Presale:

AXA Home Loan SFH (French Legislation-Enabled Covered Bond Program)

June 20, 2019

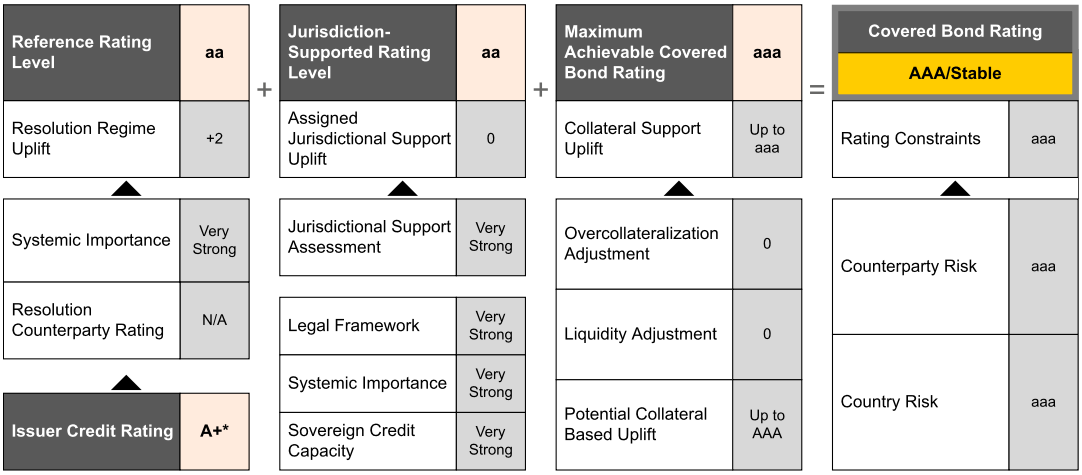
Note: This presale report is based on information as of June 20, 2019. The ratings shown are preliminary. Subsequent information may result in the assignment of final ratings that differ from the preliminary ratings. Accordingly, the preliminary ratings should not be construed as evidence of final ratings. This report does not constitute a recommendation to buy, hold, or sell securities.

PRIMARY CREDIT ANALYST

Alice Delemarle-Charton, CFA
London
(44) 20-7176-3594
alice.delemarle
@spglobal.com

SECONDARY CONTACT

Maria Luisa Gomez Grande
Madrid
(34) 91-788-7208
marisa.gomez
@spglobal.com



*Under our group rating methodology, AXA Banque Home Loan SFH is a core subsidiary of AXA Banque S.A. We therefore raise the ratings on the covered bonds according to the long-term issuer credit rating on AXA Banque. N/A--Not applicable.

Major Rating Factors

Strengths

- The rating on AXA Banque is high, at 'A+'.
- An asset cover test (ACT) in the program documentation protects the program from asset depletion.
- The proposed covered bond features a soft-bullet extendible maturity.

- The portfolio of residential loans in France is granular and exhibits low loan-to-income ratios.

Weaknesses

- The limited liability profile makes the transaction's asset-liability mismatch and target overcollateralization sensitive to any new issuance.
- Original loan-to-value (OLTV) ratios are relatively high, as 81% of the loans in the pool have OLTVs above 70%. This is, however, partly due to a conservative approach by the issuer on the remortgage loans, whose property value is equated to the loan balance.

Outlook

S&P Global Ratings' stable outlook on the preliminary rating on AXA Home Loan SFH's legislation-enabled mortgage covered bonds (obligations à l'Habitat [OHs]) reflects the fact that there are three unused notches of jurisdictional uplift and two unused notches of collateral uplift. We would lower our rating on the program and the bond should we lower the rating on AXA Banque S.A. by five or more notches or if the available credit enhancement were to decrease below the target credit enhancement commensurate with the rating.

Rationale

S&P Global Ratings has assigned its preliminary 'AAA' credit rating to the first residential loan-backed covered bond program and inaugural public issuance from AXA Home Loan SFH, a special-purpose entity owned by AXA Banque (see "AXA Home Loan SFH's French Covered Bonds Assigned Preliminary 'AAA' Rating; Outlook Stable").

Our covered bond ratings process follows the methodology and assumptions outlined in our "Covered Bonds Criteria," published on Dec. 9, 2014, and "Covered Bond Ratings Framework: Methodology And Assumptions," published on June 30, 2015.

We consider that the legal and regulatory framework for covered bonds in France will effectively isolate the cover pool assets for the benefit of the covered bondholders. This asset isolation allows us to assign a higher rating to the covered bonds than our long-term issuer credit rating (ICR) on AXA Banque ('A+').

We conducted a review of AXA Banque's mortgage operations, which we view as prudent. We believe satisfactory procedures are in place to support our rating on the covered bonds.

Under our covered bonds criteria, we first assess the reference rating level (RRL), which for AXA Banque covered bonds is 'aa'. This reflects the ICR on the issuer, plus two notches of uplift to reflect our view of the protection offered to covered bondholders by the bail-in provisions specified under the EU's Bank Recovery and Resolution Directive (BRRD) in France.

Our assessment of the expected jurisdictional support for AXA Home Loan SFH's covered bond program, which is backed by French residential loans, is very strong. Under our covered bonds criteria, this could result in a potential uplift from the RRL of up to three notches. However, the number of notches of uplift is constrained to the rating level on the sovereign, limiting the jurisdiction-supported rating level (JRL) at 'aa'.

We have reviewed the asset information provided as of March 2019. The provisional portfolio comprises loans backed by guarantees on residential properties in France. Based on our cash flow

analysis, we believe that the available credit enhancement exceeds the required credit enhancement for a 'AAA' rating.

There are currently no rating constraints to the 'AAA' rating relating to counterparty or country risks.

We have based our analysis on our criteria referenced in the "Related Criteria" section.

Program Description

Program Overview*

Jurisdiction	France
Type of covered bonds	Legislation-enabled
Underlying assets	Residential mortgages
Outstanding covered bonds (bil. €)	0.75
Expected rating at closing/year	'AAA'/2019
Extendible maturities	Yes
Target credit enhancement (%)	8.72
Credit enhancement for current rating	2.5
Available credit enhancement (%)	125.53

*Based on data as of March 31, 2019, worst scenario run.

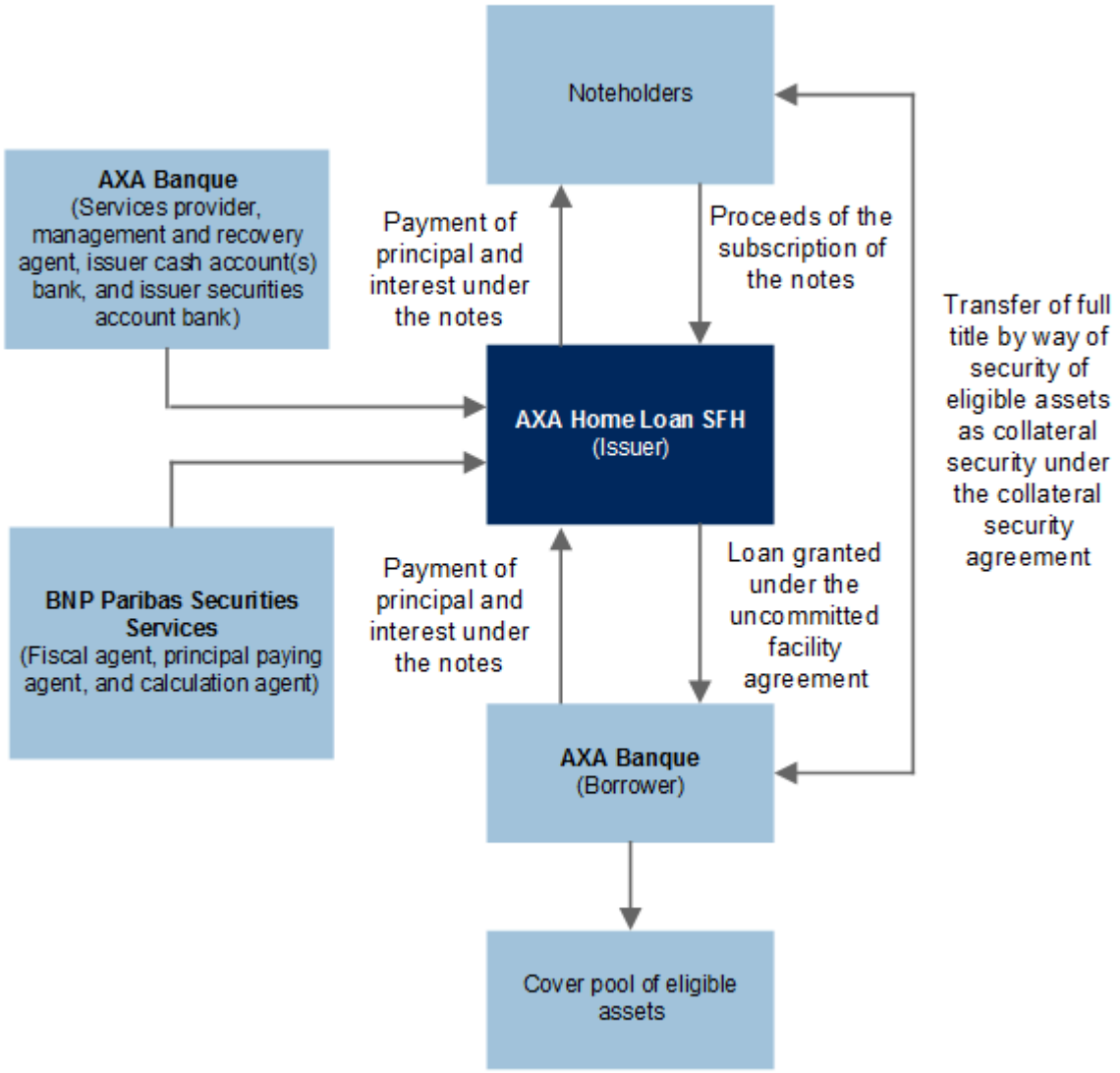
The AXA Home Loan SFH covered bond program is expected to provide some funding diversification for AXA Banque and replace its Belgian covered bond program currently outstanding.

The issuer, AXA Home Loan SFH, is a société de financement à l'habitat (SFH), a French credit institution licensed and regulated by the French banking regulator Autorité de Contrôle Prudentiel et de Résolution, as well as the European Central Bank. It is 100% owned by AXA Banque.

Under the program's terms, AXA Home Loan SFH uses the issuance proceeds to fund a credit facility to be made available to AXA Banque. The advances match the covered bonds' terms and conditions to ensure full and timely payment on the covered bonds. However, the covered bond maturity extension is not mirrored in the advance to AXA Banque. A prepayment on the advance is not contractually mirrored by a compulsory prepayment on the corresponding covered bond but leads to breakage costs payable to the SFH. If AXA Banque defaults, a pool of residential loans belonging to AXA Home Loan SFH (remise en pleine propriété à titre de garantie) is effectively transferred to its balance sheet. Loans must meet a set of eligibility criteria in order to be included in the cover pool. These assets secure AXA Home Loan SFH's financial obligations and allow us to assign a higher rating to the program than the long-term ICR on the issuer.

Chart 1

Transaction Structure



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A monthly ACT monitors the available assets' and collection loss reserve's credit enhancement level compared to the outstanding advances. If this level falls below the contractual commitment currently set at 108.1%, the bank will assign additional loans to the cover pool to ensure that the program meets the ACT by the next monthly evaluation. Such a breach will prevent the issuer from making an advance to the bank. If the issuer fails to assign sufficient collateral by the following

month, an event of default will occur, the advances will be accelerated, and the cover pool will be effectively transferred to the SFH. The payments on the covered bonds, however, will not be accelerated. The ACT is independent from the legal overcollateralization requirement, which the program must also meet at all times.

The issuer will pay interest and principal on each series of covered bonds on the respective scheduled payment dates. If AXA Banque defaults, the notes' redemption date will switch to the legal final maturity date. Our preliminary rating addresses timely payment on the legal final maturity date. We understand that only soft-bullet bonds are contemplated, however, the program documentation does not exclude hard-bullet bonds. There will be no swaps in the program at closing.

Table 2

Program Participants

Role	Name	Rating	Rating dependency
Issuer	AXA Home Loan SFH	NR*	Yes
Bank account provider	AXA Banque S.A.	A+/Stable/A-1+	Yes
Collection loss reserve provider	AXA Banque S.A.	A+/Stable/A-1+	Yes
Servicer	AXA Banque S.A.	A+/Stable/A-1+	No
Sub-servicer	Crédit Foncier de France	A/Stable/A-1	No
Arranger	Natixis	A+/Stable/A-1	No

*We apply the potential notches of uplift to the long-term rating on AXA Banque S.A. to derive the covered bond rating. NR--Not rated.

Rating Analysis

Legal and regulatory risks

In our view, France's legal framework for OHs, a type of covered bond, defined in article L515-34 and related articles of the "Code Monétaire et Financier", addresses the legal aspects in our covered bonds criteria, enabling us to rate the covered bonds higher than the issuer. Only a SFH can issue OHs under the framework, with OH-holders having recourse first to the issuer and, second, to the assets in the cover pool.

Under French law, holders of privileged liabilities, such as covered bonds, have a preferential claim to the SFH's assets ahead of all other creditors.

Under the SFH framework, overcollateralization for privileged debt must be at least 5%, weighted in accordance with the legal framework; 180 days of liquidity must be available at all times; and provisions for continued servicing must be in place if the bank defaults. The framework also provides further liquidity options by allowing the SFH, as a last-resort funding option, to subscribe to its own privileged covered bonds (up to 10% of total privileged liabilities), provided that the self-held OHs are used as collateral with the Banque de France or cancelled within eight days. The requirements applicable to the SFH's assets and liabilities are monitored by an independent supervisor ("contrôleur spécifique").

We base our analysis of legal risk on the guidelines in our "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017, and other criteria articles listed in our covered bonds rating framework.

We have reviewed a legal opinion addressing set-off risk, in the case of an AXA Banque default, of any borrower on a deposit account held with AXA Banque, and the risk of set-off of an AXA Group employee on their salary. The opinion concluded that there could be no set-off risk.

Operational and administrative risks

AXA Banque is the integrated, albeit small, banking arm of AXA's insurance operations in France. It leverages the group's insurance customers to build its retail-banking base.

We have not identified any operational or administrative risks that would affect our assessment of the program. A legal servicer replacement framework mitigates any operational risk associated with AXA Banque's insolvency as servicer of the cover pool loans. We consider that a substitute servicer would be available to take over servicing the cover pool.

As a regulated entity, AXA Home Loan SFH is subject to quarterly audits of its compliance with legal covenants from the contrôleur spécifique.

Our analysis of operational and administrative risks follows the principles described in our covered bonds rating framework criteria.

Resolution regime analysis

Under our covered bonds criteria, the rating on the covered bonds is linked to the issuer's RRL.

The BRRD was transposed into French law on Jan. 1, 2015. We assess the systemic importance for mortgage and public sector programs in France as very strong (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria," published on Oct. 16, 2018).

Under our covered bonds criteria, a very strong systemic importance means the RRL is the higher of the long-term ICR plus a two-notch uplift and the resolution counterparty rating (RCR). Resolution support uplift recognizes that resolution regimes such as the BRRD increase the probability that an issuer could service its covered bonds--even following a default on its senior unsecured obligations--because the law exempts covered bonds from bail-in risk in the event of bank resolution. We consider this an internal form of support because the bail-in of certain creditors of the issuer does not require direct government support.

Under our group rating methodology, we consider the issuer to be a core entity of AXA Banque, and therefore we uplift our rating on the bonds from the long-term ICR on AXA Banque. Given that our long-term ICR on AXA Banque is 'A+', the RRL is 'aa', which reflects the two-notch uplift.

Jurisdictional support analysis

In our jurisdictional support analysis, we assess the likelihood that a covered bond program facing stress would receive support from a government-sponsored initiative instead of from the liquidation of collateral assets in the open market.

Our assessment of the expected jurisdictional support for French mortgage programs is very strong. Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift over the RRL. However, because the rating on the sovereign, France (AA/Stable/A-1+; unsolicited), caps the JRL, the covered bonds cannot benefit from notches of jurisdictional uplift from the RRL, resulting in a JRL of 'aa' and three notches of unused jurisdictional uplift.

Collateral support analysis

The cover pool comprises prime French residential loans, all benefitting from a guarantee from specialist financial institution Crédit Logement.

Table 3

Cover Pool Composition*

Asset type	Amount (€)	(%)
Residential loans	1,691,461,895	100
Substitute assets	0	0
Total	1,691,461,895	100

The residential loans included in the provisional cover pool have to fulfill a list of eligibility criteria.

We assessed the cover pool's credit quality by estimating the credit risk, at the 'AAA' level of stress, associated with each loan in the pool. We based this loan-level analysis on the application of the specific stresses defined for France under our European residential loans criteria (see "Criteria - Structured Finance - General: Methodology And Assumptions: Assessing Pools Of European Residential Loans," published on Aug. 4, 2017). We then weighted each loan's foreclosure frequency by its percentage of the pool balance to obtain the pool's weighted-average foreclosure frequency (WAFF) and each loan's loss severity to obtain the pool's weighted-average loss severity (WALS). We have applied an originator adjustment above one to reflect the fact that the program does not currently play a crucial role in the bank's refinancing strategy. This adjustment also reflects that rental income is fully accounted for in the debt-to-income calculation of the buy-to-let (BTL) assets and that another entity, Crédit Foncier de France, partly services some of the assets (those originated before 2017).

Based on the pool's March 31, 2019, cut-off date, we estimate a WAFF of 14.00% and a WALS of 39.14% for the cover pool.

Tables 4 through 9 provide an overview of the provisional cover pool's composition.

Of the residential loans, 60% are for property purchase purposes, 19% are re-mortgages, and 21% are for construction and renovation. In addition, 71% of the loans finance a property that is occupied by the owner, 26% are for BTL properties, and a limited share are for second homes. We determined a weighted-average OLTV of 88.73%, which exceeds our 80% archetypical OLTV assumption for French residential mortgages, above which we make upward adjustments to the base foreclosure frequency. The presence of loans with OLTVs that exceed our 80% assumption leads, all else equal, to a higher residential WAFF. This is mitigated by the pool's low debt-to-income ratios (see table 7). Another factor influencing the WAFF is the assets' seasoning (see table 6). The higher the seasoning, the lower the WAFF, all else equal. We calculated a WAFF of 14.00%.

Based on our analysis of these house prices in relation to income, we apply a property indexation adjustment, and we adjust our market value decline (MVD) assumptions by applying an overvaluation adjustment to determine the residential WALS.

Furthermore, we have determined a weighted-average current LTV ratio for the cover pool of 71.3%. Current LTV ratios and MVD assumptions are two main considerations we use to determine the WALS for residential loans. The higher these variables are, the higher our WALS, all else equal. In addition, the cover pool's residential WALS is affected by jumbo valuations. We believe

properties with higher valuations could experience higher loss severities, owing to their smaller and less liquid market. To take this into consideration, we applied a multiple of 1.2x to our MVD assumption on the excess valuation above the limit of €650,000 in Paris and €375,000 in other regions. Finally, 100% of the pool is backed by a caution by Crédit Logement. Given our assessment of Crédit Logement's creditworthiness compared to the rating on the bonds, we consider that a proportion of defaulted loans will have no recovery and stress the WALS accordingly. We calculated a WALS of 39.14%.

Table 4

Key Credit Metrics

	As of March 31, 2019
Weighted-average original LTV (%)	88.73
Weighted average debt-to-income*	20.97
Weighted-average LTV (%) after HPI	71.3
Weighted-average loan seasoning (months)§	45.02
Weighted-average remaining loan term (months)	195.31
Balance of loans in arrears (%)	0.00
Buy-to-let loans / second homes(%)	25.92/3.47
Loans backed by a caution (guarantee)	100.00
Credit analysis results	
Weighted-average foreclosure frequency (WAFF; %)	14
Weighted-average loss severity (WALS; %)	39.14

*Debt-to-income refers to the debt service coverage ratio. §Seasoning refers to the elapsed loan term. LTV--Loan-to-value. HPI--House price index. N/A--Not applicable.

Table 5

Original Loan-To-Value Ratio

	As of March 31, 2019
(%)	Percentage of cover pool (%)
0-40	4.46
40-70	14.31
70-90	16.41
90-110	63.06
Above 110	1.76
Weighted-average original LTV	88.73

Table 6

Loan Seasoning Distribution*

	As of March 31, 2019
Seasoning (months)	Percentage of portfolio (%)
0-60	78.31
60-72	9.97

Table 6

Loan Seasoning Distribution* (cont.)

	As of March 31, 2019
Seasoning (months)	**Percentage of portfolio (%)**
72-84	3.93
84-96	4.07
96-108	1.88
108-120	0.48
more than 120	1.36
Weighted-average loan seasoning (months)	45.02

*Seasoning refers to the elapsed loan term.

Table 7

Cover Pool Assets By DTI

	As of March 31, 2019
(%)	**Percentage of cover pool (%)**
0-10	9.3
10-25	55.6
25-30	23.9
30-35	11.2
>35	0.0
Weighted-average DTI (%)	20.97

DTI--Debt service to income.

Table 8

Loan Geographical Distribution

	As of March 31, 2019	
(%)	**Percentage of cover pool (%)**	**Breach in geographical concentration ?**
Auvergne-Rhone-Alpes	5.8	No
Bourgogne-Franche-Comte	1.4	No
Brittany	1.6	No
Centre-Val de Loire	1.8	No
Corsica	0.8	No
Grand Est	2.4	No
Hauts-de-France	7.1	No
Ile-de-France	40.0	No
Normandy	3.3	No
Nouvelle-Aquitaine	10.1	No
Occitanie	10.7	No

Table 8

Loan Geographical Distribution (cont.)

	As of March 31, 2019	
(%)	Percentage of cover pool (%)	Breach in geographical concentration ?
Pays-de-la-Loire	3.3	No
Provence-Alpes-Cote d'Azur	11.6	No

Table 9

Current Loan-To-Value Ratios After HPI

	As of March 31, 2019
(%)	Percentage of cover pool (%)
0-20	2.46
20-40	7.94
40-60	14.83
60-80	32.94
80-100	41.1
Above 100	0.72
Weighted-average LTV	71.3

HPI--House Price Index.

Our analysis of the covered bond payment structure shows that cash flows from the cover pool assets would be sufficient, at the assigned rating level, to make timely payment of interest and principal to the covered bond on its legal final maturity.

In our cash flow analysis, we use the pool-level WAFF of 14.00%, and the recovery obtained from (1-WALS) equivalent to 60.86%, as well as the remaining credit parameters described in the "Credit analysis" section.

We stress the cover pool's cash flows by incorporating various default patterns, default timings, various interest rate stresses, prepayment rates, and delinquencies assumptions, among other factors.

The program will have no swap at closing that would mitigate the interest rate risk. The first issuance is planned as a fixed-rate issuance against fixed-paying assets.

We also model the possibility that the spread on the loans compresses over time due to defaults, prepayments, and product switches. To account for this, we reduce margins, assuming that a percentage of the higher-yielding loans exit the portfolio.

Our cash flow model bridges potential liquidity gaps by selling assets from the cover pool. The assets are sold at a determined discount above the then-prevailing interest rate. The discount applied to prime residential assets with a proportion of BTL loans above 15%, as described in our covered bonds criteria, is the weighted average of 850 basis points (bps) for the BTL loans and 425 for the others (see "Assessments For Target Asset Spreads According To Our Covered Bonds Criteria," published Oct. 16, 2018). The target asset spread used is 471 bps.

Because no notch of jurisdictional uplift is used due to the cap on the JRL by the sovereign rating, the program can reach a 'AAA' rating from a cash flow perspective by covering the 'AAA' credit risk

only, under our covered bonds criteria.

We have run a number of scenarios proposed by the issuer. In all cases, the available credit enhancement greatly exceeds the 'AAA' credit risk but also the target credit enhancement. This means that there are two notches of unused collateral uplift. Below are the cash flow metrics of the scenario which yields the most conservative results: a €750 million, fixed-rate seven-year bond with a one-year maturity extension.

Additional issuances from the program may change the current cash flow profile.

Table 10

Collateral Uplift Metrics

Proposed issuance	Seven-year bond with a one-year maturity extension
Asset WAM (years)	8.65
Expected liability WAM after extension (years)	8.00
Maturity gap (years)	0.65
Available credit enhancement (%)	125.53
AAA credit risk (%)	2.50
Coverage of 'AAA' credit risk	2.50
Coverage of 'AAA' credit risk	2.50
Coverage of 'AAA' credit risk and 75% of refinancing costs(%)	6.42
Target credit enhancement for maximum uplift (%)	8.72
Potential collateral-based uplift (notches)	4
Adjustment for liquidity (Y/N)	N
Adjustment for committed overcollateralization (Y/N)	N
Collateral support uplift (notches)	4

WAM--Weighted-average maturity.

Counterparty risk

We have identified several counterparty risks to which the covered bonds are exposed. However, as these are structurally addressed in line with our current counterparty criteria, we believe that they do not constrain the rating from a counterparty risk perspective (see "Counterparty Risk Framework: Methodology And Assumptions," published on March 8, 2019).

The SFH's bank account, held with AXA Banque, will house proceeds from the assets following an event of default in which the cover pool is effectively transferred to the SFH. The bank account contract reflects our counterparty criteria with replacement language in line with a 'AAA' rating.

The commingling risk in the program is mitigated through the ACT and the collection loss reserve provisions: should we downgrade AXA Banque below 'A', it will fund a collection loss reserve in the name of the SFH, which houses three-and-a-half months' worth of collection. This would compensate any erosion of the portfolio between a successful ACT and the moment all borrowers have redirected their payment to the SFH's account

There are currently no swaps in the program.

Country risk

We analyze country risk according to our "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019. The assets in the cover pool are residential loans located in France, which is within the European monetary union. The planned inaugural issuance benefits from a year's worth of maturity extension. We therefore conclude that it has low sensitivity to sovereign default, leading to a potential uplift of five notches above the rating on France. Given our 'AA' long-term unsolicited rating on France, country risk does not constrain our rating on the covered bonds.

Related Criteria

- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Criteria | Structured Finance | General: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Criteria | Structured Finance | General: Methodology And Assumptions: Assessing Pools Of European Residential Loans, Aug. 4, 2017
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria | Structured Finance | Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Criteria | Structured Finance | Covered Bonds: Covered Bonds Criteria, Dec. 9, 2014
- General Criteria: Methodology: Credit Stability Criteria, May 3, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- AXA Home Loan SFH's French Covered Bonds Assigned Preliminary 'AAA' Rating; Outlook Stable, June 17, 2019
- European Economic Snapshots: Domestic Demand Still A Safety Net, April 12, 2019
- Global Covered Bond Characteristics And Rating Summary Q1 2019, April 11, 2019
- Global Covered Bond Insights Q1 2019, April 11, 2019
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Oct. 16, 2018
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, Oct. 16, 2018
- French Financing Institution AXA Banque S.A. Rated 'A+/A-1+'; Outlook Stable, Sept. 3, 2018
- Europe's Housing Markets Are Staging A Soft Landing, Sept. 3, 2018
- Glossary Of Covered Bond Terms, April 27, 2018

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