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INVESTORS SERVICE

CREDIT OPINION
23 October 2017

Update

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RATINGS

First Nations Finance Authority

Domicile	British Columbia, Canada
Long Term Rating	A2
Type	LT Issuer Rating - Dom 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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First Nations Finance Authority

Update Following Recent Rating Action

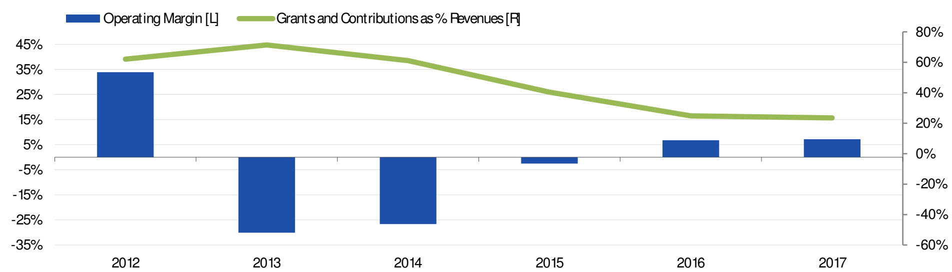
Summary Rating Rationale

FNFA's A2 ratings reflect the continued strong operating performance and sound institutional framework and governance of FNFA, and improved diversification and solid credit quality of its borrowing members. FNFA's ratings remain constrained by geographic and single-name concentration of the loan portfolio despite improved diversification, and FNFA's relatively short borrowing and operating history.

FNFA's institutional framework and governance and management structure provide debenture holder security, including structural mechanisms from a debt reserve fund (5% of outstanding borrowing), credit enhancement fund and sinking fund, and the joint and several obligation of borrowing members to replenish the debt reserve fund in case of a shortfall. This is supported by extensive membership requirements of a First Nation to become a borrowing member and be granted a loan from FNFA.

Exhibit 1

FNFA continues to see lower reliance on government grants and contributions, and stronger operating profitability



Source: Moody's Investors Service, FNFA financial statements

Credit Strengths

» Strong oversight and intervention power support quality of loan portfolio

» Reserve funds provide additional credit protection

» Solid governance and management structure

» Increasing diversification of the loan portfolio

Credit Challenges

» Rapid growth adds pressure on relative reserve levels

» Limited track record of operations and reliance on government grants

Rating Outlook

The outlook is stable, reflecting our expectations of FNFA's continued stable institutional framework, continued solid operating performance and ongoing diversification of the borrowing base.

Factors that Could Lead to an Upgrade

» Sustained improvement in the credit quality, size and diversity of the participant pool

» Increase in liquidity relative to outstanding debt

Factors that Could Lead to a Downgrade

» Sustained deterioration in the size, diversity or credit quality of the loan portfolio or participant pool

» Material reduction in reserves

» Indications of dilution of support from the federal government

Recent Developments

On October 17, 2017, Moody's upgraded FNFA's issuer and senior unsecured debt ratings to A2 and revised its baseline credit assessment of baa1. At the same time, the outlook was revised to stable from positive.

Key Indicators

Exhibit 2

First Nations Finance Authority

(Year Ending 3/31)	2013	2014	2015	2016	2017
Total Direct Debt (C$000)	20,776	54,049	107,736	249,840	315,978
Loans Outstanding to Clients (C$000)	20,778	54,143	103,367	246,022	308,569
Total Cash and Investments (C$000)	12,237	13,597	19,820	33,008	59,319
Interest Income as % of Revenues	19.2	33.4	56.4	69.8	71.5
Net interest margin (%)	0.10	0.11	0.16	0.21	-0.03
Operating Margin as % of Revenues	-30.1	-26.7	-2.6	6.8	7.2
Cash and Investments as % of Net Debt	119.1	30.9	21.4	14.7	22.1

Source: Moody's Investors Service, FNFA financial statements

Baseline Credit Assessment

The A2 ratings of FNFA reflect the application of Moody's Joint Default Analysis rating methodology for government-related issuers. In accordance with this methodology, Moody's first establishes the baseline credit assessment (BCA) of baa1 for FNFA, and then considers the likelihood of extraordinary support from the Government of Canada (Aaa stable) in the event that FNFA faced acute liquidity stress, should this unlikely scenario occur.

Profile

The First Nations Finance Authority (FNFA) is a non-profit organization without share capital that serves First Nation governments. It is one of three First Nation-led national institutions legislated under the First Nations Fiscal Management Act by the Government of Canada. The First Nations Fiscal Management Act (FNFMA) came into force on 1 April 2006 and established three institutions (1) First Nations Finance Authority (FNFA), (2) First Nations Tax Commission (FNTC) and (3) First Nations Financial Management Board (FMB).

FNFA acts as a central borrowing agency for financing capital requirements and economic and social development projects of member First Nations. In addition to providing long-term capital financing for member First Nations, the stated objectives of the Authority include the provision of interim financing and short-term investment opportunities for First Nations. FNFA is not an agent of the crown nor a crown corporation; obligations of FNFA are not obligations of Canada and are not guaranteed by the federal government.

Detailed Rating Considerations

STRONG OVERSIGHT AND INTERVENTION POWER SUPPORT QUALITY OF LOAN PORTFOLIO

The quality of FNFA's loan portfolio is supported by a stringent qualification process for becoming a borrowing member, a revenue interception mechanism and debt coverage ratio covenants as well as strong intervention powers granted to the authority under the FNFMA.

A First Nation must first request to the Minister of Indigenous and Northern Affairs Canada (INAC) to be scheduled to the FNFMA, which sets out its obligations including obligations to FNFA. A potential member must then pass a band council resolution to apply to become a member and satisfy certification requirements with the FMB, which is responsible for financial management system certification for First Nations. As part of this certification process, FMB analyzes the financial performance of the First Nation. FMB also aids the First Nation in developing a Financial Administration Law, which outlines the decision making, management, monitoring and reporting with respect to financial administration of the First Nation. Moreover, in addition to the requirement of FMB certification, a First Nation must also gain unanimous approval of the FNFA board before becoming a member. This multi-step membership process aids in maintaining the credit quality of borrowing members and by extension, the loan portfolio.

The FMB conducts regular monitoring and oversight of borrowing members and has the power to intervene and arrange a co-management arrangement or third-party management of a First Nation's revenues if necessary. The FNFA also has the power to request intervention by the FMB if the First Nation fails to make a payment or fulfill an obligation under its Borrowing Agreement. The FMB has the power to take control over the treasury functions of a borrowing member that has received a loan and then has access to all revenue streams of that borrowing member.

Furthermore, the FNFMA outlines the uses for which a First Nation can borrow. Namely, it states that members can borrow for capital infrastructure when borrowing is supported by property tax, and for economic and community infrastructure when borrowing is supported by other revenues, such as for capital infrastructure and land.

Once a borrowing agreement is signed with a borrowing member, an irrevocable intercept mechanism, a Secured Revenue Trust Account (SRTA), is put in place to capture the revenue stream used to support the First Nation's loan. The trust account diverts the gross revenues of those revenues that will be used against borrowing following minimum debt coverage ratios (DCR); anything in excess of that needed for the borrowing is then diverted back to the First Nation. These DCRs depend on the type of pledged revenues in support of the loan, i.e. higher debt coverage ratios are required for higher risk revenues such as land benefit agreements versus government transfers. Invoicing is also based on revenue frequency, so if revenue streams are received monthly, monies toward repayment will be collected monthly and prior to debt service payments. This allows extra time to resolve any issues prior to any debt service payments.

RESERVE FUNDS PROVIDE ADDITIONAL CREDIT PROTECTION

FNFA maintains two important reserve funds: five percent of all loan requests are held in the Debt Reserve Fund (DRF) and the Canadian government has provided CAD30 million of funding which is held in the Credit Enhancement Fund (CEF).

As the loan portfolio continues to increase, the DRF has grown in constant proportion. As of September 30, 2017, the DRF measured CAD20.8 million, and is expected to double by 2019/20. The DRF provides liquidity in the event of non-payment by a borrowing member. Assets in the DRF are invested mostly in liquid securities. Should there be a non-payment on an obligation, the FNFA would first work to recover the payment but can also tap into the DRF. In case of a shortfall in the DRF all borrowing members would be required to replenish the DRF without limit. As debt coverage ratios are set above required debt service payments, this allows FNFA to replenish the DRF directly from the Secured Revenue Trust Account.

After an initial contribution of CAD10 million to the CEF following FNFA's initial debenture issuance in 2014, the Canadian government has twice increased this amount raising it to CAD30 million. The CEF can be used to temporarily offset shortfalls in the DRF, providing additional protection to bondholders.

In addition to the liquidity provided by FNFA's reserve funds (DRF and CEF), the Authority also earns income through its pooled investment activities and has access to CAD175 million revolving credit facility (recently increased from CAD130 million) with several Canadian chartered banks for financing loans to borrowing members.

SOLID GOVERNANCE AND MANAGEMENT STRUCTURE

FNFA's Board of Directors currently consists of nine directors. The Board is elected by borrowing and investing members, but only borrowing members can be elected to the Board. The terms are one year and renewable. With the latest election in July 2017, geographical representation of the Board continued to be diversified, which was a key objective of FNFA.

Borrowing members are First Nations that have applied to and have been accepted by the Authority's Board as a borrowing member. Investing Members are First Nations that have invested in the Authority's Pooled Investment Funds.

The Act restricts the spectrum of allowed investments to fixed-income securities issued or guaranteed by Canadian governments or Canadian chartered banks or savings institutions. No equity investments are allowed. FNFA has conservative debt and investment management policies, which limits its exposure to market-related risks.

Furthermore, there is an extensive credit approval process. First Nations borrowing through the Authority must meet financial certification requirements and each loan requested from the Authority must be reviewed by the Board and Members of the Authority and receive unanimous approval prior to funding. The annual operating budget is also approved by the Board.

INCREASING DIVERSIFICATION OF THE LOAN PORTFOLIO

Although still facing some geographic concentration with a sizeable pool of borrowing members located in the Province of British Columbia (Aaa stable), the concentration of FNFA's borrowing portfolio nonetheless continues to diversify with each debenture issuance, although some geographic and single-name concentration remains. The participating borrowing members reached 43 as of September 30, 2017, up from 13 in the original 2014 debenture issuance. An additional 29 First Nations have been approved to become borrowing members.

RAPID GROWTH ADDS PRESSURE ON RELATIVE RESERVE LEVELS

FNFA targets continued strong growth of its loan portfolio and debenture issues over the next four years. Since completing its first debenture issue (CAD90 million in 2014), we estimate that FNFA's total direct debt, reflecting the most recent debenture issue, has grown to CAD377 million. The rapid growth of the loan portfolio imposes challenges on FNFA in maintaining adequate reserve levels relative to total outstanding borrowing.

By structure FNFA will continue to transfer 5% of all loan proceeds into the DRF. As a result, the DRF will continue to increase as FNFA's loan portfolio increases. In addition, we expect that the CAD10.7 million sinking fund will increase over the medium-term as borrowers continue to repay principal under their amortizing loans well in advance of the first debenture maturity in 2024. However, as the loan portfolio grows, the CAD30 million CEF will represent a gradually declining portion of borrowing. Therefore although the absolute level of liquidity will increase in the medium term, the relative level of liquidity will represent a stable or slightly declining share of borrowing over the medium-term.

LIMITED TRACK RECORD OF OPERATIONS AND RELIANCE ON GOVERNMENT GRANTS

FNFA has a limited track record of operating as a specialized lender, which is reflected in negligible net interest margins as well consolidated deficits until 2015. FNFA also receives a significant portion of its revenues through grants and contributions from Indigenous and Northern Affairs Canada (INAC). The share of federal grants relative to total revenue fell from over 70% in 2012/13 to less than 24% in 2016/17 while at the same time the importance of interest from borrowing members has grown. Nonetheless, total grants and contributions have continued to increase, reaching CAD2.9 million in 2016/17 compared to CAD1.5 million in 2013/14, reflecting FNFA's ongoing reliance on these funds for its operations. We anticipate that FNFA will continue to rely in the intermediate term on grants from INAC, highlighting the need for ongoing support from the federal government to FNFA.

We project that FNFA will improve net interest margins over the next several years. As FNFA continues to build its loan portfolio, we expect that higher initial operating costs should decline, supporting modest improvements in its operating performance and modest surpluses going forward.

Extraordinary Support Considerations

The Joint-Default Analysis methodology also considers the likelihood of extraordinary support coming from the Government of Canada (Aaa stable) to prevent a default by the FNFA. Moody's assigns a strong likelihood of support, reflecting the creation and support of FNFA and supporting institutions by Canada through legislation as well as the important government-defined mandate of the FNFA in providing financing for First Nations in Canada.

Moody's also assigns a very high default dependence level between FNFA and the Government of Canada, reflecting the two entities' shared exposure to common economic and financial risks.

Ratings

Exhibit 3

Category	Moody's Rating
FIRST NATIONS FINANCE AUTHORITY	
Outlook	Stable
Issuer Rating -Dom Curr	A2
Senior Unsecured -Dom Curr	A2

Source: Moody's Investors Service

REPORT NUMBER 1096065

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