Compagnie de Financement Foncier - Update

French Covered Bonds – Performance Update

Rating rationale (summary)

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 2018	EUR 74.7bn	Mixed	EUR 62.8bn	AAA/Stable

The rating uplift for fundamental credit support reflects the strong French legal covered bond framework, the positive impact of the resolution framework, and the systemic importance of French covered bonds in general and those issued by CoFF in particular.

The cover pool can support a credit uplift of up to nine notches to the issuer rating. The cover pool continues to comprise high-credit quality cover assets and the programme only exhibits a low to moderate mismatch risk. The stable level of overcollateralisation (OC) continues to mitigate identified risks, creates a buffer against high stresses, and provides rating stability.

Stable Outlook

The covered bond rating is resilient against a significant deterioration in the credit quality of both the issuer and the cover pool, evidenced by the six 'unused' notches of uplift.

	D9	(Unused)	Cover pool support +9
	D8	(Unused)	Cover pool support +8
	D7	(Unused)	Cover pool support +7
Resolution regime +4	D6	(Unused)	Cover pool support +6
Resolution regime +3	D5	(Unused)	Cover pool support +5
Resolution regime +2	D4	(Unused)	Cover pool support +4
Resolution regime +1	D3	AAA	Cover pool support +3
Legal framework +2	D2	AA+	Cover pool support +2
Legal framework +1	D1	AA	Cover pool support +1
Issuer rating	D0	AA-	Issuer rating
Fundamental credit support	**Distance**	**Ratings**	Cover pool analysis

Covered bond uplift

Changes since the last performance update

CoFF's mixed cover pool, will become stronger focused on domestic sub-sovereign and lower-tier public sector exposures. Following strategic changes within the BPCE group, mortgage loan types previously underwritten by Credit Fonciere (CFF) and refinanced by CoFF are now managed and refinanced by other BPCE entities. There are no plans to actively restructure the cover pool via portfolio sales or undertake any other changes.

We expect the cover pool's size to reduce further through a reduction in international public finance exposures and ongoing mortgage amortisation. No credit impact is anticipated from this and we expect the programme to remain prudently managed.

Ratings & Outlook

Issuer rating	**AA-**
Outlook	Stable
Last rating action	Affirmed
Last rating action date	07.02.18
Covered bond rating	**AAA**
Outlook	Stable
Rating action	Affirmed
Last rating action date	17.04.19

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Related Research

Crédit Foncier de France - Issuer Rating Report, 10 October 2018

Compagnie de Financement Foncier - Covered Bonds Rating Report – 07 February 2017

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The issuer

Dedicated covered bond issuer within the BPCE group

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

Issuer rating fully aligned with those of the parent and BPCE group

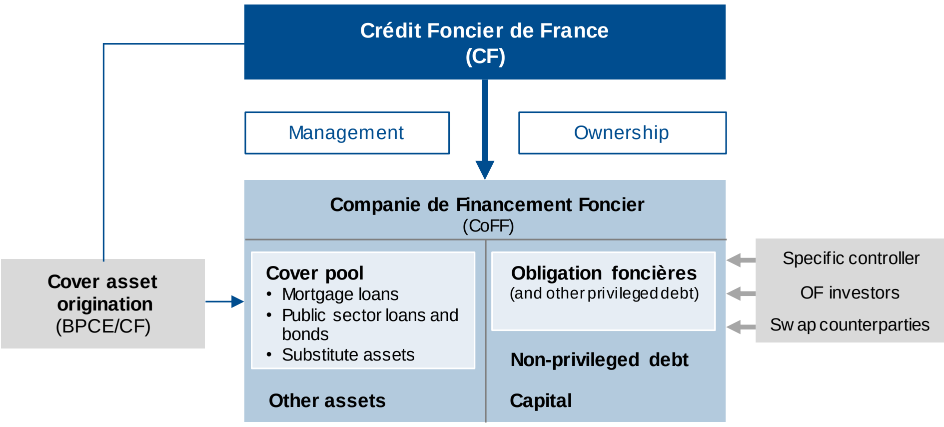
Both CFF and CoFF are rated AA-/Stable based on our credit view of the ultimate parent, BPCE. As an affiliated French regulated credit institution (FRCI) within the BPCE group, CoFF benefits from an internal guarantee and solidarity system. As such BPCE is legally obliged to guarantee the liquidity and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

BPCE has a leading position in France

Our credit view reflects the stable and generally predictable financial fundamentals of the 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 CoFF's credit assessment are available at www.scoperatings.com.

Figure 1: On-balance sheet issuance structure



Source: Scope Ratings

CoFF is an OF issuer operating as a société de crédit foncier (SCF). 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.

Fundamental credit support analysis

Only three out of six notches of uplift needed to support rating

The covered bond rating is based on fundamental credit support, which allows us to assign a positive credit differentiation of up to six notches between CoFF's issuer rating and the covered bond rating. Only three notches are needed to maintain the AAA rating. The rating uplift reflects the strength of the French covered bond framework and our credit-positive view on the resolution regime.

Legal framework analysis

Two notches of uplift based on legal framework analysis

The current French covered bond framework meets all relevant provisions established in our rating methodology, allowing up to two notches of rating differentiation. The French framework builds on individual acts that provide a legal basis for the issuance of covered bonds and their insolvency remoteness. The upcoming European covered bond harmonisation does not impact this assessment.

Resolution-regime analysis

Up to four notches of uplift based on resolution-regime analysis

CoFF's covered bonds benefit from an extra 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, these factors could, in our view, help to avoid negative credit implications for the covered bonds should the issuer fall into distress.

For more information on the legal framework and resolution regime analysis, see the initial rating report on CoFF's covered bonds: Compagnie de Financement Foncier – Covered Bond Rating Report.

Cover pool analysis

Cover pool provides up to nine notches of potential credit support

CoFF's cover pool can support at least the same rating uplift as the fundamental credit support factors. The current 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.

Mixed cover pool

CoFF's covered bond programme is secured by a mixed cover pool comprising public-sector loans (37.1%), mortgage exposures (54.0%) – thereof 53.1% residential and 0.9% commercial – and 8.8% substitute assets. Within the respective sub-pools, the asset composition has remained broadly stable.

Credit risk analysis and composition: mortgage pool

Well diversified, mainly domestic and owner-occupied mortgages

The credit quality of CoFF's mortgage sub-pool is strong, with stable lifetime default rates reflecting the beneficial economic environment in France and CoFF's prudent underwriting standards. Stable property values and loan-to-value (LTV) levels (see Figure 2) combined with state guarantees (see Figure 3) result in high recovery rates in case of a borrower default.

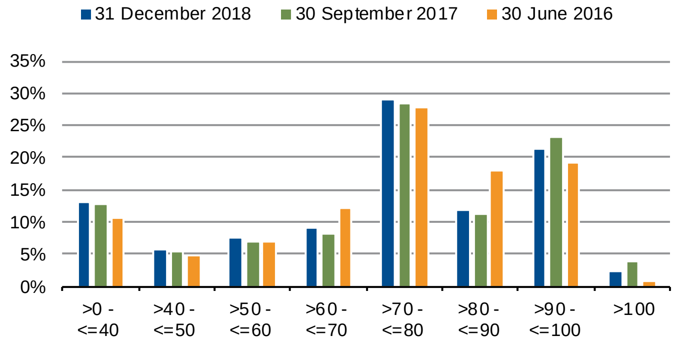
The sub-pool is highly granular with more than 600,000 loans and well diversified across France. We have not applied stresses for geographic concentrations and there were no credit-relevant aspects that would warrant a different analytical treatment for non-domestic mortgages (2.0% of the sub-pool). Owner-occupied properties make up more than three-quarters of the mortgage asset sub-pool with the remainder mainly comprising buy-to-let mortgages.

High LTV loans benefit from additional state guarantees

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

The mortgage credit risk analysis takes into account default and recovery vintage data delivered by the issuer. The analysed data provides information on the credit performance of annual origination vintages between 2000 and 2016, which contains several periods of economic stress.

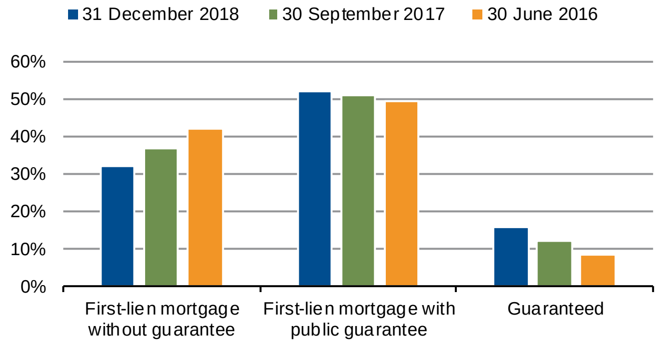
Figure 2: LTV distribution (indexed)*



*The figure shows the LTV on a whole-loan basis, including non -eligible loan parts

Source: Scope Ratings, CoFF

Figure 3: Mortgage 'guarantee' type



Source: Scope Ratings, CoFF

Credit risk analysis and composition: public sector pool

Two-thirds comprises granular domestic sub-sovereign exposures

The credit quality of CoFF's public sector sub-pool is also sound and stable. The sub-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 further increase. International exposures, currently at about a third of the sub-pool, will amortise but not become replenished upon their maturity (see Figure 4).

Average credit quality remains at the a- level

The weighted average credit quality remained stable at an 'a-' equivalent rating (see Figure 5). The changes in the credit metrices such as the mean default rate and coefficient of variation (CoV) mainly reflect: i) our downgrade of the Italian sovereign in December 2018 and its effect on the credit quality of lower-tier Italian public sector exposures in the sub-pool; and ii) the reduction of direct exposures to the French sovereign.

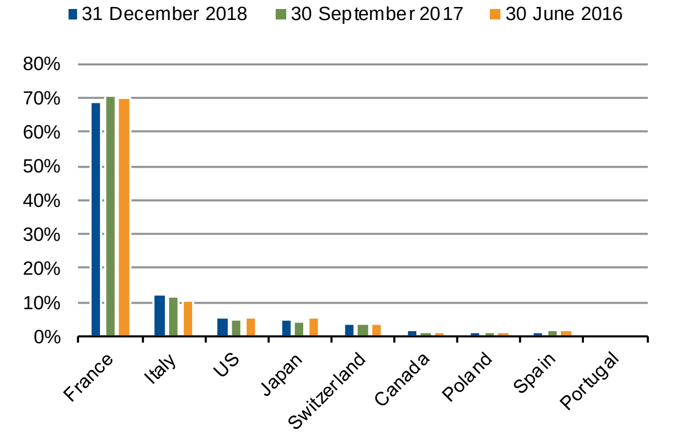
Correlation framework accounts for concentration risks

We derived a default distribution for the cover pool by using name-by-name credit assessments and generally consolidating the exposures into 'risk-representing entities'. We also used a correlation framework to incorporate the impact of both geographical and issuer concentrations.

Recovery rate assumptions based on obligor type and country

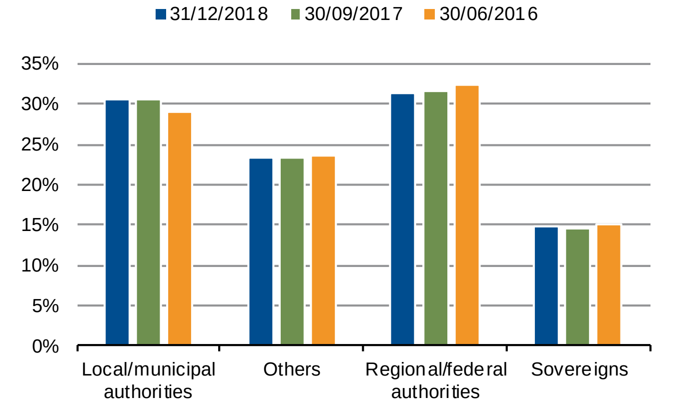
For each exposure, we applied stressed recovery rate assumptions ranging between 40% and 75% based on obligor type.

Figure 4: Geographical distribution



Source: Scope Ratings, CoFF

Figure 5: Credit quality

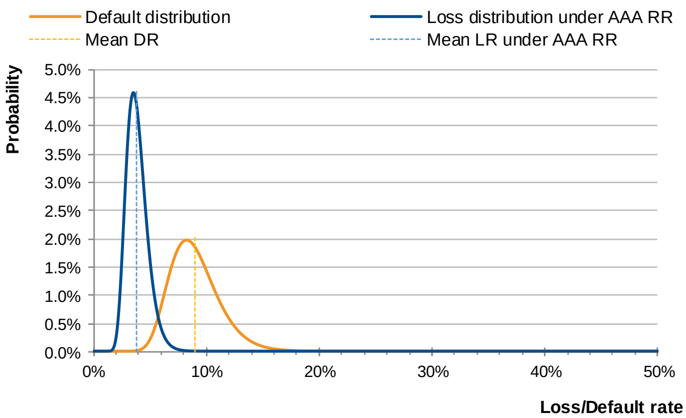


Source: Scope Ratings, CoFF

Credit risk metrices exhibit stability over time

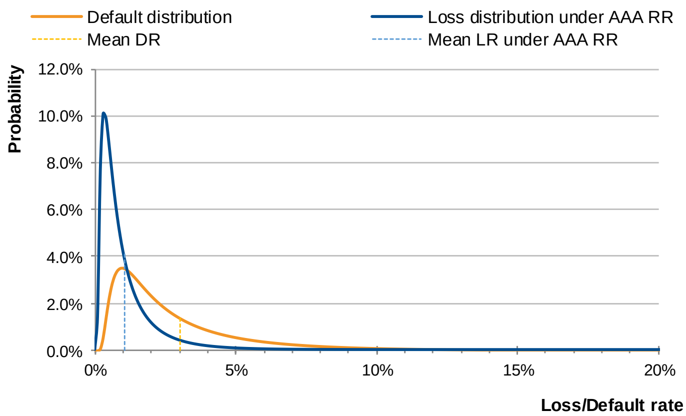
	Mortgage portfolio			Public sector portfolio		
	2016	2017	2018	2016	2017	2018
Mean default rate	8.5%	9.0%	9.0%	3.8%	2.6%	3.0%
CoV	24.6%	22.5%	24.0%	78.9%	102.6%	97.6%
D0 recovery rate	92.8%	93.5%	95.0%	100.0%	100.0%	100.0%
D9 recovery rate	55.7%	56.1%	57.0%	62.8%	62.7%	65.7%

Figure 6: Default and loss distribution, mortgages



Source: Scope Ratings

Figure 7: Default and loss distribution, public sector



Source: Scope Ratings

Cash flow risk analysis

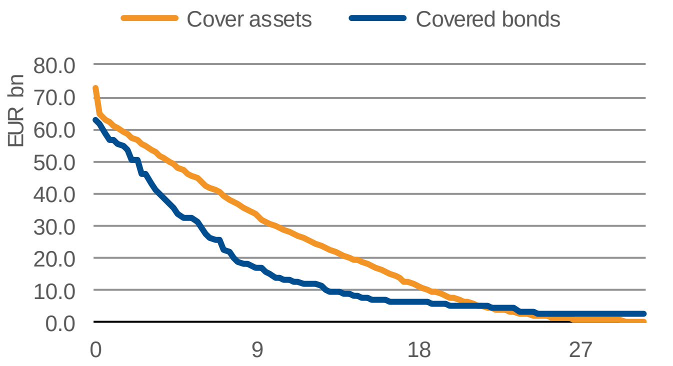
The progamme's cash flow risk profile has remained broadly stable only resulting in in a limited change to the rating-supporting OC level. In the absence of fundamental support factors, thus solely reflecting the cover pool's credit strength, a 6.0% OC would be sufficient to support the AAA rating.

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, with 58.8% of fixed-rate assets against 51.5% of fixed-rate covered bonds. The 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.

Low prepayments and high interest rates drive results

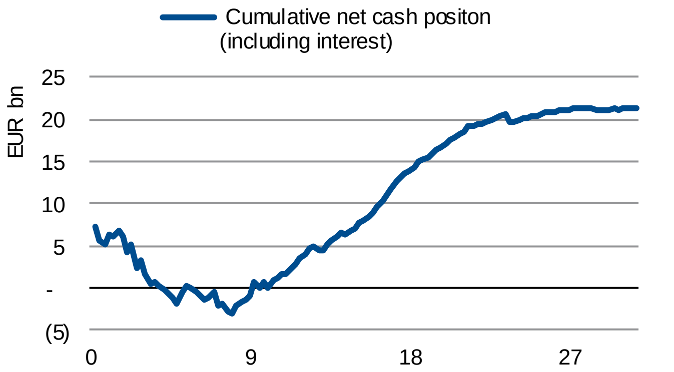
The rating-supporting OC reflects the programme's sensitivity against low prepayments in combination with increasing and non-reverting interest rates. For a scenario in which asset sales are needed to repay interest or principal, we calculate the net present value of remaining cash flows using a discount curve, adding asset-specific liquidity premiums that reflect the composition of the sub-pools. We use liquidity premiums of 300bps for mortgage assets and 293bps for public sector assets.

Figure 8: Amortisation profile



Source: Scope Ratings, CoFF

Figure 9: Cash account



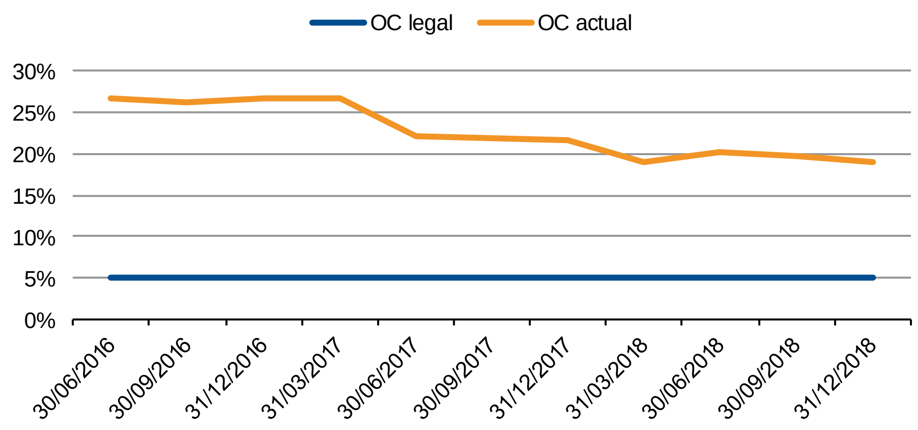
Source: Scope Ratings, CoFF

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 nor reduce available OC.

Figure 10: Programme size and OC development



Source: Scope Ratings, CoFF

Counterparty risk

Derivative counterparties are generally of high credit quality

CoFF actively uses derivatives to limit or eliminate market risk. We take comfort that the derivative counterparties are generally of high credit quality, benefit from the BRRD, and are resolvable. Further, most derivatives entered into by CoFF benefit from 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.

Country risk

Country risk currently not affecting 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 currently immaterial.

Sensitivity analysis

Three-notch rating buffer through fundamental credit 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.

Additional three-notch rating buffer through 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 significant changes in the issuer rating would require a significant adverse shock to the French economic and banking environment or significant, idiosyncratic credit-negative developments affecting either the issuer or the 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 a constant monitoring of the programme's credit quality.

I. Summary of covered bond characteristics

Reporting date	30 June 2016	30 September 2016	31 December 2016
Issuer name	Compagnie de Financement Foncier S.A. (CoFF)	Compagnie de Financement Foncier S.A. (CoFF)	Compagnie de Financement Foncier S.A. (CoFF)
Country	France	France	France
Covered bond name	Obligations foncières (French covered bonds)	Obligations foncières (French covered bonds)	Obligations foncières (French covered bonds)
Covered bond legal framework	French legal covered bond framework	French legal covered bond framework	French legal covered bond framework
Cover pool type	Mixed assets	Mixed assets	Mixed assets
Composition	Residential = 46.9% Commercial = 0.6% Public sector = 40.5% Substitute assets = 12.1%	Residential = 49.4% Commercial = 0.9% Public sector = 41.2% Substitute assets = 8.5%	Residential = 53.1% Commercial = 0.9% Public sector = 37.1% Substitute assets = 8.8%
Issuer rating	AA-/Stable	AA-/Stable	AA-/Stable
Current covered bond rating	AAA/Stable	AAA/Stable	AAA/Stable
Covered bond maturity type	Hard bullets	Hard bullets	Hard bullets
Cover pool currency	EUR (100% hedged)	EUR (100% hedged)	EUR (100% hedged)
Covered bond currency	EUR (100% hedged)	EUR (100% hedged)	EUR (100% hedged)
Fundamental cover pool support (notches)	6	6	6
Max. achievable covered bond uplift (notches)	3	3	3
Potential covered bond rating buffer	6	6	6
Cover pool / Eligible assets (EUR bn)	83.9 / XX	78.4 / XX	74.7 / XX
Covered bonds (EUR bn)	66.3	64.7	62.8
Substitute assets (EUR bn)	10.1	6.6	6.7
Current overcollateralisation / Legal minimum OC	26.7% / 5.0%	21.2% / 5.0%	19.0% / 5.0%
OC to support current uplift	0.0%	0.0%	0.0%
OC to support current rating upon a one-notch downgrade	0.0%	0.0%	0.0%
Cover pool-supported OC	4.0%	5.0%	6.0%
Duration / WA maturity of assets	9.2 / 9.8	9.0 / 9.2	9.0 / 9.2
Duration / WA maturity of liabilities	7.4 / 8	7.8 / 7.8	7.2 / 7.6
Duration gap / WA maturity gap	1.8 / 1.8	1.2 / 1.4	1.7 / 1.6
Number of exposures (public sector / mortgages)	11,506 / 612,781	11,014 / 592,870	10,309 / 600,524
Average loan size (public sector / mortgages, in EUR '000s)	2,957 / 73.81	2,933.6 / 66.5	2,709.8 / 67.7
Top-10 exposures (public sector)	26.3%	28.6%	28.8%
Top-20 exposures (public sector)	33.9%	35.8%	36.1%
Interest rate type - assets after hedge (fixed / floating)	61% / 39%	62.9% / 37.1%	57.8% / 42.2%
Interest rate type - liabilities (fixed / floating)	45.3% / 54.7%	47.7% / 52.3%	51.5% / 48.5%
Geographic split (top 3) Public sector	France (71.1%) Italy (10.3%) US (5.4%) Other (13.3%)	France (73.1%) Italy (10.6%) US (4.6%) Other (11.7%)	France (69.8%) Italy (11.7%) US (5.4%) Other (13.0)
Default measure (public sector / mortgages)	Non parametric / Inverse Gaussian	Non parametric / Inverse Gaussian	Non parametric / Inverse Gaussian
WA DR (public sector / mortgages)	3.8% / 8.5%	2.6% / 9.0%	3.0% / 9.0%
WA CoV (public sector / mortgages)	78.9% / 24.6%	102.6% / 22.5%	97.6% / 24.0%
WA recovery assumption public sector (D0/D9)	100.0% / 62.9%	100.0% / 62.9%	100.0% / 65.5%
WA recovery assumption mortgages (D0/D9)	92.8% / 55.7%	93.5% / 56.1%	95.0% / 57.0%
Current share of loans in arrears	2.80%	2.20%	1.60%
Interest rate stresses (max./min.; currency-dependent)	-1 to 10%	-1 to 10%	-1 to 10%
Forex stresses (max./min.; currency-dependent)	N/A	N/A	N/A
Liquidity premium	291bps	293bps	293bps
Servicing fee	15bps	15bps	19bps

[1] D0 or D9 denote the stresses commensurate with the rating distance between the issuer rating and the covered bond ratings
[2] For the rating analysis and the calculation of the supporting OC we only have taken into account the 'performing balance'

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