



RATING ACTION COMMENTARY

Fitch Affirms Dexia Credit Local at 'BBB+'; Outlook Stable

Fri 22 May, 2020 - 6:23 AM ET

Fitch Ratings - Paris - 22 May 2020: Fitch Ratings has affirmed Dexia Credit Local S.A.'s (DCL) Long-Term Issuer Default Rating (IDR) at 'BBB+' with a Stable Outlook. The rating action follows the revision of France's and Belgium's Outlooks to Negative. Fitch believes that the Negative Outlooks on the sovereign ratings do not materially reduce the two countries' ability to support DCL.

KEY RATING DRIVERS

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IDRS, SUPPORT RATING, SUPPORT RATING FLOOR AND SENIOR DEBT

DCL's Long-Term IDR continues to reflect Fitch's view of a high probability that additional support would be provided to DCL by Belgium (AA-/Negative) and France (AA/Negative), if required, to complete the orderly wind-down of the company. Both sovereigns are main shareholders of DCL's parent Dexia SA/NV. DCL accounts for almost 100% of Dexia SA/NV's consolidated balance sheet.

Our view is based on the ownership of Dexia SA/NV, the sizeable funding guarantees provided to DCL by Belgium, France and Luxembourg (AAA/Stable)

of up to EUR85 billion as well as the three countries' ability to provide financial support. DCL had about EUR60 billion of guaranteed debt outstanding at end-April 2020 and we expect utilisation to remain below the EUR85 billion-limit.

Fitch continues to factor in state support for DCL despite the implementation of the EU's Bank Recovery and Resolution Directive (BRRD). This reflects our view that the BRRD will not be applied retroactively to DCL, as long as its orderly wind-down progresses consistently with plans agreed with the European Commission. Fitch views the risk of senior creditor bail-in as low for DCL. We expect Belgium and France to act pre-emptively, to the extent possible, to maintain DCL's capitalisation above minimum requirements.

DCL's deleveraging is progressing well. Its balance sheet was below EUR120 billion at end-2019 compared with about EUR360 billion at end-2011, when Dexia SA/NV was placed in orderly wind-down. From 2019, the ECB requires Dexia SA/NV to meet all regulatory requirements applicable to credit institutions it supervises at each group consolidation level. This was driven by improvements in Dexia SA/NV's and DCL's financial profile.

DCL's 'F1' Short-Term IDR is the higher of the two possible options that can be assigned for a 'BBB+' Long-Term IDR. This is because we view the sovereign propensity to support as more certain in the near term. We also view the risk of the Belgian or French sovereign paying its direct obligations ahead of providing support to DCL as low and have not identified other potential impediments to the prompt flow of funds to DCL.

Fitch does not assign a Viability Rating to DCL because it cannot be meaningfully analysed as a viable entity in its own right. DCL is in orderly wind-down and relies on state guarantees for funding.

STATE-GUARANTEED DEBT

The 'AA-'/F1+' ratings of DCL's debt guaranteed by Belgium (51.4%), France (45.6%) and Luxembourg (3%) are aligned with Belgium's ratings as it is the lowest-rated guarantor. Each of the three states is responsible for a share of the overall guarantee (several but not joint guarantee) and Fitch rates DCL's state-guaranteed debt on a 'first-dollar-of-loss' basis. The guarantee is unconditional, irrevocable and timely. It covers maturities of up to 10 years and debt issued until end-2021.

In September 2019 the European Commission approved the extension of the state guarantee beyond end-2021 for 10 years. The terms of the guarantee are

substantially the same except for a lower maximum amount of EUR75 billion instead of EUR85 billion, consistent with the decline in DCL's balance sheet. The new guarantee will be extended by Belgium and France only under a 53%/47% split and the 5bp guarantee fee will be increased by a 135bp deferred fee, which will accrue at a subordinated seniority level. Debt instruments issued before end-2021 will remain covered by the current state guarantee.

DERIVATIVE COUNTERPARTY RATING

DCL's 'BBB+(dcr)' Derivative Counterparty Rating (DCR) is at the same level as DCL's Long-Term IDR as the IDR is based on sovereign support and because derivative counterparties in France have no preferential status over other preferred senior obligations in a resolution scenario.

JUNIOR SUBORDINATED DEBT

The 'C' rating on DCL's deeply subordinated Tier 1 notes (FR0010251421) reflects the continued ban imposed by the European Commission on contractually non-mandatory coupon payment on these notes and their poor recovery prospects. The securities are will be subordinated to the deferred additional guarantee fee that will accrue from 2022.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-DCL's ratings are sensitive to a weakening in Belgium's or France's ability or propensity to provide additional support. We would likely downgrade DCL's Long-Term IDR if the two sovereigns' ratings are downgraded to the 'A' category. A significant reduction in state ownership or state-guaranteed funding that is not a result of lower funding needs, leading to reduced incentive to provide additional support, would also be rating-negative.

-A material deviation from DCL's wind-down plan agreed with the European Commission would lead to a negative rating action. It would likely trigger a fresh state-aid review and heighten the likelihood of the authorities requiring more stringent measures, which could include senior creditors sharing some of the burden. However, this is not Fitch's central scenario.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-An upgrade would be contingent on the two states demonstrating even greater support, in particular a greater propensity to support, which is unlikely, in our view.

STATE-GUARANTEED DEBT

The 'AA-' long-term rating on DCL's state-guaranteed debt is sensitive to rating action on the lowest-rated guarantor, which is currently Belgium. The 'F1+' short-term rating on DCL's state-guaranteed debt would be downgraded if the Short-Term IDR of any guarantor is downgraded.

DCR

The DCR of DCL is primarily sensitive to changes in its Long-Term IDR.

JUNIOR SUBORDINATED DEBT

Fitch does not expect coupon payment to resume on DCL's deeply subordinated Tier 1 notes and therefore sees no upside for the instrument's rating.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

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

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

DCL's ratings are sensitive to rating action on Belgium or France, which may affect their ability or propensity to support the bank. DCL's sovereign guaranteed debt is sensitive to rating action on the lowest-rated guarantor, which is currently Belgium.

RATING ACTIONS

| ENTITY/DEBT | RATING | | |
|----------------------------|------------------|-----------|----------|
| Dexia Credit Local S.A. | LT IDR | BBB+ | Affirmed |
| | ST IDR | F1 | Affirmed |
| | Support | 2 | Affirmed |
| | Support Floor | BBB+ | Affirmed |
| | DCR | BBB+(dcr) | Affirmed |
| ● guaranteed | LT | AA- | Affirmed |
| ● Senior preferred | LT | BBB+ | Affirmed |

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APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 28 Feb 2020\) \(including rating assumption sensitivity\)](#)

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EU Issued

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