Moody's

Rating Action: **Moody's assigns first-time issuer rating of Aaa to British Columbia Investment Management Corporation; outlook stable**

10 Oct 2023

Toronto, October 10, 2023 -- Moody's Investors Service (Moody's) assigns a long-term issuer rating of Aaa to British Columbia Investment Management Corporation (BCI). In the same action, Moody's assigned a Baseline Credit Assessment (BCA) of aa2 and a senior unsecured rating of (P)Aaa to BCI's senior unsecured shelf. The outlook is stable.

RATINGS RATIONALE

BCI's Aaa issuer rating reflects its aa2 BCA, a high assumption of extraordinary support from the Province of British Columbia (BC, AAA stable), and our expectation that BCI creditors will have an effective priority claim over BCI's pension clients in the event of default, which provides a substantial cushion of assets and increases expected recoveries. BCI, in contrast to a pension fund, has no direct financial responsibility to fund the pension obligations of its pension clients, nor to fund the financial obligations of its non-pension clients. As such, the assets of the pooled funds are legally owned by BCI. BCI's BCA also considers the pension manager's good liquidity, conservative financial policies, and low leverage. These strengths are offset by a high level of less-liquid assets and a high proportion of high-risk assets as defined by Moody's.

BCI was established under the Public Sector Pension Plan Act (1999) (PSPPA) to provide investment management services to public sector pension and other clients in BC. The PSPPA establishes BCI as an agent of the government of the Province of British Columbia. However, the PSPPA does not mandate public sector pension plans and other clients to use BCI, but rather they have voluntarily chosen BCI as their investment/asset manager. Moody's notes that BCI has contracted with its clients, with any client withdrawals subject to BCI meeting its obligations, including funding obligations. BCI invests on behalf of over 30 public sector clients, including pension plans that provide pensions to more than 725,000 pension plan beneficiaries and 2.5 million workers in BC, and insurance funds that provide coverage for BC workers and auto insurance policy holders.

As an asset manager, BCI is not responsible for the administration of pension benefits, nor in setting actuarial assumptions of the underlying pension obligations. Rather both are the responsibility of BCI's pension plan depositors. As such, we consider BCI to be fully funded for analytical purposes since it cannot have a pension shortfall or surplus. That said, BCI does have some limited visibility around net depositor contributions or withdrawals, although BCI does regularly communicate with the BC Pension Corporation, which administers the cash flows for BCI's pension plan depositors, and its insurance clients.

Most of the assets under management are held in pooled investment portfolios (pooled funds) established by BCI pursuant to the Pooled Investment Portfolio Regulation issued pursuant to the PSPPA. As of December 31, 2022, approximately 87% per cent of BCI's total AUM was held in pooled funds, while 69% of BCI's total AUM was held in recourse pooled funds. However, BCI does maintain access and control over the remainder of the AUM in its pooled funds, including using these assets to facilitate meeting the funding obligations of its pension plan depositors.

BCI has good coverage of liquid assets to cash obligations, with a ratio of discounted liquid asset inflows to recognized obligation outflows of 184% as of 31 December 2022, which is supported by high levels of federal and provincial debt securities that offsets the limited visibility around net contribution flows from depositors. However, this ratio is at the lower end of its Canadian peers. In addition, BCI has a modest level of asset encumbrance from government bond repurchase agreements, with approximately 7.1% of gross assets funded by repos as of 31 December 2022, which is in line with the Moody's-rated pension peer average for 2022. Unlike its Canadian peers, BCI currently does not have any unsecured borrowings outstanding.

With a ratio of high-risk assets to gross assets of 55%, BCI's high risk asset exposure is at the lower end of Moody's-rated pension fund peer group. BCI has a comparably lower rate of less-liquid Level 3 assets such as infrastructure and renewable resources, and private equity relative to peers; however, like its peers, BCI's Level 3 assets have grown in recent years, representing 32% of gross assets as of 31 December 2022. While these asset classes align to BCI's depositor-driven mandates to invest with a long-term horizon and offer attractive risk-adjusted returns, they also add incremental liquidity and operational risks to the funds BCI manages on behalf of depositors. These risks are somewhat mitigated by BCI's investment portfolio being well diversified globally with almost two-thirds invested in Canada and the US. The exposure to outside of North America provides diversification away from the geographic location of its depositor pension obligations and related contribution cash flows.

For the fiscal year ending 31 March 2023, BCI posted an annualized investment return of 3.5% for its Combined Pension Plan depositors, which was above its benchmark return of 0.3%. Pension plan assets grew by CAD4.6 billion in fiscal 2023. Over a 10-year and 20-year period, BCI generated an annualized return of 8.5% and 8.4%, respectively, for its Combined Pension Plan clients compared to a benchmark return of 7.2% and 7.5%, respectively.

BCI's financial policies are broadly conservative, with the pension manager having good liquidity and risk management practices, which to date have mitigated a very modest level of leverage that creates refinancing and counterparty risks. BCI hedges currency risks within its investment portfolios. About two-thirds of BCI's investment portfolio is in USD or CAD, which aligns with its creditor obligations, much of which is denominated in CAD.

Governance was a key driver in Moody's rating action. Moody's considers that BCI's governance practices and risk management framework is aligned with the Canadian financial services sector, which includes a defined risk appetite statement as well as risk and performance benchmarks. The majority of BCI's board of directors are appointed independently, although three of its seven board members are appointed by the Minister of Finance of the Province of BC.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Given BCI's Aaa issuer rating, an upgrade is not possible. An upgrade to BCI's aa2 BCA could be driven by a sustained decrease in BCI's high risk assets or a sustained increase in liquidity.

BCI's BCA could be downgraded if there was a material reduction in the pension manager's liquid assets or a sustained and material increase in leverage above 15%. The BCA could also be downgraded if there was a change in BCI's governing legislation or a legal precedent that casts doubt on the status of BCI's obligations as having preference over pension obligations, although we view the probability of this occurring to be very low given the publicized and political nature of such an act. However, a downgrade in the BCA would not likely result in a downgrade of the long-term issuer rating because of our expectation of extraordinary support.

A downgrade in the rating of the Province of BC would lower BCI's BCA and its Aaa issuer rating as it is a BCA constraint.

British Columbia Investment Management Corporation is a public pension manager headquartered in Victoria, Canada, with total assets under management of CAD234.3 billion as of 31 March 2023.

The methodologies used in these ratings were Public Pension Managers Methodology published in February 2020 and available at https://ratings.moodys.com/rmc-documents/65347, and Government-Related Issuers Methodology published in February 2020 and available at https://ratings.moodys.com/rmc-documents/64864. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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At least one ESG consideration was material to the credit rating action(s) announced and described above.

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Robert Colangelo
VP - Senior Credit Officer

Financial Institutions Group
Moody's Canada Inc.
70 York Street
Suite 1400
Toronto, ON M5J 1S9
Canada
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Robert M. Callagy
Associate Managing Director
Financial Institutions Group
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Releasing Office:
Moody's Canada Inc.
70 York Street
Suite 1400
Toronto, ON M5J 1S9
Canada
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

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