AXA Banque

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Credit Highlights

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<th>Key risks</th>
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<td>A fully owned highly strategic subsidiary of AXA France, part of the leading global AXA insurance group.</td>
<td>Small size, affecting the cost base and profitability.</td>
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<td>High integration and continuous operational cooperation with the AXA group.</td>
<td>Low earnings capacity and business model concentrated toward French retail banking.</td>
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<td>Well-defined strategy of leveraging AXA France clients to expand the bank's commercial activity and diversify its product offering.</td>
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**Issuer Credit Rating**

A+/Stable/A-1+

**AXA Banque is a highly strategic subsidiary of AXA France.** AXA Banque is the integrated banking arm of AXA's insurance operations in France, a key market for AXA group. S&P Global Ratings views AXA Banque as a highly strategic subsidiary of the wider AXA group, reflecting the bank's high level of integration in the group's strategy, making it very unlikely to be sold or divested in the next two years.

**AXA Banque remains a small yet scalable player in the French retail banking segment with low-risk exposures.** AXA Banque offers a wide range of banking retail products such as mortgage, Lombard, and consumer finance loans, as well as savings and investment facilities. However, it remains a relatively small player in the French retail banking market with about €12 billion of loans outstanding projected at year-end 2021. Lombard, collateralized by AXA's life insurance clients, and mortgages loans make up about 95% of AXA Banque's total loan book. More than 90% of the loan book is either collateralized or guaranteed, which supports generally low cost of risk, in our view.

**The strategic plan to refocus commercial activities on AXA France's customer base and improve operational efficiencies, remains on track over the outlook horizon despite the COVID-19 pandemic.** While the refocus of the bank's commercial activities on AXA France's customer base has accelerated since 2020, 2021 was a milestone year regarding its second strategical stream, operational efficiency improvements. As part of the strategy to transform the bank's operating model, it is partnering with Arkea Banking Services (ABS) to outsource some business and information technology (IT) processes. This was largely executed in 2021 and early 2022 despite the pandemic. We understand that the partnership aims not only to allow customers to benefit from additional innovative services but more generally to improve AXA Banque's financial situation, service quality, and overall regulatory compliance. It will lead to a temporary but material cost increase, while enabling AXA Banque to reduce expenses in the medium to long run and reach a cost-to-income ratio of 70%-80%. Overall, this outsourcing should improve the bank's profitability when the full benefits are realized. This will also enable AXA Banque to finance its growth without strong support from the group, one of its medium-term objectives.
Outlook

The stable outlook on AXA Banque mirrors that on the AXA group. It also reflects our view that, in the next two years, the bank will remain a highly strategic subsidiary of the AXA group, and will successfully leverage the group's clients to expand its banking activities, creating value for the larger insurance group. Signs of a change in the bank's status within the group would include a shift in the group's strategic focus, a partial divestment, or its reluctance to provide capital, liquidity, and funding support for the bank's development. We consider these scenarios remote. As long as our assessment of AXA Banque's subsidiary status remains highly strategic, our ratings on the bank will very likely move in tandem with those on the AXA group. We could therefore upgrade or downgrade AXA Banque in the next two years if we take a similar rating action on the parent.

Rationale

AXA Banque is the integrated banking arm of AXA's insurance operations in France, a key market for AXA group (its shareholder equity amounts to about 0.7% of consolidated group capital). Therefore, we base the long-term rating on our assessment of the bank as highly strategic to AXA France, which is itself core to the AXA group. Our assessment of AXA Banque as highly strategic reflects its high level of integration in the group's strategy, making it very unlikely to be sold or divested in the next two years. We believe that, with this level of integration, the group will likely support AXA Banque in any foreseeable circumstances. We therefore rate AXA Banque one notch lower than our 'aa-' group credit profile on the AXA group. Under the bancassurance business model (the distribution of banking products by an insurance group), AXA Banque is designed to supplement the AXA group's commercial offering in France by providing a well-established banking platform to its clients and distribution networks, enhancing customer loyalty, supporting AXA's 2,400 tied agents in France, and increasing cross-selling opportunities. Therefore, the bank's rationale and business model focus on supporting AXA France's insurance business.

With total assets of about €16.7 billion in 2020, up from €11 billion in 2017, AXA Banque is a small yet scalable player in the competitive French retail banking market. As opposed to its former sister company AXA Bank Belgium (sold to Crelan on Dec. 31, 2021), the bank remains marginal by asset size, with no proprietary branch network outside the group. AXA Bank Belgium's disposal has created a need to redelegate intermediation activities it previously undertook (mainly interest rate swaps). As the bank is now European Market Infrastructure Regulation compliant, internal interest rate swap deals have moved to clearing houses. The overall effect of this has been modest, in our view. AXA Banque's integration within the group is reflected in particular by ongoing parental support in areas such as the distribution network, client base, profit sharing, and wholesale funding. We view the sale of AXA Banque by the group as a remote possibility considering the high integration of the bank's clients and distribution channels with those of the group. In response to low interest rates and the competitive environment, AXA Banque's transformation plan aims to refocus commercial activities on AXA France's insurance customer base while optimizing the operating model and targeting a lower cost-to-income ratio of 70%-80%, supported by the partnership with ABS. In our view, the bank should also benefit from improving service quality, innovation, and overall regulatory compliance as a result of this partnership. We believe the execution will remain on track over the outlook horizon despite the pandemic.

AXA Banque offers a wide range of banking products such as mortgage, Lombard, and consumer finance loans to about 580,000 customers and 294,000 current accounts, of which 232,000 had a debit/credit card at Dec. 31, 2020. We
note that 84% of new account openings come from AXA France’s agents networks. Over the past two years, the bank has expanded its distribution channels through its mobile application, with about 186,000 app users over the six months ended Sept 30, 2021. The digital channel enhances traffic for AXA group distribution networks. As an example, among the 12,000 new current accounts opened via the mobile app, 50% were from clients of AXA France versus 30% in 2018. The bank has seen twice the growth in the online segment since 2018. As such, we believe that the bank’s digital channels will further support the group’s strategy.

**Consumer finance activities (especially revolving credit) have shrunk over the past few years while mortgage and Lombard loans have expanded materially.** The consumer finance loans decrease was mainly due to consumer protection legislation in France and the French equivalent of the EU consumer credit directive. They further decreased in 2020 and 2021, mainly due to the pandemic. We expect outstanding consumer loans to total below €600 million at year-end 2021. We believe the figure will then remain stable in the coming two years. Lombard and mortgage loans outstanding remained at similar levels to 2019 (see charts 1 and 2). This is mainly due to lower production in 2020, affected by the COVID-19 pandemic. Home loans represent 61% of the bank’s lending activity and we expect loan production will remain lower than 2019 over the next two years given the refocus on existing AXA France clients. We note that about 70% of new home loans are from AXA France’s clients compared to 30% before the refocusing strategy. We expect the annual production of Lombard loans, representing about one-third of the bank’s loan portfolio, to stabilize in the coming years at about €1 billion. Overall, we expect the bank’s loan portfolio and balance sheet to stabilize at about €12 billion and €15 billion respectively in the coming two years amid its strategic refocus on commercial activity with AXA’s insurance customers.

**Chart 1**

**AXA Banque S.A.—Lombard Loans Growth**
Production and amount outstanding

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Given prolonged low interest rates, mortgages and current accounts serve mostly to attract customers and stimulate further insurance product sales for the group's insurance arm. This demonstrates the cross synergies between the bank and insurance entities, as does AXA Banque's profitable offering of Lombard loans backed by AXA's life insurance operations.

*We believe that AXA Banque's activities are low-risk in nature, because its primary activity is to provide home loans and Lombard loans that are collateralized by AXA's life insurance clients.* As a whole, 90% of AXA Banque's loan book is either collateralized or guaranteed, supporting a generally low cost of risk. However, AXA Banque's cost of risk increased in 2020 to 21 basis points (bps) after almost doubling in 2019 (17 bps versus 9 bps in 2018). Although the increase in 2019 was mainly due to one-off items amid changes in the risk model and the provisioning of two old Lombard loans, the increase in 2020 related to COVID-19. We note that most cost of risk relates to forward looking views rather than actual defaults, similar to what we have observed for peers. We expect cost of risk will decrease over our forecast horizon and be contained below 15 bps. Nonperforming assets (NPAs) doubled in 2020 but remained relatively low at 3.3% of total customer loans versus 1.6% in 2019. We expect this ratio to remain below 4%, supported by NPA disposals. AXA Banque's acceleration of its refocus on AXA France's customer base, the stronger customer selection, and the relative decrease in the consumer finance portfolio, should have a positive effect on overall asset quality in the short to medium term.
Although we monitor AXA Banque's statutory reported earnings, we believe a stand-alone view of the bank's bottom line does not truly reflect its overall contribution to the group. This is because of the cross synergies between the bank and the group. The group's strategy for banking activities is primarily to expand by leveraging AXA France's insurance clients to the point where the bank becomes costless for the group. AXA Banque's contribution to maintaining AXA group client loyalty, for instance, is something important for the group as a whole. In 2020, AXA Banque recorded net losses of €39 million, higher than €6 million in 2019 and €18 million in 2018. The bank's earnings have been affected by the reassessment at fair value of derivative instruments hedging the bank's balance sheet and increased provisions and expenses in 2020 due to the pandemic.

Current accounts growth and related costs are also weighing on profitability. Moreover, due to the bank's small size, operating expenses are very high—at 111% of operating revenue at year-end 2020. As part of its strategy, the bank is partnering with ABS to outsource some of its business processing, mostly back-office activities and IT processes. Despite the pandemic, the migration was largely executed in 2021 and early 2022. The partnership aims to allow customers to benefit from additional innovative services and more generally to improve the bank's financial situation, service quality, and overall regulatory compliance. We understand that the migration has led to a temporary but material spike in costs. However, the partnership will enable AXA Banque to reduce expenses in the long run.

Although we expect the bank will book net losses at year-end 2021 as well as in 2022 due to the investment phase, we understand it will be able to significantly improve its cost-to-income ratio in the medium term, targeting 70%-80%. Profitability should also improve in the medium term when the full benefits are realized. This will enable AXA Banque to finance its growth without strong support from the group, one of its medium-term objectives. We expect the bank to resume its loan book growth and return to profit no later than 2023-2024.

**AXA Banque's expected net losses could pressure its regulatory capital ratios over the outlook horizon.** However, we expect the bank will maintain a comfortable buffer above its total minimum regulatory capital adequacy ratio, which was 13.1% at year-end 2020 (the same as year-end 2019). The group has demonstrated its commitment to AXA Banque repeatedly by fully supporting its regular issuances, allowing the bank to keep a buffer above minimum requirements. We believe this will continue if needed until the bank is self-sufficient. We also consider capital of high quality, with a common equity Tier 1 capital ratio of 10.8% at year-end 2020. The bank expects to finance its growth with covered bonds, a cheap source of funding that better matches the longer maturities of its residential loans, issued from its new structure AXA Home Loan SFH, as well as intragroup financing, commercial paper, and medium-term notes. AXA Banque issued €0.25 billion of covered bonds in 2021 and intends to issue €500 million–€1 billion annually. Overall, its cost of funding continues to decrease more than the interest rates on its products, allowing it to partially reinforce its margins. AXA Banque positions its balance sheet to meet the European Central Bank requirements for the net stable funding ratio (NSFR) and liquidity coverage ratio (LCR) through its deposit base, which represented about 32% of its total funding base at year-end 2020, with full support from the group. The bank conservatively manages the LCR, which was stable at 198% in 2020 from 189% in 2018, compared with a minimum requirement of 100%. We expect the bank to maintain a very comfortable LCR in the coming two-to-three years.

The bank calculates a buffer based on two stress scenarios, one involving systemic stress and the other, counterparty stress. The NSFR is above the minimum requirement of 100% (115% at year-end 2020), and we expect it will remain comfortably above the minimum in the next two to three years. AXA Banque manages interest rate risks in the banking book according to Basel III standards, with alerts set up for when the net present value of its balance sheet varies by an amount equivalent to 15% of Tier 1 capital and 20% of Tier 1 plus Tier 2 capital. The bank's only negative exposure is to a drop in interest rates (short- and long-term), which is unlikely to happen again during our outlook horizon given current extremely low rates.
Environmental, Social, And Governance (ESG)

At this stage, we do not see ESG credit factors as influencing AXA Banque's credit quality more positively or negatively than peers. AXA Banque relies on AXA group policies for ESG integration. Social and environmental credit factors are in line with those of peers in the banking industry, while the bank's governance standards are comparable with the practice in its home country. Still, over time, ESG factors will have to be monitored due to the ownership structure (linked to its parent AXA France). We currently view AXA's exposure to environmental and social risk factors as consistent with the global insurance industry and we believe governance practices are in line with what we see across France and our own expectations.

Table 1

<table>
<thead>
<tr>
<th>AXA Banque--Key Figures</th>
<th>--Financial year ended Dec. 31--</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adjusted assets</td>
<td>16,643.8</td>
</tr>
<tr>
<td>Customer loans (gross)</td>
<td>11,593.0</td>
</tr>
<tr>
<td>Adjusted common equity</td>
<td>445.0</td>
</tr>
<tr>
<td>Operating revenues</td>
<td>158.0</td>
</tr>
<tr>
<td>Noninterest expenses</td>
<td>176.0</td>
</tr>
<tr>
<td>Core earnings</td>
<td>(38.1)</td>
</tr>
<tr>
<td>Return on average common equity (%)</td>
<td>(8.0)</td>
</tr>
<tr>
<td>Tier 1 capital ratio (%)</td>
<td>10.8</td>
</tr>
<tr>
<td>Total managed assets/adjusted common equity (%)</td>
<td>37.4</td>
</tr>
<tr>
<td>Net interest income/average earning assets (%)*</td>
<td>1.2</td>
</tr>
<tr>
<td>Net interest income/operating revenues (%)</td>
<td>103.1</td>
</tr>
<tr>
<td>Fee income/operating revenues (%)</td>
<td>10.9</td>
</tr>
<tr>
<td>Noninterest expenses/operating revenues</td>
<td>111.6</td>
</tr>
<tr>
<td>Preprovision operating income/average assets (%)</td>
<td>(0.1)</td>
</tr>
<tr>
<td>Core earnings/average managed assets (%)</td>
<td>0.2</td>
</tr>
<tr>
<td>Growth in customer loans (%)</td>
<td>(0.4)</td>
</tr>
<tr>
<td>Nonperforming loans (gross)/customer loans (%)</td>
<td>3.3</td>
</tr>
<tr>
<td>New loan loss provisions/average customer loans (%)</td>
<td>0.2</td>
</tr>
<tr>
<td>Loan loss reserves/gross nonperforming assets</td>
<td>24.6</td>
</tr>
<tr>
<td>Core deposits/funding base (%)</td>
<td>32.2</td>
</tr>
<tr>
<td>Customer loans (net)/customer deposits (%)</td>
<td>230.0</td>
</tr>
</tbody>
</table>

*Net interest margin. N/A--Not applicable. N.M.--Not meaningful.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
• General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
• General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
• General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
• Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Related Research

• Various Rating Actions On French Banks As Easing Macroeconomic Downside Risk Is Dampered By Structural Profit Pressure, June 24, 2021
• AXA Group, April 27, 2021

### Ratings Detail (As Of March 15, 2022)*

**AXA Banque**
- **Issuer Credit Rating**: A+/Stable/A-1+

**Issuer Credit Ratings History**
- **03-Sep-2018**: A+/Stable/A-1+

**Sovereign Rating**
- **France**: AA/Stable/A-1+

**Related Entities**

**AXA**
- **Issuer Credit Rating**: A/Watch Pos/A-1
- **Commercial Paper**: A-1/Watch Pos
- **Junior Subordinated**: BBB/Watch Pos
- **Senior Unsecured**: A/Watch Pos
- **Subordinated**: BBB+/Watch Pos

**AXA France IARD**
- **Financial Strength Rating**
  - **Local Currency**: AA-/Stable/--
- **Issuer Credit Rating**
  - **Local Currency**: AA-/Stable/--

**AXA France Vie**
- **Financial Strength Rating**
  - **Local Currency**: AA-/Stable/--
- **Issuer Credit Rating**
  - **Local Currency**: AA-/Stable/--

**AXA Home Loan SFH**
- **Senior Secured**: AAA/Stable

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings’ credit ratings on the global scale are comparable across countries. S&P Global Ratings’ credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.
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