S&P Global Ratings

RatingsDirect®

Municipal Finance Authority of British Columbia

Primary Credit Analyst:
Stephen Ogilvie, Toronto + 1 (416) 507 2524; stephen.ogilvie@spglobal.com

Secondary Contact:
Julia L Smith, Toronto + (416) 507-3236; Julia.Smith@spglobal.com

Table Of Contents

Municipal Finance Authority of British Columbia

This report does not constitute a rating action.

Major Rating Factors

Issuer Credit Rating
AAA/Stable/A-1+

Strengths	Weaknesses
• Municipal Finance Authority of British Columbia (MFABC) is the exclusive lender of long-term debt to municipalities in British Columbia (B.C.), with a unique legislatively enshrined taxing power. • The strong institutional framework that governs Canadian municipalities supports the creditworthiness of the B.C. municipal sector. • MFABC's capital framework drives its strengthening capital base. • Considerable liquid sinking fund investments and matched funding practices promote funding and liquidity ratios above 1.0x.	• Lending to Metro Vancouver represents a notable concentration in the loan portfolio.

Outlook

The stable outlook reflects MFABC's long history of prudent management and governance practices, conservative risk appetite and risk management framework, and sophisticated asset-liability management, all of which we expect will continue. S&P Global Ratings believes that the recent strengthening of the authority's capital policies will continue to support its creditworthiness. We also expect that the authority will maintain its strength in accessing capital markets through a diversified investor base, as demonstrated by consistent planned debt issuances, and that its funding and liquidity position will stay strong in the next two years. Our stable outlook also underscores the expectation that MFABC will remain the exclusive lender of long-term debt to B.C. municipalities. We also expect the authority will retain its legislatively enshrined ability to levy a provincewide tax to replenish any potential draw on its debt reserve fund (DRF).

Downside scenario

Although we do not expect it, we could lower the rating in the next two years if MFABC's taxing powers were constrained, or if capital adequacy ratios declined significantly due to a fall in capital following sustained operational losses or a full or partial distribution of the strategic retention fund to members. We could also consider a negative rating action if the authority was no longer the exclusive long-term lender to B.C. municipalities or in the case of a sustained decline in the credit quality of the B.C. local government sector.

Rationale

Our long-term issuer credit and senior unsecured debt ratings on MFABC are 'AAA'.

The authority's statutory public policy role is to be the exclusive lender of long-term debt to B.C. municipalities, and it is central to the authority's very strong business position. We consider the municipal sector in B.C. to be low risk because of its predictable and well-balanced institutional framework, and its very high economic and financial resilience. Supported by a low risk appetite and strong policy framework, MFABC's very strong management, combined with robust governance, mitigates the risk that can arise from being a moderate-size organization relative to peers, in our opinion.

MFABC's capital framework promotes the maintenance of strong levels of loss absorption. Capital scales up with new issuance and is bolstered annually by retained earnings. Funding and liquidity are strong, given prudent risk management practices that retain liquid investments in the authority's sinking funds, which stood at C$4.3 billion at the end of 2021. We believe the pass-through nature of MFABC's operations, its plain vanilla funding, and robust cash and liquid investments support a strong overall financial risk profile.

The authority, unlike peer public sector funding agencies, has taxing powers. MFABC has the unfettered ability to impose a provincewide levy on all taxable land and improvements to replenish its DRF, if needed. MFABC is already a claimant on annual local tax bills, which we believe would expedite its ability to collect on a special levy, if needed. We consider this taxing power a key strength underpinning the 'AAA' rating.

MFABC was established in 1970 to provide low-cost financing to B.C.'s municipal sector except to the City of Vancouver and South Coast British Columbia Transportation Authority. It is a not-for-profit, tax-exempt corporation without share capital controlled by its member municipalities. Despite its establishment by provincial statute, the authority has an arm's length relationship with the government, with minimal direct linkages and no provincial guarantee on its debt. As a result, we do not view it as a government-related entity.

Enterprise risk profile: A very strong public policy mandate and strengthening risk management complement the low-risk municipal sector.

- We expect the municipal sector will remain low risk because of its well-balanced and predictable institutional framework, very high economic resilience, low financial system risk, and average sector leverage levels, which strong oversight of municipal borrowings by the province buttresses.
- The authority's very strong business position arises from its public policy mandate as the exclusive long-term lender to the B.C. municipal sector.
- Management policies and governance will remain very strong, with well-established and prudent management policies and practices, especially concerning asset-liability matching.

We expect MFABC will maintain its strong public policy mandate as the exclusive lender of long-term debt to the municipal sector in B.C. The authority's very strong public policy role continues to be the provision of low-cost long-term funding to B.C.'s local and regional municipalities by pooling bond issues and creating liquidity in bond markets. Although its core business will remain the provision of long-term lending, MFABC also provides short-term revenue anticipation and construction financing to its municipal clients. We believe that MFABC's provision of this lending strengthens its relationship with borrowers and reinforces its policy role. Its exclusive lending status promotes revenue stability because capital needs and lending growth are tied to longer-term trends such as demographics rather than to the business cycle. Unlike most of its peers, MFABC does not face competition from other lenders, ensuring a high level of customer stability. The authority is one of the largest municipal borrowers in the country. MFABC also provides a suite of investment products to local governments through its pooled investment funds and pooled high interest savings accounts but faces strong competition from other financial institutions (namely banks and investment managers) in this space. MFABC's pooled investments ended 2021 at C$5.6 billion in assets under management, up C$1 billion from 2020.

Management policies and practices are prudent and contribute to our view of the authority's management and governance as very strong. MFABC's business plan sets out the organization's annual goals, both financial and nonfinancial. The board tracks progress on outcomes in regular meetings with senior staff. Risk management policies and practices reflect the organization's low risk appetite, most recently reflected in the establishment of a capital policy outlining a clear target for on-balance-sheet risk capital, the retention of operating surplus, and the ongoing management of capital. Committees must approve both loan and investment decisions. Policies cover all key aspects of MFABC's operations, including asset-liability matching as a key risk management practice. The management team is experienced; key members have long tenure with the authority. Management has a board-approved succession plan. In terms of personnel, MFABC is a relatively small organization but the pass-through nature of its business and plain vanilla funding mitigate potential risks when compared with larger peers that compete for borrowers and whose more complex funding practices expose them to higher market risks. In 2020, for the first time, MFABC began providing disclosures about its environmental, social, and governance (ESG) footprint, by mapping the end use of its bond proceeds to the U.N. sustainable development goals. The authority is committed to continuously improving this reporting.

We continue to view the B.C. municipal sector as low risk. Our public sector industry and country risk assessment is very strong because of the sector's well-balanced and predictable institutional framework, very high economic resilience, average leverage, and low financial system risk. Provincial-municipal intergovernmental arrangements are stable. B.C., like all other provinces, imposes a prudent fiscal policy framework on its municipalities. Leverage in the sector is moderate: Debt is forecast to remain close to about 80% of operating revenues and interest expense is low. As well, and like the rest of the country, the sector has very high economic resilience thanks to the province's high GDP per capita of almost C$60,000. Canada's banking system is sound, and we view financial system risk for the B.C. municipal sector as low.

Financial risk profile: Strengthened capital levels will support MFABC's financial position

- The authority's capital management policy will support the continued strengthening of capital through retained earnings.

- The scaling up of the loss absorbing DRF with each new debt issue also supports strong risk-adjusted capital (RAC) levels.
- MFABC's considerable holdings of liquid investments in its sinking funds of C$4.3 billion at year-end 2021, its solid access to capital markets, and strong secondary market liquidity will sustain strong funding and liquidity.

We expect MFABC's capital adequacy policy and framework will support strong capital. The authority has set its own capital policy far above its legislated 1% DRF. MFABC has never reported a credit loss in its 50-year history. In 2021, a higher level of portfolio concentration resulting in an increase in risk-weighted assets outweighed the growth in capital, which includes the DRF (given its loss-absorbing nature). MFABC's loan portfolio has a notable concentration due to its lending to Metro Vancouver, the province's largest population center. The RAC ratio after concentration declined slightly to 7.3% from 8.0% a year earlier. MFABC's capital increased to C$225 million (as of Dec. 31, 2021) from C$216 million in the previous year. Capital consists of C$123 million in the DRF and C$102 million in the strategic retention fund (retained earnings). The before-concentration RAC ratio increased to 30.3% from 17.6% on a changed, less conservative view of the authority's operational risk.

MFABC does not take on any transformation risk because it uses fixed-rate domestic bonds to fund its lending, which supports our strong capital adequacy assessment. Risk management practices, which include very strict asset-liability matching, are sound, in our view.

MFABC holds considerable liquid investments in its sinking funds of C$4.3 billion at the end of 2021 (equal to more than half of its gross long-term debt) and they are the foundation of the authority's very strong liquidity. For 2022, MFABC's funding ratio of assets to liabilities is 1.1x and its one-year liquidity ratio is 2.6x. The Canadian bond market, which we consider deep and diversified, provides 100% of MFABC's funding, making its funding sources slightly concentrated compared with those of peers. Although investor diversification is much stronger and continues to improve, we view the authority's investor base as slightly weaker than those of peers. Nevertheless, MFABC has unfettered access to the Canadian capital market, as has been demonstrated by oversubscribed public debt issuance during the financial crisis in 2008 and the height of pandemic market uncertainty volatility in 2020. The authority's liquidity position is also boosted by committed lines of credit totaling C$350 million, and by its access to the Bank of Canada's contingent term repo facility.

MFABC, unlike its peers, has powers to levy a tax on all taxable properties in B.C. to replenish the DRF to its required level. We consider this a significant credit strength. The authority has the unencumbered ability to impose a provincewide levy on all taxable land (assessed at approximately C$2.2 trillion) and improvements, if needed, to replenish its DRF. If the DRF falls to below 50% of its required level, MFABC must exercise this authority and levy the property tax. The board can immediately invoke taxing powers at its discretion and needs no approval from its municipal members or any higher level of government. The authority is already a claimant on annual local tax bills, and we believe this expedites its ability to collect on a special levy. MFABC has not reported a loan book default in its 50-year history, nor has it reported a DRF deficiency. The authority has never had to enact a special levy. We consider this taxing power a key strength underpinning the 'AAA' rating.

Key Statistics

Table 1

Municipal Finance Authority of British Columbia -- Selected Indicators					
	--Year ended--				
(Mil. C$)	2021	2020	2019	2018	2017
Business position					
Total assets*	10,490.8	10,083.3	9,358.0	9,244.0	8,845.0
Customer loans (gross)	5,617.7	4,946.7	4,914.0	4,972.0	4,681.0
Growth in loans (%)	13.6	0.7	(1.2)	6.2	1.6
Net interest revenues	128.4	121.8	121	119	115
Noninterest expenses	3.7	3.6	3.5	3.3	3.2
Capital and risk position					
Total liabilities*	9,948.9	9,303.3	8,866.0	8,953.8	8,494.2
Total adjusted capital	225	216.1	195	181	173
Assets/capital (%)	46.6	46.7	48	51.2	51.7
RAC ratio before diversification	30.3	17.6	16.1	14.8	14.3
RAC ratio after diversification	7.3	8	7.9	6.8	7.4
Gross nonperforming assets/gross loans	0	-	-	-	-
Funding and liquidity (x)					
Liquidity ratio with loan disbursement (1 year)§	2.6	1.4	1.6	1.8	1.2
Liquidity ratio without loan disbursement (1 year)§	2.6	2.1	2.5	1.8	1.7
Funding ratio (1 year)§	1.1	1.2	1	1.2	0.5

*As per balance sheet. §Includes sinking funds. RAC--Risk-adjusted capital. N/A--Not applicable.

Ratings Score Snapshot

Table 2

Municipal Finance Authority of British Columbia -- Ratings Score Snapshot	
Issuer Credit Rating	AAA/Stable/A-1+
SACP	aa+
Enterprise Risk Profile	Very strong (1)
PICRA	Strong (2)
Business Position	Very strong (1)
Management & Governance	Very strong (1)
Financial Risk Profile	Strong (2)
Capital Adequacy	Strong (2)
Funding	Neutral
Liquidity	Very strong (1)
Support	0
GRE Support	0
Group Support	0

Table 2

Municipal Finance Authority of British Columbia -- Ratings Score Snapshot (cont.)	
Additional Factors	1

Related Criteria

- Public-Sector Funding Agencies: Methodology And Assumptions, May 22, 2018
- Risk-Adjusted Capital Framework Methodology, July 20, 2017
- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Principles Of Credit Ratings, Feb. 16 2011
- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

Ratings Detail (As Of May 5, 2022)*		
Municipal Finance Authority of British Columbia		
Issuer Credit Rating		AAA/Stable/A-1+
Commercial Paper		
Local Currency		A-1+
Canada National Scale Commercial Paper		A-1(HIGH)
Senior Unsecured		AAA
Issuer Credit Ratings History		
19-Mar-2008	*Foreign Currency*	AAA/Stable/A-1+
29-Aug-2007		AA+/Positive/A-1+
21-Feb-2006		AA+/Stable/A-1+
19-Mar-2008	*Local Currency*	AAA/Stable/A-1+
29-Aug-2007		AA+/Positive/A-1+
21-Feb-2006		AA+/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.