MOODY'S
INVESTORS SERVICE

CREDIT OPINION
13 July 2016

Update

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RATINGS

First Nations Finance Authority

Domicile	British Columbia, Canada
Long Term Rating	A3
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

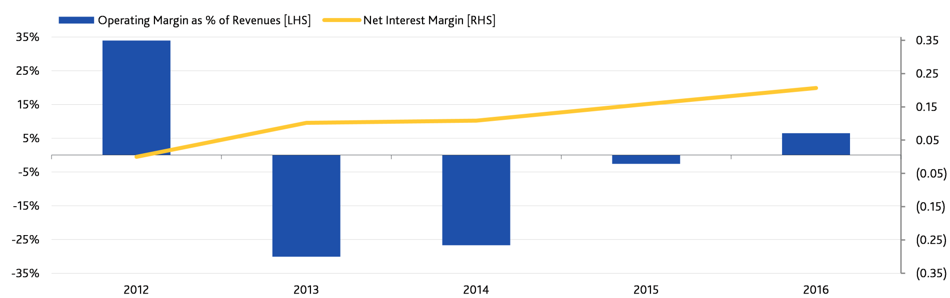
Update Following Recent Rating Action

Summary Rating Rationale

FNFA's A3 ratings reflects (1) the improved borrower and geographic diversification of the loan portfolio; (2) solid debt service coverage ratios; (3) a sound institutional framework and governance and management structure, (4) the oversight of borrowing members by the First Nations Financial Management Board; and (5) the strong likelihood of extraordinary support from the federal government.

The rating remains constrained by historical volatility in FNFA's profitability, relatively high, although declining, geographic concentration of borrowers in the Province of British Columbia, and FNFA's relatively short operating history. FNFA's institutional framework and governance and management structure provide debenture holder security, including structural mechanisms such as debt reserve funds (5% of outstanding debenture debt), a CAD10 million credit enhancement fund (with a federal commitment to increase it to CAD30 million over the next 12 months), a CAD2.1 million sinking fund which is expected to increase in the next few years, as well as a debt reserve fund replenishment requirement of all borrowing members. This is supported by extensive requirements that need be fulfilled in order for a First Nation to become a borrowing member and be granted a loan from FNFA.

Exhibit 1
Stable growth in loan portfolio has lead to increased operating profitability



Source: Moody's, FNFA financial statements

Credit Strengths

» Strong oversight and monitoring power support quality of loan portfolio

» Reserve funds provide additional protection to bondholders

» Solid governance and management structure

» Increasing diversification of borrowing portfolio

Credit Challenges

» Rapid growth adds pressure on operations and relative reserve levels

» Limited track record and marginal profitability

Rating Outlook

The outlook is stable, which reflects FNFA's improved operating performance and improved seniority ranking of the debentures.

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

In February 2016, FNFA's outstanding debentures were made pari passu in seniority ranking with its CAD130 million secured revolving credit facility. As a result, the debentures are no longer subordinated to the credit facility. This is important because bondholder positions would not be weakened by a higher amount of secured debt outstanding.

Key Indicators

Exhibit 2

(Year Ending 3/31)	2012	2013	2014	2015	2016
Total Direct Debt (C$000)		20,776	54,049	107,736	249,840
Loans Outstanding to Clients (C$000)		20,778	54,143	103,367	246,022
Total Cash and Investments (C$000)	11,638	12,237	13,597	19,820	33,008
Interest Income as % of Revenues		19.2	33.4	56.4	69.8
Net interest margin (%)		0.10	0.11	0.16	0.21
Operating Margin as % of Revenues	33.9	-30.1	-26.7	-2.6	6.5
Cash and Investments as % of Net Debt		119.1	30.9	21.4	14.7

Source: Moody's, FNFA financial statements

Detailed Rating Considerations

The A3 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 baa2 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.

Baseline Credit Assessment

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 infrastructure when borrowing supported by property tax and for economic and community infrastructure tied to social and economic development when borrowing supported by other revenues, such as for capital infrastructure and land. Currently all outstanding borrowing is only supported by other revenues and not property tax revenue.

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 PROTECTION TO BONDHOLDERS

With the recent CAD111 million reopening of its debenture, FNFA's outstanding debenture debt (due 2024) currently measures CAD251 million. As of March 31, 2016, FNFA had cash and investments on balance sheet of CAD33.0 million (around 15% of direct debt). Cash and investments include the Credit Enhancement Fund (CEF) of CAD10 million received from the Government of Canada as well as a Debt Reserve Fund (DRF) of CAD12.5 million. Following the reopening of the existing debenture, we expect the DRF to increase to around CAD18 million (9% of total outstanding debentures).

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.

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 CAD130 million secured revolving credit facility with three Canadian chartered banks for the financing of interim loans.

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 2015, 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 BORROWING PORTFOLIO

The concentration of FNFA's borrowing portfolio has diversified with the recent CAD111 million reopening of the debenture. The total outstanding debenture now amounts to CAD251 million and includes 29 participating borrowing members (up from the 13 original members). In addition, FNFA expects to continue fully utilizing its CAD130 million secured revolving credit facility in order to finance interim loans. We assume that outstanding amounts under the revolving credit facility will be refinanced with new debentures over time.

The majority of current borrowing members that received loans benefit from positive operating results. The 29 current borrowing members recorded a median consolidated surplus/revenue of 5.3% in 2015-16.

RAPID GROWTH ADDS PRESSURE ON OPERATIONS AND RELATIVE RESERVE LEVELS

FNFA's loan portfolio has grown considerably to CAD254 million at March 31, 2016 from CAD54 million at March 31, 2014, and FNFA targets continued strong growth of its loan portfolio over the next 12 months. The rapid growth of the loan portfolio imposes challenges to FNFA's relatively young organization in terms of maintaining adequate lending practices, improving operating performance as well as maintaining healthy reserve levels relative to total outstanding debt.

By structure, the DRF will equal 5% of outstanding debenture debt, while we expect the CAD2.1 million sinking fund to increase over the next few years as borrowers begin to repay principal under their amortizing loans. Given a recent commitment by the federal government, the CEF will be increased to CAD30 million from the current CAD10 million in two stages over the next year. As a result, we expect that the absolute level of liquidity will increase in the medium term. Nevertheless, as we project that the growth in FNFA's debt will outpace the growth in reserves, the level of liquidity will represent a stable (or slightly declining) but comfortable share of debt.

LIMITED TRACK RECORD AND MARGINAL PROFITABILITY

FNFA has a limited track record of operating as a specialized lender, which is reflected in a negligible net interest margin of 0.21% and consolidated deficits between 2012 and 2015. In its start-up phase as a lender FNFA has received most of its revenues through grants and contributions from Indigenous and Northern Affairs Canada (INAC). The share of federal grants relative to total revenue (25% in 2015-16) has been declining from 71% in 2012-13, and interest on client loans now accounts for the majority of revenue (70% in 2015-16, up from 19% in 2012-13). We anticipate that FNFA will continue to benefit in the intermediate term from grants from INAC, highlighting the support from the federal government to FNFA. Furthermore, we project FNFA to improving net interest margins over the next several years. However, 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	A3
Senior Unsecured -Dom Curr	A3

Source: Moody's Investors Service

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