distance-dependent market value declines to establish stressed recovery rates. Assumptions reflect the developments and unique characteristics of the French housing market. Scope also applied a fire-sale discount of 20%, reflecting a value discount on properties sold under non-standard market or distressed conditions. Scope's stressed security value haircuts for properties securing mortgage loans ranged between 47.5% and 52.5% (depending on the property's location).

Scope used a market-standard portfolio analysis to estimate default statistics for the public sector pool, taking the exposure's credit quality, its amortisation profile and asset correlation assumptions into account. A default distribution was derived for the cover pool using name-by-name credit assessments. A correlation framework accounting for geographical and issuer concentration was also applied. The resulting non-parametric default distribution had a mean default rate of 2.3% and a coefficient of variation of 117.3%. For each exposure, Scope applied obligor-type-specific stressed recovery rates ranging between 40.0% and 75.0%.

The resulting loss distribution and default timing were used to project the covered bond programme's losses and reflect its amortisation structure. The analysis also incorporated the impact of rating distance-dependent interest rate stresses. The covered bond programme is most sensitive to a scenario in which interest rates increase after two years and plateau at 10% thereafter. Foreign exchange risk is fully mitigated via eligible derivatives.

Scope added a liquidity premium for French residential mortgage loans of 300 bps to the rating distance and scenario-dependent discount curve to calculate the cover pool's net present value in the event of an asset sale. This reflects the large share of mortgages that are guaranteed but have high loan-to-value ratios, which Scope considers to be less liquid than 'standard' French mortgage loans. For the public sector pool, Scope applied a weighted average liquidity premium of 289 bps reflecting debtor type and location.

For the mortgage assets, Scope tested for low (1%) and high (up to 15%) prepayments to stress the programme's sensitivity to unscheduled repayments. No prepayments were assumed for the public sector pool as these typically have no prepayment rights. The programme is most sensitive to low prepayments because a maturity mismatch would result in asset sales being necessary to make timely payments on the bonds.

Scope assumed recovery lags of 36 months for unguaranteed mortgage loans and 96 months at the most for guaranteed loans as it expects a significant delay on recovery proceeds due to the government guarantee. A 48-month recovery lag was also assumed for the public sector assets.

Scope assumed servicing fees of 25 bps for the mortgage loans and 10 bps for the public sector pool.

Rating driver references

1. Compagnie de Financement Foncier – Issuer rating
2. Fundamental support assessment France
3. Confidential quarterly cover pool reporting (confidential)

Stress testing

No stress testing was performed.

Cash flow analysis

The Credit Rating uplifts are based on a cash flow analysis using Scope Ratings' covered bond model (Covered Bonds Expected Loss Model 1.0). The model applies Credit Rating distance-dependent stresses to scheduled cash flows to simulate the impact of increasing credit and market risks. The model outcome is the expected loss for a given level of overcollateralisation.

Methodology

The methodologies used for these Credit Ratings and Outlooks, (Covered Bond Rating Methodology, 18 May 2021; General Structured Finance Rating Methodology 14 December, 2020), are available on https://www.scoperatings.com/#!methodology/list.
The models used for these Credit Ratings and Outlooks are (Covered Bonds Expected Loss Model version 1.0 and Portfolio Model 1.0), available in Scope Ratings' list of models, published under https://www.scoperatings.com/#!methodology/list.
Scope Ratings GmbH and Scope Ratings UK Limited apply the same methodologies/models and key rating assumptions for their credit rating services, while Scope Hamburg GmbH's methodologies/models and key rating assumptions are different from those of Scope Ratings GmbH and Scope Ratings UK Limited.
Information on the meaning of each Credit Rating category, including definitions of default, recoveries, Outlooks and Under Review, can be viewed in 'Rating Definitions – Credit Ratings, Ancillary and Other Services', published on https://www.scoperatings.com/#!governance-and-policies/rating-scale. Historical default rates of the entities rated by Scope Ratings can be viewed in the Credit Rating performance report at https://www.scoperatings.com/#governance-and-policies/regulatory-ESMA. Also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope Ratings' definitions of default and Credit Rating notations can be found at https://www.scoperatings.com/#governance-and-policies/rating-scale. Guidance and information on how environmental, social or governance factors (ESG factors) are incorporated into the Credit Rating can be found in the respective sections of the methodologies or guidance documents provided on https://www.scoperatings.com/#!methodology/list.
The Outlook indicates the most likely direction of the Credit Ratings if the Credit Ratings were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The Rated Entity and/or its Related Third Parties participated in the Credit Rating process.
The following substantially material sources of information were used to prepare the Credit Ratings: public domain, the Rated Entity, third parties and Scope Ratings' internal sources.
Scope Ratings considers the quality of information available to Scope Ratings on the Rated Entity or instrument to be satisfactory. The information and data supporting these Credit Ratings originate from sources Scope Ratings considers to be reliable and accurate. Scope Ratings does not, however, independently verify the reliability and accuracy of the information and data.
Prior to the issuance of the Credit Rating action, the Rated Entity was given the opportunity to review the Credit Ratings and Outlooks and the principal grounds on which the Credit Ratings and Outlooks are based. Following that review, the Credit Ratings were not amended before being issued.

Regulatory disclosures

These Credit Ratings and Outlooks are issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0. The Credit Ratings and Outlooks are UK-endorsed.
Lead analyst: Reber Acar, Associate Director
Person responsible for approval of the Credit Ratings: Antonio Casado, Executive Director
The Credit Ratings/Outlooks were first released by Scope on 7 February 2017. The Credit Ratings/Outlooks were last updated on 9 April 2020.

Potential conflicts

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Scope Ratings GmbH is part of the Scope Group with headquarters in Berlin and offices in Frankfurt, London, Madrid, Milan, Oslo and Paris. As the leading European credit rating agency, the company specialises in the analysis and ratings of financial institutions, corporates, structured finance, project finance and public finance. Scope Ratings offers a credit risk analysis that is opinion-driven, forward-looking and non-mechanistic, an approach which adds to a greater diversity of opinions for institutional investors. Scope Ratings is a credit rating agency registered in accordance with the EU rating regulation and operating in the European Union with ECAI status.

Contact

Analyst	Reber Acar	r.acar@scoperatings.com
Team leader	Karlo Fuchs	k.fuchs@scoperatings.com

Scope Ratings GmbH • Lennéstraße 5 • D-10785 Berlin • Phone: +49 30 27891-0 • Fax: +49 30 27891-0
www.scoperatings.com