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CREDIT OPINION
30 June 2023

Update

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RATINGS

Municipal Fin. Authority of British Columbia

Domicile	British Columbia, Canada
Long Term Rating	Aaa
Type	Senior Unsecured - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Municipal Fin. Authority of British Columbia (Canada)

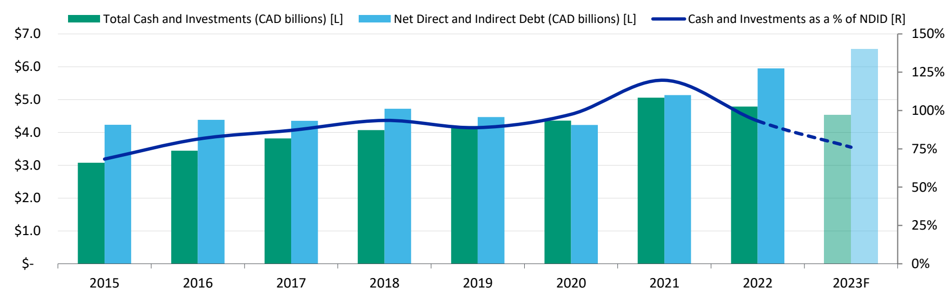
Update following rating affirmation

Summary

The credit profile of the Municipal Finance Authority of British Columbia (Aaa stable) (MFABC) reflects very strong management and an institutional framework, and robust credit protection mechanisms which provide significant bondholder protections. High levels of liquidity also ensure robust cash flow coverage. MFABC's credit profile and key performance metrics have not weakened during the pandemic, which reflects strong mitigants and the stability of its borrowers' revenue bases. MFABC's credit profile is supported by its taxing powers on all taxable properties in British Columbia. Geographical and single-name concentration could present a challenge in case of an unexpected severe event that would lead to a deterioration of credit quality of borrowers, however the concentration reflects the geographical concentration of borrowers in the Metro Vancouver region.

Exhibit 1

The recent decline in liquidity coverage reflects a return to more stable long-term levels (years ending Dec 31)



Sources: MFABC and Moody's Investors Service

Credit strengths

» Very strong management and institutional framework

» Robust credit protection mechanisms provide debenture holder security

» Borrowing structure and substantial liquidity ensure strong cash flow coverage, while rollover risk of short-term debt is mitigated

Credit challenges

» Single-name and geographic concentration of the loan portfolio

Rating outlook

The stable outlook reflects continued strong governance and credit protection mechanisms within a stable institutional framework which ensures ongoing strong performance of the loan portfolio. We expect that the credit quality of borrowing members will remain solid, supported by predictable revenue sources.

Factors that could lead to a downgrade

A substantial decline in MFABC's reserves and liquidity leading to weaker coverage levels, weaker loan portfolio quality or a significant weakening of the credit protection mechanisms could lead to a downgrade of the rating.

Key indicators

Municipal Fin. Authority of British Columbia

(Year Ending 12/31)	2017	2018	2019	2020	2021	2022
Total Direct Debt (CAD millions)	8342.1	8809.8	8717.5	9145.0	9784.0	10350.2
Loans Outstanding to Clients (CAD millions)	4681.1	4972.3	4913.6	4946.3	5617.7	5764.5
Total Cash and Investments (CAD millions)	4071.0	4192.5	4359.3	5060.3	4789.6	4528.1
Operating Margin as % of Revenues [1]	31.1	31.6	32.2	33.1	36.5	36.3
Debt Burden [2] (%)	0.3	0.3	0.3	0.2	0.2	0.2
Cash and Investments as % of Direct Debt	48.8	47.6	50.0	55.3	49.0	43.7
% Change in Loans Outstanding	1.6	6.2	-1.2	0.7	13.6	2.6

[1] Before gains/losses from change in fair value of derivative contracts
[2] Net direct debt (total debt less sinking funds and unused commercial paper) as % of assessed property value
Sources: MFABC and Moody's Investors Service

Detailed credit considerations

On 23 June 2023, we affirmed MFABC's aaa baseline credit assessment (BCA) and Aaa debt ratings with a stable outlook, and its short-term P-1 commercial paper rating.

The credit profile of MFABC, as expressed in its Aaa stable rating, combines a BCA of aaa, and a high likelihood of extraordinary support coming from the Province of British Columbia (Aaa stable) in the event MFABC faced acute liquidity stress.

Baseline credit assessment

Very strong management and institutional framework

We characterize MFABC's management as very strong with prudent, forward looking credit and debt policies. Its strong management also allows MFABC to continue to record consistent positive operating results and to refinance maturing debentures at favourable terms. Management maintains strong relations with capital market participants, resulting in ongoing solid market access at favourable rates and strong secondary market trading liquidity, despite recent coronavirus-related market pressures.

MFABC issues debt in its own name, and on-lends the proceeds to the borrowing regional districts. At year-end 2022, MFABC's loan portfolio stood at CAD5.8 billion including both long-term and short-term loans to clients. MFABC maintains stringent guidelines for monitoring its loan borrowers' credit quality, and had no loan defaults or missed payments from any of its borrowers in its 53-year history, further supporting the Authority's management strength.

In addition, MFABC operates within a strong institutional framework. Municipalities in British Columbia, with the exception of the City of Vancouver which operates under a special charter, are prohibited from issuing debt directly. Instead, they borrow long-term through their respective regional districts, which in turn borrow from MFABC.

As with other Canadian provinces, the Province of British Columbia exercises a high degree of oversight over municipal financial activities: (1) municipalities cannot run operating deficits; (2) municipalities can only borrow long-term for capital spending; (3) long-term borrowing requires a comprehensive public approval process prior to MFABC approval; and (4) municipalities have to adhere to a debt service limit according to which only 25% of recurring revenues are eligible to service debt. This frameworks supports the quality of MFABC's loan portfolio. Municipal debt issuance for capital spending is also limited by the reliance on other funding sources such as pay-as-you-go financing, reserves as well as provincial and federal government grants.

Besides loans to regional districts/municipalities, MFABC provides loans to regional hospital districts (CAD716 million, or about 12% of long-term loans in 2022) with an estimated CAD814 million in additional borrowing needed between 2025 and 2027. TransLink, the transit authority in the Metro Vancouver Area, also has CAD337 million, or slightly below 6% of MFABC long-term loans outstanding at year end 2022. This share will continue to decrease over time as TransLink now issues debt directly in its own name in the capital markets.

In addition to lending, MFABC also provides pooled investment services to regional entities, including pooled investment funds and high-interest savings accounts. Starting in 2022, MFABC also launched a long-term new Diversified Multi-Asset Class pooled investment fund designed to invest those regional government reserves not needed for at least 10 years. Pooled investment fund balances stood at CAD5.3 billion at year-end 2022.

During the pandemic, MFABC implemented several strategies to improve its risk management and controls to ensure early detection of any credit stress of a borrowing member. It updated its technology policies and standards, implemented a transaction control framework, and modernized its IT infrastructure, cybersecurity and enterprise architecture to better detect threats and reduce organizational risk.

Robust credit protection mechanisms provide debenture holder security

The Local Government Act of British Columbia includes a general liability provision, whereby municipalities are jointly and severally liable for all obligations of their regional district, providing considerable strength to MFABC's institutional structure and promoting fiscal discipline across borrowers. MFABC's unlimited taxing power and the joint and several liability of borrowing municipalities are key factors in MFABC's credit rating.

MFABC withholds 1% of principal borrowed of long-term loans into a debt reserve fund (DRF). Funds in the DRF must be accessed first (90% of which is available on a 1-day notice) if MFABC does not have sufficient funds to meet payments due on its obligations. MFABC has never been required to tap the DRF.

If the DRF cannot be replenished in a reasonable time, MFABC has the option to levy a tax on all taxable properties in British Columbia in order to replenish the DRF to its required level. If the DRF falls to below 50% of its required level, MFABC is mandated to exercise this authority and levy a tax. MFABC currently sets a nominal tax rate on properties to ensure that the charge is already present on all property tax notices. This credit protection ensures that MFABC has access to CAD2.4 trillion (2022) in property values across the province. The increase of the tax rate would not require any further legislative approvals. Due to the maximum potential delay of 14 months before enacting the property tax provision, MFABC ensures it maintains sufficient liquidity to cover at least 14 months of its funding requirements. MFABC's continued strong credit metrics despite the coronavirus pandemic reflect the stability of its borrowers' revenue bases – which benefitted from provincial and federal support - and improvements in its due diligence and loan monitoring.

MFABC was created in 1970 by an act of provincial legislature, the Municipal Finance Authority Act. MFABC acts as the central borrowing agency in British Columbia for financing, through loans, the capital requirements of municipalities and regional districts, including hospital districts and other municipal-related bodies. MFABC operates at arm's length from the province, and obligations of MFABC are not the obligations of the province and are not guaranteed by the province.

Borrowing structure and substantial liquidity ensure strong cash flow coverage, while rollover risk of short-term debt is mitigated

MFABC maintains a robust liquidity profile and its liquidity sources continue to fully cover its commercial paper maturities and provide strong liquidity coverage ratios. The majority, or approximately 95%, of its cash and investments (which totalled CAD4.5 billion at year-end 2022) includes sinking fund investments set aside for future debt repayment, providing 44% coverage of total direct debt, a level we consider to be very strong. The rest of cash and investments includes CAD120 million held in the DRF at December 31, 2022, and CAD105 million in the Strategic Retention Fund, an additional liquidity reserve fund. We expect that these balances will continue to grow with the growth in MFABC's loan portfolio.

MFABC maintains long-term debt with a well-structured maturity profile. The majority of debt is in the form of long-term debentures issued with a typical term of 5-10 years, although we expect that in the current rising interest rate environment the authority may look to extend the debt maturity profile by issuing longer term (e.g. 20-year) bonds to minimize refinancing risk and volatility and improve pricing. It most recently issued longer than 10-year tenor bonds in 2021 (CAD350 million 20-year debenture) and 2017 (CAD61 million 25-year debenture). In 2023, MFABC expects to refinance approximately CAD935 million of maturing long-term debentures in the capital markets, with additional new borrowing estimated at CAD275 million. All debt is issued in Canadian dollars.

While MFABC almost exclusively issues debentures with bullet maturities, the amortizing structure of loan agreements with regional districts provides security for debenture holders. This structure enhances cash flow coverage, and funds paid to MFABC in excess of immediate debt service requirements are allocated to investments.

MFABC has access to short-term borrowings through its commercial paper (CP) program which is used to finance short-term loans and investments. The CP program has an active limit of CAD700 million, but it could be increased up to CAD1,250 million based on pre-authorization by MFABC's board. At year-end 2022, the CP program had an outstanding balance of CAD600 million, although MFABC is looking to fully utilize the CP program in 2023 which exposes it to rollover risk in the current high interest rate environment. However, MFABC is largely sheltered from the risk of interest rate increases given that the anticipated increase in CP debt would be offset by higher short-term lending rates. In addition, MFABC also has full access to committed credit lines in the combined amount of CAD350 million, representing half of the active CP program limit, as well as access to a CAD100 million uncommitted credit line.

Single-name and geographic concentration of the loan portfolio

The loan portfolio has a high concentration of borrowers in the Vancouver region, especially the Metro Vancouver Regional District which account for approximately 51% of long-term loans. The geographical and single-name concentration results in a lack of diversity of the loan portfolio and could represent a challenge in case of an unexpected severe event that would lead to a substantial deterioration of credit quality and municipal fiscal performance in the region.

Nevertheless, the loan portfolio concentration closely reflects the geographical concentration of borrowers in the Metro Vancouver region, and the risks stemming from a concentrated loan portfolio are mitigated by MFABC's strong liquidity profile and institutional strength and robustness of the economy in British Columbia. In addition, the majority of individual borrowers' share is less than 1% each of the overall loan portfolio, mitigating concentration risk.

Extraordinary support considerations

While MFABC's BCA of aaa already places it in the Aaa rating bracket, the Joint-Default Analysis methodology also considers the likelihood of extraordinary support coming from the Province of British Columbia. Moody's assigns a high likelihood of support, reflecting the strategic importance of the MFABC in providing financing for municipalities in the province. A default by the MFABC could raise the cost of borrowing for all municipalities in the province, thereby offering an incentive for the province to provide the necessary liquidity to avoid a default.

Moody's also assigns a very high default dependence level between MFABC and the Province of British Columbia, reflecting the two entities' shared exposure to common economic and financial risks.

ESG considerations

How environmental, social and governance risks inform our credit analysis of MFABC

Moody's takes into account of the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of MFABC, the materiality of ESG to the credit profile is as follows:

The exposure to environmental risks is low. MFABC's limited operations as a financial authority do not expose it to natural capital, water management or other environmental risks. Some of the more rural municipalities within the regional borrowing districts may be exposed to environmental risks including wildfires, however the joint and several obligations of municipalities within each region and disaster relief from the provincial and federal governments mitigate this risk.

The exposure to social risks is low. MFABC's exposure to social risks, such as demographics and health and safety related risks, is indirect through the pressure these may have on the borrowing members' financial health and in turn their ability to pay their debt service to MFABC.

MFABC's governance is very strong, with a track record of positive operating results and forward looking credit and debt policies. Strong management and institutional characteristics allow MFABC to maintain robust relations with capital market participants and refinance maturing debt at favourable terms.

Further details are provided in the “Detailed credit considerations” section above. Our approach to ESG is explained in our cross-sector methodology 'General Principles for Assessing Environmental, Social and Governance Risks'.

Rating methodology and scorecard factors

The assigned BCA of aaa is in line with the scorecard-indicated BCA of aaa. For details about our rating approach, please refer to the Public Sector Pool Programs and Financings Methodology (April 2020) and Government-Related Issuers Methodology (February 2020).

Exhibit 3
MFABC
Public Sector Pool Programs and Financings Methodology

Baseline Credit Assessment (BCA) – Scorecard	Base Weight	Sub Factor	Score
Factor 1: Credit Strength and Default Tolerance (50%)			
Credit Quality and Default Tolerance Score	50%	Aaa	Aaa
Factor 2: Diversity of Portfolio (20%)			
Number of Borrowers	10%	49	A
Percentage of Loan Principal to Borrowers that Represent Less than 1% of the Pool	5%	9.30%	Ba
Percentage of Loan Principal to the Top 5 Borrowers	5%	67.41%	Ba
Factor 3: Debt Structure (30%)			
Cash Flows	20%	Aa	Aa
Counterparties	10%	A	A
Notching Factors			
Unusually Strong or Weak Management		2	
Concentration of Pool Participants in a Volatile Sector		0	
Total Notching Adjustments		2	
Scorecard-Indicated BCA Outcome			aaa

Financial year-end 31 December 2022
Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
MUNICIPAL FIN. AUTHORITY OF BRITISH COLUMBIA	
Outlook	Stable
Baseline Credit Assessment	aaa
Senior Unsecured	Aaa
Commercial Paper -Dom Curr	P-1

Source: Moody's Investors Service

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