FRENCH REPUBLIC

Rating Analysis - 12/21/10
Debt: EUR1,489.0B, Cash: EUR57.1M

EJR Sen Rating(Curr/Prj) AA-/ A+
EJR CP Rating: A1+
EJR's 1 yr. Default Probability: 1.3%

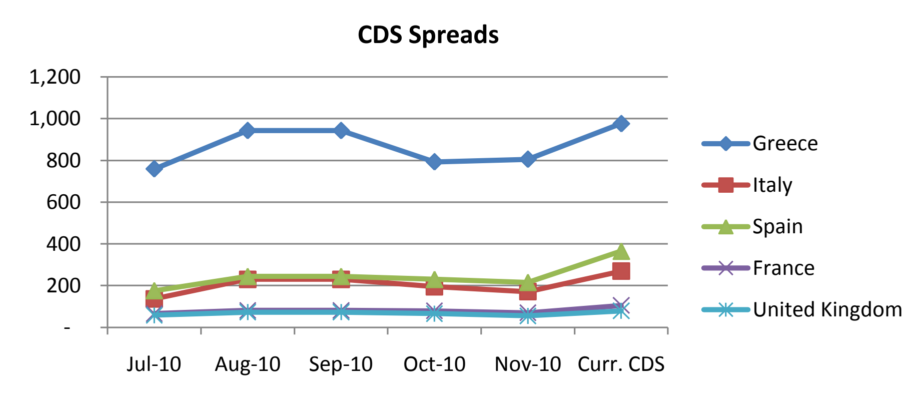
The French economy grew at a slower than expected 0.4% in Q3 2010 following 0.7% growth in Q2 2010. Imports were up 4.1% following 3.9% growth in the previous quarter while exports were up 2.5% following 2.6% growth in the previous quarter. As a result, the weakened trade balance contributed negatively (-0.5%) to overall GDP growth. Total domestic demand (excluding inventory changes) contributed positively (0.5%) to GDP growth. The economy is expected to grow 1.5% by year-end 2010, 2% in 2011 and 2.5% in 2012. In October, industrial production decreased by 0.8% from the month prior while private consumption decreased by 0.7%. In November, the CPI increased by 0.2% seasonally adjusted (1.6% YoY). Energy prices were up 10% YoY while food prices were up 0.9% YoY. Unemployment remained stable at 9.7% in the third quarter.

The cost of insuring French sovereign debt against default has risen to all-time highs in recent sessions with CDS spreads currently trading at 108bps. Yields on 10-yr debt have fallen. French banks' exposures to Greece, Ireland, Portugal and Spain are $83.1B, $77.3B, $48.5B and $201.3B, respectively.

	Annual Ratios					
INDICATIVE CREDIT RATIOS	Dec-08	Dec-09	Dec-10	Dec-11	Dec-12	Dec-13
Debt/ GDP (%)	60.3	73.6	80.5	88.1	94.2	100.7
Govt. Sur/Def to GDP (%)	-3.3	-7.5	-3.9	-3.6	-3.5	-3.5
Adjusted Debt/GDP (%)	74.0	88.4	95.3	103.0	108.8	115.0
Interest Expense/ Taxes %	10.8	9.5	12.5	13.5	14.2	15.1
GDP Growth (%)	-1.9	-0.5	-0.5	-0.5	2.0	2.0
Foreign Reserves/Debt (%)	2.3	1.5	1.4	1.3	1.2	1.1
Implied Sen. Rating	BBB+	BBB	BBB	BB	BB	BB-

INDICATIVE CREDIT RATIOS	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	40.0	50.0	60.0	80.0	120.0	150.0
Govt. Sur/Def to GDP (%)	5.0	3.0	0.5	-2.0	-5.0	-9.0
Adjusted Debt/GDP (%)	45.0	55.0	65.0	85.0	125.0	155.0
Interest Expense/ Taxes %	7.0	9.0	12.0	15.0	22.0	26.0
GDP Growth (%)	5.0	4.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	25.0	20.0	15.0	12.0	9.0	7.0

PEER RATIOS	S&P Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio-Implied Rating*
United Kingdom	AAA	76.1	-11.4	95.3	6.9	-5.0	B+
Federal Republic Of Germany	AAA	69.2	-3.0	75.8	10.7	-2.0	BB
Kingdom Of Spain	AA	50.3	-11.1	54.8	9.6	-3.0	BB+
Italian Republic	A+	109.3	-5.3	115.3	15.9	-2.8	B
Hellenic Republic (Greece)	BB+	118.3	-15.4	121.4	25.8	-3.2	CCC+



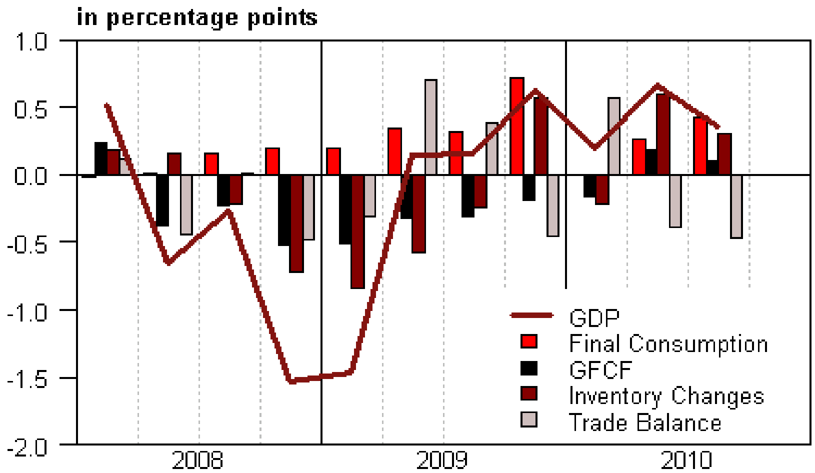
Country (EJR Rtg*)	Current CDS	Targeted CDS
Greece(BB)	976	400
Italy(BBB+)	269	158
Spain(A-)	365	117
France(A+)	105	60
United Kingdom(AA)	79	30

* Projected Rating

Economy

France constitutes the world's fifth largest economy (seventh in terms of purchasing power parity) with a total GDP of US$2.7 trillion, or 4.6% of the world economy, and GDP per capita of US$41,216 (2009). The country weathered the global economic crisis relatively well with the help of resilient consumer and government spending. France's GDP grew by a mere 0.2% in 2008 before contracting by 2.6% in 2009. The economy has continued to underperform in recent quarters, with Germany's economy growing at more than double the pace. Growth returned to 0.2% in the first quarter of 2010 followed by a gain of 0.7% in the second quarter and a lesser gain of 0.4% in the third quarter. While Germany expects its economy to expand at a rate of approximately 3.7% this year, France expects its economy to grow by 1.5%. The economy is forecast to expand by 2% in 2011 and 2.5% in 2012 with the help of business investment and exports.

Gross Domestic Product and Components: 2008-2010 YTD



Source: INSEE

France's Medium-Term Objective: Restoring Structural Balance of Public Finances

France allowed its debt to rise substantially during the global economic downturn. It's debt-to-GDP of nearly 80% was the fourth-highest in the euro zone in 2009 and is expected to continue to rise. Last year, the government launched an Economic Recovery Plan aimed at consolidated the country's public finances. In the past, deficit reduction has been achieved during periods of strong economic growth. As a result, the government's current strategy is to pursue structural reforms that encourage growth and, rather than raising taxes, reduce public spending. The government remains committed to not increasing the tax burden as it is already among the highest in Europe (40% top personal tax rate, 34.4% top corporate tax rate).

Multiyear Public Finance Trajectory

	2008	2009	2010	2011	2012	2013
Public balance (% GDP)	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
Public debt (% GDP)	67.4	77.4	83.2	86.1	87.1	86.6

Source: France Stability Program 2010-2013

Inflation: Slight Rise in CPI

The CPI increased by 0.1% in November 2010 over the month prior (+1.6% YoY). The slight increase in prices was due in large part to a rise in energy prices, which were up 0.9% in the month (10% YoY). A slight seasonal increase in prices of food products (+0.5% month-on-month, +0.9% YoY) also contributed to the upward shift. Meanwhile, gains were offset by the seasonal decline of prices of services linked with tourism as well as a weakening of the prices of manufactured products.

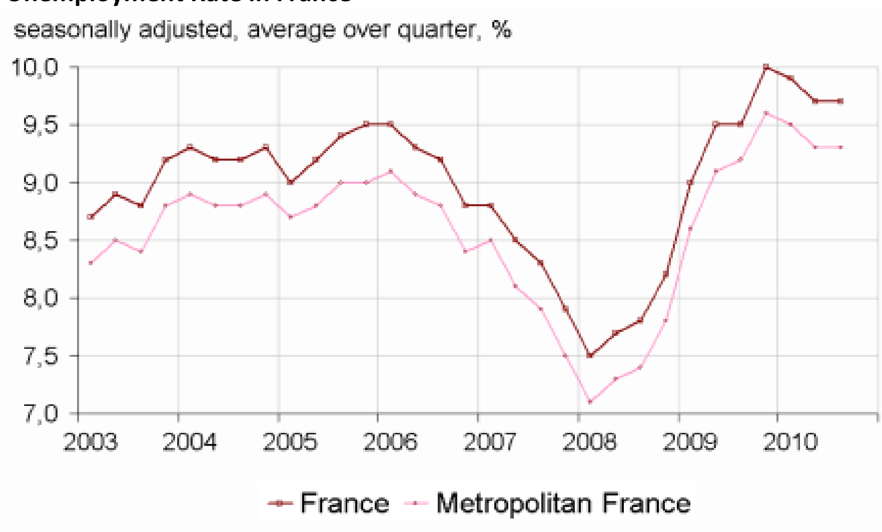
Unemployment Rate Stable

France's unemployment rate has risen sharply over the past two years since the onset of the global economic crisis. The rate has risen 2.4% from a low of 7.5% in Q1 2008 to a near high of 9.9% in Q1 2010 (1.3% more than the OECD average). In Q2 2010, the average unemployment rate in metropolitan France and overseas departments decreased 0.2% to 9.7%. The rate remained stable in Q3 2010.

Unemployment is highest among young persons aged 15-24 years with such rates currently exceeding 24%. Unemployment among adults aged 25-49 years fell 0.1% to 8.3% in Q3 2010 while rates among persons aged 50 years and older rose 0.2% to 6.4%. France's overall jobless rate remains below the euro zone average of 10.1%.

Meanwhile, underemployment decreased by 0.1% to 5.6% in the third quarter while the rate of employment (specifically among those aged 15-64 years) was stable at 63.8% as a result of an increase in temporary contracts.

Unemployment Rate in France



Source: INSEE

Pension Reform

The cost of the public pension system in France continues to rise. To date, the system runs a $13B deficit. The deficit is expected to continue to rise to as much as $123B by 2050 as the nation's generation of baby boomers retire. As the population continues to age rapidly, the workforce is left with fewer active workers to fund the system. As a result, in June 2010 Labor Minister Eric Woerth announced France's plans to raise the retirement age from 60 to 62 (with full benefits available at age 67) in order to take pressure off of the country's overwhelmed pension system. Moreover, the government recently announced plans to seize the €36B in assets of the Fonds de Reserve pour les Retraites, the country's reserve pension fund. The assets will be used to pay off the debts of France's welfare system in the amount of €2.1B per year.

Business Environment

France's regulatory environment allows for relative ease in owning and operating a business. Obtaining a business license requires less than the world average of 18 procedures and 218 days. Moreover, starting a business takes less than the world average of 35 days. The corporate tax rate remains high at 34.4% (33.3% plus a 3.3% surcharge applicable to companies with a turnover exceeding a certain threshold).

Assumptions for Projections

	Peer Median	Issuer Average	Base Case Yr 1&2	Base Case Yr 3,4,5
Income Statement				
Taxes Growth%	(4.8)	(7.9)	**1.0**	**3.0**
Social Contributions Growth %	(1.8)	0.6	**0.6**	**0.6**
Grant Revenue Growth %	0.0	0.0		
Other Revenue Growth %	0.1	(2.2)	**(2.0)**	**(2.0)**
Other Operating Income Growth%	0.0	0.0		
Total Revenue Growth%	(6.4)	(4.3)	**(1)**	**2.0**
Compensation of Employees Growth%	5.2	2.9	**(1.0)**	**(0.5)**
Use of Goods & Services Growth%	5.4	7.3	**(0.5)**	**1.0**
Social Benefits Growth%	8.7	5.2	**0.5**	**0.8**
Subsidies Growth%	2.3	15.9		
Other Expenses Growth%	7.2	7.2	**1.0**	**3.0**
Special Items (millions EUR)	0.0	0.0		
Balance Sheet				
Currency and Deposits Growth%	0.4	42.7	**1.0**	**(4.8)**
Securities other than Shares LT Growth%	7.8	(19.9)	**2.0**	**(19.9)**
Loans Growth%	2.4	26.6	**2.0**	**23.9**
Shares and Other Equity Growth%	14.8	8.8	**2.0**	**8.8**
Insurance Technical Reserves Growth%	2.8	5.6	**2.0**	**5.6**
Financial Derivatives Growth%	0.0	0.0		
Other Accounts Receivable LT Growth%	8.0	9.3	**1.0**	**(4.8)**
Monetary Gold and SDR's Growth %	0.0	0.0	**2.0**	**5.0**
Other Accounts Payable Growth%	9.2	NMF		
Currency & Deposits Growth%	4.5	(13.7)	**0.5**	**0.5**
Securities Other than Shares Growth%	16.3	14.1	**9.9**	**9.9**
Growth%	0.0	0.0		
Loans Growth%	0.8	9.9	**9.9**	**9.9**
Insurance Technical Reserves Growth%	0.0	0.0		
Financial Derivatives Growth%	0.0	0.0		
Addl debt. (1st Year) million EUR	0.0	0.0		

Base Case

ANNUAL REVENUE AND EXPENSE STATEMENT (MILLIONS EUR)

	Dec-07	Dec-08	Dec-09	PDec-10	PDec-11	PDec-12
Taxes	511,062	520,103	478,927	483,716	488,553	503,210
Social Contributions	339,731	349,815	351,807	353,810	355,825	357,851
Grant Revenue	0	0	0	0	0	0
Other Revenue	88,802	94,112	92,050	90,209	88,405	86,637
Other Operating Income	0	0	0	0	0	0
Total Revenue	939,592	964,031	922,781	927,736	932,783	947,698
Compensation of Employees	241,736	247,268	254,327	251,784	249,266	248,020
Use of Goods & Services	93,947	96,606	103,666	103,148	102,632	103,658
Social Benefits	437,223	454,820	478,423	480,815	483,219	485,635
Subsidies	27,612	27,402	31,769	31,772	31,775	31,779
Other Expenses	74,586	80,324	86,074	5,126	86,074	88,656
Grant Expense	0	0	0	0	0	0
Depreciation	47,773	50,934	51,941	51,941	51,941	51,941
Total Expenses	922,877	957,354	1,006,200	924,586	1,004,907	1,009,689
Operating Surplus/Shortfall	16,715	6,677	-83,419	3,150	-72,124	-61,991
Interest Expense	50,948	56,212	45,551	60,441	65,781	71,648
Net Operating Balance	-34,233	-49,535	-128,970	-57,291	-137,905	-133,639

ANNUAL BALANCE SHEETS (MILLIONS EUR)

ASSETS	Dec-07	Dec-08	Dec-09	PDec-10	PDec-11	PDec-12
Currency and Deposits	24,081	40,027	57,121	124,503	125,748	119,712
Securities other than Shares LT	34,548	46,621	37,321	38,067	38,829	31,083
Loans	30,984	30,198	38,232	38,997	39,777	49,301
Shares and Other Equity	462,969	374,100	407,200	415,344	423,651	461,135
Insurance Technical Reserves	703	709	749	764	779	823
Financial Derivatives						
Other Accounts Receivable LT	132,411	139,624	152,664	154,191	155,733	148,257
Monetary Gold and SDR's						
Additional Assets	0	0	0	0	0	0
Total Financial Assets	685,696	631,279	693,287	771,865	784,516	810,311

LIABILITIES	Dec-07	Dec-08	Dec-09	PDec-10	PDec-11	PDec-12
Other Accounts Payable	92,619	95,844	100,158	100,158	100,158	100,158
Currency & Deposits	19,034	23,648	20,406	20,406	20,406	20,406
Securities Other than Shares	1,026,560	1,167,690	1,332,390	1,463,941	1,608,481	1,767,292
Loans	189,269	189,647	208,500	208,500	214,516	215,140
Insurance Technical Reserves						
Financial Derivatives						
Other Liabilities	(2)	1	(4)	4,318	4,318	4,318
Liabilities	1,327,480	1,476,830	1,661,450	1,797,323	1,947,879	2,107,313
Net Financial Worth	(641,788)	(845,549)	(968,167)	(1,025,458)	(1,163,363)	(1,297,002)
Total Liabilities & Equity	685,692	631,281	693,283	771,865	784,516	810,311

Sovereign Rating Methodology

Egan-Jones takes the perspective of the investor as its primary point of view when developing the ratings it issues for sovereigns. Therefore, in the case of sovereign ratings, we attempt to take a more holistic view of credit quality to include not only analytic comparisons of various sovereign issuers but also the impact on our quantitative and qualitative analyses by current global, sovereign, governmental and market events, including the effects of government investments in speculative, volatile or other high risk investment products. For example, many sovereign issuers have taken on significant exposures of major financial institutions over the past several years. Hence, we calculate the under-funding of financial institutions and include this amount in the total indebtedness of sovereigns. (We use a base assumption that no country can afford to allow its major banks to fail and therefore we believe that there will almost always be an intervention by either a host or allied nation should financial institutions or markets require support at some measurable level.)

Generally we devise modeling calculators and do an analysis that examines the debt load of a country with respect to its GDP and other economic indicators. The analysis is then adjusted to reflect the outlook on a myriad of factors that reflect the firm’s overall view of the sovereign debt and the quality of the country’s ability to meet and thrive under such load. Some of the qualitative factors that impact our ultimate assessment of credit quality such as the flexibility, stability and overall strength of the economy, ease of tax collection, acceptance of contract law, ease of doing business, and prospects for future growth and health. The non quant issues are generally subjective and a moving target, so each rating of a sovereign may differ because of the non-quantitative nuances being addressed.

Nota Bene

History has proven that defaults on domestic public debt do occur. In fact, seventy out of three hundred twenty defaults since 1800 have been on domestic public debt (1). Egan-Jones does not view a country's ability to print its own currency as a guarantee against default. Additionally, Egan-Jones generally views cases of excessive currency devaluation as a de facto default.

1. "This Time Is Different: Eight Centuries of Financial Folly", Reinhart & Rogoff, p.111, 126