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French banks' performance in 2017

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Executive summary

In 2017, the six major French banking groups reported robust performances in a gradually improving macroeconomic environment that was nonetheless marked by continuing very low interest rates and market volatility that was also at historically very low levels.

- In 2017, the six main French banking groups recorded a 0.5% increase in net banking income (NBI), which amounted to EUR 146.4 billion. This apparent stability was accompanied by significant disparities between both banks and business lines. For example, income from retail banking and corporate and investment banking increased quite modestly, up 0.5% and 0.8%, respectively, whereas income from asset management and insurance rose sharply by 9.6%.
- Net interest income from retail banking activities continued to decline both in France and internationally due to the continuing very low interest rate environment. The increase in outstanding loans and the dynamism of fees and commissions (which were up overall by 6.2% year-on-year) were not enough to offset the low income margins (net interest flows were down 2.3% in 2017).
- Due to a 2.7% increase in operating expenses, which outpaced NBI, the cost-to-income ratio again deteriorated at end-2017 to 69%, thus positioning French banks very close to the median for major European banks (69.4%).
- The cost of risk dropped by 18% in 2017 to its lowest level since 2007 and as a proportion of total assets dipped by 2.7 basis points (bps) to 0.11%. However, litigation costs had a significant negative impact in 2017 whereas in 2016 profit was boosted by the Visa Europe disposal that generated a capital gain of nearly EUR 3 billion.
- Operating profitability improved resulting in a 3.6% growth in pre-tax income. Net profit remained stable (up 0.3%) as did return on assets (RoA), which was unchanged at 0.36% and therefore well below the median for European banks, which improved sharply compared with 2016 to 0.43% (up 17 bps). This represents a marked departure from the situation that could be observed since 2012.[1] Return on equity (RoE) declined slightly year-on-year by 0.2 percentage point (pp) to 6.3% but was still higher than the RoE of comparable major European banks (5.9%).

The major French banks continued to improve the quality of their balance sheets and their prudential ratios while preparing for compliance with new regulatory requirements.

- The aggregate total assets of the five major French banking groups were down 3.3% year-on-year to EUR 6,282 billion at end-2017. This was mainly due to the reduction in the size of the banks' trading books and in assets available for sale (down 17% overall). These changes were offset by a 14.9% increase in cash and cash balances at central banks and a 9.6% growth in non-financial corporation loans and receivables. On the liabilities side, customer deposits other than from credit institutions rose by 3.2% and total equity (group share) grew by 2%.
- The quality of the loan portfolio continued to improve, with the impaired loan rate falling again in 2017 by 45 bps to 3.45%, mainly driven by outstanding loans to households and non-financial corporations. This improvement was due to growth in total outstanding loans while the total value of impaired loans contracted. Since 2015, the coverage ratio for impaired loans has remained stable at 56%.
- The average Common Equity Tier 1 (CET1) solvency ratio of the six French banking groups further improved by 50 bps to 13.8%, driven by both a 3.4% increase in CET1 capital (EUR 306 billion at end-2017) and a 0.4% reduction in risk-weighted assets (EUR 2,221 billion at end-2017). The median CET1 ratio of the French banks, driven by the mutual banking groups, was slightly higher than

[1] See Bulletin de la Banque de France No. 216/3, March-April 2018

that of the sample of major European banks (14.1% compared with 13.9%). Although none of the banks had applied IFRS 9 at end-2017, the groups anticipate a negative impact of between 10 bps and 30 bps on their CET1 solvency ratio upon its initial application due to an increase in provisions for credit losses.

- French banks slightly improved their liquidity ratios compared with 2016. At end-2017, the average liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) of the six groups stood at 131.7% and 107%, respectively.
- Lastly, the French global systemically important banks fully met the new total loss absorbing capacity (TLAC) requirements, which will come into effect in 2019.

Despite the considerable progress made by French banks in strengthening their balance sheets and financing structures since the crisis, supervisory vigilance in a number of respects remains essential.

- Changes in operating expenses remain an area to watch and a significant challenge. For the six French banking groups, they have increased for the second consecutive year despite numerous transformation plans since 2013. Nevertheless, the average cost-to-income ratio of the French banking groups is similar to the median calculated for the major European banks with international reach.
- These transformation plans are intended to respond to the key challenges of cost reduction, the digital revolution and the emergence of new players. Consequently, banks are reviewing their business models, streamlining their networks, improving the outsourcing of support functions, investing in IT system adaptation and further acquiring or multiplying partnerships with Fintechs. Certain developments are likely to create new risks, particularly in terms of business continuity, cybersecurity and data handling, and will have to be regulated.
- The continuing low interest rate environment could undermine the rebound in net interest income and could also lead institutions to take greater risks in certain sectors. Thus, in order to maintain bank resilience in a context of steady growth in large corporations' debt since 2005, the *Haut conseil de stabilité financière* (High Council for Financial Stability – HCSF), in accordance with the provisions of Article 458 of the Capital Requirements Regulation (CRR), decided in May 2018 to apply a targeted measure for the exposures to highly indebted large corporations.
- The finalisation of the Basel III Accord on 7 December 2017 is a major step forward. It aims to guarantee the right balance between reducing risk-weighted asset variability and preserving risk sensitivity. The full implementation of the Basel III reforms package is therefore essential for financial stability.

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Key words: net banking income, operating expenses, cost-to-income ratio, cost of risk, net profit, solvency ratio, key risk indicators

JEL code: G21

Foreword

This analysis focuses on the consolidated accounts of the six main French banking groups: BNP Paribas (BNPP), Société Générale (SG), Crédit Agricole Group (GCA), BPCE Group (GBPCE), Crédit Mutuel Group (GCM) and La Banque Postale (LBP).

For some risk indicators, French banks are compared with their main European competitors using the key risk indicators (KRIs) calculated every quarter by the European Banking Authority (EBA) for a sample of European banks. Individual comparisons are also shown with leading European banks with international reach. However, data on some indicators may not be available for certain banks; where this is the case, it is indicated in a footnote to the relevant table and/or chart.

1. Profitability

1.1. Stable performance in 2017

In 2017, in a gradually improving economic environment and despite protracted very low interest rates, the six major French banking groups reported stable financial performances relative to 2016 (Table 1):

- Aggregate net banking income (NBI) rose 0.5% to EUR 146.4 billion from 2016 to 2017.
- Operating expenses increased by 2.7% and the cost-to-income ratio deteriorated by 1.5 percentage points (pp) to 69%.
- The cost of risk continued to fall sharply (down 18% compared with 2016).
- Net profit grew 0.3% to EUR 26.2 billion.

Table 1
Profit and loss account

	2016	2017	Change 2017/2016
Net banking income	**145.7**	**146.4**	**+0.5%**
Operating expenses	98.4	101.0	**+2.7%**
Cost-to-income ratio	67.5%	69.0%	+1.5 pp
Gross operating profit (GOP)	**47.4**	**44.9**	**-5.2%**
Cost of risk (CR)	10.3	8.4	**-18.0%**
Net operating profit (GOP-CR)	**37.1**	**36.4**	**-1.6%**
Other gains (+) and losses (-)	0.5	2.5	NA
Pre-tax income	37.6	38.9	**+3.6%**
Tax	11.5	12.7	**+11.1%**
Discontinued or held-for-sale operations	0.1	0.0	NA
Net profit	**26.1**	**26.2**	**+0.3%**
Minority interests	1.8	2.3	**+30.6%**
Net profit (group share)	**24.3**	**23.9**	**-1.9%**

Source: financial disclosures from the six groups (BNPP, SG, GCA, GBPCE, GCM, LBP).

1.1.1. A slight increase in underlying income

NBI increased slightly (0.5 % year-on-year) without any material effect of own debt revaluations.

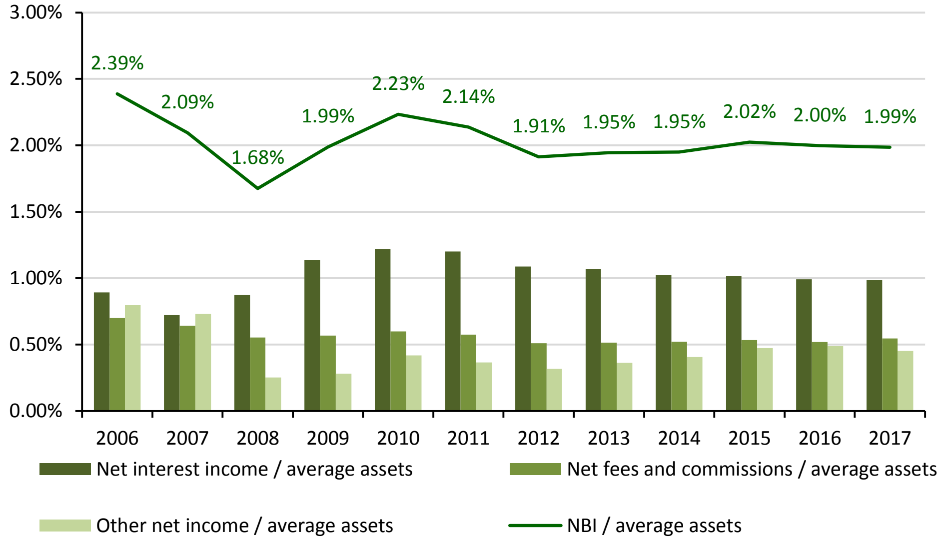
However, excluding the significant increase in litigation costs, which amounted to EUR 1.1 billion in 2017 and were mainly borne by SG, and capital gains on disposals (EUR 0.7 billion compared with EUR 2.5 billion in 2016), adjusted NBI rose by 2.6% to EU 147.3 billion.

As a proportion of average total assets, which increased by 1% in 2017, NBI declined by 1 basis point (bps) compared with 2016 to 1.99% (Chart 1). However, the various components of NBI followed different trends:

- Net interest income equated to 0.99% of average total assets (i.e. half of NBI) and has thus been remarkably stable over the past four years. Gross interest income declined by 2.3% while interest expenses dropped more sharply by 4.8%.
- Fees and commissions, which had been extremely stable as a proportion of average total assets since 2012, increased by 3 bps to 0.55%. In value terms, they were up by 6.2% year-on-year.
- Other net income, which is generated by a wide range of sources including

trading activities on financial instruments, insurance and leasing activities, capital gains on disposals of financial fixed assets, etc., corresponded to 0.45% of average total assets, down 4 bps year-on-year but still at the relatively high level observed since 2015.

Chart 1
Structure of NBI by income stream (as % of average total assets)



Source: financial disclosures – GCM data not available at the time of writing this issue of Analyses et Synthèses.

1.1.2. A further deterioration in the cost-to-income ratio

Given the relative stability of NBI and the 2.7% upturn in operating expenses, the average cost-to-income ratio (operating expenses as a proportion of NBI) increased by 1.5 pp on 2016 to 69% (Table 2). The cost-to-income ratio adjusted for exceptional items and the effects of own debt revaluations has also grown over the past four years.

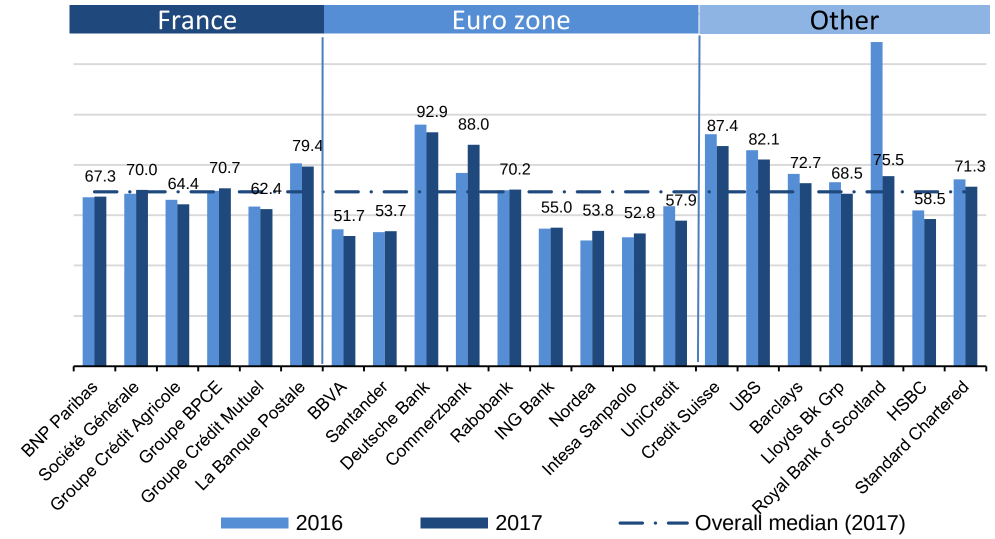
Table 2
Change in the cost-to-income ratio

	2014	2015	2016	2017
Cost-to-income ratio	67.4%	66.5%	67.5%	69.0%
Adjusted cost-to-income ratio	66.7%	67.2%	67.2%	68.7%

Source: financial disclosures (excluding GCM) – weighted average.

Although the cost-to-income ratios of the major French banking groups are quite varied, ranging from 62% to 79% in 2017, they are all similar to the median calculated for the major European groups with international reach (Chart 2), which stood at 69.4% in 2017, down 2.2 pp on 2016.

Chart 2
Cost-to-income ratios of European banks with international reach (%)



Source: SNL and ACPR calculations.

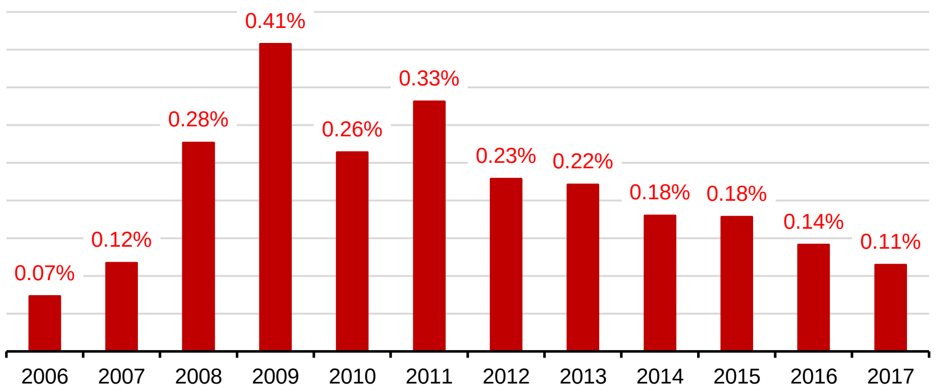
1.1.3. A continuing downward trend in the cost of risk

The aggregate cost of risk[2] of the six main French banks further declined in 2017 by 18% to EUR 8.4 billion from EUR 10.3 billion in 2016 and EUR 12.9 billion in 2015.

This additional downturn in the cost of risk again reflects the improved economic environment, particularly in Europe, and the funding conditions that remained extremely favourable to businesses and individuals in 2017.

The cost of risk as a proportion of average total assets amounted to 0.11% in 2017 and thus approached the levels observed before the financial crisis (Chart 3). Furthermore, the cost of risk of SG, GCA and LBP were equal to the European median but this level was exceeded by GBPCE, GCM and particularly BNPP (Chart 4).

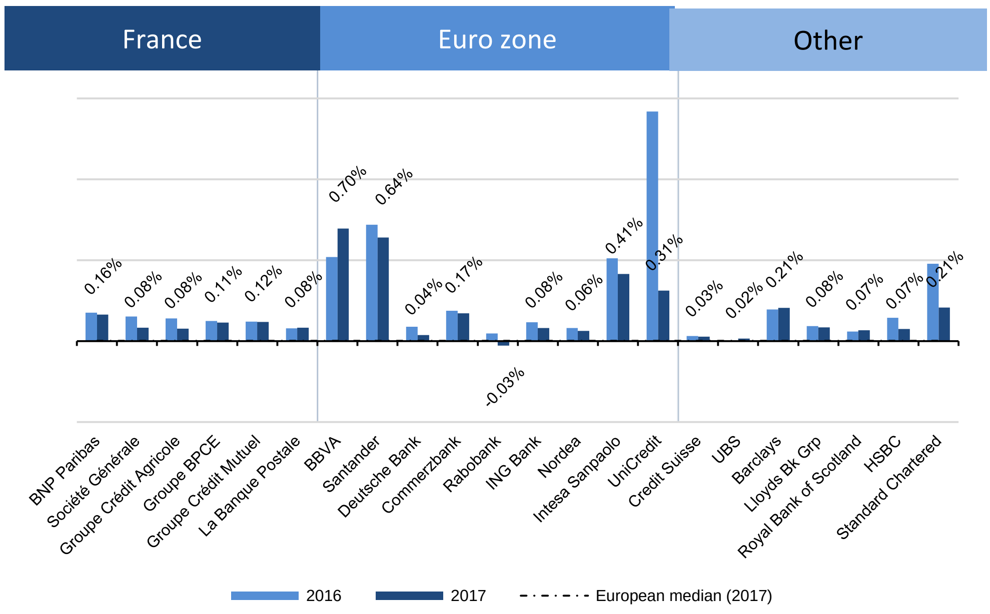
Chart 3
Cost of risk as % of average total assets



Source: financial disclosures.

2 The cost of risk includes net additions to provisions and impairment for credit risk on loans and receivables, financing and guarantee commitments and fixed income securities, as well as losses on unrecoverable loans net of recoveries of loans written off.

Chart 4
Cost of risk as % of total assets of European banks with international reach



Source: SNL; RBS's cost of risk is not represented here as it is negative (-5.6%).

The cost of risk of French banks as a proportion of income also declined from 7.1% of NBI in 2016 to 5.8% in 2017 but remained higher than the median of other comparable European banks, which amounted to 3.9% in 2017 (down 2.4 pp, year-on-year).

1.1.4. A strengthening of net profit

The total pre-tax income of the six major French banks amounted to EUR 38.9 billion in 2017, up 3.9% compared with the 2016 level. The EUR 2.6 billion increase in operating expenses was offset by a EUR 0.7 billion improvement in income and above all a EUR 1.9 billion decrease in the cost of risk.

Corporate income tax for the 2017 financial year was up by 11% (or EUR 1.2 billion) to EUR 12.7 billion and corresponded to 32.7% of pre-tax income. Furthermore, litigation costs had a significant negative impact in 2017 whereas in 2016 profit was boosted by the Visa Europe disposal that generated a capital gain of nearly EUR 3 billion.

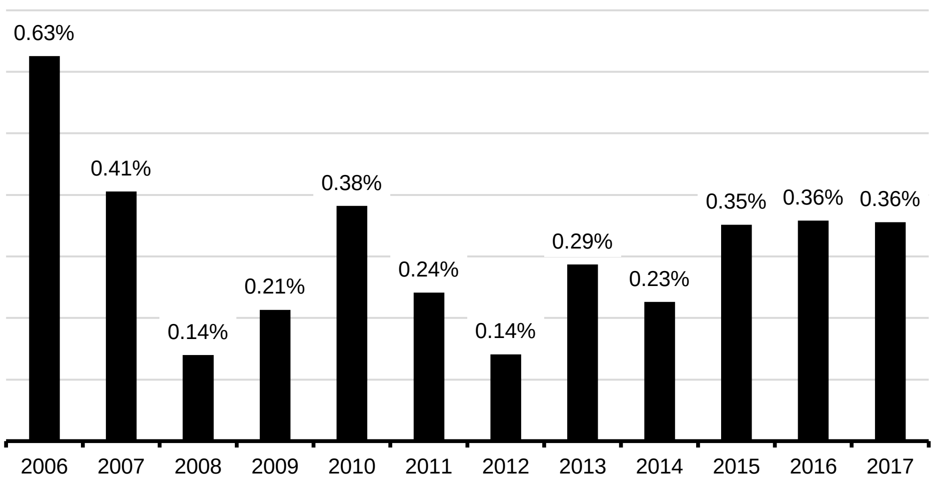
Ultimately, net profit amounted to EUR 26.2 billion and thus remained very close to 2016's level of EUR 26.1 billion. The average planned dividend distribution rate for 2017 of the four listed banks[3] came to 56.8% compared with 50.8% for the 2016 financial year.

1.1.5. Lower returns on assets and on equity for French banks than for European banks

French banks' net profit as a proportion of average total assets (return on assets – RoA) was largely unchanged from the previous two years at 0.36% (Chart 5).

3 Weighted average for BNP Paribas, Société Générale, Crédit Agricole SA and Natixis.

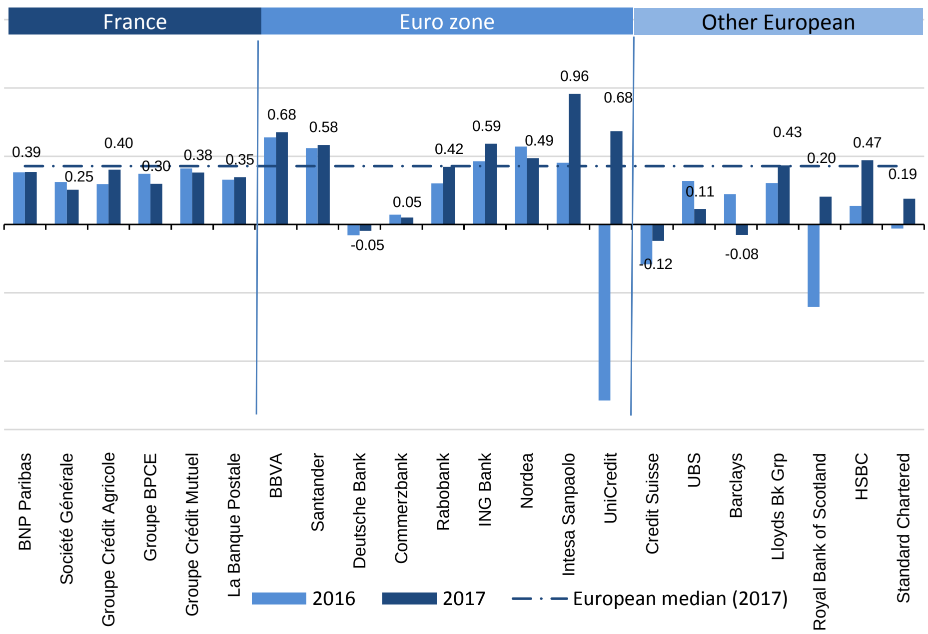
Chart 5
Net profit as % of total assets (return on assets)



Source: financial disclosures.

The RoA of French banks moved below the median of comparable major European competitors, which improved sharply from 0.26% in 2016 to 0.43% in 2017, mainly as a result of improved performances by Italian and UK banks (Chart 6).

Chart 6
RoA of European banks with international reach (%)

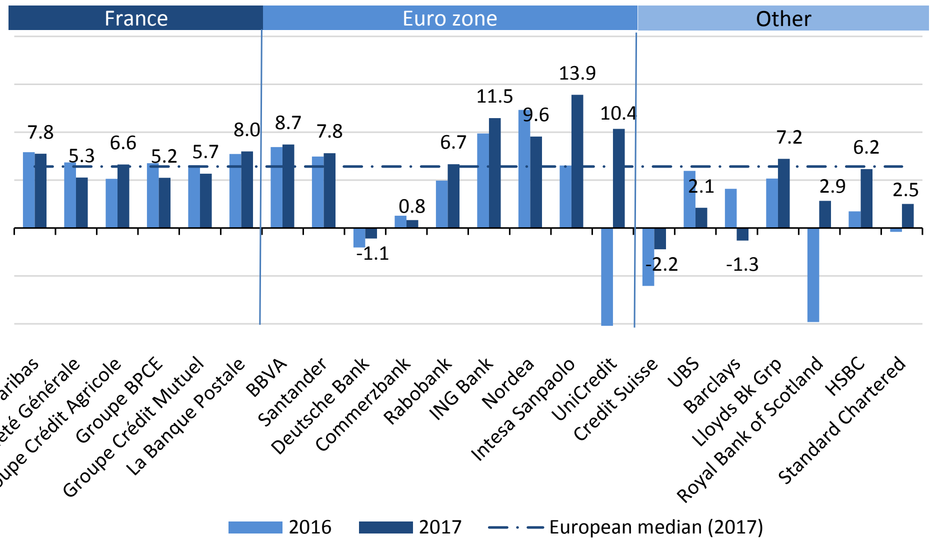


Source: SNL and ACPR calculations.

Note: in 2016, the RoAs of RBS and Unicredit were -0.60% and -1.29%, respectively; the histograms were cropped to improve readability.

French banks' net profit as a proportion of equity (return on equity – RoE) was close to the 6.4% median observed for major European banks in 2017 (Chart 7). Quite significant disparities in performances persist in Europe however, with three major banks reporting negative RoEs in 2017.

Chart 7
RoE of a sample of European banks with international reach (%)



Source: SNL.

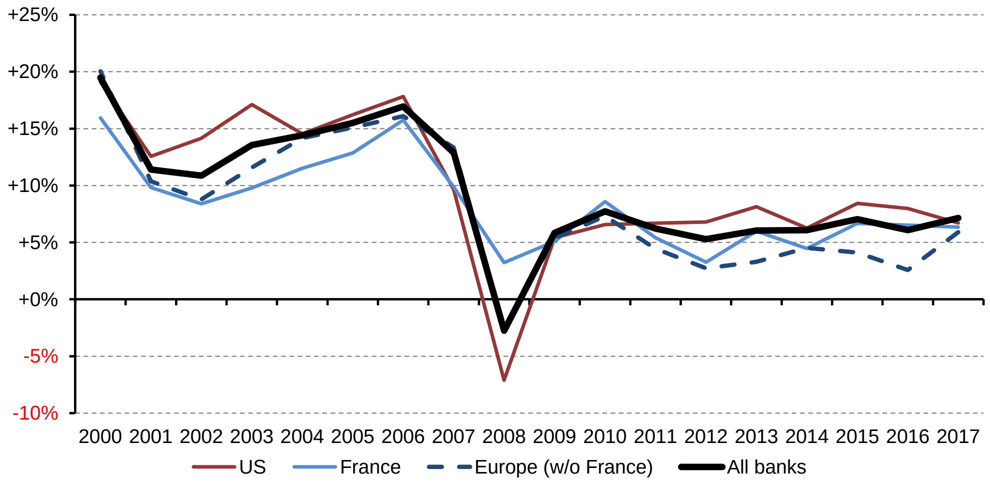
Note: in 2016, the RoEs of RBS and Unicredit were -9.8% and -21.5%, respectively; the histograms were cropped to improve readability.

The average RoE for the five main French banks for which information was available amounted to 6.3%, down slightly by 0.2 pp compared with 2016 (Chart 8), and was still higher than the RoE of other major European banks (5.9%, weighted average), which increased significantly in 2017 by 3.3 pp.

Extended to a sample of major international banks, the average RoE rises to 7.1% (up 1 pp) and reflects a far less varied picture than in 2016. The RoE of US banks fell back by 1.3 pp in 2017 to 6.7% as a result of the substantial deferred tax asset impairments recorded due to tax reform in the United States.

Generally, improved solvency (see below) and the resulting higher RoE denominator, combined with more modest results, kept return on equity significantly below pre-crisis levels.

Chart 8
RoE – international comparisons



Source: SNL and ACPR calculations (a sample of 51 banks)

Note: "All banks" is the weighted average of the 51 banks in the sample, across all geographical regions (European Union, Switzerland, United States and Canada) excluding China.

1.2. Contrasting business line performances[4]

While retail banking and corporate and investment banking (CIB) contributions to NBI remained relatively constant compared with 2016, the contributions of the specialised finance along with asset management and insurance business lines increased considerably to 9.3% and 15.2%, respectively (Table 3 and Chart 9).

The growth in income from specialised finance activities can be interpreted as a rebound after bottoming out in 2016. The strengthening of the share attributable to asset management is exceptional in character, marked by sharp improvements in income from both private banking and insurance activities.

Table 3
Change in NBI structure by business line

	2011	2012	2013	2014	2015	2016	2017
Corporate and investment banking	16.7%	17.9%	17.1%	17.3%	17.4%	18.9%	18.9%
French retail banking	42.5%	45.0%	46.5%	46.1%	44.6%	43.8%	43.5%
International retail banking	13.4%	15.5%	14.7%	14.3%	13.2%	13.3%	13.2%
Specialised finance	10.6%	10.3%	10.0%	9.0%	9.3%	8.9%	9.3%
Asset management and insurance	12.6%	14.1%	14.2%	14.9%	14.6%	14.0%	15.2%
Other	4.2%	-2.7%	-2.5%	-1.2%	0.7%	1.1%	-0.2%

Source: financial disclosures and ACPR calculations

Note: The “Other” line item in the table refers to activities that have not been assigned to a specific business line, such as income related to changes in own credit risk, the centralisation of intra-group funding or equity holdings. It also incorporates non-recurring items that are not attached to a business line and that negatively impact profitability, such as provisions or litigation costs.

As had already been seen in 2016, retail banking operating expenses rose by 1.9%, which is reflected in the higher cost-to-income ratio, up 1.1 pp to 67% (Chart 10). The CIB cost-to-income ratio remained relatively unchanged at 66.7% (down 0.1 pp) while the ratio for the asset management lines declined sharply by 1.7 pp to 50.6%

Chart 9
NBI by business line (EUR billions)

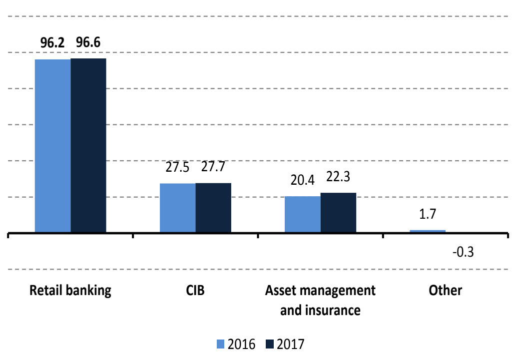
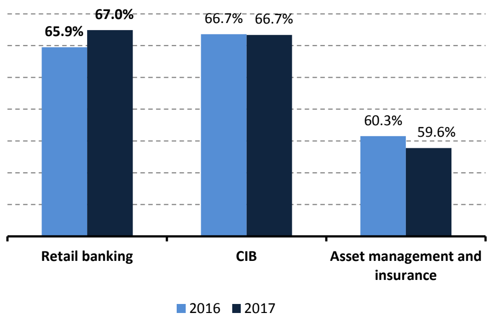


Chart 10
Cost-to-income ratio by business line



Source: financial disclosures and SGACPR calculations.

The downward trend in the cost of risk is particularly significant in the case of retail banking and CIB (Chart 11).

The 3.4% improvement in pre-tax income was driven by solid performances in CIB and asset management (Chart 12), which reported increases of 10.9% and 18%, respectively, thereby offsetting the negative contribution from "other" activities.

4 For consistency of presentation, certain figures reported by the banks in their financial disclosures have sometimes been adjusted. See the box on page 18 of *Analyses et Synthèses* No. 63 for further details.

Chart 11
Cost of risk by business line (EUR billions)

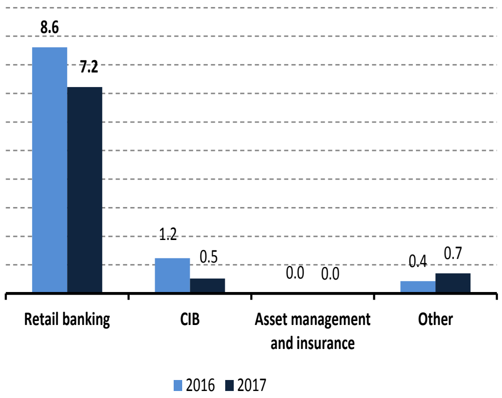
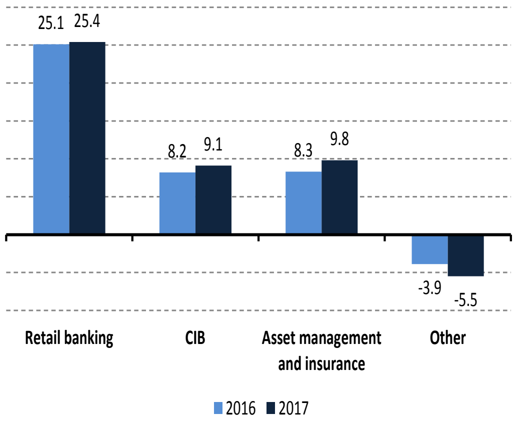


Chart 12
Pre-tax income by business line (EUR billions)



Source: financial disclosures and SGACPR calculations.

A detailed analysis of performance by business line is set out below.

1.2.1. A slight improvement in retail banking profitability

Despite a relatively constant NBI (up only 0.2%), the gross operating profit of retail banking and specialised finance dropped by 2.9% as a result of a substantial 1.9% increase in operating expenses due to one-off costs arising from network restructurings or the digital transformation. However, thanks to the sharp drop in the cost of risk (down 16.3%), operating profit was up 1.8% and pre-tax income rose by 1.5% (Table 4).

Table 4
Key figures for retail banking and specialised finance

Net banking income	**63.6**	***-0.6%***	**19.3**	***+0.0%***	**13.6**	***+4.4%***	**96.6**	***+0.2%***
Operating expenses	44.8	*1.8%*	12.6	*-0.3%*	7.3	*+5.9%*	**64.7**	***+1.9%***
Cost-to-income ratio	70.5%	*+1.7pt*	65.1%	*-0.2pts*	53.5%	*+0.8pt*	**67.0%**	***+1.1pt***
Gross operating profit	**18.8**	***-5.9%***	**6.8**	***+0.6%***	**6.3**	***+2.7%***	**31.9**	***-2.9%***
Cost of risk	**3.5**	***-15.3%***	**2.1**	***-24.5%***	**1.7**	***-5.9%***	**7.2**	***-16.3%***
Operating profit	**15.3**	***-3.4%***	**4.7**	***+17.9%***	**4.7**	***+6.2%***	**24.7**	***+1.8%***
Other gains and losses	0.1	*-59.2%*	0.3	*NA*	0.4	*+22.4%*	**0.8**	***NA***
Pre-tax income	**15.4**	***-4.2%***	**5.0**	***+16.6%***	**5.1**	***+7.4%***	**25.4**	***+1.5%***

Source: financial disclosures from the six groups and ACPR

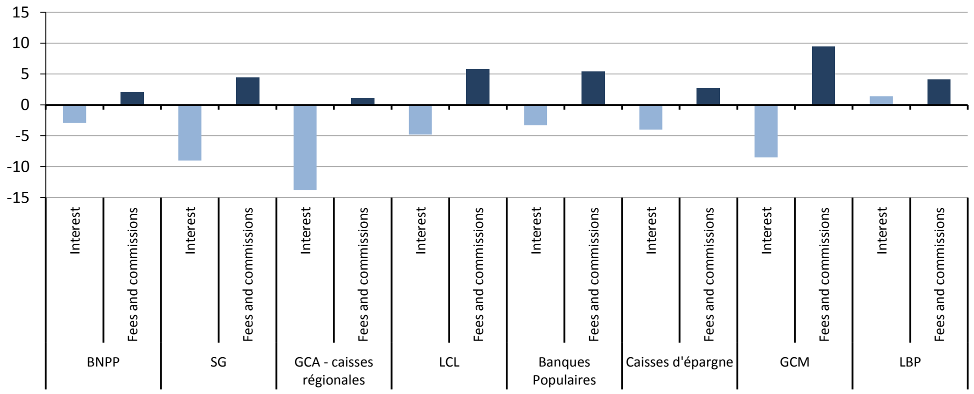
French retail banking income declined by 0.6% mainly as a result of lower net interest income, which fell back by between 2.9% (BNPP) and 9% (SG), depending on the network.

In terms of volume, business remained buoyant: outstanding loans continued to increase in 2017, both to individuals (up 5.9%) and to non-financial corporations (up 5.8%), although new lending dropped off during the second half of 2017 driven mainly by a 45% reduction in home loans compared with the first half of the year due to a major decline in renegotiations and refinancing.

Banks continued their efforts to diversify their income streams. In particular, they all reported an increase in fees and commissions but to very different extents, with variations even observed between different entities within the same group

(Chart 13). Service fees and commissions[5] were buoyed by the expansion of products and services available to customers as well as higher rates (notably for account handling) whereas financial fees and commissions were hit by an unfavourable market environment, particularly in the first half of 2017.

Chart 13
Change in net interest income and fees and commissions compared with 2016 (%)



Source: financial disclosures; Caisses régionales and Crédit Agricole data reconstructed by deduction.

The cost-to-income ratio of French retail banks increased by 1.7 pp to 70.6% during the period as a result of the implementation of plans to streamline the networks and digitise management processes, which generated additional operating expenses.

As the 15.3% fall in the cost of risk did not fully offset the increase in operating expenses, operating profit came in 3.4% down on the previous year. However, the deterioration was far less dramatic than in 2016.

International retail banking income remained constant at EUR 19.3 billion while operating expenses were also relatively stable, recording a 0.3% reduction. Income benefited from a favourable sales dynamic in corporate business and the individual customer segment, particularly in Belgium, Italy and Spain and even in the United States. Against this backdrop, the significant improvement in operating profit (up 17.9%) is explained by the substantial 24.5% reduction in the cost of risk and follows a trend that began in 2014.

Lastly, despite a 5.9% increase in operating expenses, **specialised finance**[6] reported clearly improved results thanks to a 4.4% rise in income (notably driven by Crédit Mutuel's acquisition of GE Europe's factoring operations) and a sharp drop in the cost of risk.

1.2.2. A decline in the cost of risk that continued to boost corporate and investment banking profitability

CIB income rose slightly in 2017 (up 0.8%) as it did in 2016. With operating expenses rising at a similar rate (up 0.7%), the increase in CIB operating profit (up 10.1%, Table 5) can mainly be traced to the sharp fall in the cost of risk (down 73%).

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5 Although there is no precise definition common to all banks, service fees and commissions cover, in particular, costs associated with account operations (bank card costs, sending chequebooks, payments outside the euro area, interbank credit transfers, etc.), and financial fees and commissions cover costs of security transactions, custody fees, etc.

6 Entities offering consumer loan, lease finance and leasing products and services in France and abroad.

Table 5
Key figures for CIB

	Corporate banking			Investment banking			Total		
	2017	2016	*chg on 2016*	2017	2016	*chg on 2016*	2017	2016	*chg on 2016*
Net banking income	**8.6**	**8.6**	***0.9%***	**13.5**	**13.8**	***-2.1%***	**27.7**	**27.5**	***0.8%***
Operating expenses	4.9	5.0	*-0.4%*	10.3	10.4	*-0.1%*	18.5	18.4	*+0.7%*
Cost-to-Income ratio	57.2%	58.0%	*-0.8 pts*	76.4%	74.8%	*+1.6 pts*	66.7%	66.7%	*-0.1 pts*
Gross operating profit	**3.7**	**3.6**	***+2.7%***	**3.2**	**3.5**	***-8.3%***	**9.2**	**9.2**	***+0.9%***
Cost of risk	**0.3**	**1.1**	***x2.3***	**0.1**	**0.0**	***nm***	**0.5**	**1.2**	***x2.3***
Operating profit	**3.4**	**2.5**	***+34.0%***	**3.1**	**3.5**	***-11.9%***	**8.7**	**7.9**	***+10.1%***
Other gains and losses	0.3	0.3	*+28.7%*	0.0	0.0	*nm*	0.4	0.3	*+35.6%*
Pre-tax profit	**3.7**	**2.8**	***+33.5%***	**3.1**	**3.5**	***-11.8%***	**9.1**	**8.2**	***+11.0%***

Source: Financial disclosures, breakdowns between corporate and investment banking are not available for GBPCE, GCM and LBP, which accounts for the difference between the sum of the first two columns and the sum of the "Total" column.

Corporate banking income was up 0.9% in 2017, but this apparent stability actually conceals contrasting positions. The cost of risk reflected the litigation between SG and the Libyan sovereign fund LIA, which gave rise to a net allocation to provisions for liabilities and charges of EUR 400 million and was finally resolved with a EUR 963 million settlement in 2017.

In **investment banking**, and in a context of low volatility, NBI declined by 2.1% despite a 6.8% increase in equity and derivatives income, which failed to fully offset the 4.7% decline in earnings from fixed income, credit, currency and commodity activities (Table 6). Equity and derivative income performances varied dramatically though, as illustrated by the 6.1% reduction reported by SG.

Table 6
Changes in investment banking income in 2017

	BNPP	SG	GCA	BPCE	Total
Fixed income, credit, currencies and commodities	-11.0%	-7.1%	+3.1%	+6.4%	**-4.7%**
Equities	+19.2%	-6.1%	-1.6%	+21.5%	**+6.8%**

Source: financial disclosures.

1.2.3. A more robust contribution to income growth from insurance and asset management

The insurance and asset management business line posted robust performances with income up 9.8% on 2016 (Table 7) and gross operating profit up 11.6% despite an 8.5% increase in operating expenses.

Income generated by **insurance** activities rose 6.9% on average, with two groups (GBPCE and GCM) posting particularly substantial growth of 13.4% and 16%, respectively. This upward trend can be explained by a positive market effect in the life insurance sector, which buoyed unit-linked policy inflows, while the property damage and personal protection insurance businesses also sold strongly.

In sharp contrast to 2016, the **asset management** sector also reported very dynamic growth in income with increases in NBI and operating profit of 11.6% and 20%, respectively. Natixis and GCA reported particularly robust growth, with income up 22% and 25%, respectively. The sharp improvement in asset management and private banking income (an increase in operating profit of 20% on average, and as much as 30% at BNPP and 200% at SG) was made possible by cost and earning synergies between collective investment management and private banking and by generally favourable market conditions that helped to boost outstanding amounts under management and bolstered net positive inflows.

Table 7
Key figures for insurance and asset management in 2017

	2017	*Chg. on 2016*
Net banking income	**22.3**	***+9.8%***
o/w insurance	*9.1*	*+6.7%*
Operating expenses	**13.3**	***+8.5%***
Cost-to-income ratio	**59.6%**	***-0.7 pp***
Gross operating profit	**9.0**	***+11.6%***
Cost of risk	**0.0**	***NA%***
Operating profit	**9.0**	***+11.9%***
Other gains and losses	**0.8**	***x2.8%***
Pre-tax income	**9.8**	***+17.5%***

Source: financial disclosures.

2. Balance sheets[7]

At end-2017, the five main French banking groups had aggregate total assets of EUR 6,282 billion, compared with EUR 6,498 billion at end-2016, equating to a 3.3% reduction over the period (Table 8).

Table 8
Aggregate total assets of the five main French banking groups (EUR billions)

	2016	2017	Change 2017/2016	Contribution to total balance sheet change
ASSETS	**6,498.4**	**6,282.3**	**-3.3%**	
Cash and cash balances at central banks	491.7	564.9	+14.9%	+1.1%
Financial assets held for trading	1,492.1	1,235.3	-17.2%	-4.0%
Financial assets designated at fair value through profit or loss	81.8	75.4	-7.9%	-0.1%
Available-for-sale financial assets	456.4	392.6	-14.0%	-1.0%
Loans and receivables: non-financial corporations	1,140.9	1,250.0	+9.6%	+1.7%
Loans and receivables: households	1,515.6	1,521.6	+0.4%	+0.1%
Other loans and receivables	672.1	661.2	-1.6%	-0.2%
Held-to-maturity investments	41.3	48.3	+17.0%	+0.1%
Derivatives – hedge accounting	79.3	58.4	-26.4%	-0.3%
Other assets	527.1	474.6	-10.0%	-0.8%
LIABILITIES	**6,498.4**	**6,282.3**	**-3.3%**	
Financial liabilities held for trading	1,325.8	1,099.0	-17.1%	-3.5%
Financial liabilities designated at fair value through profit or loss	216.1	230.8	+6.8%	+0.2%
Derivatives – hedge accounting	79.3	58.4	-26.4%	-0.3%
Deposits: central banks	147.8	195.6	+32.3%	+0.7%
Deposits: credit institutions	235.6	197.3	-16.3%	-0.6%
Deposits: other than credit institutions	2,823.9	2,914.5	+3.2%	+1.4%
Debt securities (including bonds)	807.4	786.7	-2.6%	-0.3%
Provisions	33.1	32.5	-1.7%	-0.0%
Subordinated debt	89.3	81.1	-9.2%	-0.1%
Total equity (group share)	377.9	385.3	+2.0%	+0.1%
Other liabilities	362.3	301.1	-16.9%	-0.9%

Source: FINREP – FIN1, FIN4 and FIN8 templates.

2.1. Improvements in cash and non-financial corporation lending partially offset the decline in market activities

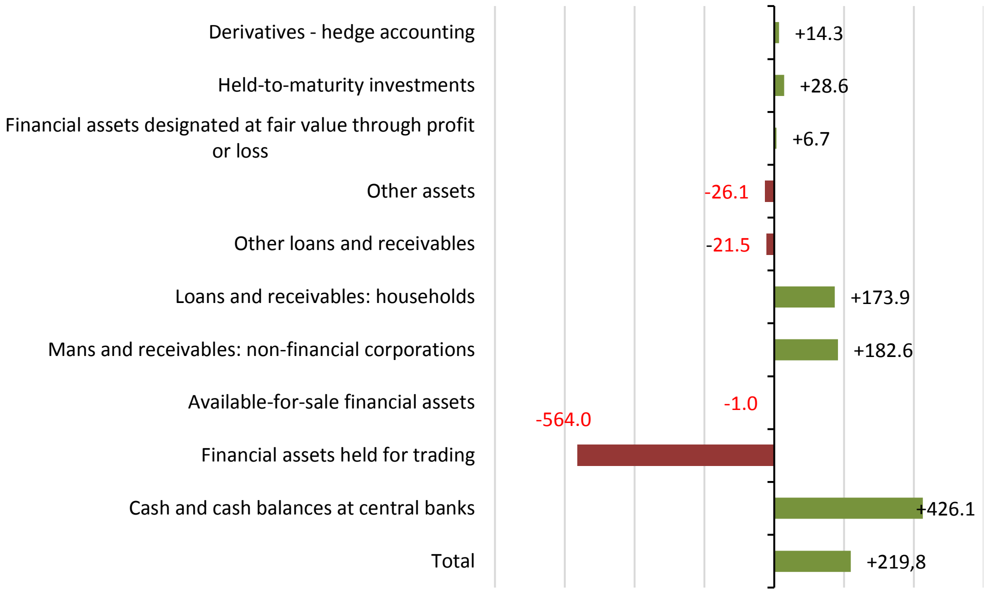
As in 2015 and 2016, banks continued to reduce their capital market activities in 2017 while stepping up their lending activities, but the EUR 104 billion increase in loans and receivables (up 3%) was not enough to fully offset the sharp 16% (EUR 327 billion) reduction in financial assets, particularly assets held for trading, which declined by EUR 257 billion, or 17.2%. The significant increase in non-financial corporation loans and receivables (up EUR 109 billion, or 9.6%) and the relative stability of household lending should however be viewed with caution as both trends mainly reflect a post-inspection accounting reclassification made by a bank. The adjustment involved transferring a major portfolio of individual entrepreneurs from "Individuals" to "Non-financial corporations".

Furthermore, as in previous reporting periods, "Cash and cash balances at central banks" continued to increase significantly (up 15%, or EUR 73 billion), reflecting further growth in reserves deposited with central banks, which qualify as liquid assets under liquidity coverage ratio (LCR) requirements.

The changes in 2017 are consistent with trends observed over a longer period: a EUR 565 billion drop in financial assets and increases in loans and receivables (up EUR 335 billion) and cash and cash balances at central banks (up EUR 426 billion) since 2009.

7 Unless otherwise indicated, this section covers BNPP, SG, GCA, GBPCE and GCM.

Chart 14
Change in the structure of assets between 2009 and 2017 (EUR billions)



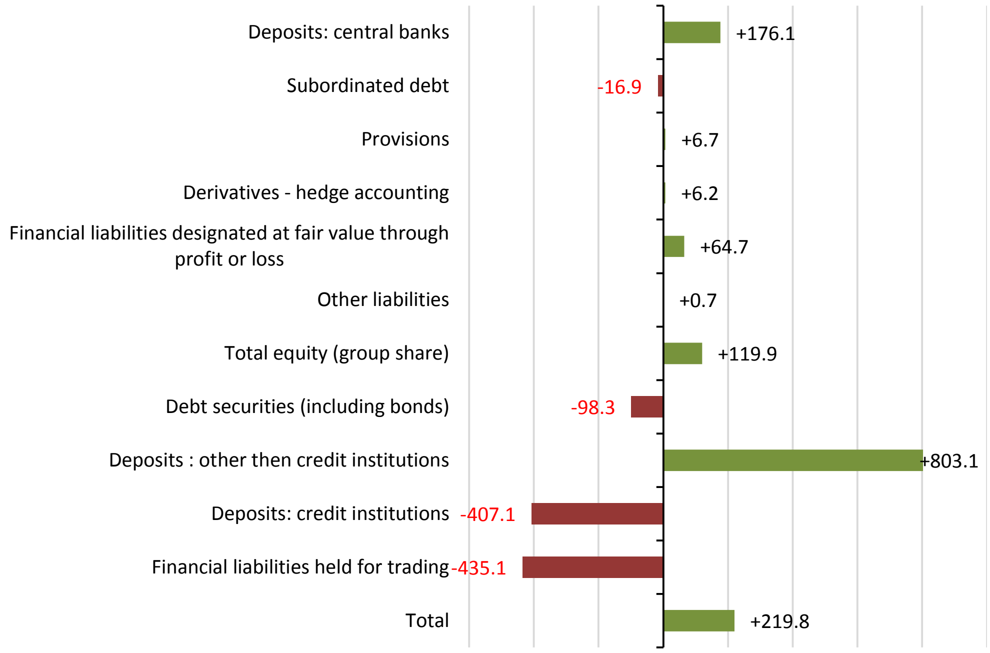
Source: FINREP – FIN1, CRD III and CRR templates.

2.2. Changes in liabilities mirrored changes in assets

Financial liabilities mirrored the changes observed in assets and continued to contract, down EUR 233 billion, or 14%, in 2017. The EUR 227 billion reduction in "financial liabilities held for trading" (down 17%) largely accounts for this contraction, despite the increase in deposits (up EUR 100 billion, or 3%), and particularly "deposits other than from credit institutions" (up EUR 91 billion, or 3%), which was insufficient to make up the shortfall. Furthermore, although they may be less significant in terms of absolute value, "deposits from central banks" increased dramatically by 32%, or EUR 48 billion, in 2017 while "deposits from credit institutions" fell by 16%, or EUR 38 billion.

As was the case for assets, the changes in the various liability items between 2016 and 2017 are consistent with trends observed over the long term: increases in "deposits other than from credit institutions" and "deposits from central banks" and decreases in "deposits from credit institutions" and "financial liabilities held for trading".

Chart 15
Change in the structure of liabilities between 2009 and 2017 (EUR billions)

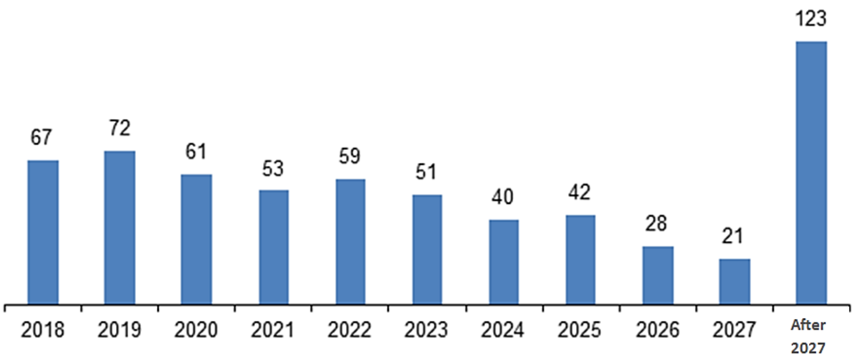


Source: FINREP – FIN1, CRD III and CRR templates.

To a lesser extent, the significant increase in "total equity (group share)" (up EUR 120 billion) highlights the scale of the improvement in banks' solvency since 2009 (see also Chart 36 below).

Meanwhile, the maturity profile of "debt securities", which have declined significantly since 2009 and accounted for a little over 13% of total liabilities at end-2017, remains relatively evenly spread over the coming years, thus reducing short and medium-term refinancing risk (Chart 16). The majority of securities issued are denominated in euro (70.1%), far ahead of the US dollar (20.4%). With the exception of the yen (3.7%), the use of other currencies is negligible.

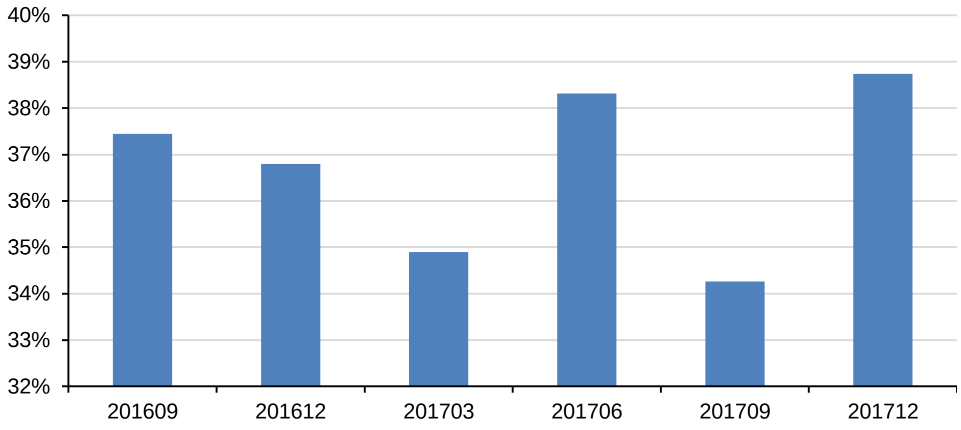
Chart 16
Long-term debt maturity profile of the main French banking groups at end-2017 (EUR billions)



Source: SNL and ACPR calculations.

Nevertheless, a significant proportion of French banks' financing is denominated in US dollars. At end-2017 they accounted for 38.7% of all liabilities excluding equity (Chart 17).

Chart 17
Proportion of French banks' financing in USD



Source: COREP – SF61 data.

The four major groups that report on this topic all achieved their medium and long-term financing objectives for 2017 (Table 9).

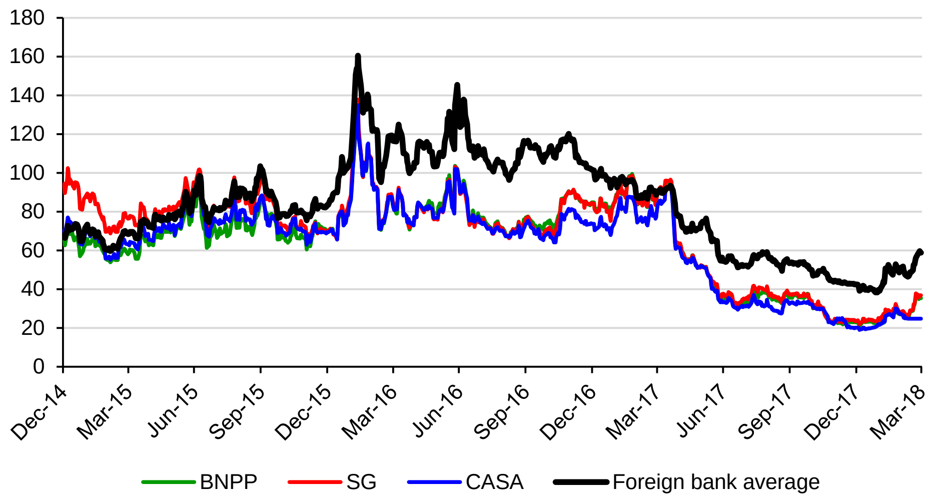
Table 9
Medium- and long-term financing programme for 2017 (EUR billion)

	Objective	Placed	Placement rate	Average Maturity
BNPP	33, of which 30.9 in senior debt, 1.25 in Tier 2 and 0.75 in Tier 1	34, of which 30.9 in senior debt, 1.25 in Tier 2 and 0.75 in Tier 1	100%	Not disclosed
SG	24.1 of which 71% in structured issues	30	125%	4.5 years
GCA (CASA)	16	16.6, of which 10.4 in preferred senior debt and collateralised senior debt and 6.2 in non-preferred senior debt	104%	Not disclosed
GBPCE	20	23, of which 64% in collateralised debt and 36% in non-collateralised debt	115%	7.1 years

Source: financial disclosures.

French banks' credit default swap (CDS) premiums contracted in 2017 (Chart 18) and remained lower than the average premium of foreign banks of comparable size, reflecting a decline in risk perception. However, CDS premiums for French banks, and for our entire sample with the exception of CASA, appear to be rebounding in 2018.

Chart 18
Change in CDS premiums of the main French banking groups

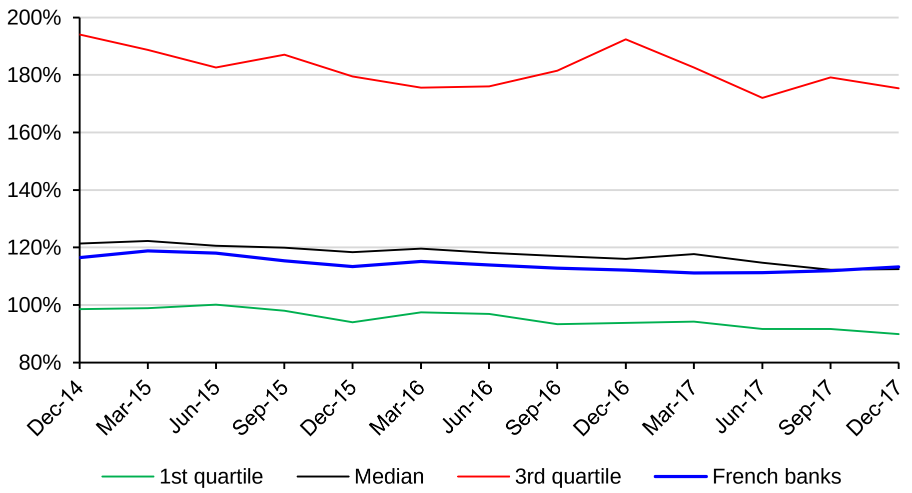


Five-year CDS premiums in basis points; average for a panel of foreign banks comparable in size to the French banks: Deutsche Bank, Commerzbank, ING, BBVA, Santander, Intesa SanPaolo, Unicredit, UBS, Crédit Suisse, Barclays, HSBC, RBS, Bank of America, JP Morgan, Citigroup and Wells Fargo.

Source: Bloomberg and ACPR calculations.

Lastly, French banks' average loan-to-deposit (LTD) ratio[8] increased slightly by 1.1 pp from 112.2% at end-2016 to 113.3% at end-2017,[9] consistent with the median of European banks (Chart 19).

Chart 19
Loan-to-deposit ratio for non-financial corporations and households in France and the European Union



Source: ACPR and EBA (FND_32).

8 LTD is calculated across a scope including non-financial corporations and households.

9 This calculation, which is performed by the EBA, does not take into account the adjustment for regulated savings (which would result in a higher ratio), unlike the calculation in the ACPR's report.

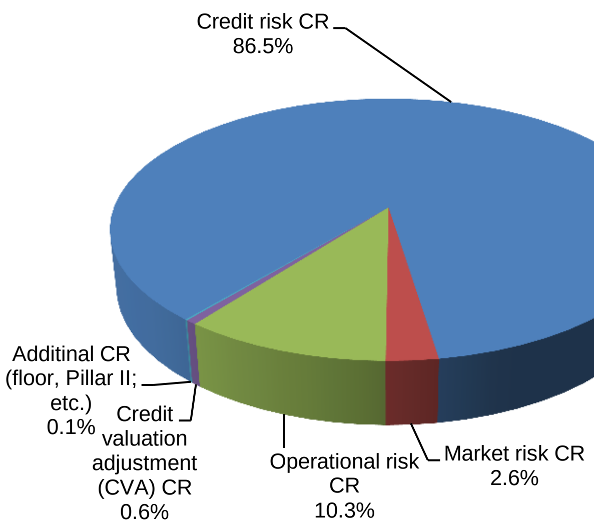
3. Risks

A detailed analysis of capital requirements, which form the denominator in the solvency ratio calculation, allows to identify the types of risks to which banks are exposed and examine their evolution.

3.1. A decrease in overall capital requirements

The credit risk component accounts for the vast majority of the capital requirements of the five main French banks[10] (Chart 20). Operational risk is the second most significant component, accounting for a little over 10% of total capital requirements, while the market risk component lags far behind at 3% and the other capital requirement components are negligible.

Chart 20
Breakdown of total capital requirements (CR) at end-2017



Source: COREP disclosures – CA template.

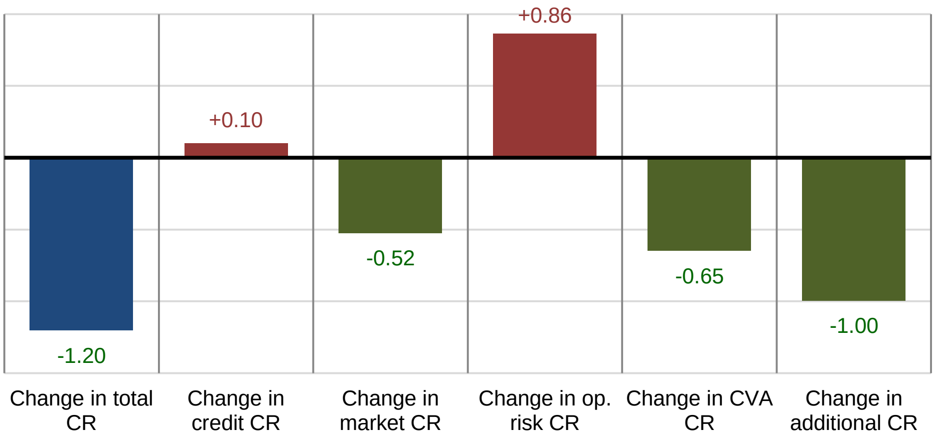
After the increases of recent years (EUR 3.7 billion from 2014 to 2015 and EUR 3.2 billion from 2015 to 2016) total capital requirements decreased in 2017 by EUR 1.2 billion to EUR 172.5 billion. Capital requirements for market risk continued to trend downwards while the operational risk component went up once again and credit risk capital requirements stabilised (Chart 21).

However, additional capital requirements[11] reduced significantly as a result of an ECB Governing Council decision of 6 February 2017 allowing one of the five groups to use its own loss-given-default estimations instead of the floor it had previously been required to apply to the weighted exposure amounts in its "corporate" portfolio.

[10] Unless otherwise indicated, this section covers BNPP, SG, GCA, GBPCE and GCM.

[11] Additional capital requirements mainly include stricter specifications set by supervisory bodies (safety margins for internal models, etc.) as well as those referred to in Articles 458 and 459 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 (CRR).

Chart 21
Change in capital requirements (CR) between 2016 and 2017 (EUR billions)



Source: COREP disclosures – CA template.

3.2. Capital requirements for credit risk stabilised

The analysis of capital requirements for credit risk covers both an estimate of the unexpected cost of future defaults and the cost of observed defaults, as measured by changes in arrears and loans in default.

3.2.1. Stable capital requirements for credit risk despite a very slight increase in the risk level of exposure

At end-2017, almost the entire exposure of French banks was concentrated in four portfolios: corporates, retail, governments and institutions The "Other" category includes exposures related to equity and securitisations, arrears and loans in default and other items under the standardised approach that represent a particularly high risk.[12]

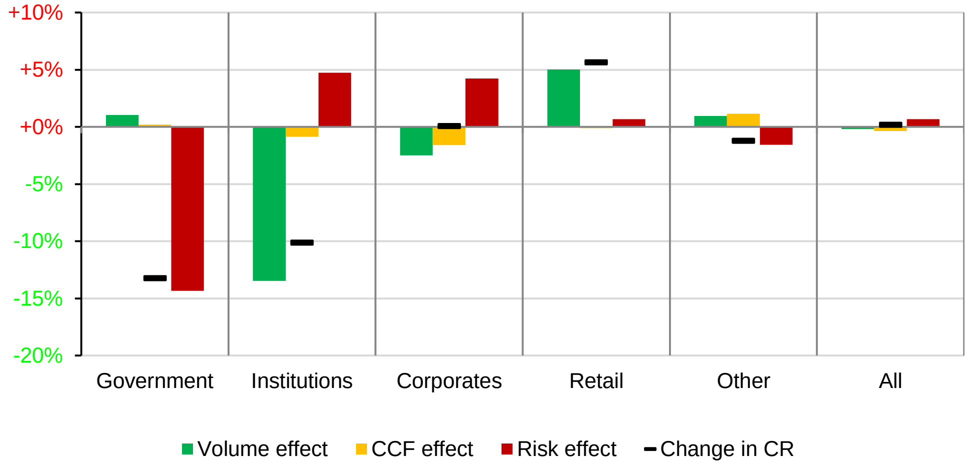
After rising by 2.2% in 2016, capital requirements for credit risk stabilised in 2017, increasing by only 0.1%: the slight rise in the risk of exposure[13] of 0.7% was partly offset by a reduction in loan volumes (down 0.2%) and a 0.3% decrease in the average credit conversion factor[14] (Chart 22).

12 In accordance with Article 128 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 (CRR), items with particularly high risks include certain shares or units in a collective investment undertaking, particularly investments in venture capital firms or alternative investment funds, investments in private equity or speculative immovable property financing. These exposures are assigned a risk weight of 150%.

13 Measured by the average weighting of loans. A change in the average weighting of exposures may reflect an actual change in the level of risk but may also result from a change in the method used to calculate risk-weighted assets (e.g. in the event of a change from the standardised method to the advanced method).

14 The credit conversion factor (CCF) measures the probability of off-balance sheet exposures shifting onto the balance sheet and becoming outstanding loans.

Chart 22
Change in credit risk capital requirements (CR) by portfolio between 2016 and 2017[15]



Interpretation: between 2016 and 2017, the "Corporates" loans exposure decreased by 2.5% (volume effect – green bar) and the CCF decreased by 1.6% (CCF effect – yellow bar) while average weighting increased by 4.2% (risk effect – red bar). All in all, capital requirements for this portfolio were unchanged (black marker).[16]

Source: COREP disclosures – CRSA and CRIRB templates.

However, the overall stabilisation in capital requirements incorporates a wide variety of developments from one portfolio to another:

- The "Corporates" and "Institutions" portfolios recorded a reduction in volumes whereas the level of risk increased. With regard to institutions, the reduction in volumes was significant at 13.5% while the level of risk rose by 4.7%. As for corporates, volumes decreased markedly overall (down 2.5%) but volumes of loans to SMEs remained buoyant (up 6.2%) while the level of risk remained under control. Conversely, there was a fall in volumes of specialised finance and loans to other businesses of 6.9% and 0.8%, respectively, while the levels of risk increased by 3.4% and 0.7%.
- Capital requirements with regard to the "Retail" portfolio increased by 5.6% from 2016 to 2017 as a result of higher volumes (up 5%, particularly driven by housing loans) and greater risk (up 0.7%).
- The "Governments" portfolio was characterised by a limited increase in volumes of 1.1% from 2016 to 2017 but a dramatic reduction in the level of risk (down 14.3% during the same period), mainly due to a decrease in risk weighted under the standardised method.

3.2.2. The quality of credit portfolios remained above the European bank average

Between 2016 and 2017, the impaired loan rate[17] fell again, down from 3.90% to 3.45% (Chart 23). This change, driven by a sharp 8.8% decline in impaired assets, can primarily be seen for non-financial corporations (down 65 bps to 5.05%) and households (down 58 bps to 3.30%).

The impaired asset ratio for credit institutions and other financial corporations was

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15 See the box on "analysing the change in capital requirements for credit risk" in Chapter 3.2.1 of Analyses et Synthèses No. 63, "French banks' performance in 2015".

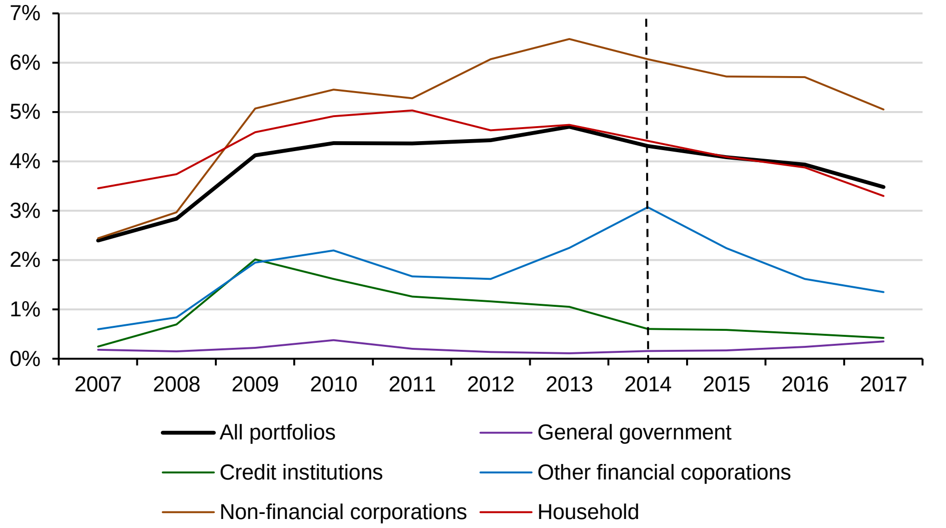
16 It can be shown that credit CR_y = credit CR_{y-1} x [(1+volume effect) x (1+ CCF effect) x (1+ risk effect) -1].

17 Within the "loans and receivables" category of the FINREP FIN6 templates, the impaired loan rate is defined as the ratio of "gross impaired loans and advances" to the sum of "loans and advances not impaired" and "gross impaired loans and advances". Moreover, the notion of doubtful loans, as defined in the French accounting rules used by credit institutions when drawing up their individual financial statements, does not exist under IFRS, which are the standards applied by the major French banks when preparing their consolidated financial statements.

also down due to a substantial reduction in impaired loans even though total outstanding loans declined less significantly.

By contrast, the impaired loan rate for general government is slightly higher (up 11 bps to 0.35%), as in 2016.

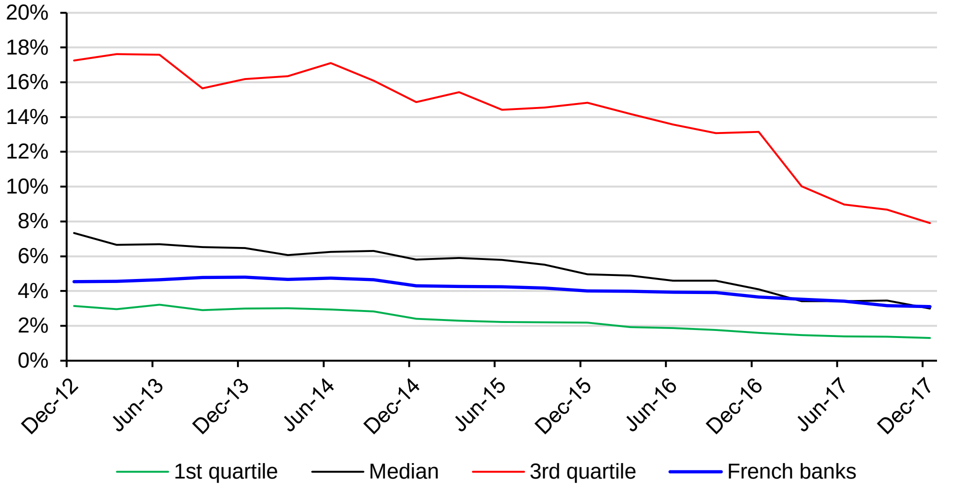
Chart 23
Impaired loan rates for the main French banking groups



Source: FINREP disclosures – FIN6 template; the dotted line indicates the change to CRD IV.

French banks'[18] non-performing loan ratio[19] was similar to those of their European competitors, as shown in Chart 24: having declined by 0.6 pp against 2016 to 3.1%, it was close to the EBA sample median.

Chart 24
Non-performing loan ratios for the main European banks



Source: ACPR and EBA (AQT_3.2), FINREP data (FIN18 template).

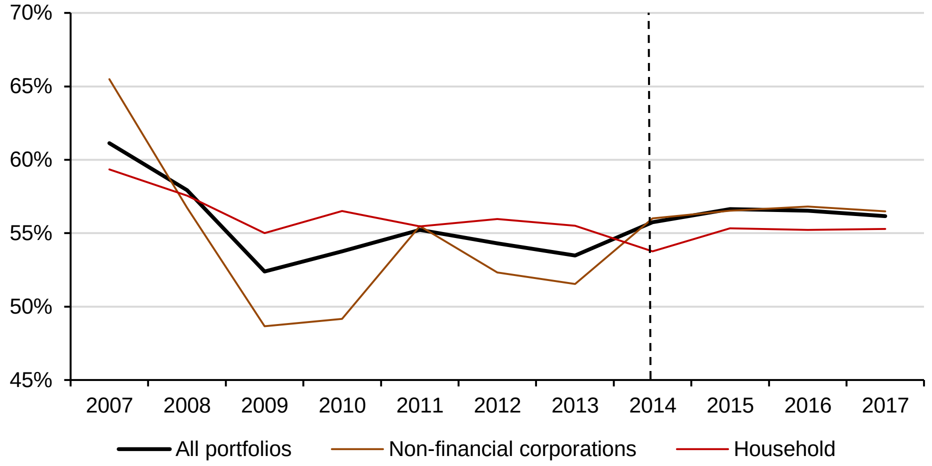
18 The French banks included in the EBA's key risk indicators calculations are as follows: Banque Centrale de Compensation, BNPP, BPIFrance, Crédit Mutuel group, Caisse de Refinancement de l'Habitat, BPCE group, Crédit Agricole group, HSBC France, La Banque Postale, RCI Banque, Société de Financement Local and Société Générale.

19 The FINREP templates use two different definitions of impaired loans:

- in the FIN6 template, the banks list their estimated impaired loans on the basis of national accounting rules;
- by contrast, in the FIN18 template, the banks list estimated impaired loans on the basis of the EBA's harmonised definition.

The overall coverage ratio[20] for French banks' impaired loans stabilised after bottoming out at 52.1% in June 2010, to stand at 56.4% in December 2016 and 56.1% in December 2017 (Chart 25). The coverage ratios for non-financial corporations and households remained largely unchanged at 56.5% and 55.1%, respectively.

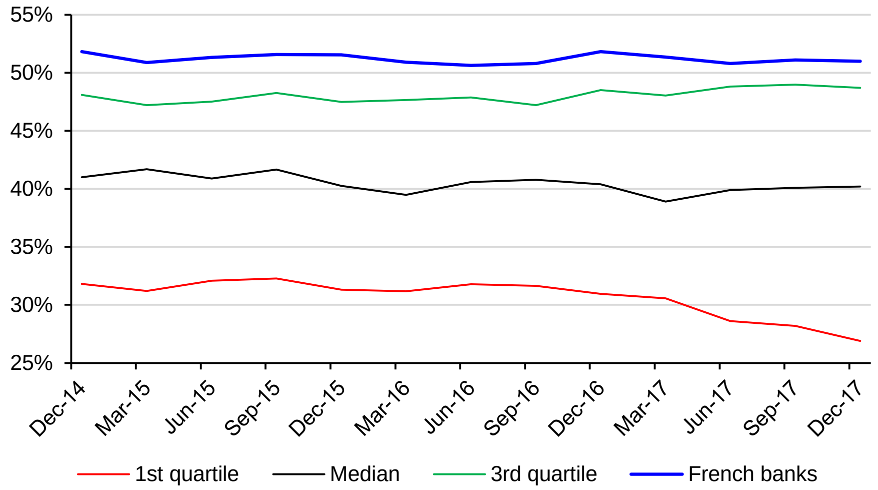
Chart 25
Impaired loan coverage ratios for the main French banking groups



Source: FINREP disclosures – FIN6 template.

French banks'[21] coverage ratios continued to be relatively higher than those of their European counterparts according to the EBA's common European definition of key risk indicators, exceeding the third quartile of European banks (Chart 26).

Chart 26
Impaired loan coverage ratios for the main European banks



Source: ACPR and EBA (AQT_41.2), FINREP data (FIN18 template).

20 The impaired loans coverage ratio in table FIN6 is defined as the ratio of "individual impairment losses" on "loans and advances" to "gross impaired loans and advances". The overall ratio includes loans and advances to non-financial corporations, households, general government, credit institutions and other financial corporations.

21 Sample of banks included in the EBA's key risk indicators calculations and therefore broader than the sample of the six major French banking groups (see above).

3.3. Reduction in capital requirements for credit valuation adjustments

At 31 December 2017, capital requirements for credit valuation adjustments (CVAs)[22] amounted to EUR 0.95 billion, or 0.6% of total capital requirements, down 13% year-on-year.

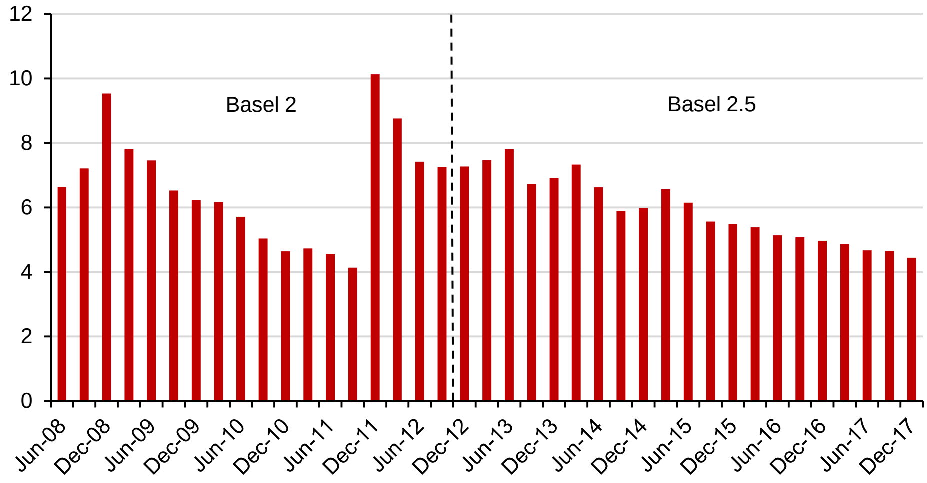
3.4. Continued reduction in capital requirements for market risk

3.4.1. An assessment that is common to the five groups

Capital requirements for market risk once again declined in 2017, down 10.5% year-on-year to EUR 4.4 billion, following a 9.5% reduction between 2015 and 2016 (Chart 27). They accounted for 2.6% of total capital requirements in 2017 compared with 2.9% in 2016.

However, this steady reduction in capital requirements for market risk since 2015 conceals a range of varied trends depending on the different regulatory models adopted (Chart 28), under supervisory authority control. For example, capital requirements for portfolios measured for regulatory purposes using the standardised method (excluding securitisations and the correlation trading portfolio) rose sharply by 30.7%, largely due to an increase in capital requirements for foreign exchange risk under the standardised method of a bank that corrected its calculation approach. Conversely, there was a further decline in the capital requirements calculated on portfolios whose risks are measured using internal models, driven by historically low levels of VaR[23] and SVaR[24] (an aggregate amount of EUR 2.1 billion, down 27.6% on 2016). These levels are mainly the result of a low volatility regime in place since the second half of 2016, despite certain limited periods of greater volatility (mainly related to Brexit and the election of Donald Trump), as well as changes in some institutions' hedging positions and strategies in their regulatory trading portfolio.[25] Lastly, the diversification effects of the different risk factors incorporated in internal models, which reduce capital requirements, amounted to EUR 1.2 billion, up 15.8% compared with 2016.

Chart 27
Capital requirements for market risk
(EUR billions)



Source: COREP disclosures – CA template.

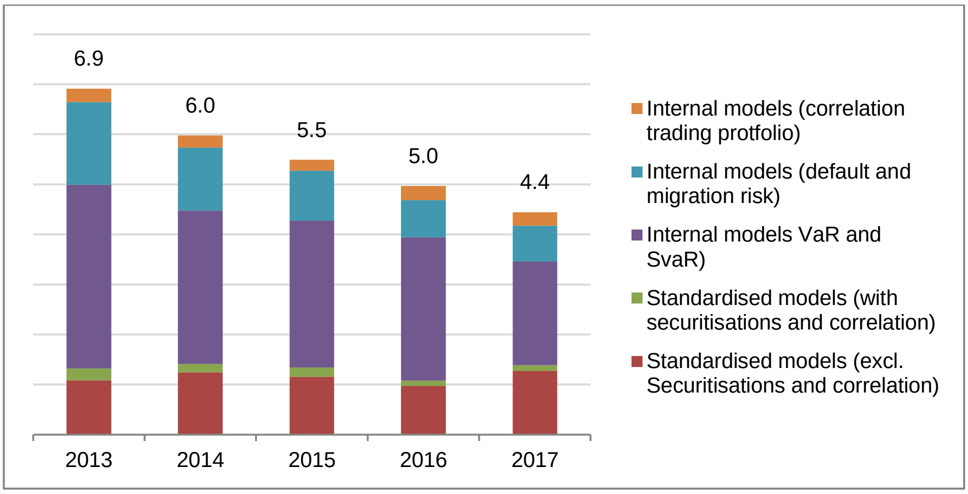
22 CVAs are intended to measure counterparty default risk on OTC derivatives other than credit derivatives recognised to reduce risk-weighted exposure amounts for credit risk.

23 Value at Risk measures the potential loss on risk positions over a given time horizon and for a given level of probability.

24 Stressed VaR (SVaR) is designed to correct the procyclicality of VaR, as it is calibrated to a period of financial market stress.

25 Explanations taken from banks' reference documents and Pillar III disclosures.

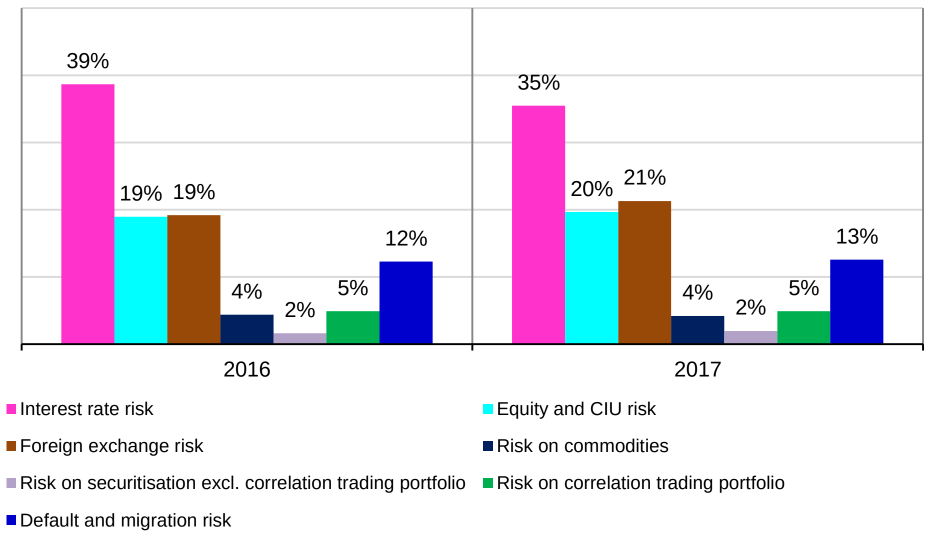
Chart 28
Breakdown of capital requirements for market risk by calculation method
(EUR billions)



Source: COREP disclosures – MKR template.

In terms of changes in the breakdown by risk factor of capital requirements for market risk (Chart 29), the main development was the reduction in the share associated with interest rate risk, which declined from 39% at end-2016 to 35% at end-2017. This decrease resulted from the part measured in internal models linked to changes in the positions mentioned above. The remainder of the breakdown is largely unchanged, with the contributions from equity and CIU risk and foreign exchange risk increasing from 19% in 2016 to 20% and 21%, respectively, in 2017.

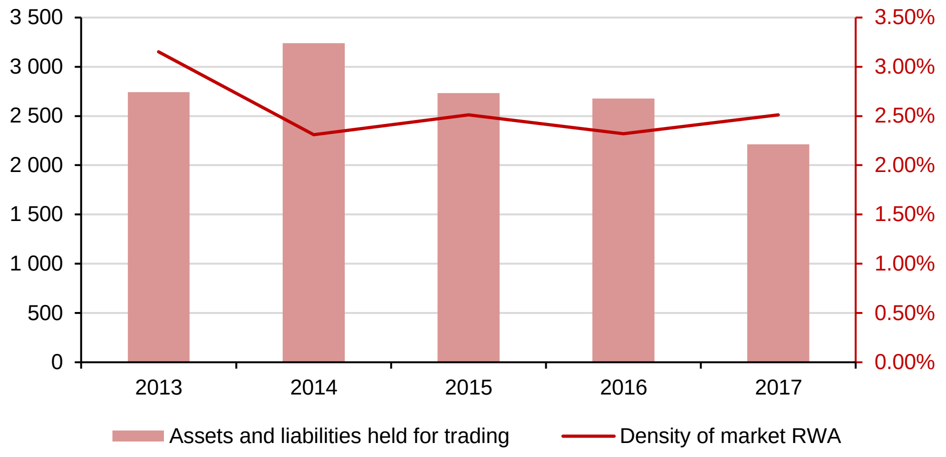
Chart 29
Change in the breakdown by risk factor of capital requirements for market risk between December 2016 and December 2017



Source: COREP disclosures – MKR template.

The balance sheet of the regulatory trading book on which the calculation of capital requirements for market risk is based can be proxied through the total of assets and liabilities held for trading, including derivatives. The density of market risk-weighted assets can therefore be measured using a ratio of market risk-weighted assets to total assets and liabilities held for trading. Since 2014, this ratio had been relatively stable at around 2.5% (Chart 30).

Chart 30
Density of market risk-weighted assets
(EUR billions)

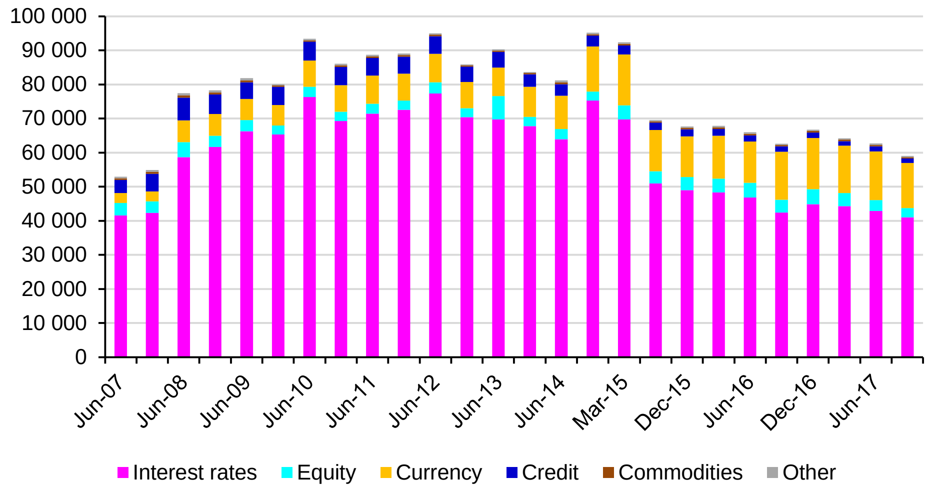


Sources: FINREP disclosures – FIN1.1 and 1.2 templates and COREP disclosures – CA template.

Furthermore, the notional amount of derivatives held for trading (Chart 31) fell by 6% between December 2016 and December 2017 after a significant decrease of 23% from 2015 to 2016. At end-2017, they accounted for 44% of assets held for trading (down from 50.3% at end-2016) and 51.5% of liabilities held for trading (compared with 56.6% at end-2016).

This downturn was mainly driven by decreases in the notional amounts of interest rate derivatives (down 3%, but accounting for 70% of total notional amount) and foreign currency derivatives (down 6%, but accounting for 22% of total notional amount).

Chart 31
Notional amount of derivatives held for trading
(EUR billions)



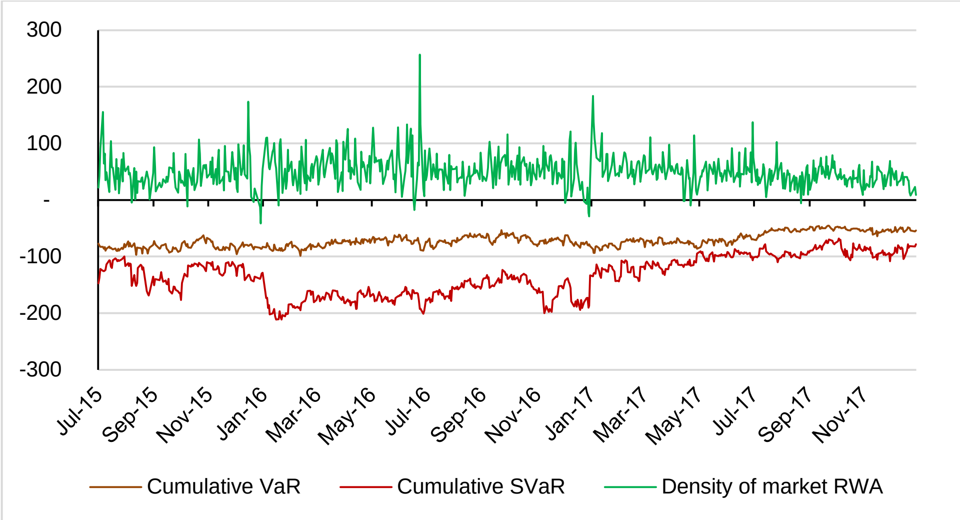
Source: FINREP disclosures – FIN3 template (FIN10 since 2014).

3.4.2. Additional information on groups using internal models for their capital requirements for market risk calculations

Four institutions – BNPP, SG, GCA and GBPCE – determine part of their capital requirements for market risk using internal models. Using past series of daily data, which these institutions are required to disclose, it is clear that since the second half of 2017, cumulative measurements of VaR and SVaR are similar and are at historically low levels (Chart 32). This is consistent with the market conditions observed during the period, which were characterised by extremely low volatility.

At the same time, income from market activities (actual total cumulative P&L) in 2017 was down by 13.3% year-on-year at EUR 12.6 billion compared with EUR 14.6 billion in 2016.

Chart 32
Changes in risk measurements (VaR and SVaR) and daily P&L (EUR millions)



Source: regulatory data.

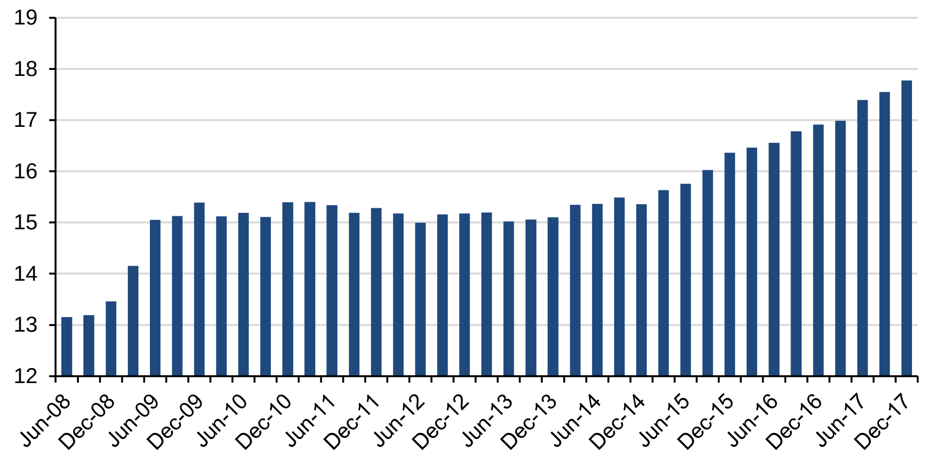
Backtesting[26] VaR measurements against hypothetical profit or loss identified four occasions when actual losses exceeded predicted losses in 2017, compared with three in 2016. Two of the four were recorded on the same day – 24 April 2017 – following a normalisation of market parameters (mainly reduced equity market volatility, appreciation of the euro against the dollar and less volatility in the euro-dollar currency pair) and the flight-from-quality observed after the results of the first round of the French presidential election. The two others were due to (i) losses on several activities related to exchange and interest-rate markets and (ii) accounting for technical adjustments arising from changes in market parameters, respectively.

3.5. A further increase in capital requirements for operational risk in 2017

Capital requirements for operational risk increased again in 2017 by 5.1% year-on-year to EUR 17.8 billion, after rising by 3.3% from 2015 to 2016 (Chart 33). The total increase from December 2013 to December 2017 amounted to almost 18%.

[26] Backtesting is a regulatory requirement intended to ensure the accuracy and appropriateness of the models applied. It is used to check that the number of days in which actual losses exceed predicted losses from calculated VaR comply with the 99% confidence level incorporated into the models.

Chart 33
Capital requirements for operational risk (EUR billions)



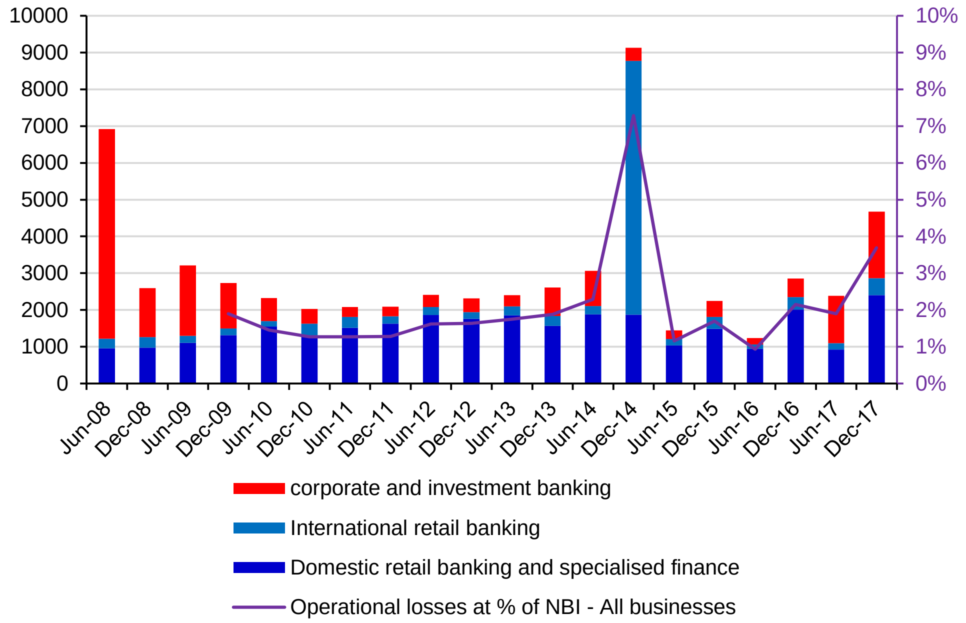
Source: COREP disclosures – CA template.

Importantly, even if the ratio of operating losses to NBI is well below its 2014 peak, it was still relatively high at end-December 2017 at 3.7% (Chart 34).

All business lines recorded significant increases in operating losses in 2017:

- In retail banking and specialised finance, operating losses were up 19.4% to EUR 2.4 billion.
- In international retail banking, operating losses were up 38.3% to EUR 464 million.
- In corporate and investment banking, operating losses more than tripled to EUR 1.8 billion.

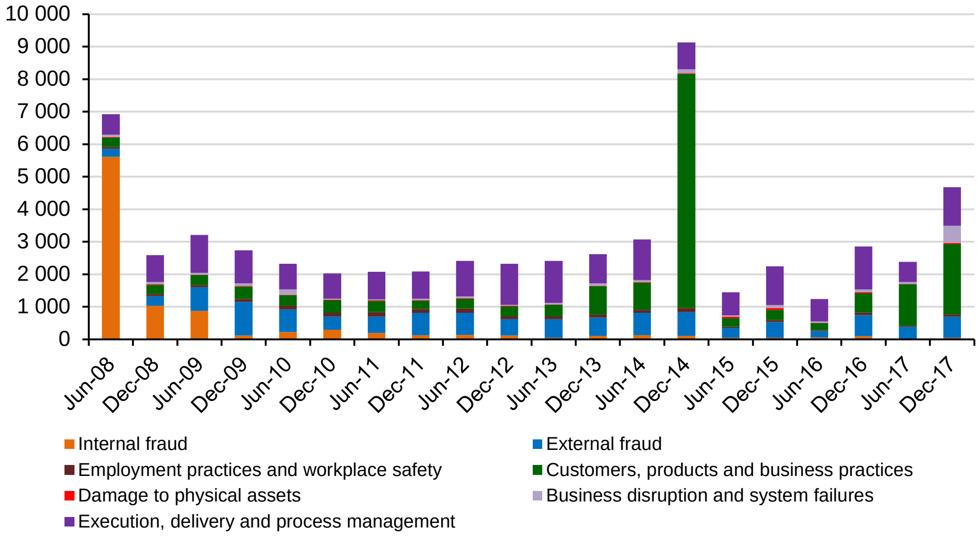
Chart 34
Operational losses by business line (EUR millions)



Source: COREP disclosures – OPR template – and financial disclosures (BNPP, SG, GCA and GBPCE).

Although the most significant risks until end-2016 were those associated with execution, delivery and process management, operational losses related to customers, products and business practices more than tripled from 2016 to 2017 and losses associated with business disruption and system failures (IT risk) went up six-fold. The other aspects of operational risk appear to be better managed (Chart 35).

Chart 35
Breakdown of operational losses (EUR millions)

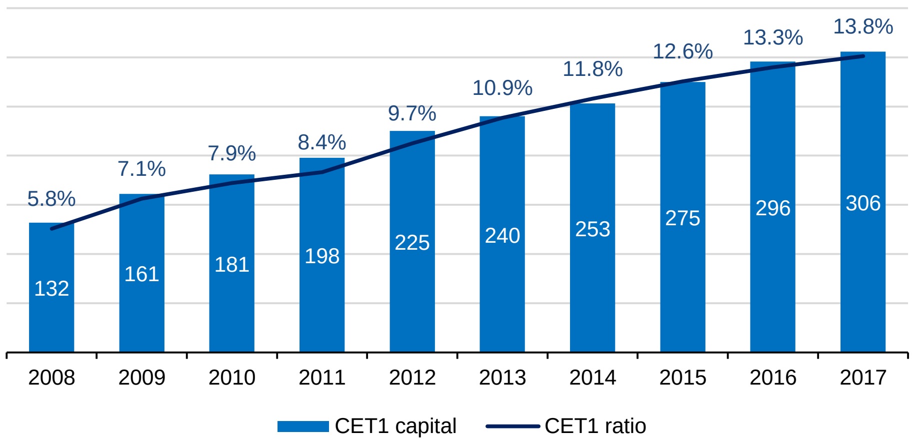


Source: COREP disclosures – OPR template.

4.1. Continued improvement in French banks' solvency

In 2017, the average Common Equity Tier 1 (CET1) solvency ratio of the six main French banks further improved by 0.5 pp compared with 2016 (Chart 36), driven by a 3.4% increase in CET1 capital and a 0.4% reduction in risk-weighted assets.

Chart 36
Change in average CET1 ratio of the main French banks since 2008[27]



Note: changes resulting from regulatory developments and updated reporting requirements have been restated as far as possible to show consistent "full CRR/CRD IV" CET1 capital ratios and RWAs over time.

Source: BAFI/SURFI and COREP reports, Basel III Quantitative Impact Study (QIS) and BNPP, SG, GCA, GBPCE, GCM and LBP financial disclosures; ACPR calculations.

While French banks as a whole continued to improve their solvency in 2017 with ratios that all exceeded post-transition period requirements ("full CRR/CRD IV"), trends differed depending on the bank. For example, GCM and GBPCE boosted their ratios by 170 bps and 120 bps, respectively, while LBP's ratio fell by 90 bps and SG's ratio declined by 10 bps (Table 10).

Of all the banks in the sample, GCM had the highest CET1 ratio having increased its CET1 capital by around 6% and reduced its risk-weighted assets (RWAs) by almost 4% in 2017. Over the same period, GBPCE augmented its equity by 6.5% while lowering its RWAs by 1.3%. Conversely, the 90 bps reduction in LBP's ratio is mainly due to a near 9.5% increase in RWAs (primarily related to loans) despite this being only partially offset by a 2.6% growth in equity. And while SG's RWAs remained relatively stable (down slightly by 0.6%), it reported a 1.7% decrease in equity as a result of more prudential deductions and restatements.

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27 Due to the significant regulatory developments since 2008 and the changes they imposed on the calculation of the CET1 ratio, a long-term analysis of changes in the CET1 ratio is only possible if specific adjustments are made to ensure comparability over time. Equity has thus been adjusted to recalculate "CRR equivalent" data based on Basel II data from 2008 to 2011 and Basel II.5 data from end-2011 to end-2013.

With respect to pre-CRR regulatory restatements, the following assumptions have been made: the 50/50 deductions applied to Tier 2 have been fully deducted from CET1; hybrid securities eligible for Tier 1 have been excluded; and the equity method adjustment has been risk-weighted instead of being deducted from equity.

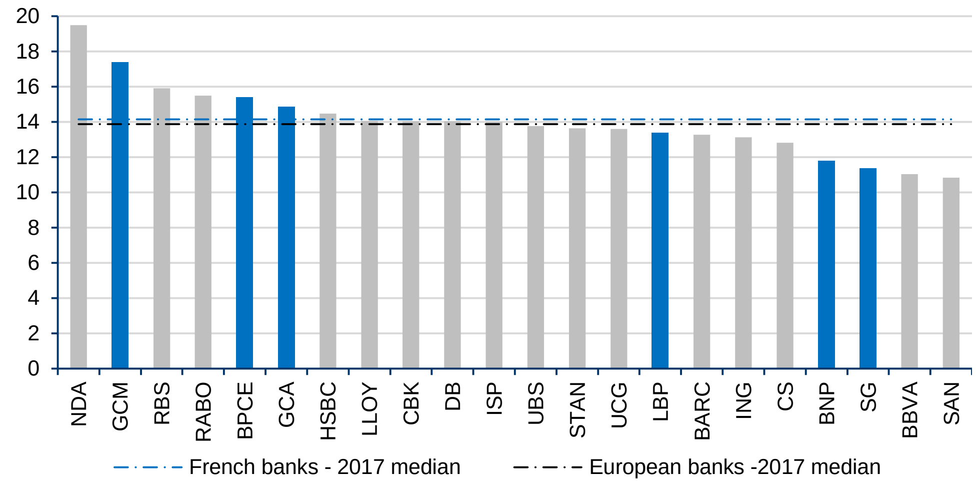
Table 10
"Full CRR/CRD IV" CET 1 ratio

	BNPP	SG	GCA *(CASA)*	GBPCE *(Natixis)*	GCM	LBP	All
December 2016	11.5%	11.5%	14.5% *(12.1%)*	14.2% *(10.8%)*	15.7% phased	14.3%	**13.3%**
December 2017	11.8%	11.4%	14.9% *(11.7%)*	15.4% *(10.6%)*	17.4% phased	13.4%	**13.8%**

Source: financial disclosures.

French banks' median CET1 ratio in 2017 was slightly higher than the median of European banks (14.1% compared with 13.9% – see Chart 37). Three French banks reported among the highest CET1 ratios (over 14.9%). Despite a 40 bps improvement in 2017, BNPP remained at the lowest end of the CET1 ratio classification, just above SG.

Chart 37
"Full CRR/CRD IV"/Basel III CET1 solvency ratios at end-2017 (%)



Source: SNL.

Box: IFRS 9's[28] modest impact on French banks' CET1 ratios

As part of the publication of their results for 2017, French banks disclosed the impacts of the new standard, IFRS 9, that became applicable for annual periods beginning on or after 1 January 2018 (although application may be deferred until 1 January 2021 for financial conglomerates' insurance subsidiaries). Generally, the impact is relatively limited, ranging from a 10 bps decline in the CET1 ratio for BNPP to a maximum 30 bps decline for LBP (Table 11).

Table 11
Impact of IFRS9 application on the "full CRR/CRD IV"/CET1 ratio of French banks

BNPP	SG	GCA	GBPCE	GCM	LBP
-10 bps	+15 bps	-30 bps	-20 bps	-20 bps	-30 bps

Source: financial disclosures.

More specifically, we find that:

- the impact of asset reclassification based on the standard's new allocation criteria is deemed immaterial by the two banks that reported on the issue;
- French banks do not intend to spread the impact of the standard over a transition period, as authorised by Regulation (EU) 2017/2395;[29]
- the two banks that reported the smallest impact on CET1 (SG and BNPP) are also those that decided to defer application of IFRS 9 for their respective insurance subsidiaries, while GCA and GBPCE chose to include them within the standard's scope with effect from 1 January 2018.

Lastly, the standard states that the impact of a fair value adjustment attributable to changes in credit risk should no longer be taken directly to profit or loss and instead should be recognised in equity. Based on published data, this change in method would have a negative impact on CET1 of approximately EUR 547 million, or around 22 bps, at end-2017 for the three banks concerned.

Furthermore, all the European banks' leverage ratios exceed the minimum regulatory threshold of 3% while the medians for French and European groups are almost identical (Chart 38). In addition, all the French institutions with the exception of GCA improved their ratio during 2017 (Table 12).

28 IFRS 9 was published in July 2014 as a phased replacement of IAS 39 for the measurement and recognition of provisions for credit losses and includes requirements for hedge accounting methods.

29 In order to spread the standard's impact over time, Regulation (EU) 2017/2395 authorises banks to include the increased impairment provisions caused by the application of IFRS 9 in CET1 capital, and decrease those amounts to zero over a transitional period.

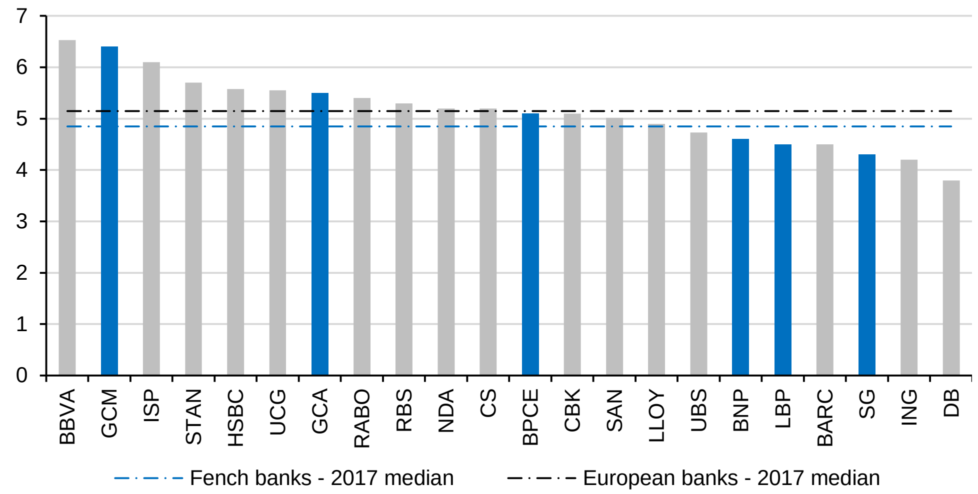
Table 12
CRR leverage ratios[30]

	BNPP	SG	GCA	GBPCE	GCM	LBP
December 2016	4.4%	4.2%	5.7% (5.0% CASA)	4.9% (4.2% Natixis)	6.1%	4.6%
December 2017	4.6%	4.3%	5.6% (4.4% CASA)	5.1% (4.1% Natixis)	6.4%	4.5%

Source: financial disclosures.

On the whole, the leverage ratios of French banks are less favourable than their CET1 solvency ratios, placing their median leverage ratio below that of their European competitors (Chart 38). However, given the divergence in the methods employed by French banks to calculate their ratios, which could equally apply to the ratios declared by other European Union banks, individual positions should be treated with caution.

Chart 38
Leverage ratios at 31 December 2017 (%)



Source: SNL and financial disclosures.

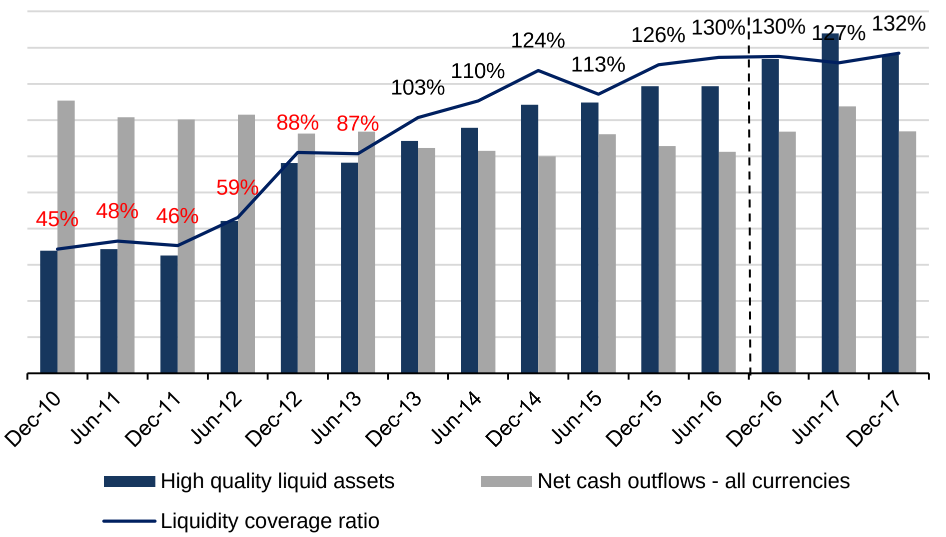
4.2. Liquidity ratios exceeded regulatory requirements

At 31 December 2017, the average liquidity coverage ratio (LCR) of the six major groups amounted to 131.7%, compared to 130.1% in December 2016 (Chart 39).

[30] Leverage ratios are calculated differently depending on the bank:

- ratios calculated excluding transitional measures (BNPP and SG);
- ratios calculated in accordance with the requirements of the European Commission delegated act of 10 October 2014 (GBPCE, GCA and LBP), with regulated savings amounts held with the CDC included in the denominator in the case of GBPCE and LBP, but not included in the case of GCA;
- ratios calculated in accordance with the requirements of the European Commission delegated act of 10 October 2014, with no indication of treatment of amounts held with the CDC (GCM).

Chart 39
LCR of French banks



Sources: QIS data until June 2016 and COREP date from December 2016.

Individually, each bank complies with the minimum liquidity coverage requirement of 100% as from 1 January 2018, in accordance with Article 460 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 (Table 13).

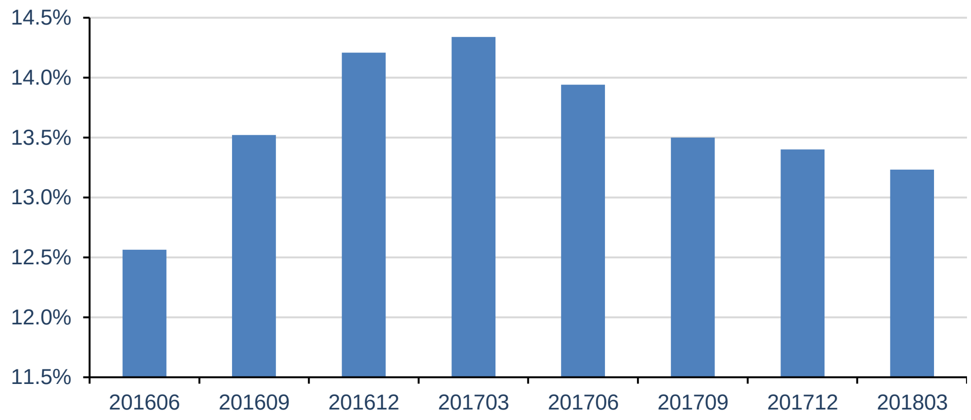
Table 13
LCR at 31 December 2017

	BNPP	SG	GCA	GBPCE	GCM	LBP
December 2017	121%	140%	≈133%	>110%	134%	157%

Source: financial disclosures; GCA publishes an average LCR for the 12 month period, but the other institutions publish year-end values.

Between December 2016 and December 2017, the banks strengthened the value of their LCR numerator (high-quality liquid assets – HQLA) by 1.1%, by increasing their reserves deposited with central banks, which increased by nearly 19.5% during the period to account for 54.7% of total HQLAs (Chart 41). At end-December 2017, central bank reserves of eligible liquidity accounted for 13.4% of the main French banking groups' total assets (Chart 40).

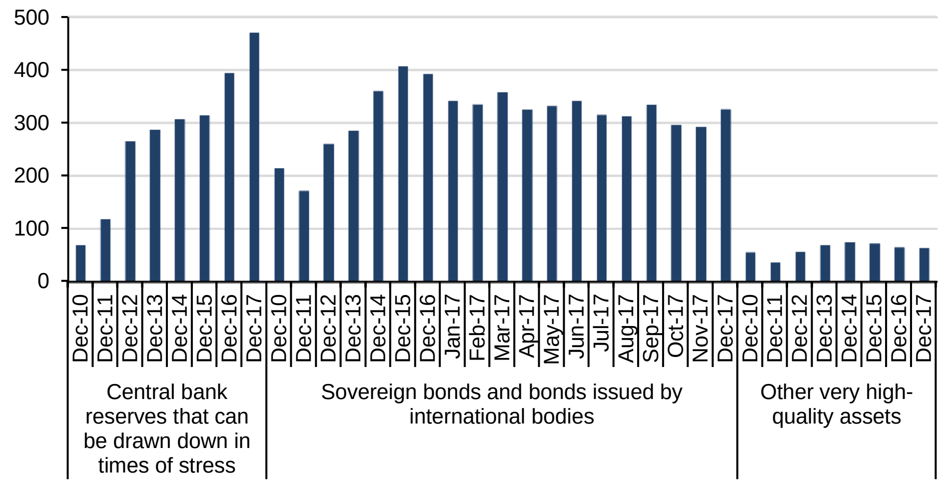
Chart 40
French banks' liquidity buffer eligible to central banks to total assets



Source: FINREP and COREP (C71) data.

By contrast, sovereign bonds and bonds issued by international bodies only accounted for 37.8% of total HQLAs in December 2017, compared with 46.1% at end-2016.

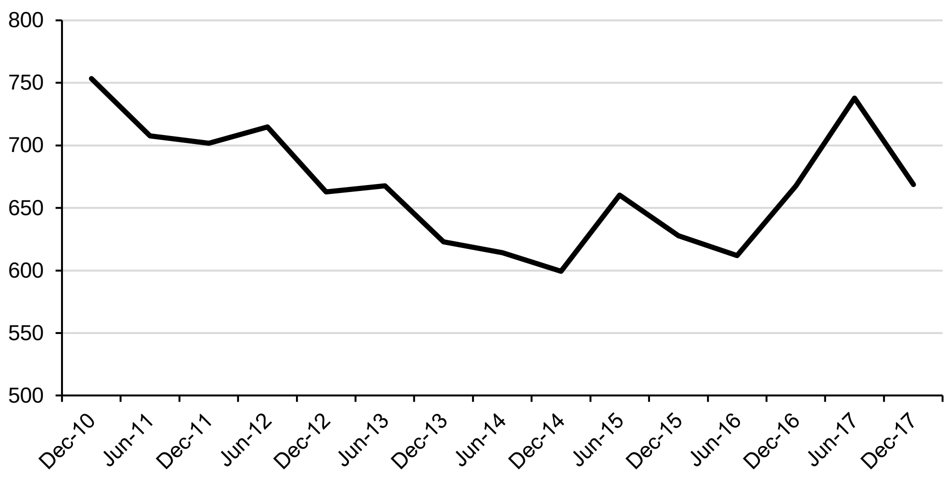
Chart 41
Breakdown of French banks' HQLAs (EUR billions)



Sources: QIS data until June 2016 and COREP date from December 2016.

In December 2017, the LCR denominator (net cash outflows) was unchanged from December 2016 (Chart 42).

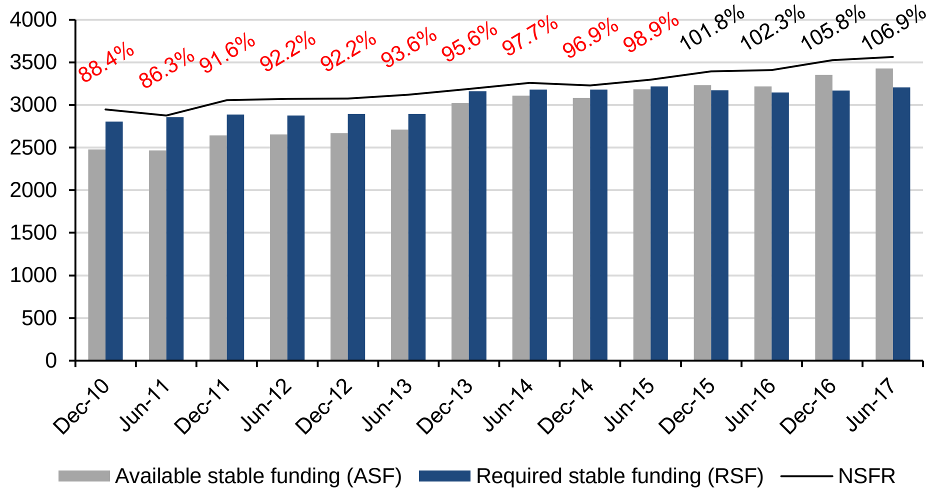
Chart 42
Net cash outflows (EUR billions)



Sources: QIS data until June 2016 and COREP date from December 2016.

The net stable funding ratio (NSFR) of the main French banks increased by 1.1 pp during the first half of 2017 to 106.9% at end-June 2017 (Chart 43). Available stable funding (up 2.3% during the half-year period) exceeded required stable funding (up 1.3% over the same period) by EUR 221.3 billion. The major French banks now each individually meet the regulatory threshold of 100% that came into effect on 1 January 2018.

Chart 43
Available and required stable funding (EUR billions) and NSFR



Source: QIS half-yearly data.

4.3. Substantial progress in complying with TLAC requirements

In addition to meeting minimum capital requirements, global systemically important banks (G-SIBs) must also maintain a minimum total loss-absorbing capacity (TLAC) in the event of resolution. G-SIBs will be required to meet an RWA minimum of 18% and a leverage ratio exposure (LRE) minimum of 6.75% as from 1 January 2022, following a transitional phase of a minimum 16% of RWA and 6% LRE applicable from 1 January 2019. The TLAC standard is a "pillar 1" requirement and thus takes priority over capital buffers.

During 2017, the banks continued to issue non-preferred “senior junior” debt, a new class of senior debt available to absorb losses, which ranks between subordinated debt and senior debt and was created in December 2016 by the *Code monétaire et financier* (the French Monetary and Financial Code) in its Article L. 613-30-3-I-4.

Several groups reported changes in their total loss-absorbing capacity in their 2017 financial disclosures (Table 14). The banks estimated their TLAC ratios on the basis of data for end-December 2017.[31]

At end-2017, SG already reported ratios that exceeded the Financial Stability Board requirements for 2019, with a TLAC ratio of 21.4% of RWAs and 6.6% LRE. GBPCE estimated its TLAC ratio at 20.8% and intends to reach 21.5% by end-2019 by issuing EUR 4 billion to EUR 5 billion of non-preferred senior debt per year. It does not foresee any need to issue preferred senior debt. GCA reported a TLAC ratio of 20.6% at end-December 2017, excluding eligible preferred senior debt, and restated its target of 22% in 2019. It is planning a possible adjustment to its TLAC debt issuance programme of a cumulative EUR 2 billion to EUR 3 billion during 2018 and 2019.

31 Three banks – GCA, GBPCE and SG – disclosed estimates of their TLAC ratio. BNPP does not report on TLAC.

Table 14
TLAC ratio financial disclosures

BNPP	- TLAC ratio (% of RWAs): not disclosed - Target: 21% in 2020
SG	- TLAC ratio (% of RWAs): 21.4% - TLAC ratio (% LRE): 6.6%
GCA	- TLAC ratio (% of RWAs): 20.6%, excluding eligible preferred senior debt - Target: 22%, excluding eligible preferred senior debt, by 2019
GBPCE	- TLAC ratio (% of RWAs): 20.8% (up 150 bps in 2017) including the issuance of EUR 1.6 billion in non-preferred senior debt in January 2017 - Target: 21.5% at end-2019

Source: financial disclosures, fourth-quarter 2017.

Tables and charts

Tables

Charts