

Research Update:

Dexia Downgraded To 'BBB-/A-3' On De-Banking; Off CreditWatch; Outlook Stable

January 2, 2024

Overview

- On Jan. 1, 2024, Dexia (previously Dexia Credit Local) relinquished its banking license and will therefore continue its orderly wind-down as a nonbank entity.
- In turn, we now analyze Dexia as a nonbank financial institution (NBFi) and no longer a bank.
- While partially mitigated by the creation of a new surveillance body by the guarantor states and the maintenance of Dexia's high-quality liquid assets level 1 eligibility, we believe NBFIs face incremental risk relative to banks because they operate outside a regulated framework.
- We therefore lowered our long- and short-term issuer credit ratings on Dexia to 'BBB-/A-3' from 'BBB/A-2'.
- The stable outlook reflects our expectation that Dexia will implement an orderly wind-down of its operations and continue to benefit from the very strong commitments of the Belgian and French governments in this process over the next two years.

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Rating Action

On Jan. 2, 2024, S&P Global Ratings lowered its long and short-term issuer credit ratings on Dexia (previously Dexia Credit Local) to 'BBB-/A-3' from 'BBB/A-2'. The outlook is stable.

Rationale

We now analyze Dexia as a nonbank financial institution (NBFi) and no longer as a bank. In our view, NBFIs face incremental risk relative to banks because they operate outside a regulated framework. We now use the NBFi anchor as the starting point in assigning our issuer credit rating (ICR) to Dexia. Although the usual anchor for French NBFIs is three notches below the bank anchor, we acknowledge the Dexia group has markedly different characteristics than most NBFIs. In particular, while Dexia now falls outside banking prudential regulatory requirements and no longer has access to central bank liquidity, it remains a government-related entity (GRE) in run-off, benefiting from state-guaranteed funding. Moreover, as opposed to most NBFIs, it does

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not face competition. We therefore apply a 'bb+' anchor in assessing Dexia's ICR--two notches below the previous 'bbb' bank anchor.

The rating action follows the European Central Bank (ECB)'s approval of the withdrawal of Dexia's credit institution license and investment services authorizations. The approval follows Dexia's request, initiated in July 2023, to de-bank and continue its run-off with the support of the French and Belgian governments (see "Dexia Group Entities Placed On CreditWatch Negative On Announced De-Banking," published July 7, 2023, on RatingsDirect). The withdrawal of authorization from Dexia was effective from Jan. 1, 2024. At the same time, Dexia Credit Local changed its corporate name to Dexia.

Dexia remains dependent on confidence-sensitive market funding and investor appetite for government-guaranteed debt, which is its primary funding source. In our view, the loss of the emergency liquidity assistance weakens Dexia's group stand-alone credit profile (SACP). However, maintaining the high-quality liquid assets level 1 eligibility for its guaranteed debt is a supporting factor to the funding from its current investor base, particularly when compared with NBFIs. Over the past few years, Dexia's funding plans have focused on further reducing its dependence on the ECB via short- and medium-term government-guaranteed market issuances and market repurchase agreement funding. Dexia has discontinued its recourse to ECB funding since year-end 2017. Considering the new anchor, we now see its funding and liquidity profile as less negative for the SACP than previously. Under its new framework, we also believe the French and Belgian governments will have more leeway to support Dexia in case of financial stress.

In our view, the group will maintain a robust risk management and risk appetite framework. This framework will replace the supervision previously performed by the National Bank of Belgium and Autorité de Contrôle Prudentiel et de Résolution, and banking and investment services regulations the Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRR/CRD) and Markets in Financial Instruments Directive (MIFID). An independent Surveillance Committee, set up by the guarantor states, took over from the banking supervisors on Jan. 1, 2024, particularly in terms of risk monitoring and the organization of internal controls. This committee comprises four members, appointed equally by the Belgian and French governments, with solid banking supervision expertise.

We believe the loss of the banking license and the new structure will reinforce Dexia's importance to its shareholders. This is because both states will now become the ultimate and sole supervising entities to ensure effective governance and a controlled wind-down of the entity. The creation of a surveillance body in lieu of the previous banking supervision reflects the governments' willingness to manage the run-off and minimize losses to taxpayers, in our view. As a result, we now believe that Dexia would be highly likely to receive extraordinary support from the French and Belgian governments in the event of stress. Therefore, Dexia is now rated four notches above the 'b+' SACP at 'BBB-'.

Outlook

The stable outlook reflects our expectation that Dexia will implement an orderly wind-down of its operations and continue to benefit from the very strong commitments of the Belgian and French governments in this process over the next two years. The ratings already factor in our expectation that, although Dexia will be loss-making for several years, its capitalization will adequately cover risks as deleveraging continues. A downgrade of Belgium or France would not, in itself, prompt us

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to lower the ICRs on Dexia. However, it would affect the issue ratings assigned to Dexia's debt that is guaranteed by these states.

Downside scenario

We might lower the ratings on Dexia if, contrary to our expectations, it cannot maintain sufficient access to market funding to implement its wind-down plan. We could also lower the ratings if the likelihood of government support diminishes, or if there are material delays in Dexia's deleveraging plan or effects on its results and solvency beyond our expectations.

Upside scenario

Ratings upside is remote, but we might raise the ratings on Dexia if we upgrade both Belgium and France.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	BBB-/Stable/A-3	BBB/Watch Neg/A-2
SACP	b+	bb
Anchor	bb+	bbb
Business position	Adequate (0)	Adequate (0)
Capital and earnings	Adequate (0)	Adequate (0)
Risk position	Constrained (-2)	Constrained (-2)
Funding and liquidity	Adequate and Moderate (-1)	Moderate and Moderate e (-2)
Comparable ratings analysis	0	1
Support	0	0
ALAC support	0	0
GRE support	4	3
Group support	0	0
Sovereign support	0	0
Additional factors	0	0

SACP--Stand-alone credit profile.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021

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- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Banking Industry Country Risk Assessment: France, Dec. 13, 2023
- Dexia Credit Local S.A., Oct. 11, 2023
- Dexia Group Entities Placed On CreditWatch Negative On Announced De-Banking, July 7, 2023

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Dexia Credit Local		
Issuer Credit Rating	BBB-/Stable/A-3	BBB/Watch Neg/A-2
Certificate Of Deposit	BBB-/A-3	BBB/Watch Neg/A-2
Senior Unsecured	BBB-	BBB/Watch Neg

Ratings Affirmed

Dexia Credit Local		
Junior Subordinated	D	
Dexia Funding Luxembourg S.A.		
Junior Subordinated	D	

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