Template for notifying intended measures to be taken under Article 458 of the Capital Requirements Regulation (CRR)

Please send this template to

- notifications@esrb.europa.eu when notifying the ESRB;
- macropru.notifications@ecb.europa.eu when notifying the ECB;
- notifications@eba.europa.eu when notifying the EBA.

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1. Notifying national authority and scope of the notification	
1.1 Name of the notifying authority	Haut Conseil de stabilité financière (HCSF, French Macroprudential Authority)
1.2 Categorisation of measures	The HCSF intends to make use of Article 458(2) (d) (ii)
1.3 Request to extend the period of application of existing measures for one additional year **(Article 458(9) of the CRR)**	
1.4 Notification of measures to which Article 458(10) of the CRR applies ('notification only procedure')	The proposed measure is not subject to the notification procedure as specified in Art. 458 (10) of the CRR. The tightening of the large exposure limits would result in a level below 15 %; therefore, Article 458(10) of the CRR does not apply
2. Description of the measure	
2.1 Draft national measures **(Article 458(2)(d) of the CRR)**	The proposed measure consists of a tightening of large exposure limits applicable to highly indebted large non-financial corporations that are resident in France. French Systemically Important Institutions shall not incur an exposure that exceeds 5 % of their eligible capital for NFCs or group of connected NFCs assessed to be highly indebted.
2.2 Scope of the measure **(Article 458(2)(d) of the CRR)**	The large exposure limit is implemented according to the rules stated in CRR article 395 to the exposures fulfilling all the following criteria : - Exposures defined in CRR – articles 389/390 - that are larger than or equal to EUR 300 million before taking into account the effect of

	credit risk mitigation techniques and exemptions in line with article 9 of the Commission Implementing Regulation (EU) No 680/2014[1]. - Exposures of globally or domestically important institutions (6 institutions[2]) at the highest level of consolidation of the banking prudential perimeter. - Exposures to non-financial corporations[3]: • For NFCs resident in France: the sum of the net exposures towards the whole group of connected clients. • For NFCs resident in France belonging to a foreign group, the large exposure limit applies to the sum of the exposure to NFCs resident in France at the highest level of consolidation, along with the exposures to economically dependent entities, as assessed following Part 6 of the EBA's GL-2017-15 Guidelines.[4] NFCs that are not resident in France and are not a subsidiary, a parent company or an economically dependent entity of a French resident NFC are not in the scope of the measure because the diagnosis justifying this macroprudential measure rests on an analysis of resident NFCs' indebtedness (cf. section 4). - The NFC's ultimate parent company is fulfilling the two following criteria computed on a consolidated basis[5] • The leverage ratio (defined as total financial debt less outstanding liquid assets on total equity) is higher than 100%. • The interest coverage ratio (defined as Earnings before interest and taxes[6]/ interest expenses) is lower than 3 (i.e. interest expenses are above 1/3 of the EBIT). **Operationalization of the measure** Banks will be in charge of computing the financial indicators by requesting the appropriate information from their counterparties. Guidelines and specifications for computing the two indicators above will be made available to the institutions concerned and to competent supervisory authorities from other Member States. No additional supervisory reporting data will be requested to the institutions

[1] Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to CRR.
[2] https://acpr.banque-france.fr/sites/default/files/20171201_liste_aeis_0.pdf
[3] The measure is fully aligned with Article 394 CRR with regard to the identification of groups of connected clients.
[4] Guidelines on connected clients under Article 4(1)(39) of Regulation (EU) No 575/2013: https://www.eba.europa.eu/documents/10180/2025808/Final+Guidelines+on+connected+clients+%28EBA-GL-2017-15%29.pdf/a77be1e9-7564-47d2-a9d1-b7da98220352
[5] Both indicators are considered as important indicators of corporate financial soundness. See in particular the work of IMF staff on the assessment of corporate vulnerability.
[6] Given that the focus of the measure is on firms' medium-term vulnerability, the concept of EBIT—rather than EBITDA— is preferred because it allows assessing whether a firm is economically viable. Rating agencies and analysts use in general EBITDA because they have a different perspective and focus more on firms' short-term cash position.

	because the measure does not deviate from the current CRR framework with regard to the computation of Large Exposures amounts.
2.3 Calibration of the measure	The calibration of the measure has two objectives: - Resilience: by limiting concentration risk and the risk of shocks propagation in case of corporate defaults, this measure mitigates the impact such defaults could entail on the most systemic institutions. These institutions being the most likely to spill over to the rest of the financial system, such a measure promotes financial stability. - Prevention: it sends a strong warning signal and intensifies the vigilance of financial institutions and investors regarding the increased leverage of large French NFC. Preventing the build-up of unsustainable risk developments in the NFC sector is less costly than addressing vulnerabilities when they become too high. The measure is calibrated as follows: • The calibration of the thresholds for the two indicators of corporate vulnerability is based on an assessment of their predictive power with regard to deteriorating NFC credit quality. The simulations indicate that the combination of the two thresholds might be sufficient to avoid excessive risks for the banks themselves. • Exposure after credit risk mitigation and exemptions (as in CRR article 395) has to be lower than 5% of eligible capital. The choice of the exposure threshold is the result of a trade-off between the resilience objective of the measure (i.e. sufficiently low to protect efficiently the financial institutions) and the preventive objective of the measure (i.e. not too restrictive, to avoid an excessive reduction of bank exposures to large NFCs, triggering undesirable deleveraging). The measure will be regularly monitored and reviewed on the basis of its impact on banks' resilience and on the observed build-up of risks in the NFC segment. **Impact analysis of the measure** The limit of 5% of eligible capital has been calibrated in order to act as a backstop (i.e. a forward-looking approach with the aim to prevent the build-up of excessive vulnerabilities) while not being too restrictive at the current juncture (i.e. at no significant costs for the real economy).
2.4 Suitability, effectiveness and proportionality of the measure **(Article 458(2)(e) of the CRR)**	**Suitability** Concerning the scope, the measure is focused on large NFC exposures, since the macroprudential risk confronting the French financial system according to the Banque de France, the ECB and the HCSF relates to an upward trend in the debt of large and highly indebted NFCs (see 4.1 below). By deducting liquid assets from total debt, the indicator takes into account the accumulation of liquid assets by corporates, hence acknowledging the reduced threat posed by NFCs holding larger liquidity buffers. **Effectiveness**

	The effectiveness of the measure is assessed according to its capacity to ensure the resilience of the banking sector and to signal to all investors the risk inherent to the accumulation of debt by large and highly indebted NFCs. The measure is assessed to be effective: - Large exposures incorporate all the bank's exposure to NFCs which takes into account not only bank loans but all their balance sheet / off-balance sheet exposures. This is particularly relevant to capture the specificities of large NFCs, who tend to rely on various sources of funding, including market based finance. - The definitions of the two ratios used to assess NFC indebtedness (leverage ratio and interest coverage ratio) take into account the whole debt, including credit by foreign banks and market debt financing. They are widely used as indicators of financial soundness. - The conditionality of the measure is based on standard financial indicators, easily computable by the banks and based on available public information. However, by default, if the financial indicators for a particular NFC were not available, the firm would be assumed to have reached the threshold level of both financial indicators. - The measure covers the largest 6 banks whose market share among French banks in the NFC segment in France is 95% (see 5.2 below for an assessment of the potential leakages to non-systemic banks). **Proportionality** The measure is seen as proportionate as it strengthens the resilience of the banking sector in case of losses in the NFC sector while not having an impact on limiting lending to sound NFCs, which could, in turn, have an adverse effect on the recovery of the real economy. For this purpose, the levels chosen for the financial indicator thresholds, which define the conditionality of the measure, are deemed appropriate as these levels enable to capture large NFCs which are the most vulnerable (less than 10% of the sample of large corporates). According to computations regarding the impact of the measure, the number of NFC counterparties impacted by the measure would be low, in accordance with the preventive aim of the measure. In addition, the proposed measure (with the threshold of EUR 300 million) would have no impact on SMEs that are not present in large exposures. Although the measure applies only to systematically important banks in France and not to the other French banks (small SIs and LSIs), as the measure is to be made public, it also provides guidance to those smaller banks - not directly concerned by the measure - in their assessment of NFC overall indebtedness when financing French NFCs.
2.5 Other relevant information	In case the tighter limit defined in this measure has been exceeded, the procedure as described in CRR article 396 applies i.e. the institution shall report the amount of the excess and the name of the client concerned and,

	where applicable, the name of the group of connected clients concerned, without delay to the competent authorities. In case of a breach of the 5% limit, compliance with the limit on large exposures can be met through an increase in the level of capital held by the bank and/or through a reduction in the exposures to individual counterparties or groups of connected counterparties. The measure will be monitored by the designated authority, i.e. the HCSF, with the support of Banque de France and ACPR. The HCSF will regularly monitor the evolution of risks and the overall implementation of the measure as well as the potential impacts on the institutions which are not in the scope of this measure.
3. Timing of the measure	
3.1 Timing of the Decision	May 2018
3.2 Timing of the Publication	May 2018
3.3 Disclosure	The HCSF announced on 15 December 2017[7] that it was considering a macroprudential measure consisting of a tightening of the large exposures limits for large and highly indebted non-financial corporates' exposures. The measure will be officially communicated to the market by a press release of the HCSF and with the publication of the legal text.
3.4 Timing of Application (Article 458(4) of the CRR)	1 July 2018
3.5 Phasing in	No phasing-in is planned. The measure would be fully applied on 1 July 2018.
3.6 Term of the measure **(Article 458(4) of the CRR)**	The measure is intended to be implemented for two years and possibly renewed afterwards
3.7 Review **(Article 458(9) of the CRR)**	The calibration and appropriateness of the measure will be reviewed regularly, with possible revisions of the overall measure when circumstances warrant it. In line with Art 458, the HCSF – upon the request of the Governor of the Banque de France – could reconsider the calibration and could lower this

[7] https://www.economie.gouv.fr/files/files/directions_services/hcsf/HCSF_171215_-_Communique_de_presse.pdf

	threshold, for instance down to 3%, if the build-up of risks in large and highly indebted firms were to continue.
4. Reason for the activation of the stricter national measure	
4.1 Description of the macro-prudential or systemic risk in the financial system **(Article 458(2)(a) of the CRR)**	The HCSF diagnosis confirms the acceleration of the financial cycle in France during the last quarters. Although this acceleration goes hand in hand with the improvement of economic conditions, it can overshoot its economic fundamentals and may cause a build-up of risks whose materialization could weaken the financial system. Macroprudential authorities pay particular attention to the continuous increase in the indebtedness of non-financial corporations (NFC). The HCSF identifies some risk areas prompting for action of the macroprudential authority. Credit to NFCs has increased as a share of GDP over the past few years, in contrast to other large economies of the euro area. The growth in the outstanding debt of Large Corporates (LC) contributed significantly to the overall trend: their debt increased by 225 bn. €, compared to a total increase in NFC debt of 410 bn. €. This growth is encouraged by low interest rates and finances an increase in cash holding as well as external growth. The situation of NFCs is heterogeneous and some areas seem more prone to risk accumulation, notably LBO operations. The heterogeneity is also observed among LCs: the average indebtedness net of cash holdings has shown only a modest increase, but some LCs, whose indebtedness is already high, have experienced a continuous increase. It is necessary to pay close attention to the sustainability of the trajectory of NFC debt, especially in the aforementioned areas, and the sensitivity of their financial soundness to a hike in interest rate. The current situation prompts the use of a targeted preventive measure, used as a backstop to limit the counterparty risk that banks may face vis-a-vis highly indebted large NFCs. Such a measure is consistent with the objective of the HCSF, which aims at signaling and preventing an excessive credit expansion that could lead to the build-up of systemic risk, while being proportionate by targeting specific sectors whose debt dynamic calls for particular attention. The HCSF published a report presenting its diagnosis on the indebtedness of non-financial corporations. The main messages are reproduced and translated below. The macro-prudential risk related to NFC indebtedness in France has been noted by other institutions and analysts. For instance, in its latest Article IV Consultation for France, the IMF stresses the need to remain vigilant with respect to the rise in corporate indebtedness; in its 2017 in-depth report for France, the Macroeconomic Imbalance Procedure of the European Commission notices that non-financial corporations debt, combined with still low profitability, is a potential source of concern for France, should this trend persist. Finally the ECB also noticed in the June issue of its Economic Bulletin that the dynamics of the private sector indebtedness for France contrasts with the euro-area dynamics. The HCSF conducted several meetings and workshops with relevant

	stakeholders (credit institutions, insurance companies, large NFCs) in order to gather complementary information to discuss and confirm the diagnosis. **Large Corporates represent a significant proportion of NFCs' indebtedness and contributed to its increase** LC account for a hefty part of total corporate debt with their debt amounting, in Q2 2017, to € 685 billion (of which € 140 billion of bank loans and € 545 billion of debt securities) of the total € 1,615 billion (of which € 1,010 billion of bank loans and € 605 billion of debt securities). Moreover, LCs have been an important driver of debt growth in the past years. Between 2011 and 2016, indebtedness has increased at an average annual rate of + 4.9% for all NFCs, but + 7.5% for Large Corporates. **Increase of large corporates' market debt** Debt securities issuance has risen sharply in recent years, both for NFC in general and Large Corporates in particular, reflecting a shift in the corporate finance mix towards market debt. From 2010 to 2015, LCs mainly experienced a sharp increase in their debt securities (+ 49%) and a weaker increase in their bank indebtedness (+ 4%). In 2016 and the first half of 2017, Large Corporates' debt dynamics have been based on a more uniform growth of loans and debt securities (around + 10% each). **Lower interest rates have mitigated the impact of higher indebtedness on interest expenses** The increase in NFCs' debt is to be viewed in the context of the sharp drop in interest rates since 2011. The bank credit rate for LCs reached 1% in 2016, and only slightly increased since (1.3% in Q3 2017). The cost of financing by bonds issuance has followed the same downward trend, falling below the bank credit rate in 2013, and has remained around 0.8% since mid-2016. Given the fall in interest rates, the financial burden of LCs compared to the gross operating surplus decreased from 19% in 2011 to 14% in 2015, but climbed to 16% in 2016. The low financial burden of French NFCs could be challenged by a rise in borrowing rates: (i) a large part of this debt is at variable rate and would therefore be directly affected by a rise in rates; (ii) unlike households, NFCs often have to refinance their debt, making them more sensitive to a rate hike, even on their fixed rate debt. However, companies have benefited from a favorable period to extend the maturity of their debt, thus partially offsetting the effect of higher rates. While a gradual rise in rates during the recovery of activity would be offset by a rising EBIT, a faster rate rise could however be challenging, as the accumulated liquidity buffers may be insufficient. **An increasing debt linked to an acceleration in investment and a change in cash management practices.** <u>Investment and acquisitions:</u> The investment rate of NFCs (ratio of investment over value added) has increased sharply since 2012 and stands at 22% in 2016, a high point for 30 years. However, the self-financing rate (ratio of savings over investment flows and changes in inventories) has decreased since the end of the 1990's, when it reached a peak at 100% : the financing of investment and

	stock changes are now only covered by corporate savings of up to 80%, which explains the recourse to debt. An important share of the LCs' debt is used to finance acquisitions, especially abroad. In 2016, the debt of LCs increased by € 87 billion (€ 77 billion in 2015) and the need for financing linked to French direct investment abroad increased by € 18 billion to € 52 billion (€ 34 billion in 2015). There is a strong dynamism of structured issues and LBO transactions, although still lower than in 2008, driven by abundant liquidity and high profitability. The following is observed: (i) a gradual loosening of covenants; (ii) importance of debt rollover, under sometimes more aggressive conditions than before the rollover and (iii) significant competition, with in particular an increase in the share of financing coming from non-bank players. The default rate of LBO financed by French banks remains under the average of the SSM (around 8% compared to 10.2%), but is sensitive to a turnaround, especially as a large portion of the loans maturing in 2018-2019. Cash management: Increase in corporate debt has to be put in the context of a large increase in cash holding. Whereas the gross debt of NFCs as a share of GDP reached 71.7 pp in 2017Q2, up from 57.0 in 2008, the net debt[8] experienced a more muted growth, from 45.9 pp in 2008 to 48.6 pp in 2017Q2. This is particularly true for LCs. For instance, the important increase in debt of the largest 80 listed NFCs (9.2% in 2016) is partly compensated by their higher cash holding (+3.5% in 2016). Cash holding of LCs amounted to 31% of their equity in 2016, compared to 19% in 2011. However, LCs whose net leverage was already high (last quartile) have a disproportionate contribution to the increase of LCs' net debt. **A rise in goodwills** The increase in LC's debt partially corresponds to external growth operations, which can be related to the rise of the goodwill in the assets of the acquiring company. A downward revision of those goodwills could thus directly weaken equity positions, and increase credit risk on their debt. The average goodwill-to-equity ratio stands in 2016 (55%) below the level reached in 2012 (60% in 2012). However, an important share of corporates with a high goodwill-to-equity ratio belongs to the most indebted corporates, consistent with the fact that debt is more specifically associated with external growth operations, while investments are rather self-financed Given the sources of the systemic risk described above, the HCSF considers appropriate to take a macroprudential action against a targeted risk that has potential systemic consequences were risks to materialize. The measure attempts to tackle the intertwined risks between systemic banks and systemic corporates (section 4.2)

[8] Net of cash holdings.

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<tr><td>4.2 Analysis of the serious negative consequences or threat to financial stability

(Article 458(2)(b) of the CRR)</td><td>The indebtedness of NFCs relative to GDP displays a continuous increase since 2005. Large companies make a very large contribution to this development. Among them, the most indebted companies contribute significantly to the increase in net debt.

If this trend were to persist over the next quarters, the vulnerability of the most indebted NFCs to a risk of interest rate changes and abrupt repricing of risk premium would increase inducing sustainability issues.

Unsustainable debt levels of large companies could generate substantial negative impact on credit institutions' solvency position, if the credit institutions' exposures towards them were to reach high levels. This could in turn have negative consequences on the real economy, through second round effects induced by banks' reactions (restriction of credit), which may have systemic consequences.

Moreover, in view of the importance of cross-border banking groups in France and the degree of openness of the French economy, safeguarding financial stability in France will also have positive effects on financial stability in Europe.</td></tr>
<tr><td>4.3 Indicators prompting use of the measure</td><td>The main indicators prompting the use of the measure are:

• Credit Growth (total and for LCs): loans, and market debt instruments.
• Indebtedness (total and for LCs): gross and net debt, gross and net leverage.
• Use of funds: holdings of liquid assets, investments, goodwills (with an emphasis on the most indebted large groups).
• ICR: ratio of interest coverage by EBIT (emphasis on the proportion of LC with low ICR).</td></tr>
<tr><td>4.4 Justification why the stricter national measure is necessary

(Article 458(2)(c) of the CRR)</td><td>Given the risks identified in the NFC segment, the HCSF considers that the application of Art. 458 is justified.

The main objectives of the measure are:
- <u>To limit concentration risk with regard to highly indebted large French NFCs</u> and as a result, preserve the overall resilience of the large French banks. The tightening of large exposures puts an upper bound on the losses from individual defaults in the NFC sector and therefore mitigates the propagation of shocks between the NFC sector and the banking sector. In addition, this measure publicly signals to large banks the importance of maintaining sound lending standards at the origination of NFC loans.
- <u>To reduce the risk of further increases in the debt of the most indebted large French NFCs</u>. As large exposures capture all the exposures towards a specific counterparty, these new limits will cover NFC bank loans and also market debt financing of the NFC sector.

Why other measures or legal basis are not adequate?

Since the risks mentioned above are for a significant part due to an increase in market corporate debt of NFCs, it would be natural to adopt a measure directly related to the corporate debt markets. However, such a</td></tr>
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	measure is not feasible and its effectiveness would not be ensured since: - A significant share of large French NFCs issue bonds on foreign markets. - The French Financial Markets Authority (AMF) does not have the power to limit the issuances of highly indebted NFCs. Similarly, the HCSF does not have restricting powers over bond issuances by NFCs. - The AMF could alternatively reinforce the information requirements on issuing NFCs, in order to underline the risk associated with the targeted segment of firms. Nevertheless, the effectiveness of such a measure would probably be low since these firms may choose to shift their issuance to foreign markets, in particular in Europe, with the same market depth and same investors' base. Given the arguments above, this measure using Art 458 addresses indirectly this source of systemic risk coming from the NFC sector: - Market corporate debt is taken into account in large exposure amounts and will limit the exposures of banks to corporate debt. This is consistent with the objective of bank resilience. - With regard to the other sectors not covered by the measure, but which hold substantial amount of corporate debt (insurance sector, asset management), the signalling function of the Art 458 should raise awareness of the risks. **Explanation why measures under Articles 124 and 164 of the CRR and Articles 101, 103, 104, 105, 133 and 136 of the CRD cannot adequately address the macro-prudential or systemic risk identified, taking into account the relative effectiveness of those measures** **Article 124 and 164 of the CRR – Risk Weight / Loss Given Default (LGD) on exposures secured by mortgages on immovable property** The purpose of these provisions is to address risks identified in relation to the real estate sector. Since the HCSF aims at addressing risks arising from increasing indebtedness of large French corporates, those provisions are not relevant. **Article 101 to 105 of the CRD Articles – Ongoing review of the permission to use internal approaches / Application of supervisory measures to institutions with similar risk profiles and Supervisory powers / Specific liquidity requirements** The SSM regulation implies that the competent authority under articles 101 to 105 is the SSM for all the institutions covered by the proposed measure. This distribution of responsibilities means that those provisions are not designed within the current institutional set-up to be used as macro-prudential tools. In our context, one of the objectives of the macroprudential measure is to contain the global debt dynamics of the NFC sector, by targeting specifically the more dynamic part of this sector in order to avoid penalizing the less dynamic ones. To this end, the approach we propose relies on bank's balance sheet to limit private sector indebtedness, while the SSM would not have such a preventive objective. Beyond this governance issue, there are also justifications not to retain

	article 101 to article 105 of the CRD based on the substance: • Articles 101 and 102: the latest review of internal credit risk model did not raise concern about potential breach with CRR. Existing models are indeed based on valid historical data. Articles 101 and 102 are also microprudential in nature, which prevents any consideration of the macroprudential aspect of the measure we propose. • Articles 103 and 104: related measures should be based following the assessment under article 97 of the CRD. Although Pillar II measures could be envisaged for similar risks, the SREP process is mainly a micro-prudential assessment and cannot capture macro-prudential concerns. On a bank-by-bank basis, the risk stemming from the increase in NFC indebtedness has not been identified, which is consistent with the preventive nature of the measure based on art 458 CRR. However, such continuous increase has been identified by the HCSF as a macroprudential or systemic risk that poses a threat to financial stability at national level. In addition, the Pillar II requirements are currently defined as capital ratio. Increasing this requirement would lead – in a similar fashion as the CCyB and the systemic risk buffers – to increase capital requirements against all exposures while the risk identified is limited to a specific segment. Finally, the lack of disclosure underlying the pillar II requirements would not allow raising public awareness through a signalling effect about the issue related to the growing debt of French corporates. • Article 105 of the CRD: this provision aims at addressing liquidity risk in relation for instance to a specific feature of the business model of the institution. It would not therefore address concerns about the exposures of bank to increasingly indebted French corporates which by nature is related to credit risk. **Articles 133 and 136 of the CRD – Requirement to maintain a systemic risk buffer and Setting countercyclical buffer rates (CCyB)** First, as specified in the recital 85 of the capital requirement directive, the systemic risk buffer shall address long-term non-cyclical risks, whereas the identified risks are of a cyclical nature. Second, the systemic risk buffer would apply equally to all exposures across all segments while the risks identified stems from the specific segment of some large French corporates. The main identified risk is specific to the segment of large corporates. The CCyB is not suited to address this targeted risk, but may be complementary to the current measure if further developments in the financial cycle confirm the global increase in credit. The HCSF announced on 15 December 2017 that it would consider further measures, including an increase of the CCyB rate, should cyclical risks remain at the current levels in the coming months.

<table>
<tr><th colspan="2">5. Cross-border and cross-sector impact of the measure</th></tr>
<tr><td>5.1 Assessment of cross-border effects and the likely impact on the internal market

(Article 458(2)(f) of the CRR and Recommendation ESRB/2015/2)</td><td>Assessment of cross-border effects

The cross-border effects of the measure have been assessed in accordance with ESRB Recommendation (ESRB/2015/2) on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures.

• As the measure applies only to the non-financial corporations whose residence is in France, there is no indication that it may have any direct impact on NFCs outside France, except for foreign subsidiaries or economically dependent entities of NFCs resident in France. This latter point has been added to avoid excessive leakages and regulatory arbitrage from the French NFCs: otherwise, the French parent company could use its foreign subsidiary to contract debt and channel it to France via intragroup lending.
• The tightening of large exposure requirements could reduce the capacity of French systemically important banks to lend to indebted NFCs; this could lead to a shift of the credit demand of highly indebted NFCs from large French banks to foreign banks. Based on statistical information and other available evidence, the role of some foreign EU banks in the loan market for French NFCs is not insignificant. However, foreign banks would also have strong incentives to limit their exposures to highly indebted French NFCs – especially given the warning issued by the HCSF.

Likely impact on the internal market
Overall, this measure would strengthen the resilience of the French banking sector against shocks from the large French NFC sector and reduce the risk of contagion from France to other EU Member States (see 4.2).</td></tr>
<tr><td>5.2 Assessment of leakages and regulatory arbitrage within the notifying Member State</td><td>As the measure has a specific scope, some adverse effects may theoretically appear within France :

• NFCs may try to increase market-based financing; as of September 2017, 40% of the NFCs financing was provided by the market. However, the measure indirectly addresses market-based debt since the latter is included both in large exposures and in the criteria assessing NFCs' indebtedness; in addition, we expect that the signalling effect of the measure will enhance market discipline.
• NFCs may seek an increase of their financing by non-systemic banks. But this adverse effect is rather contained: the share of systemic banks on the total financing of NFCs is around 95%. Smaller French banks could only take over these risks to a limited extent, as they are also bound by the generic CRR large exposure</td></tr>
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	regulation. This would also require a change in business models, as smaller banks usually cater to the need of SMEs. • Regulatory arbitrage could also appear by actors increasing NFC lending through the shadow banking sector or insurance companies. So far, these sources of NFC financing are contained. Overall, incentives for such regulatory arbitrage appear for the moment quite limited but the HCSF and the ACPR will regularly monitor possible leakages or regulatory arbitrage going forward.
5.3 Reciprocation by other Member States **(Article 458(8) of the CRR and Recommendation ESRB/2015/2)**	. According to Article 458 (5), other Member States may recognise the measure and apply it to at the same level of consolidation for EU O-SII as their banking sector may be exposed to the risk addressed by this measure. The HCSF asks the ESRB to recommend that other Member States recognize the measure, as their banking sector may be exposed directly or indirectly (via branches) to the risk related to NFCs' indebtedness in France. In particular, the reciprocity is deemed appropriate from other EU jurisdictions whose systemic institutions are the most likely to fund French large corporates, in order to limit individual exposures of these institutions to large and highly indebted French NFCs. There are three reasons leading to this request for reciprocity : • Financial stability: the banking sector of other member states may be exposed directly or through their branches to the risk of NFCs' indebtedness in France. • Reducing leakages risks: as stated, the measure aims at limiting the risk exposure of banks towards large corporates but also to keep under control their debt dynamics. This second goal would be easier to achieve in a situation where foreign EU banks were subject to the same limit. • Ensuring a level playing field across the Internal Market: the aim of European Union through the Capital Market Union and the Banking Union is to ensure that one corporate should face the same financing conditions across jurisdictions. Limiting the measure to French systematically important banks would be contradictory to this objective. In order to limit implementation costs for reciprocating Member States, the HCSF will propose an institution-level materiality threshold to be applied when reciprocating the measure.
6. Miscellaneous	
6.1 Contact person(s) at notifying authority	- ACPR Risk Analysis Division : SATRISK-2777@acpr.banque-france.fr - Banque de France HCSF Secretariat : secretariat.hcsf@banque-france.fr - French Treasury HCSF secretariat hcsf@dgtresor.gouv.fr

6.2 Any other relevant information	