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INVESTMENT NOTE **06 MAY 2015**

HERMES: FRENCH BANKS STRUGGLING TO GENERATE CAPITAL

Filippo Alloatti, Senior Credit Analyst, Hermes Credit, reviews Société Générale Q1 results announced today.

Société Générale (SocGen) first quarter results released this morning share a few similarities with BNP Paribas' numbers last week.

While there was a decent earnings beat, there was also a lack of quarter-on-quarter capital generation. Both banks reported profits ahead of consensus forecasts – helped by higher trading revenues and more benign asset quality trajectories.

SocGen's net profit of €868mn was 9% ahead of consensus, while its 4% revenue beat at €6.35bn was particularly strong. Its Corporate & Investment Banking division revenue of €2.3bn, propelled by strong equity trading, stole the show from a rather lacklustre retail performance, down 6%.

SocGen Russia reported a €91m loss on higher provisioning – up €10m – as well as a shrinking loan book, down 9.7% quarter-on-quarter. This was progress on the €530m loss booked in the corresponding quarter last year.

On capital, common equity tier 1 (CET1) was flat at 10.1%. The (fully-loaded) leverage ratio was 3.7% – down 10bp on higher leverage exposure of €1.25bn, against €1.17bn at year-end 2014. SocGen confirmed its 2016 leverage ratio target of 4%. This figure reinforces the view BNP Paribas' 3.4% leverage ratio is simply too low and the group should consider starting its additional tier 1 program.

The capital ratios at both banks look adequate, but far from stellar. Indeed, one common factor we have seen during this reporting season is the lack of capital generation. That was mostly due to FX swings and risk weighted asset parameter changes. An exception to this trend was UBS, which recorded a strong 30bp quarter-on-quarter CET1 increase to 13.7%.

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Notes to Editors:

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