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Research Update:

French Social Security Agency ACOSS 'A-1+' Short-Term Rating Affirmed

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Overview

- We think Agence Centrale des Organismes de Sécurité Sociale (ACOSS) plays a critical role for the French government, enshrined in constitutional laws, in collecting and redistributing France's general scheme social security contributions.
- ACOSS' status as a state public agency implies strong state supervision and support, and therefore an integral link between ACOSS and the central government, in our opinion.
- In our view, there is an almost certain likelihood that the French government would provide timely and sufficient extraordinary support to ACOSS if needed.
- We are affirming our 'A-1+' short-term issuer credit rating on ACOSS.

Rating Action

On April 29, 2016, Standard & Poor's Ratings Services affirmed its 'A-1+' short-term issuer credit rating on France's central social security agency, Agence Centrale des Organismes de Sécurité Sociale (ACOSS).

At the same time, we affirmed our 'A-1+' issue ratings on ACOSS' €25 billion French commercial paper (CP) program and €20 billion Euro CP program.

Rationale

We equalize our rating on ACOSS with our short-term sovereign credit rating on France (unsolicited AA/Negative/A-1+). This is because, according to our criteria, there is an almost certain likelihood that the French government would provide timely and sufficient extraordinary support to ACOSS in the event of financial distress.

In accordance with our criteria for government-related entities (GREs), such as ACOSS, we base our rating approach on our view of ACOSS' critical role for and integral link with the French government. Furthermore, we consider that the French government's limited level of contingent liabilities does not constrain its capacity and willingness to support ACOSS in a timely manner if the agency is in financial distress. More generally, we don't consider the government's general propensity to support the GRE sector to be doubtful.

France's constitutional laws, set in 1945, safeguard the French population's right to receive social protection. We consequently consider ACOSS' role for the French government to be critical and that it will remain so, since it primarily consists of supervising and centralizing the collection of contributions to France's Social Security General Scheme and ensuring their timely redistribution. These social transfers include one-half of health, work accident, and illness benefits; one-third of old age pensions; and family benefits. Theses transfers concern the majority of French people, and their timely payment, especially of pensions, is crucial. General scheme expenditures will likely account for about 60% of France's total social security expenditures and 16% of GDP in 2016.

Furthermore, as part of the French social security system, ACOSS was set up in 1967 as a state public administrative agency ("Établissement Public à Caractère Administratif"; EPA). Owing to this status, we view the government as ultimately responsible for ACOSS' solvency. ACOSS' legal status, mission, and funding are precisely framed by law, which, in our opinion, entails an integral link between the agency and the French government. We don't expect any change in ACOSS' legal status.

The Ministry of Health and Social Affairs and the Ministry of Finance and Public Accounts provide strong and broad state supervision of ACOSS. ACOSS' director is appointed by decree and reports directly to the ministries. The director's main mandate is to strictly implement the central government's decisions and policies on the social security system. Since 1996, ACOSS has signed multiyear contracts with the government laying out its objectives. Under the current contract (which runs until 2017) ACOSS has launched several ambitious projects to improve its operational efficiency.

As part of the tight framework regulating ACOSS' activities, the French parliament sets ACOSS' external funding ceiling in its Social Security Funding Laws. For 2016, ACOSS' external funding ceiling is set at €40 billion through July, and at €30 billion from August to December, compared with €36.3 billion in 2015 and €34.5 billion in 2014. The 2016 ceiling takes into account the deficits accumulated by the Social Security General Scheme over previous years (€38.5 billion at the end of 2015 and €37.5 billion in 2014); the expected additional shortfall of €10.5 billion as of the end of 2015, highlighting the persistent gap between social contributions and drawings; and a pursuit of the gradual debt transfers to the sinking fund, Caisse d'Amortissement de la Dette Sociale (CADES; the social debt amortization fund), which redeems France's social debt. In 2016, €23.6 billion is scheduled to be transferred to CADES, which would result in a significant improvement in ACOSS' balance sheet position and explains the decrease of the external funding ceiling from August this year. These transfers testify to the ongoing financial support extended by the state through CADES.

The funding ceiling for 2016 appears adequate and in our view ACOSS is unlikely to exceed it. Slippage risks are mainly linked to a potential deviation of health care expenditures beyond the 1.75% targeted growth on the outflow side, and on the inflow side to an underperformance of the job market compared with official projections. Forecasting assumptions are, however, realistic, and the risk of large deviations appears subdued. Driven by a revaluation of various social security payments and by the introduction of a new compensation scheme (prime d'activité), payments are expected to outgrow inflows for the first time in six years. However, growth of receipts will be constrained by the rollout of the second tranche of payroll tax exemptions under the Responsibility and Solidarity Pact and by slower growth in public sector employment.

Liquidity

ACOSS manages more than €2 trillion per year in cash flows from social security contributions for the general scheme or on behalf of third parties, drawings on social benefits, and debt refinancing. We estimate that its daily average short-term funding needs will decrease to about €21 billion in 2016, compared with €26.3 billion in 2015.

In our view, ACOSS' liquidity-management challenges are increased by two main constraints: It is prohibited by law from taking on long-term debt, and there is no systematic and full transfer of previously accumulated deficits to CADES.

Nonetheless, cash management is sophisticated; it is based on prudent and precise planning, and clear and efficient policies and procedures. ACOSS has significantly increased the predictability of its cash inflows, which pose the biggest risk, by securing hundreds of agreements with counterparties that specify the exact day of payment. ACOSS has also increased the monitoring of its cash outflows through information technology systems that set the dates for drawings, putting an end to the historical liquidity risk related to drawing rights granted to social-benefit paying funds on ACOSS' operational account. As a consequence, ACOSS benefits from very limited deviations between its cash flow planning and corresponding actual cash flow. More generally, the development of a system of netting cash flows with partners has limited intraday risk.

In February 2016, ACOSS took over from Agence France Trésor (AFT), the central government's debt management agency, the full management of its Euro CP program, created in 2010. The complete internalization of the Euro CP has not generated any discontinuity. It will add to ACOSS' ability to centralize its liquidity management, and maintain a good level of responsiveness to market dynamics. ACOSS has been managing a CP program since 2006.

ACOSS' funding strategy for 2016 deviates only marginally from that of 2015. It continues to prioritize the diversification of liquidity sources through three channels: cash pooling with social security entities, short-term borrowing from cash-rich bodies and state agencies (chiefly AFT and CADES) and issuance of short-term notes via a CP and Euro CP programs totaling €45 billion. ACOSS has also diversified its currency exposures and issued in 12 different currencies, with a systematic swap to avert exchange rate risks. ACOSS has decided to do without medium-term funding from the Caisse des Dépôts et Consignations (CDC, the French government's financial arm), given its decreasing funding needs and the favorable interest rate environment. Rather, it will focus exclusively on short-term issuance, with maturities only days long. ACOSS will still maintain €3.4 billion in short-term facilities with CDC as back-up instruments, however. Although ACOSS officially qualifies for the European Central Bank's extended asset-purchasing program, its short term maturities effectively exclude it from the program. Nevertheless, ACOSS has been able to benefit from the favorable liquidity conditions and cover its funding with limited costs.

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It is very unlikely, in our opinion, that ACOSS will face liquidity stress, given its tight management of incoming and outgoing cash flows. Moreover, ACOSS secures its short-term funding in advance of required payments. In addition, we consider part of ACOSS' payments to be deferrable for a short period, if needed, particularly some health insurance benefits. We would not expect any deferral of pension payments.

We believe that, as a last resort, ACOSS would have prompt access to emergency funding from the French treasury, either through purchases of CP, as allowed for EPAs under France's finance law, or through funding from the state's public debt fund, Caisse de la Dette Publique. We also believe that ACOSS would anticipate well in advance any need for--and swiftly obtain--a further extension of its annual borrowing ceiling, as was the case in July 2009.

Related Criteria And Research

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Criteria - Governments - Sovereigns: Sovereigns And Equalized GREs Commercial Paper Rating Methodology - March 29, 2012

Ratings List

	Rating	
	To	From
Agence Centrale des Organismes de Securite Sociale (ACOSS)		
Issuer Credit Rating		
Foreign and Local Currency	--/--/A-1+	--/--/A-1+
Commercial Paper		
Foreign and Local Currency	A-1+	A-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information.

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