

Research Update:

Municipal Finance Authority of British Columbia 'AAA' Ratings Affirmed On Strong Loan Portfolio Quality; Outlook Stable

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Overview

- We are affirming our ratings, including our 'AAA' long-term issuer credit rating, on the Municipal Finance Authority of British Columbia (MFABC or the authority).
- The ratings reflect our view of the strong overall credit quality of MFABC's loan portfolio, strong legal framework through which it borrows on behalf of members, and the authority's solid liquidity profile.
- The stable outlook reflects our expectations that B.C. municipalities' consolidated operating revenue growth and operating surpluses will remain in line with the average of the past five years, and that the sector's overall debt will remain comparable with those of 'AAA' rated municipalities outside the U.S.

Rating Action

On March 23, 2010, Standard & Poor's Ratings Services affirmed its ratings, including its 'AAA' long-term issuer credit rating, on the Municipal Finance Authority of British Columbia (MFABC or the authority). The outlook is stable.

Rationale

The ratings on MFABC reflect Standard & Poor's opinion of the following factors:

- The strong overall credit quality of its loan portfolio. B.C.'s 28 regional districts that borrow for their own purposes and on behalf of their member municipalities are the main loan obligors, although the South Coast British Columbia Transportation Authority (TransLink) is the biggest single-name obligor. We think the regional districts' credit qualities reflect the credit qualities of their respective member municipalities, which jointly and severally guarantee their debt, including their loan obligations to MFABC. In our view, the province has played a key role in shaping and sustaining the municipal sector's credit strength. Its legislation requires municipalities to, among other things, consult with the public and obtain the acceptance of member municipalities before taking on debt; adhere to prescribed debt servicing ceilings; limit the use of debt proceeds to capital infrastructure; and adopt balanced annual operating budgets. Furthermore, while instances of municipal distress have been rare, B.C. has a record of supporting those

in need through loan workouts and other measures. These factors, in concert with what we judge to be municipalities' generally conservative management practices and, more importantly, their solid local economies, have contributed to the sector's fairly modest leverage, ample liquidity, and consistently strong operating and after-capital financial results;

- The strong legal framework through which it borrows on behalf of members. MFABC withholds 1% of each loan obligor's gross cash request in a debt reserve fund (DRF) for the life of their loans. It would draw on the DRF if delinquencies in the loan portfolio impaired its ability to meet sinking fund contributions or debt payments. The authority has the unfettered ability to levy a property tax on all taxable land and improvements in B.C. to recoup a potential shortfall in the DRF. It has never experienced a default in its loan portfolio, so it has never needed to draw on the DRF nor levy a property tax for DRF purposes. Nevertheless, it is registered as a claimant on local tax bills, which we think mitigates the risk of a delay in accessing the property tax base. In our opinion, MFABC's ability to levy a province-wide property tax creates a de facto joint and several liability among B.C.'s municipalities in respect of its debt obligations; and
- Its solid liquidity profile. MFABC maintains a C\$200 million on-demand bank facility, as well as two C\$250 million banks lines that backstop its C\$500 million commercial paper program. It also has access to sinking funds and the DRF for liquidity purposes. The sinking fund and DRF totaled about C\$1.35 billion, or about 22% of total debt outstanding, as at Dec. 31, 2009. In addition, we think the authority has demonstrated strong access to the capital markets, even during periods of capital market stress.

In our view, the following factors offset these strengths somewhat:

- The significant increase in its debt burden to meet members' demand for loans. We project MFABC's debt burden (net of sinking funds) to potentially reach about C\$6.2 billion by 2012, from about C\$5.0 billion as at Dec. 31, 2009. As a proportion of its members' consolidated operating revenue, we project the authority's debt burden to potentially reach about 65% by 2012, from about 53% in 2009. This is little changed from what we forecasted last year. We expect MFABC's net new issuance go to Metro Vancouver's water and sewer utilities, other regional district governments, and TransLink in about equal portions. In our view, members' continued strong operating growth and operating surpluses, which underpin their abilities to service their loans, will be important in keeping the authority's debt burden consistent with the 'AAA' rating; and
- The large single-name concentrations in its loan portfolio. Metro Vancouver and the region's transportation provider, TransLink, accounted for about 55% of the loan portfolio, although this was down from about 57% in 2006. The concentration is consistent with the population distribution in B.C., where close to 60% of people live in Metro Vancouver. As a result, we believe the credit qualities of these two entities are important components of the overall credit quality of the authority's loan portfolio.

Outlook

The stable outlook reflects our expectations that B.C. municipalities' consolidated operating revenue growth and operating surpluses will remain in line with the average of the past five years, and that the sector's overall debt will remain comparable with those of 'AAA' rated municipalities outside the U.S. We also expect the authority's new issuance to remain in line with our expectations. Larger-than-expected borrowing, a material change in MFABC's powers, or a significant and sustained retrenchment in members' operating revenue growth and operating surpluses relative to historical averages could place downward pressure on the ratings.

Related Criteria And Research

Rating International Local And Regional Governments, Jan. 5, 2009

Ratings List

Ratings Affirmed

Municipal Finance Authority of British Columbia

Issuer credit rating	AAA/Stable/A-1+
Senior unsecured debt	AAA
Commercial paper	
Global scale	A-1+
Canada scale	A-1(High)

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