

## Business Development Bank of Canada

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# Business Development Bank of Canada

## Major Rating Factors

### Strengths:

- Status as an agent Crown Corporation (an agent of Her Majesty in right of Canada)
- 100% government ownership
- The provision that its debt constitutes a direct obligation of the Government of Canada and is a charge on, and payable out of, the central government's Consolidated Revenue Fund
- Stable track record of financial self-sustainability on core lending business
- Good capitalization

### Counterparty Credit Rating

AAA/Stable/A-1+

### Weaknesses:

- High-risk nature of the mandate, which focuses on small and midsize enterprises, including subordinate financing investments and venture capital equity investments

## Rationale

The ratings on Business Development Bank of Canada (BDC) reflect Standard & Poor's Ratings Services' assessment of the following factors:

- The bank's status as an agent Crown Corporation (an agent of Her Majesty in right of Canada);
- Its ownership by the Government of Canada (AAA/Stable/A-1+); and
- The provision that BDC's debt constitutes a direct obligation of the government and is a charge on and payable out of its Consolidated Revenue Fund (CRF).

Although BDC normally services debt from its own resources, its obligations are full-faith and credit obligations of Canada, with access to the CRF assuring the timeliness of debt service. Because of this, we have equalized the ratings on the bank with those on its owner.

In addition, BDC has a stable track record of financial self-sustainability on its core business of providing long-term loans to Canadian businesses, especially small and midsize enterprises (SMEs). Such loans have for many years accounted for 80%-90% of total assets, and more than 75% of revenue; in fiscal 2010 these loans dipped to 72% of total assets, as BDC took on responsibility for administering the temporary Canadian Secured Credit Facility (CSCF), expanding its balance sheet by C\$3.3 billion (27% of 2009 total assets) as a result. Net interest income from loans, together with the much smaller line of subordinate financing loans and investments, has held at about 4%-5% of average assets, always positive, in each of the past 15 fiscal years. This stability has more than offset habitual-but-minor losses (below 3% of average assets) on venture capital investments and consulting. Overall, return on assets has declined slowly during fiscals 2006-2009 (to 0.8% from 1.4%), and fell dramatically in fiscal 2010 (to almost zero), although this measure avoided negative territory. Return on equity followed a similar pattern, declining slowly during fiscals 2006-2009 (to 4.5% from 8.5%) and then dropping sharply in fiscal 2010 (to 0.2%), although still avoiding a loss. By both measures, BDC has avoided a net loss in each of the past 15 fiscal years (and,

in many years, been quite profitable).

Moreover, the bank has long been well-capitalized. Total equity to assets has been more than 16% in each of the past five fiscal years, and was 21% at March 31, 2010.

These strengths counterbalance what we view as BDC's principal credit weakness: its high-risk mandate. Canada expects the bank to concentrate on long-term loans, subordinate financing and investments, and venture capital equity investments in Canadian SMEs. Those SMEs, by their nature, are unlikely to have well-established credit histories, track records, or proven technologies. BDC's mandate means it is likely to finance businesses that would have difficulty obtaining similar financing from private-sector institutions.

Still, because it has no legislated monopoly on the provision of credit to any Canadian business sector, in our opinion it does not face policy environment pressures akin to those faced by the Canadian Wheat Board (AA/Stable/--). On the contrary, with recession and the global financial crisis, the Canadian government has lately been encouraging BDC to play a larger role in credit provision to the private sector. As part of the temporary, countercyclical Extraordinary Financing Framework announced in its 2009 budget, the government created both the Business Credit Availability Program (BCAP) and the CSCF. BDC participates jointly in the BCAP, together with Export Development Canada (senior unsecured debt rating: 'AAA') and private-sector banks. Together these lenders were mandated to provide an additional C\$5 billion in loans and other credit support to creditworthy businesses. They have already surpassed this goal (C\$8 billion as of July, 2010), with BDC providing C\$2.8 billion (23% of fiscal 2009 assets) via BCAP. In its 2010 budget, the government added the Vehicle and Equipment Financing Partnership to the BCAP framework, with an initial allocation of C\$500 million. The CSCF could potentially have become a much larger undertaking: Here, the government mandated the bank to invest up to C\$12 billion (100% of fiscal year-end 2009 assets) in 'AAA' rated asset-backed securities (ABS) backed by loans and leases on vehicles and equipment, purchased from regulated financial institutions. By the CSCF's expiry (March 31, 2010), BDC had in fact purchased only C\$3.3 billion (27% of 2009 total assets) of such ABS. We expect the BCAP will also expire on schedule (by March 31, 2011). The government provided additional capital to BDC, to help it handle its larger role, injecting C\$350 million in 2009 and C\$1.5 billion in 2010, as well as promising a further C\$225 million by the end of fiscal 2012.

Since April 21, 2008, Canada has met all of BDC's borrowing needs by direct lending (effectively consolidating the bank's borrowing with that of Canada). The bank's debt issued before then remains outstanding, with the support structure described above (involving the CRF) unchanged as far as such debt is concerned.

## Outlook

The stable outlook on BDC mirrors that on Canada, and reflects Standard & Poor's expectation that the bank will continue to play an important role in Canadian public policy. Policy developments that, in our opinion, signal noticeably waning government support for BDC would be required to cause us to detach the rating and outlook on BDC from those on its owner.

## Related Criteria And Research

Rating Sovereign-Guaranteed Debt, April 6, 2009

## Business Development Bank of Canada--Financial Statistics

--Year ended March 31--

(C\$000s)	2010	2009	2008	2007	2006
Assets	17,679,927	12,090,911	11,423,566	10,804,081	10,311,423
% change	46.22	5.84	5.73	4.78	9.17
Loans (net)*	12,718,724	10,607,243	9,637,607	8,770,936	8,273,781
% change	19.91	10.06	9.88	6.01	9.11
Total equity	3,643,016	2,189,564	1,867,317	1,807,718	1,691,277
% change	66.38	17.26	3.30	6.88	7.75
Revenues	572,743	697,413	520,204	536,584	522,737
% change	(17.88)	34.07	(3.05)	2.65	12.63
Noninterest expense	350,150	304,230	299,405	296,006	270,219
% change	15.09	1.61	1.15	9.54	8.51
Net oper income before loss provisions¶	222,593	393,183	220,799	240,578	252,518
% change	(43.39)	78.07	(8.22)	(4.73)	17.39
Loss provisions (LP)	216,534	302,616	136,236	102,571	114,337
% change	(28.45)	122.13	32.82	(10.29)	12.52
Net income	6,059	90,567	84,563	138,007	138,181
% change	(93.31)	7.10	(38.73)	(0.13)	21.76
<b>Profitability(%)</b>					
Revenues/average assets	3.94	6.09	4.79	5.08	5.29
Net interest income/average assets	4.41	4.85	4.54	4.38	4.39
Non-interest income/average assets	(0.47)	1.25	0.25	0.70	0.91
Non-interest expense/average assets	2.41	2.66	2.76	2.80	2.74
Net operating income before LP/average assets	1.53	3.43	2.03	2.28	2.56
LP/average assets	1.49	2.64	1.25	0.97	1.16
Net income/average assets (ROA)	0.04	0.79	0.78	1.31	1.40
Net interest income/revenues	111.97	79.56	94.74	86.14	82.88
Non-interest income/revenues	(11.97)	20.44	5.26	13.86	17.12
Non-interest expense/revenues	61.14	43.62	57.56	55.16	51.69
Net operating income before LP/revenues	38.86	56.38	42.44	44.84	48.31
LP/revenues	37.81	43.39	26.19	19.12	21.87
Net income/revenues	1.06	12.99	16.26	25.72	26.43
Net income/average total equity (ROE)	0.22	4.53	4.75	7.89	8.48
<b>Liquidity (%)</b>					
Loans (net)/assets	71.94	87.73	84.37	81.18	80.24
<b>Capital (%)</b>					
Total equity/assets	20.61	18.11	16.35	16.73	16.40
Total equity/loans (net)	28.64	20.64	19.38	20.61	20.44
Dividend payout ratio§	236.29	17.62	25.42	15.63	11.92
<b>Asset quality (%)</b>					
LP/average purpose-related portfolio (gross)**	1.50	2.71	1.33	1.08	1.30
Loan loss provisions¶¶/average loan portfolio (gross)	2.10	2.08	1.04	0.75	1.05

**Business Development Bank of Canada--Financial Statistics (cont.)**

Loan loss reserves/loan portfolio (gross)	5.82	5.90	5.24	5.45	5.67
Impaired loan portfolio/loan portfolio (gross)	4.59	4.58	2.89	3.09	3.41
Loan loss reserves/impaired loan portfolio	126.57	128.82	181.52	176.44	166.09

\*Include subordinate financing assets. ¶Loss provisions include provision for credit losses, change in unrealized depreciation of both venture capital and subordinate financing assets, and loss or gain on initial recognition of asset-backed securities. §Aggregate dividend paid on preferred and common shares together. \*\*Purpose-related portfolio (gross) includes gross loans as well as subordinate financing, venture capital, and securitization assets. ¶¶Loan loss provisions include provision for credit losses and change in unrealized depreciation of subordinate financing assets.

**Ratings Detail (As Of December 20, 2010)\*****Business Development Bank of Canada**

Counterparty Credit Rating AAA/Stable/A-1+

**Counterparty Credit Ratings History**

11-Mar-2003 AAA/Stable/A-1+

**Sovereign Rating**

Canada AAA/Stable/A-1+

**Related Entities****Bank of Canada**

Issuer Credit Rating AAA/Stable/A-1+

**Canada**

Issuer Credit Rating AAA/Stable/A-1+

Transfer & Convertibility Assessment AAA

Commercial Paper A-1+

*Canadian National Scale Commercial Paper Rating* A-1(HIGH)

Senior Lien (1 Issue) AAA

Senior Unsecured (180 Issues) AAA

Short-Term Debt (2 Issues) A-1+

**Canada Mortgage and Housing Corporation**

Issuer Credit Rating AAA/Stable/A-1+

Senior Unsecured (27 Issues) AAA

**Canada Post Corporation**

Issuer Credit Rating AAA/Stable/A-1+

Senior Unsecured (2 Issues) AAA

**Canadian Wheat Board**

Issuer Credit Rating AA/Stable/--

**Export Development Canada**

Senior Unsecured (9 Issues) AAA

**Farm Credit Canada**

Commercial Paper A-1+

*Local Currency* A-1+

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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