FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Credit Mutuel Alliance Federale at 'A+'; Outlook Stable

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Fitch Ratings - Paris - 18 Sep 2023: Fitch Ratings has affirmed Credit Mutuel Alliance Federale's (CM Alliance Federale) Long-Term Issuer Default Rating (IDR) at 'A+' and Viability Rating (VR) at 'a+'. The Outlook on the Long-Term IDR is Stable.

A full list of rating actions is below.

KEY RATING DRIVERS

Decentralised Cooperative Banking Group: Fitch rates CM Alliance Federale as a core part of the wider Groupe Credit Mutuel (Groupe CM), which comprises nearly 2,000 local banks and 18 regional federations grouped into four main sub-groups, among which CM Alliance Federale (about 80% of group assets) and CM Arkea (over 15%) are the largest. We believe the existing solidarity mechanism binding all affiliated CM entities is cohesive enough to substantially equalise their default risk. This is supported by a legally established and effective support mechanism, as the central body (Confederation Nationale du Credit Mutuel; CNCM) can access the group's resources to support its affiliated members. In addition, CM Arkea's recent decision to abandon its independence project has strengthened the group's cohesion.

Groupe CM publishes consolidated audited accounts, is supervised as a group and assigned consolidated resolution debt requirements, which further supports our assessment. There is a common risk framework and overarching risk supervision from the central body, which can prevent affiliated banks from taking on excessive risks. That said, regional groups run independent risk functions and strategies.

Business Profile, Capital Drive Ratings: CM Alliance Federale's ratings primarily reflect our assessment of Groupe CM's stable and profitable retail-and-commercial banking business model. The group leverages on strong franchises in French bancassurance and in consumer finance, and its main autonomous regional sub-groups continue to diversify into insurance, wealth and asset management and corporate banking

The ratings also factor in sound asset quality, a low risk appetite and stronger capitalisation than most French banks'. Stable funding and conservative liquidity also support the ratings.

A Leading Bancassurer in France: Groupe CM has the third-largest retail- and commercial-banking franchise in France, and has well-established market positions in life and non-life insurance. The group generates most of its revenue domestically, but has notable diversification in Germany through CM Alliance Federale, where it is primarily active in consumer finance, leasing and factoring and is rolling out insurance activities and, to a lesser extent, in Belgium.

Groupe CM's main regional groups have well-articulated strategies, and follow conservative and credible long-term goals where they prioritise sustainable organic growth and strong capitalisation.

Conservative Risk Profile: Groupe CM's cooperative status supports a low risk appetite and conservative underwriting standards in key lending products across the group. Regional sub-groups have limited tolerance for traded market risks, compared with larger French peers, which benefits their risk profile.

Similar to other French banks, Groupe CM has high exposure to structural interest rate risks due to the excess of long-dated fixed-rate assets over liabilities, but these risks are managed conservatively by the main regional groups. CM Alliance Federale's and CM Arkea's net interest income in retail banking in 1H23 was more resilient than French peers'.

Sound Asset Quality: Groupe CM's 2.4% impaired loans ratio at end-2022 remained higher than that of similarly rated European peers. However, this is mitigated by the group's high coverage by loan loss allowances and lower exposure to vulnerable corporate sectors and borrowers.

The current economic slowdown and higher-rate environment will only moderately weaken the group's asset quality, and we expect the impaired loans ratio to increase slightly but to remain below 3% by end-2025. We forecast that Groupe CM's loan impairment charges (LICs) will continue normalising from their low levels to around 25bp of gross loans for 2023-2025.

Resilient Profitability, Good Cost-Efficiency: Groupe CM has a sound and consistent profitability record, which benefits from the group's diversification. But its operating profit/risk-weighted assets (RWAs) will likely remain below 2% in 2023-2024 (2022: 2.1%) due to interest margin pressure in France, reduced private-equity results, rising LICs and sustained underlying cost inflation. Despite being more decentralised than French peers, Groupe CM's main regional groups have a sound cost efficiency, in particular at CM Alliance Federale.

Very Strong Capitalisation: Groupe CM's very strong capitalisation underpins the ratings and compares favourably with most French and European banks'. This is because the main regional groups adopt prudent capital planning and have limited pay-outs to cooperative owners.

The group's end-2022 common equity Tier 1 (CET1) ratio of 18.8% provided an ample buffer above regulatory requirements, despite a material drop of 70bp in 2022. We project the CET1 ratio to remain above 18% in 2023 and to gradually converge towards 20% in the medium term. The group's 6.7% leverage ratio at end-2022 is well above the peer average and supports our assessment.

Stable Funding, Conservative Liquidity: Groupe CM benefits from a large and stable deposit base, originating mainly from its local retail banking networks in France, although it structurally has a slightly higher loans/deposits ratio than that of large French peers, at around 110% at end-2022.

Liquidity is managed conservatively by the main regional groups, which hold large buffers of liquid assets. The group's large buffer of cash, central-bank placements and high-quality liquid assets (about 17% of total assets excluding insurance at end-2022), comfortably covers short-term funding and long-term debt falling due in the next 12 months, despite significant repayments of targeted longer-term refinancing operations in 1H23.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

The ratings are primarily sensitive to a sharp deterioration in the French operating environment leading to an unmitigated marked weakening of group's financial profile. In particular, the ratings could be downgraded on the combination of a sustained reduction of Groupe CM's operating profitability/RWAs to below 1.5%, deterioration of its CET1 ratio to below 14% and a sustained increase in the impaired loans ratio to materially above 3%, which we view as unlikely in our baseline scenario.

Although not expected, a material increase in risk appetite, for instance leading to outsized and uncontrolled expansion in volatile businesses or geographies and reduced capital targets, could put pressure on CM Alliance Federale's ratings.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

An upgrade would require a significant strengthening of Groupe CM's franchise and increased geographic and business diversification, while further improving operating profit/RWAs to levels consistently above 2.5% while maintaining a conservative risk appetite and very strong capitalisation. A sustained improvement in the impaired loans ratio to 1% or lower, which is unlikely given the current ratio, would also be rating-positive.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

CM Alliance Federale's 'a+' score for funding and liquidity results in a Short-Term IDR of 'F1', which is the lower of two possible Short-Term IDRs mapping to an 'A+' Long-Term IDR.

The total minimum requirement for own funds and eligible liabilities (MREL) is set at the level of Groupe CM at 20.99% of RWAs. As Groupe CM does not have a central debt-issuance entity, each of the CM sub-groups, including CM Alliance Federale and CM Arkea, will need to have own funds and eligible liabilities above this threshold for Groupe CM to comply with MREL.

We expect Groupe CM will continue to meet MREL without recourse to senior preferred debt. Groupe CM reported a subordinated MREL ratio (excluding senior preferred debt) of 22.8% at end-2022. We estimate the ratio to have increased further at end-June 2023, as Banque Federative du Credit Mutuel S.A. (BFCM) recently issued large amounts of Tier 2 and senior non-preferred debt.

BFCM's and Credit Industriel et Commercial's (CIC) long-term deposits and senior preferred debt ratings are one notch above CM Alliance Federale's Long-Term IDR to reflect the protection that would accrue to their depositors and senior preferred creditors in a resolution from the sizeable equity and more junior debt buffers available within Groupe CM. For the same reasons, we rate BFCM's senior non-preferred long-term debt in line with its Long-Term IDR.

BFCM's and CIC's 'F1+' short-term deposit and senior preferred debt ratings are the only options mapping to their 'AA-' long-term ratings. BFCM's Derivative Counterparty Rating (DCR) of 'AA-(dcr)' is in line with its equally ranking senior preferred debt and deposits.

We rate BFCM's subordinated Tier 2 debt two notches below CM Alliance Federale's VR for loss severity as we expect poor recoveries for this type of debt in a bank failure or resolution. Deeply subordinated legacy Tier1 securities are rated four notches below CM Alliance Federale's VR to reflect the high loss severity risk of these securities (two notches from the VR), and a higher risk of non-performance (an additional two notches) relative to CM Alliance Federale's VR.

Government Support Ratings (GSR)

CM Alliance Federale's, BFCM's and CIC's GSRs of 'no support' reflect Fitch's view that although possible, sovereign support cannot be relied on. Legislative, regulatory and policy initiatives, including the implementation of the EU's Bank Recovery and Resolution Directive, have substantially reduced the likelihood of sovereign support for EU commercial banks in general, in our view. This implies that senior creditors would probably be required to participate in losses, if necessary, instead of the bank receiving sovereign support, despite Groupe CM's systemic importance in France.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

Fitch would downgrade CM Alliance Federale's Short-Term IDR in case of a combined two-notch downgrade of the Long-Term IDR and of the funding and downward revision of the liquidity score. Conversely, we could upgrade the Short-Term IDR either if the Long-Term IDR is upgraded to 'AA-' or if the funding and liquidity score is revised up to 'aa-'.

The senior preferred and senior non-preferred debt, deposit ratings and DCRs are sensitive to CM Alliance Federale's Long-Term IDR. They could also be downgraded if Fitch no longer expects Groupe CM to meet its MREL exclusively with senior non-preferred debt and more junior instruments.

The ratings of the subordinated debt and deeply subordinated debt issued by BFCM are primarily sensitive to a change in CM Alliance Federale's VR.

An upgrade of CM Alliance Federale's, BFCM's and CIC's GSRs would be contingent on a positive change in the French sovereign's propensity to support domestic banks. While not impossible, this is highly unlikely, in Fitch's view.

SUBSIDIARIES & AFFILIATES: KEY RATING DRIVERS

Fitch assigns a group VR to CM Alliance Federale and its subsidiaries, BFCM and CIC, which are core banks for Groupe CM. This is because the two subsidiaries are large and highly integrated domestic banks. Their credit profiles cannot be disentangled from those of CM Alliance Federale and Groupe CM and we view their failure risk as substantially the same as the group as a whole.

Only BFCM is affiliated to Groupe CM's central body and as such it could benefit from the national-support mechanism, which by extension could also benefit CIC if BFCM is unable to provide the necessary support to CIC, because it would find itself in financial difficulties.

BFCM made up about 65% of Groupe CM's consolidated assets at end-2022. BFCM is the group's main issuing vehicle on financial markets and it coordinates the activities of CM Alliance Federale's subsidiaries. CIC is owned by BFCM and accounts for about 40% of group assets. It is one of the group's two retail and commercial networks in France and hosts the group's modest corporate- and investment-banking activities. BFCM and CIC are highly integrated with CM Alliance Federale in management, systems, capital and liquidity.

As a result of the above, the IDRs of BFCM and CIC are equalised with those of CM Alliance Federale.

SUBSIDIARIES AND AFFILIATES: RATING SENSITIVITIES

BFCM's and CIC's ratings will move in tandem with those of CM Alliance Federale, unless Fitch ceases to view BFCM and CIC as core banks within the group, which we do not expect given their role and importance within CM Alliance Federale.

VR ADJUSTMENTS

CM Alliance Federale's implied VR Key Rating Drivers are derived from Groupe CM's consolidated accounts.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation of the materiality and relevance of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Credit Mutuel Alliance Federale	LT IDR	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Stable
	ST IDR	F1	Affirmed	F1
	Viability	a+	Affirmed	a+
	Government Support	ns	Affirmed	ns
Banque Federative du Credit Mutuel S.A.	LT IDR	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Stable
	ST IDR	F1	Affirmed	F1
	Viability	a+	Affirmed	a+
	DCR	AA-(dcr)	Affirmed	AA-(dcr)
	Government Support	ns	Affirmed	ns
junior subordinated	LT	BBB	Affirmed	BBB

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Bank Rating Criteria (pub. 01 Sep 2023) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Credit Industriel et Commercial	EU Issued, UK Endorsed
Credit Mutuel Alliance Federale	EU Issued, UK Endorsed

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