ANALYSES ET SYNTHESES

French banks' lending to the professional real estate sector in 2014

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Contents

Overview

- Against the backdrop of generally buoyant European commercial real estate markets and overall moderate price increases, new lending by French banks to the professional real estate sector rose by 8% in 2014. While France continues to account for over 70% of new loans, its share contracted for the third consecutive year, due to the much stronger lending growth in other countries (+28.1%), in particular in the United States and in Asia, than in France (+2%). While some of the growth observed outside the euro area can be attributed to exchange rate effects (appreciation of sterling and the US dollar), volumes also rose sharply. Furthermore, new lending was driven by investors and property companies whose share (40.5% - up steadily since 2011) is now almost equal to that of property developers (41.7% - falling constantly since 2008). Lastly, while residential property continues to account for the bulk of new lending, its share fell in 2014 to the benefit of offices.
- Total exposures increased slightly (+1.7%) to EUR 185.8 billion. Two-thirds of exposures were to France, and the remaining third was split between Europe and the rest of the world. In Europe, outside France, the main recipients were Belgium and Italy while the United States was the main recipient outside Europe. Moreover, investors and property companies continued to account for the bulk of exposures (45.2%), with their share rising by a further 0.5 percentage point in 2014. Lastly, the breakdown of exposures by asset type has changed slightly due to the rise in residential property, which remains by far the main recipient of new lending.
- The quality of exposures has improved as the non-performing loan ratio fell to its lowest level since 2009, to stand at 6.56%. This chiefly reflects the resolution of disputes or their out-of-court settlement, as favourable market conditions facilitated asset sales by troubled borrowers. Furthermore, the coverage ratio increased slightly to 37.2%, its highest level since 2008.
- Lastly, French banks' exposures to illiquid assets inherited from the financial crisis are now minimal.

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JEL Code: G21

Key words: banks, professional real estate sector

Preliminary comments

- This issue of "*Analyses et Synthèses*" is based on responses collected in the framework of the 2014 annual survey on lending to the real estate sector, conducted by the General Secretariat of the ACPR (SGACPR).
- This survey, covering the main French banks[1], includes, on the one hand, data on the new lending and exposures of the banks in question to real estate professionals and, on the other hand, more qualitative information about notably commercial policy, the risk management framework and market perception and developments.
- The survey covers all types of exposures (in particular loans, leasing and similar transactions, credit derivatives, etc.) of the relevant credit institutions to real estate professionals (developers, institutional investors, property companies, real estate brokers, etc.), including entities held by credit institutions and consequently integrated into their consolidation scope, whose business consists of financing property development activities, buy-to-let investment operations and property restructuring. It therefore does not cover exposures to individuals (home buyers) or loans granted to non-financial corporations that purchase or build a property (e.g. hotels, shopping centres, leisure centres, production plants, etc.) to be used for their own purposes. Nor does it cover intermediaries such as estate agents.
- From the 30th of June 2015, the format of the questionnaire will be changed in order to collect more granular information on both new and existing loans, and for an increased number of risk indicators. Moreover, the new template cross-references both the different types of borrowers (whose list has been extended: large listed property companies, specialised finance companies, developers, property brokers, etc.), and geographical areas. The first data are expected on 30 September 2015.

[1] BNP Paribas (BNPP), Société Générale (SG), Groupe Crédit Agricole (GCA) – Caisses régionales de Crédit agricole and LCL –, Groupe bpCE (GBPCE) and Groupe Crédit Mutuel (GCM) – CIC and Banque européenne du Crédit mutuel (BECM).

1. Commercial real estate markets in 2014

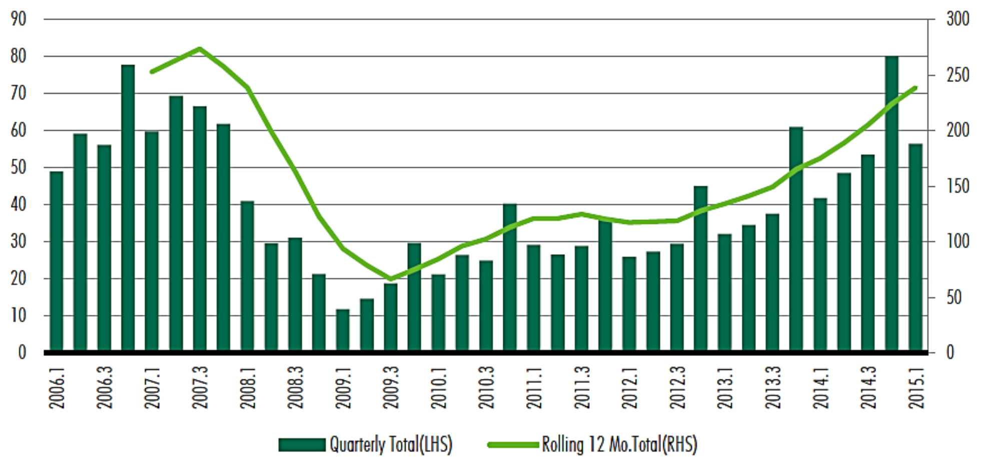
The main commercial real estate markets have a strong European or even international component as investments come from a wide range of geographical areas. In this context, the assets financed by French banks may be located in different countries (see Sections 2 and 3) and the risks to which they are exposed partly reflect the situation of these markets and their developments.

1.1. The commercial real estate market in Europe

1.1.1 Continued growth in commercial real estate transactions[2]

Activity on European commercial real estate markets has become buoyant again thanks to renewed growth in several euro area countries, the increased volume of liquidity and the decline in interest rates resulting from the European Central Bank's quantitative easing, and the continued sell-off of assets by some large European banks. Standing at EUR 223 billion at end-2014 (up 30% on 2013), the total amount of transactions thus returned to the level observed in Q1 2008, with the volume of transactions in Q4 2014 even exceeding the peak reached in Q4 2006 (Chart 1).

Chart 1
European investment turnover (EUR billions)[3]



Source: CBRE

This surge in activity was driven by foreign investors (which accounted for around EUR 100 billion of transactions volumes in 2014), especially from the United States, as well as by the increase in the share of high value transactions (the number of transactions over EUR 100 million in particular rose by 39% in 2014 in Europe).

London and Paris are the first two recipients of commercial real estate investment in Europe with a total market share of 26%. With a 52% rise in volumes, Paris saw a particular dynamic year, while London experienced a 9% fall. In the rest of Europe, the Irish and Spanish markets saw a sharp pick-up in investment after several sluggish years; Dublin and Madrid in particular posted rises of 131% and 103% respectively.

Within commercial real estate, the offices segment remained the main recipient of investment; while take-up[4] in this segment reached in Q4 2014 its highest level

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[2] Corporate real estate covers in particular offices, business premises and retail outlets; residential property is excluded.

[3] Transactions of above EUR 4 million concerning offices and business premises, warehouses and stores.

[4] Take-up corresponds to premises sold or rented during the period under review.

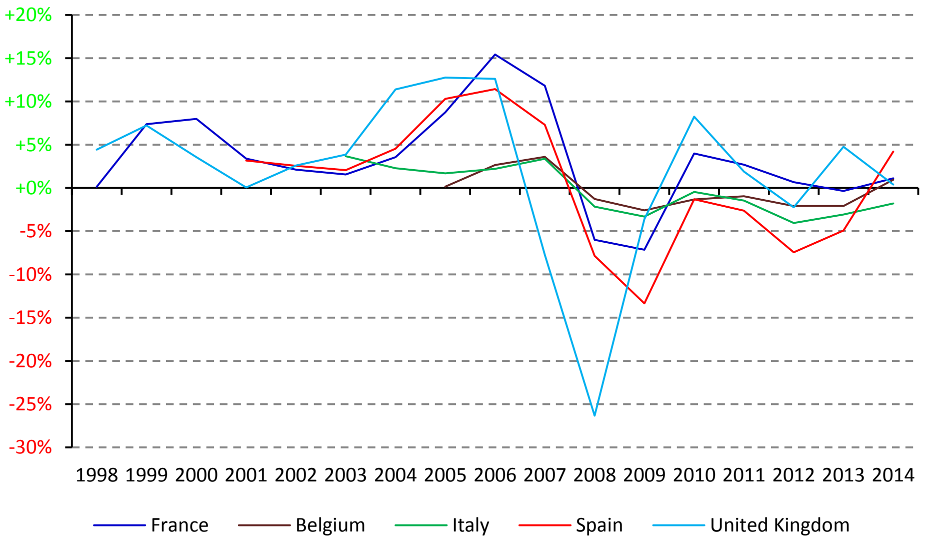
since the 2009 crisis, its market share in total investment nevertheless declined in 2014, as did that of the retail segment, due to the rise in transaction volumes in the hotel segment. Lastly, there was a sharp rise in activity in the industrial and logistics sector (+49%).

For its part, residential real estate[5] generally posted sharp growth in the main European markets but tended to lose momentum compared with 2013.

1.1.2 Moderate price growth on the main markets to which French banks are exposed

Among the main markets to which French banks are exposed (see Section 3), Spain recorded a price rise of 4.2%, with more moderate increases in France (+1.1%), Belgium (+1%) and the United Kingdom (+0.4%). Italy however suffered a seventh year of falling prices (-1.8%; Chart 2).

Chart 2
Commercial real estate prices in Europe (%)



Source: MSCI[6]

Overall, prices tended to fall in other European markets (-3.9% in Sweden, -1.1% in the Netherlands) or increased very slightly (+0.8% in Germany, +1.3% in Portugal); Ireland, which appears to be a particularly cyclical market, nevertheless registered an exceptionally large rebound of 30.7%.

Lastly, and more specifically, the rise in demand with relatively constrained supply may be a factor driving property price increases: for instance, prices rose by 9.5% in London, 18.1% in Paris and 2.2% in Frankfurt[7].

1.1.3 A slight decline in returns

Continuing the trends underway since 2010 for the first two countries and 2012 for the third, rental returns[8] fell in the United Kingdom (-81 basis points (bps)), France (-26 bps) and Italy (-28 bps); conversely, they rose in Belgium (39 bps) and Spain (15 bps), where they have alternated between rises and falls for several years (Chart 3).

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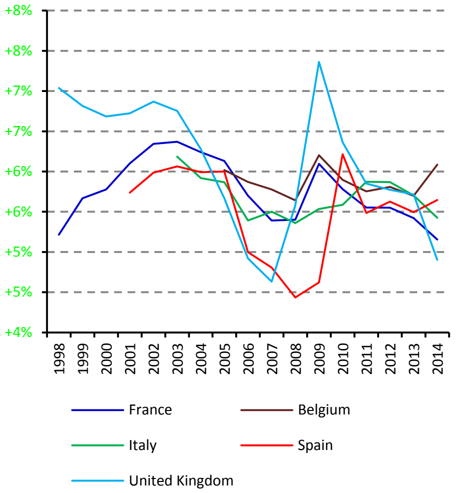
[5] Rental investment (concerning individual properties (flats, houses) or collective (appartment buildings)) and new housing purchases.

[6] Formerly IPD

[7] Source: CBRE

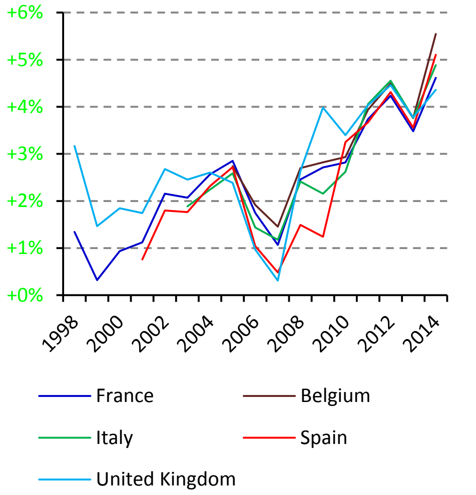
[8] Rental investment in commercail real estate corresponds to the ratio of the amount of rents to the purchase value of the rented properties.

Chart 3
Income returns on commercial property for a selection of European markets



Source: MSCI

Chart 4
Risk premia[9] on commercial property for a selection of European markets



Source: MSCI, Banque de France and ACPR calculations

The increase in the value of assets (see above) in the United Kingdom and France at least partially explains the decline in returns in both countries. Conversely, in Italy, it is explained by a faster fall in rents than that of the value of assets. Lastly, rents in Belgium and Spain seem to have increased more rapidly than asset values.

The decline in rental returns in France, the United Kingdom and Italy was nevertheless less rapid than that of long-term interest rates. All the countries under review saw a rise in their risk premia, in line with their trend underway since 2007 and reached their highest levels since 1998 (Chart 4).

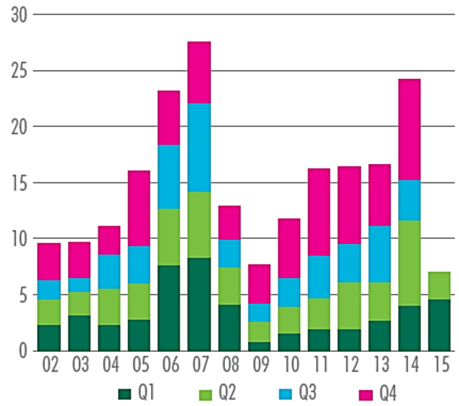
1.2. The French market

1.2.1. A sharp rise in transactions

In line with trends in European markets, the French commercial real estate market ended 2014 with a 46% rise in transactions compared with 2013 after three years in which volumes had remained relatively stable, at around EUR 16 billion. Standing at EUR 22.7 billion, transactions returned to their level of 2006 (Chart 5).

[9] The risk premium was estimated by the difference between the rental return of each country and the yield on Germany's 10-year Bund, taken as a proxy for the risk-free rate.

Chart 5
Amounts invested in standard commercial property in France by quarter
(EUR billions)



Source: CBRE and Immostat

Like on European corporate real estate market, offices continued to attract the bulk of investments, notably on account of the large number of high-value transactions (over EUR 100 million). The market share of this segment nevertheless contracted by 6 percentage points (pps) compared with 2013 owing to the sharp rise in the volume of transactions involving retail outlets, which almost doubled in one year, due in particular to the numerous disposals of shopping centres. Similarly, the logistics sector was dynamic, driven by property companies' sales. Conversely, transactions involving smaller assets (i.e. with a unit price of under EUR 10 million) fell by around one-third compared with the average level observed between 2011 and 2013.

Most transactions concerned assets located in Île de France, even though the share of the Paris Central Business District (CBD)[10] almost halved between 2013 and 2014. Outside Paris, the Rhône Alpes region was the most buoyant, but its relative share declined in favour of the PACA region (south-east), whose size nevertheless remains twice as small.

French investors were the most active, even though their share contracted slightly in 2014, from 62% in 2013 to 59%[11]. These investors comprised mainly investment funds (27%) followed by, in almost equal measure (between 15% and 16%), unlisted property companies, insurance firms and real estate investment companies (SCPI). Others included listed property companies and sovereign wealth funds as well as real estate collective investment funds (OCPI)[12] and private investors (via real estate companies (SCI) in particular).

Lastly, transactions carried out by US investors almost doubled compared with 2013. These transactions, which were mainly made by pension funds, private equity firms or asset management companies, chiefly concerned prime real estate.

Residential real estate for its part remained relatively subdued: in year-on-year terms, housing starts were only just above the level observed in 2000 and household investment in housing reached its lowest level for almost 16 years at end-2014. A recovery nevertheless appears to be underway since Q4 2014, with a revival of sales of new dwellings.

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[10] The CBD comprises the 1st, 2nd, 8th, 9th, 16th and 17th arrondissements of Paris. It extends westward to Porte Maillot, the avenue de Malakoff and Trocadéro; northward to Porte Champerret, the avenue de Villiers and Gare Saint Lazare; eastward to rue Montmartre and rue du Louvre; and southward to rue de Rivoli (source: Immostat).

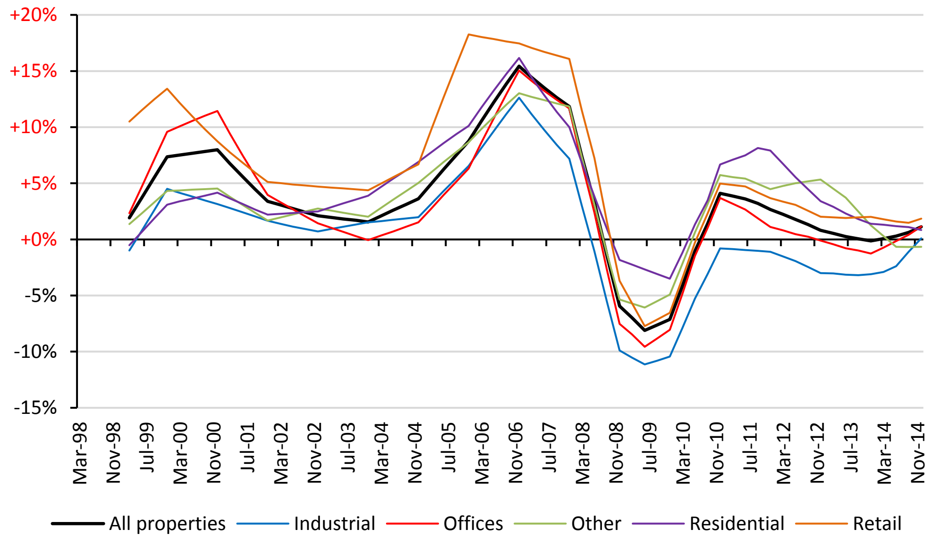
[11] Source: DTZ

[12] OPCI are collective vehicles investing 60% of their assets in physical tertiary real estate.

1.2.2. Moderate growth in prices

With the exception of the other asset segment, all other segments recorded price increases in 2014. These rises nevertheless remained modest and relatively homogeneous across sectors. With an increase of 1.85%, the retail segment was the most dynamic. As regards the industrial premises sector, after over six years in negative territory, it returned to growth, inching up by 0.1% (Chart 6).

Chart 6
Changes in property prices in France by segment



Source: MSCI

1.2.3. Falling rents

With ongoing rises in prices, underpinned by strong demand, average returns contracted further in 2014, falling for example from 4.25% to 3.75% in the CBD or from 5.75% to 5.5% outside Paris.

While, in Île de France, the slight increase in headline rents[13] somewhat limited the decline in yields, real rents, which notably take account of renegotiations during tenancy, rent rebates and aid measures (covering cost of work, etc.) granted by landlords to tenants, continued to fall. According to estimates by Crédit Foncier de France, compared to headline rents, real rents may now represent a discount of between 6% and 30 % in La Défense, 8% and 22% in Lyon, and 6% and 25% in Lille.

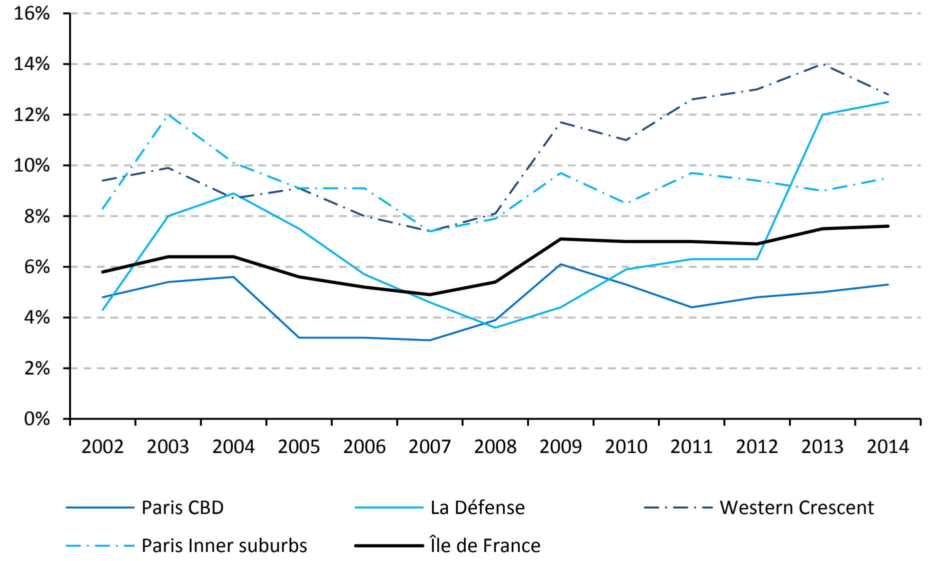
However, the decline in rental returns was less rapid than that of long-term yields. In these conditions, risk premia, measured by the difference with the 10-year French sovereign interest rate (OAT), rose again.

[13] Contractual rents as set out in leases between tenants and landlords.

1.2.4. Office vacancy rates stable in Île de France

The office vacancy rate[14] in Île de France stood at an average level of 7.6% (up 10 bp) but remained lower than the European average (9.6% according to JLL). It nevertheless differs considerably between the CBD (5.2%) and La Défense or the Western Crescent[15] (12.5% and 12.8% respectively). Lastly, with the exception of this latter area, where there was a marked slowdown (-1.2 pp), the vacancy rate continued to increase in other areas (Chart 7).

Chart 7
Changes in the office vacancy rate in Île de France



Source: DTZ

[14] Ratio between space available (for leasing or sale) and the total available space for a given geographical sector.

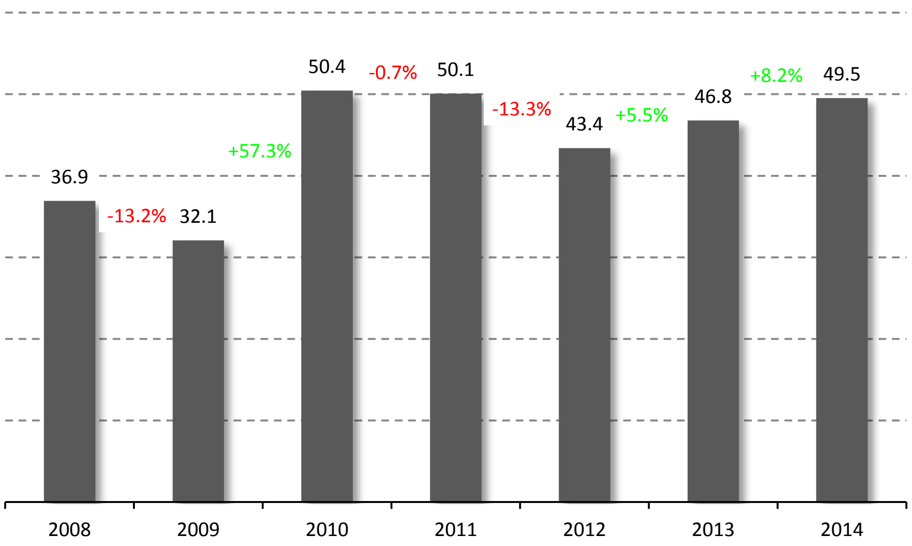
[15] The Western Crescent covers the following towns: Courbevoie, Nanterre, Puteaux, Rueil-Malmaison, Suresnes, Neuilly-sur-Seine, Levallois-Perret Boulogne-Billancourt, Issy-les -Moulineaux, Meudon, Sèvres, St-Cloud, Asnières-sur-Seine, Bois-Colombes, Clichy, Colombes, Gennevilliers, La Garenne-Colombes and Villeneuve-La-Garenne (source: Immostat)

2. New lending to real estate professionals

2.1. Growth in new loans picked up in 2014

Total new lending stood at EUR 49.5 billion in 2014, up 8.2% on the previous year (Chart 8). Two groups nevertheless saw a decline in their new lending (-1.8% and -3.6% respectively), while three others registered growth of between 5% and 69%.

Chart 8
New lending in EUR billions



Source: SGACPR annual survey

New loans granted still account for the bulk of new lending (EUR 31.1 billion, up 10.5%) whilefunding commitments and guarantee commitments amount to EUR 18.4 billion, up 8.2%. As a result, the share of loans in new lending increased slightly to 62.8% whereas that of off-balance sheet commitments contracted to 37.2%, its lowest levels since 2008 (Chart 9). Lastly, funding commitments continued to account for a growing share of total new commitments, while that of guarantee commitments declined (Chart 10).

Chart 9
Breakdown of new lending

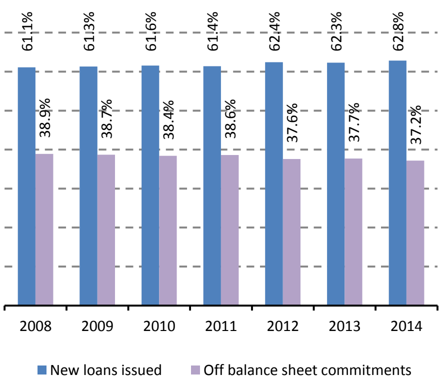
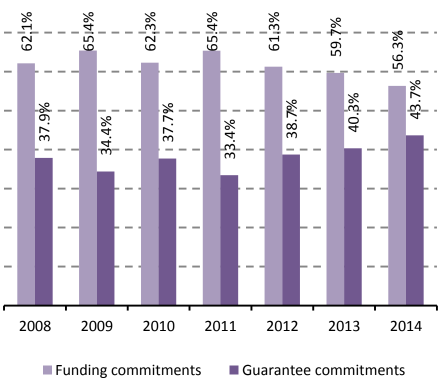


Chart 10
Breakdown of off-balance sheet commitments



Source: SGACPR annual survey

2.2 Faster growth in new lending in other countries

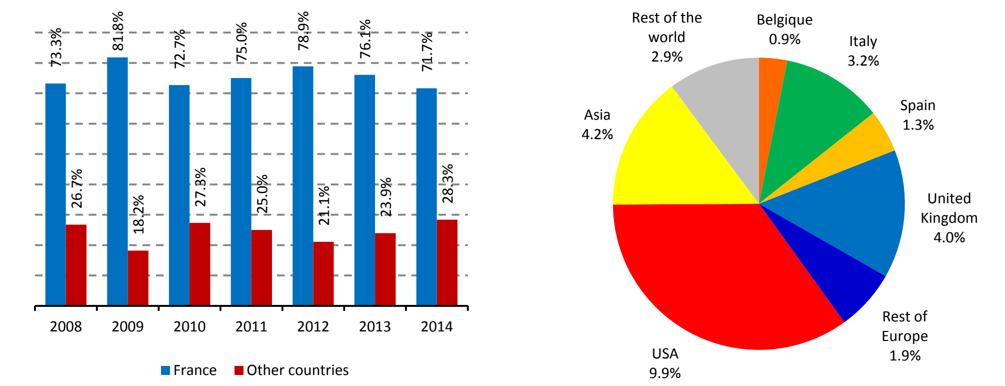
Following the 2013 trend, France's market share contracted further in 2014 whereas new lending in other countries reached its highest level since 2008 at 28.3% (Chart 11). This rise reflects the faster growth of new lending in other countries compared with that of France (+28.1% against +1.9%).

New lending growth was particularly strong in the United States, Asia, the United Kingdom and Spain, whose shares rose by 3.6 pps, 1.8 pp, 1.6 pp and 1 pp respectively (Chart 12). Even though, outside the euro area, growth in new lending reflects an exchange rate effect (appreciation of sterling and the US dollar by 7% and 13.6% respectively), the growth in volumes remained significant in the United Kingdom (+64.1%), the United States (+50%) and Asia[16] (+64.8%). In the United Kingdom and Spain, new lending growth exclusively stemmed from the non-residential segment, on which it more than quadrupled between 2013 and 2014. In the United States it was more balanced (+71.4 % against +67.8% on the residential segment).

Conversely, Belgium, the rest of Europe and Italy saw their shares of new lending contract by 2 pps, 1.2 pp and 0.9 pp respectively. While, in the case of Belgium, the decline stemmed from both the residential and the non-residential segments (-84.7% and -40.6%), only the former segment contracted in the case of Italy (-23.5%).

Chart 11
Share of France and other countries in new lending

Chart 12
Breakdown of new lending to other countries in 2014

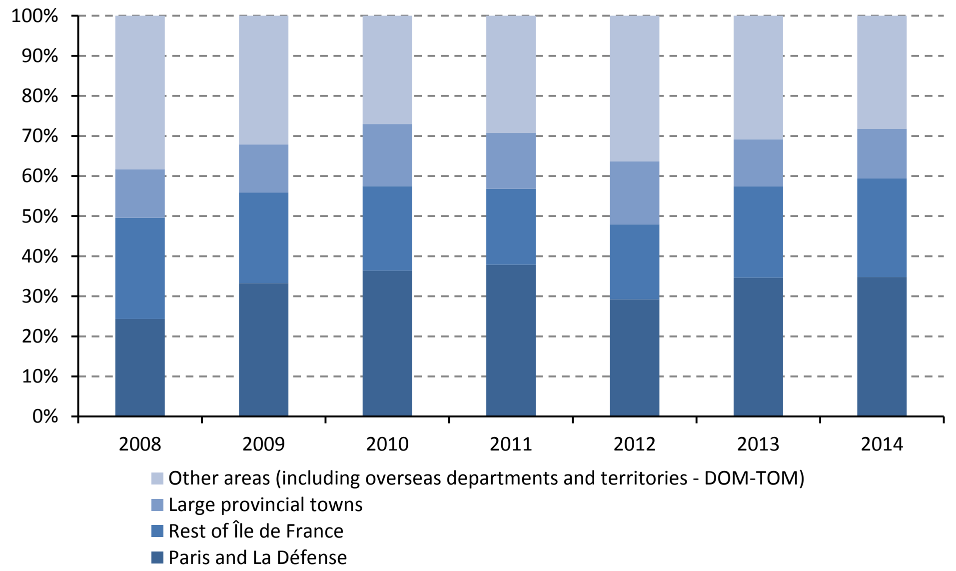


Source: SGACPR annual survey

On the non-residential segment, where new lending rose by 12.5% compared to 2013, Paris, la Défense and Île de France continued to account for the bulk of new lending (59.4% in 2014). Some other developments should also be noted concerning smaller areas (Chart 13): for instance, after contracting by 14.6% in 2013, "other areas" rose by 2.8% in 2014; similarly, "large provincial towns and cities" saw their new lending rise by 18.9% after falling by 24.5% in 2013. Like in 2013, the "rest of Île de France" posted a well above average rise (+21.3%). The geographical breakdown of new lending flows in France nevertheless remained unchanged on the previous year.

[16] Assuming that all new flows in the region were dollar-denominated.

Chart 13
Breakdown of new lending in France

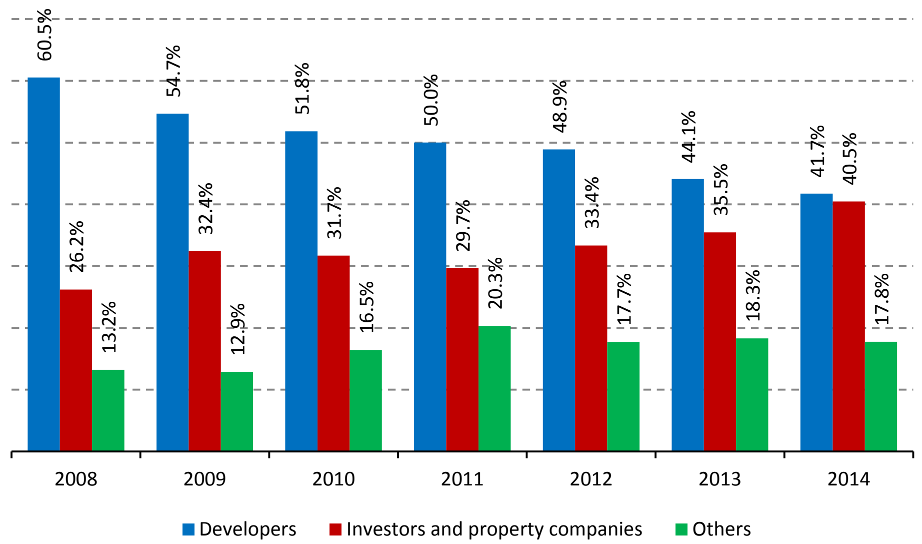


Source: SGACPR annual survey

2.3 Increase in the share of investors and property companies

The breakdown of new lending by type of recipient continued the trend underway since 2011: indeed, the share of developers (41.7%) contracted further in 2014 (-3.4 pps) while that of investors and property companies rose (40.5%, +4.3 pps); with these two segments now standing at similar levels (Chart 14).

Chart 14
Breakdown of new lending by type of recipient



Source: SGACPR annual survey

The share of the "Others" segment[17] contracted by 0.9 pp to stand at 17.8%, which chiefly reflects the decline in "credit derivatives", which had risen sharply for one of the banks in 2013. Moreover, only one bank increased its new lending to other recipients and the two main components of the segment saw diametrically opposed developments (-84% for private-public partnerships and up 80% for social housing).

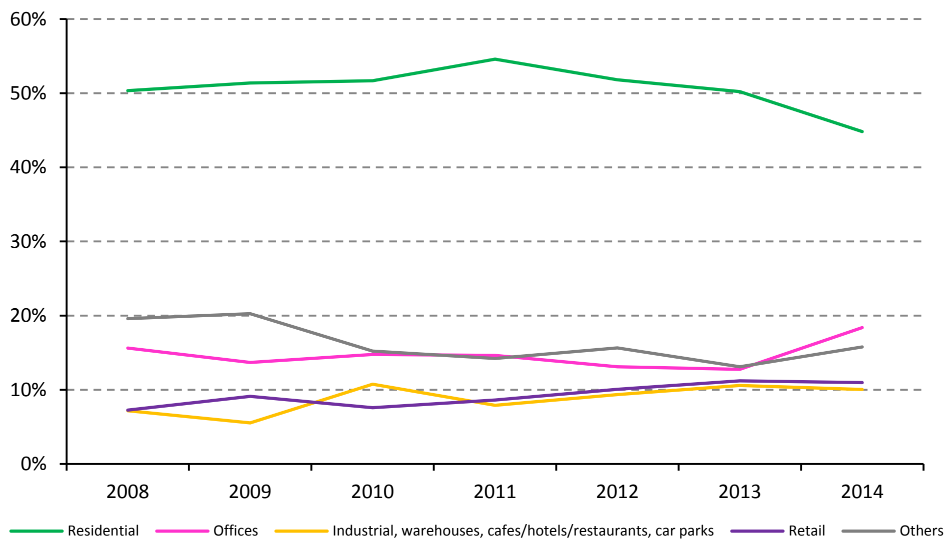
[17] The "others" segment includes notably social housing organisations (public low-income housing bodies, other low-income housing bodies, etc.).

2.4 Although declining, residential real estate continued to account for the lion's share

Although this segment continued to attract the bulk of new lending, the share of residential real estate declined by 6.5 pps in 2014 to stand at a much lower level than it had reached in 2008 (50.3%). This reflects the sharp rise in the offices segment (+5.4 pps, to stand at 18.4%), due to the doubling of new lending by two of the banks in the sample, and, to a lesser extent, in that of "other types of assets"[18] (+2.4 pps to stand at 15.8%; Chart 15).

Contrary to the two previous years, the shares of business premises, warehouses, cafés/hotels/restaurants and car parks, on the one hand, and retail outlets, on the other, declined slightly on 2013 due to the fact that their new lending grew at a rate that was slightly lower than average (3.6% and 0.4% respectively). The former segment nevertheless displayed mixed developments: while cafés/hotels/restaurants and warehouses recorded growth of 63.1% and 31.8% respectively, that of business premises contracted by 27%.

Chart 15
Breakdown of new lending by asset type



Source: SGACPR annual survey

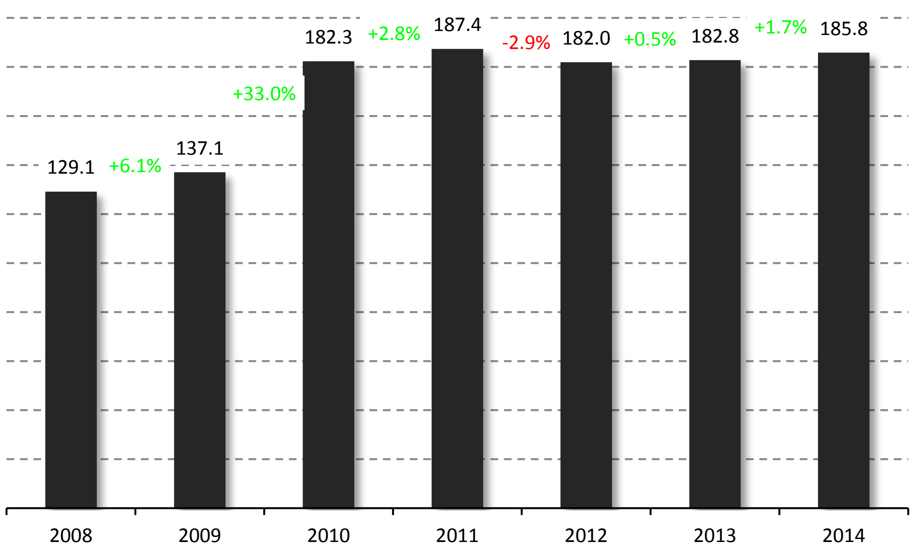
[18] The "Others" segment covers a wide range of business premises (educational buildings, clinics, retirement homes, theatre and entertainment venues, etc.)

3 Banks' exposures to real estate professionals

3.1 Slight rise in exposures in 2014

Total gross outstanding exposures have remained relatively stable since 2010; they stood at EUR 185.8 billion at end-2014, they rose by 1.7% compared with 2013 but remained below their peak of 2011 (Chart 16).

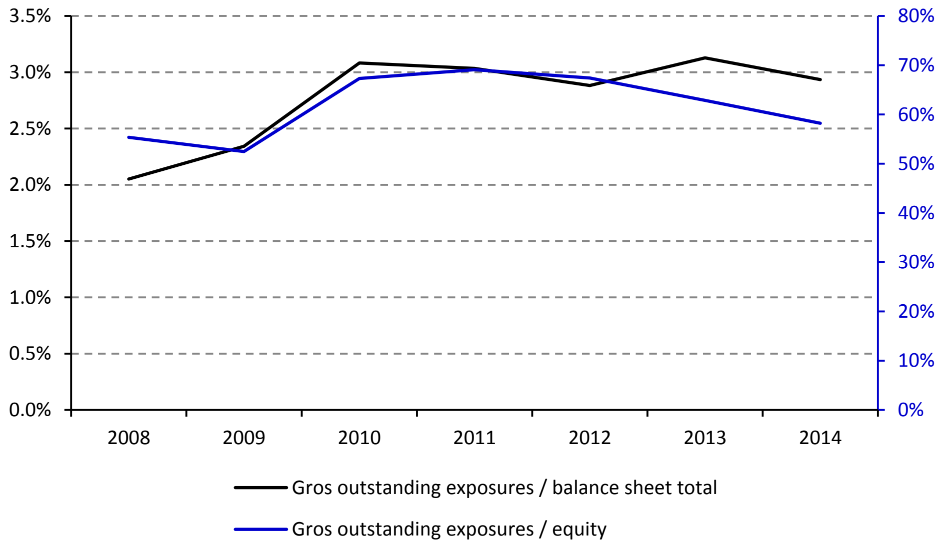
Chart 16
Total gross outstanding exposures (EUR billion)



Source: SGACPR annual survey

In relation to the balance sheet total, gross outstanding exposures also appear to have remained relatively stable since 2010, fluctuating at around 3%. However, in relation to equity, they have declined since 2011, reflecting a rise in equity over the period (Chart 17).

Chart 17
Gross exposures to balance sheet total and to total equity



Source: SGACPR, COREP, FINREP and annual survey

Lastly, the structure of outstanding exposures changed little, with loans still accounting for 2/3 of the total (Chart 18). Similarly, breaking with the trend observed since 2008, the respective shares of funding and guarantee commitments were perfectly stable within the off-balance sheet commitments (Chart 19).

Chart 18
Breakdown of gross exposures

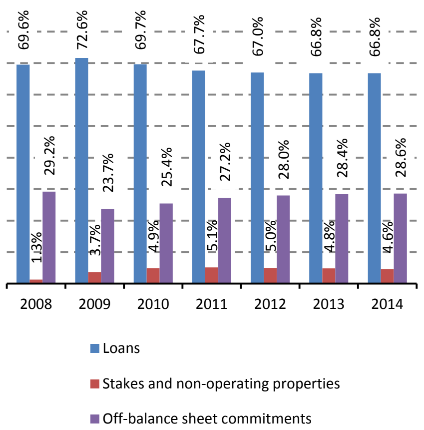
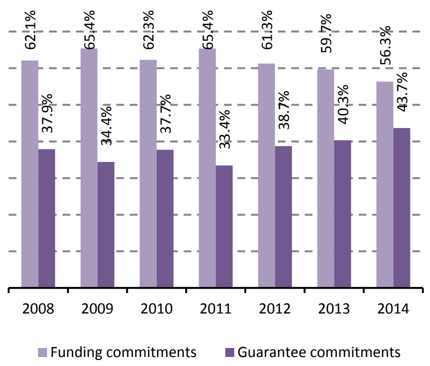


Chart 19
Breakdown of off-balance sheet commitments



Source: SGACPR annual survey

3.2 Breakdown of exposures between France and other countries

France accounted for 67.8% of exposures in 2014 against 32.2% for other countries. However, for the first time since 2010, France's share fell in 2014 by 1 pp compared with 2013 due to the more sluggish growth in France than in other countries (+0.2% against +5%; Chart 20).

Abroad, exposures continued to be highly concentrated to Europe, and in particular to Italy and Belgium. With the exception of the latter, for which they rose by 0.3 pp, the share in outstanding exposures to all the other European countries decreased in 2014, while those to the United States and Asia rose by 1.5 pp and 0.7 pp respectively (Chart 21). Like in the case of new lending, these changes partly reflect an exchange rate effect but also a rise in volumes of 6.9% and 31.7% respectively.

Chart 20
Geographical breakdown of gross exposures

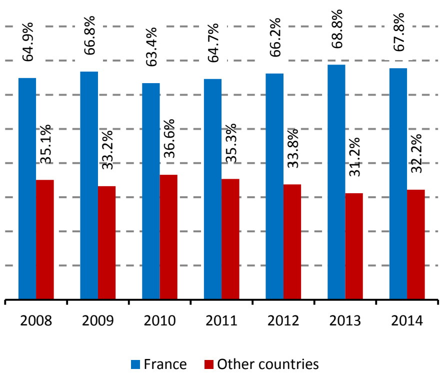
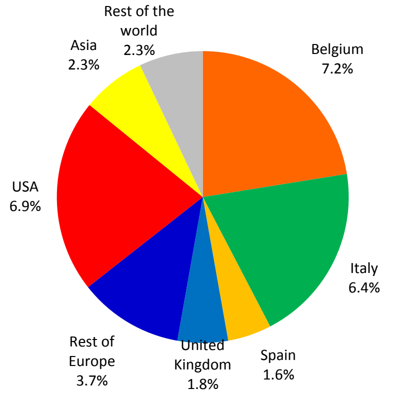


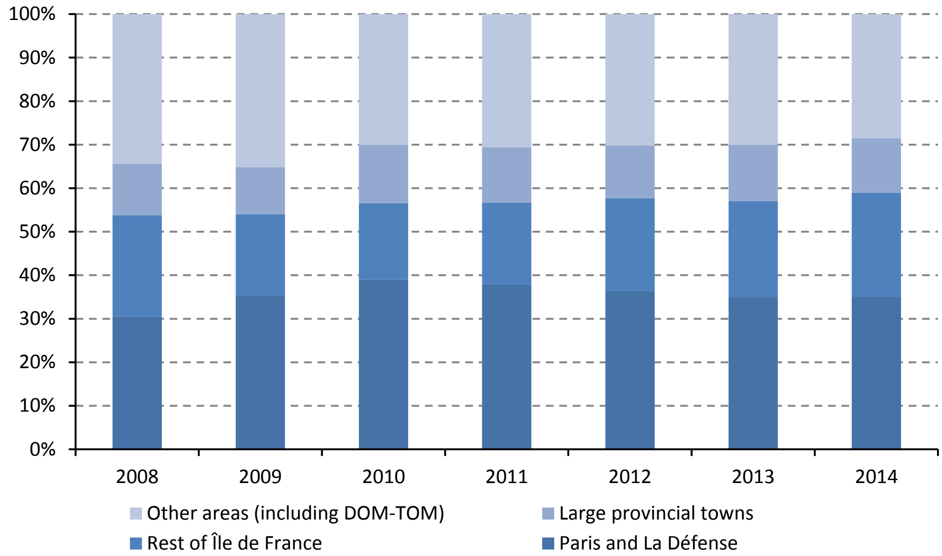
Chart 21
Geographical breakdown of gross exposures to other countries



Source: SGACPR annual survey

Lastly, the geographical breakdown of exposures excluding residential property in France has continued to gradually change since 2010, with the main increase being to the rest of Île de France, where the share of banks' exposures rose sharply by 7.8% (from 22.1% to 23.9%). Paris and la Défense nevertheless remained the region with the highest exposure (35%), while the large provincial towns and cities and the rest of France (including the overseas departments and territories – DOM-TOM), where exposures declined by 3.6% and 5.3% respectively, saw their shares fall by 0.5 pp to 12.5% and by 1.6 pp to 28.5% (Chart 22).

Chart 22
Breakdown of gross exposures (excluding residential) in France

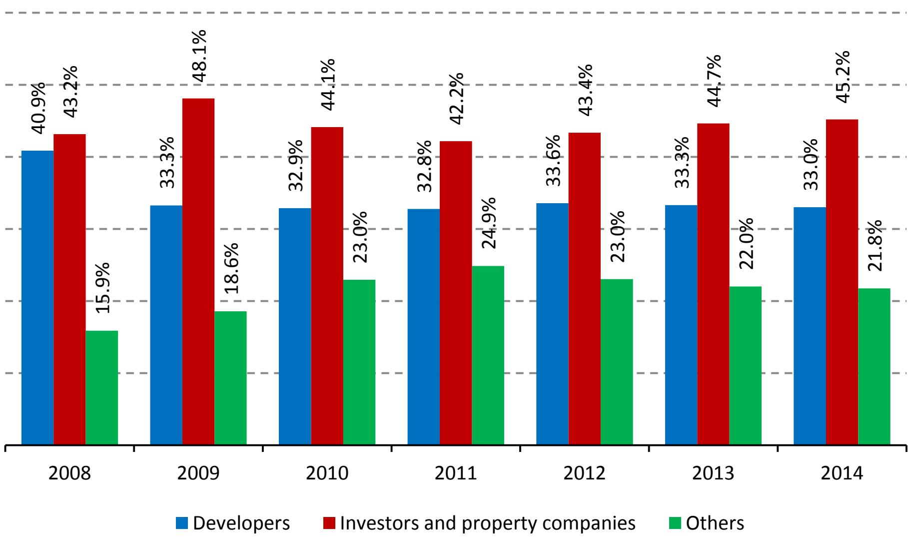


Source : SGACPR annual survey

3.3 Exposure to the different categories of investors

As has been the case since 2011, the share of other recipients in gross exposures continued to contract in 2014 with exposure to investors increasing. The latter category still accounts for the bulk of exposures, with that to developers remaining relatively stable (Chart 23).

Chart 23
Gross exposures by type of recipient



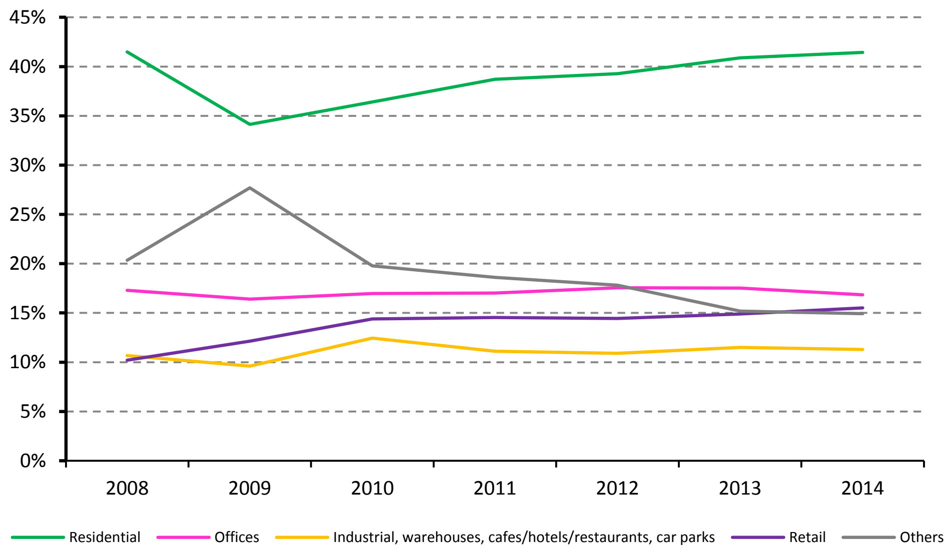
Source: SGACPR annual survey

3.4 Residential real estate continues to account for the bulk of exposures

French banks' exposures to residential real estate continued to increase, rising by 3% in 2014. Exposure rose more rapidly only to retail outlets and cafes/hotels/restaurants (+5.8% and +5% respectively). Conversely, exposure to the offices segment dropped by 2.3%, causing its share to decline by 0.7 pp, to stand at 16.8%. Similarly, exposure to business premises contracted by 2.2% (Chart 24).

These developments reflect notably a sharp rise in the loan amortisation rate for the offices segment whereas it fell for residential real estate, retail outlets and other assets[19].

Chart 24
Breakdown of exposures by type of product



Source: SGACPR annual survey

3.5 Risks remained contained

3.5.1 Real estate risk selection policy

Financing activities are generally hosted by specialised structures that have dedicated credit standards (assets financed collateral requirements, maturities, etc.) and a specific internal rating method, approved by the group's risk committee.

Banks' risk selection policies were largely the same as those of the previous year. Credit standards take account of many qualitative elements (location and use of the real estate asset) and financial elements (debt service coverage ratio (DSCR), rental vacancy rate, loan-to-value (LTV) ratio when the loan is granted). Offices, retail and residential assets are generally favoured over industrial and commercial premises, which often have specific features that can make their disposal more complicated if borrowers experience difficulties.

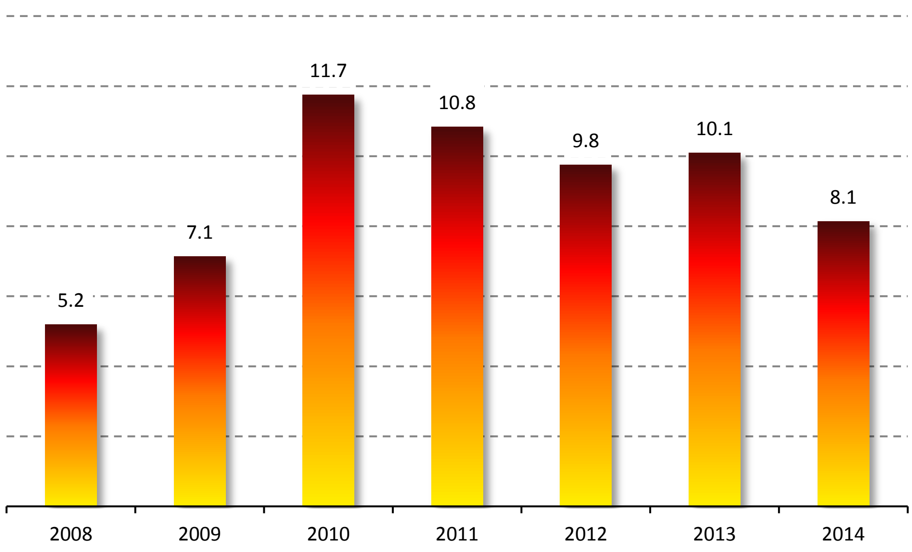
Real estate risk selection also takes account of expected returns on financing expressed as the rate of return on equity. Overall, gross margins on new lending, which are set according to the characteristics of the counterparty and the asset, contracted in 2014 against the backdrop of increased competition between banks. This decline is likely to continue in 2015, especially since, at the European level, banks face growing competition from "alternative lenders" such as debt funds or insurance companies.

3.5.2 Fall in the non-performing loan (NPL) ratio

Overall, the outstanding gross NPLs fell by 19.3% in 2014, to EUR 8.1 billion (Chart 25). Two banks nevertheless saw a rise in their NPL ratio compared with 2013.

[19] The ratio between redemptions during the year and outstandings at the end of the previous year increased from 18.4% to 31.5% between 2013 and 2014 on the offices segment. At the same time, it fell from 38.1% to 35.4% for residential real estate, from 16.3% to 14.1% for retail outlets and from 33.3% to 28.2% for other types of assets.

Chart 25
Non-performing loans (in EUR billions)

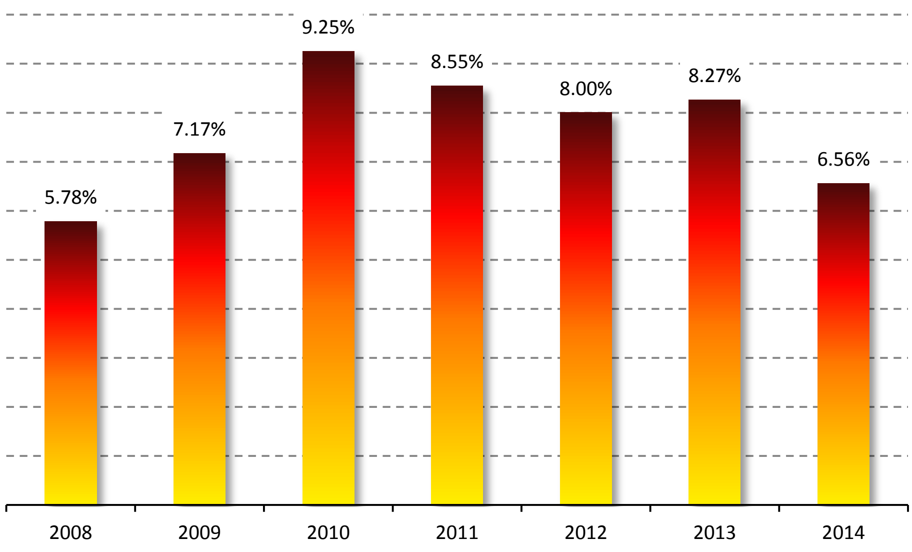


Source: SGACPR annual survey

The marked decline in the outstanding NPLs can largely be ascribed to successful out-of-court debt restructuring measures or the resolution of ongoing disputes, while improved market conditions allowed some troubled borrowers to sell off assets and settle part or all of their arrears.

Furthermore, benefiting from a rise in gross lending, the NPL ratio fell sharply in 2014 to stand at a lower level than that of 2009 (Chart 26). One bank nevertheless saw an increase in its gross NPL ratio, for the third time since 2011.

Chart 26
Gross NPL ratio

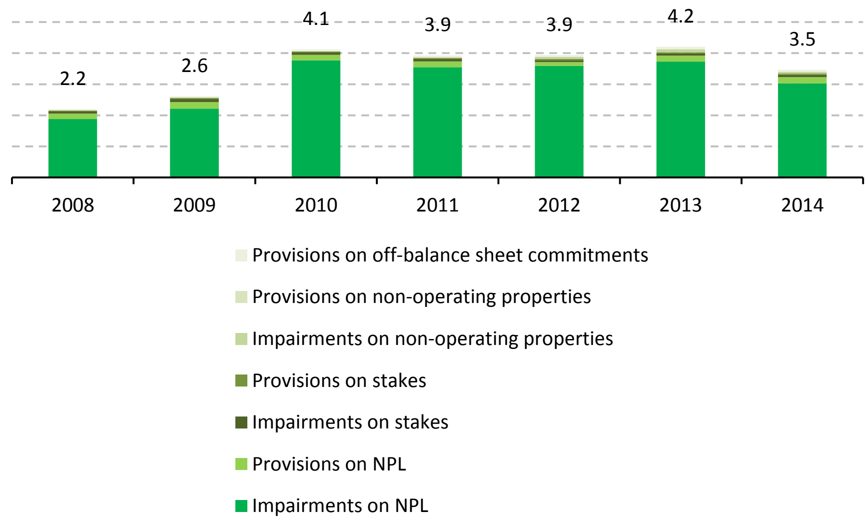


Source: SGACPR annual survey

3.5.3 Decline in the amount of impairments and provisions

The total amount of impairments and provisions contracted by 17.6% compared with 2013 to stand at EUR 3.5 billion, its lowest level since 2010. This decline mainly reflects that of impairments on NPLs, which decreased by 18.8% thanks to the resolution of ongoing disputes (Chart 27).

Chart 27
Impairments and provisions (in EUR billions)

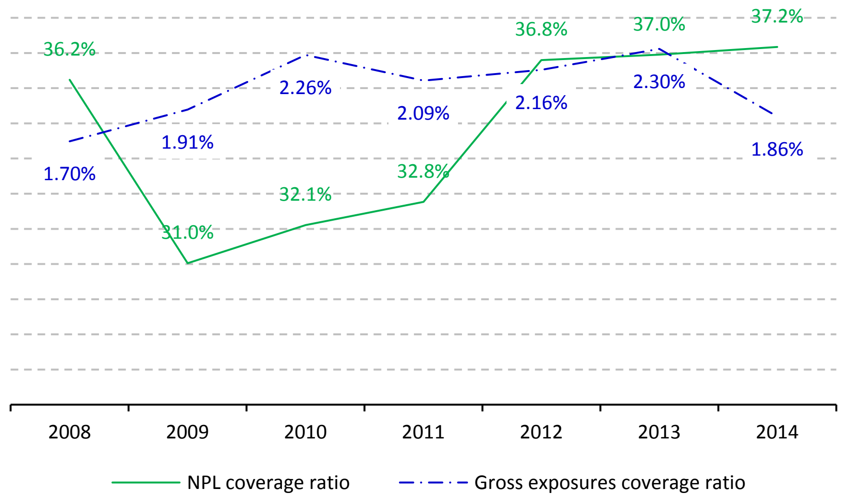


Source: SGACPR annual survey

One bank nevertheless saw an increase in its impairments on NPLs (+4.2%) while provisions on NPLs rose by 6.3% on average compared with 2013 for all banks.

The more rapid decline in the outstanding NPLs nevertheless resulted in a 20 bps rise in their average coverage ratio to stand at 37.2% (Chart 28). Nonetheless, this rise was driven by only one bank, whose coverage ratio increased by 9 pps. At end-2014, coverage ratios were relatively consistent across banks, with only one displaying a ratio over 50%. The relatively modest average coverage ratio can mainly be ascribed to the fact that lending is generally secured by a first mortgage on the financed property.

Chart 28
Coverage ratio for NPLs and gross exposures



Source: SGACPR annual survey

Together with the rise in exposures, the decline in total impairments and provisions nevertheless resulted in a significant fall in the gross exposure coverage ratio, which decreased to a lower level than that observed in 2009. Here again, with the exception of one bank for which it improved by 3 bps, this coverage ratio fell for all banks between 2013 and 2014, and significantly in some cases (between -2 pps and -0.2 pp). Furthermore, contrary to the provisioning rate for gross NPLs, gross exposure coverage ratios were relatively consistent, ranging from 1% to 3%.

3.5.4 A continued decline in toxic assets

Toxic assets refer to a variety of derivatives based on underlying “real estate” securities that include monolines, credit derivatives, asset backed securities (ABS) or even subprime collateralised debt obligations *(*CDO). Banks try to unwind them gradually in the market when opportunities arise.

After recognition of provisions, the net exposure of French banks to these assets only amounted to EUR 1 billion, down 31% on 2013.

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