FitchRatings

RATING ACTION COMMENTARY

Fitch Assigns Initial 'AAA'/'F1+' Ratings to Public Sector Pension Investment Board; Outlook Stable

Thu 03 Jun, 2021 - 10:04 AM ET

Fitch Ratings - New York - 03 Jun 2021: Fitch Ratings has assigned a Long-Term Issuer Default Rating (IDR) of 'AAA' and a Short-Term IDR of 'F1+' to Public Sector Pension Investment Board (PSP) and its debt-issuing subsidiary, PSP Capital, Inc. Fitch has also assigned ratings of 'AAA' and 'F1+' to PSP's unsecured debt and commercial paper (CP), respectively. The Rating Outlook is Stable.

Feedback

KEY RATING DRIVERS

PSP's ratings reflect its exceptionally strong asset overcollateralization and liquidity levels, creditor priority of debtholders to amounts coming due under the relevant pension plans, the captive nature of asset inflows, experienced management team, solid long-term investment track record, strong corporate governance, and a supportive regulatory framework. Ratings also reflect PSP's role as an investment manager, which means it is not directly responsible for the payment of pension obligations. Fitch believes this profile is incrementally favorable relative to peers that are pension funds.

Offsetting factors include the competitive investment environment, which may make it more challenging to identify attractive investment opportunities particularly at scale and the relatively high proportion of less liquid and private assets in the portfolio, which could result in higher performance volatility.

At March 31, 2020 (fiscal year-end 2020, FYE20), PSP had CAD169.8 billion of net assets, making it the fifth largest Canadian pension fund asset manager. PSP's captive contributions are highly predictable over time, and allow PSP to invest on a long-term horizon while maintaining appropriate liquidity levels. Net annual contributions averaged 2.5% of beginning of period net assets from fiscal years 2017-2020, which is strong relative to peers. PSP's assets are well-diversified by asset class, geography and industry, which mitigates the potential adverse correlation risk with developments in the Canadian economy and the risks related to the lower relative liquidity of its private investments.

PSP has a strong track record of investment performance, outperforming its total fund benchmarks by 0.7% and 1.0% on a five and 10-year basis at FYE20. Despite initial performance challenges in 2020, resulting from the coronavirus pandemic, Fitch expects PSP to generate a materially stronger annual return in FY21, driven by the rebound in asset prices in the second half of the year.

Fitch utilizes gross debt (excluding repurchase agreements and securities sold short) to net assets, as its primary leverage ratio for PSP and other pension plan investment managers, given Fitch's focus on asset overcollateralization, while liabilities from securities financing transactions could be satisfied via associated collateral. Based on this measure, leverage was 0.09x at FYE20; in line with historical levels and within Fitch's 'aa and above' benchmark range of 0.15x or lower for investment companies.

Leverage was also below PSP's internal limit for recourse debt of 0.10x, viewed favorably by Fitch. Fitch expects PSP's leverage not to materially exceed historical averages absent a substantial deterioration in asset prices. As a complementary leverage metric, Fitch also considers debt, including repurchase agreements and securities sold short, to net assets, which was a relatively low 0.19x at FYE20.

Liquidity is viewed as exceptionally strong given predictable and reliable contributions, cash on hand, liquid investments, and the ability to use net pension contributions to satisfy debt obligations. At FYE20, PSP had CAD4.8 billion in balance sheet cash and money market securities, CAD76.9 billion in marketable equity and fixed income investments and CAD3 billion of unutilized revolver capacity, split into CAD2 billion committed revolving credit facility and CAD1 billion in uncommitted demand lines of credit. This compared with

CAD15.5 billion of outstanding CP and unsecured term notes, at par. PSP did not need to access additional term funding despite outsized market volatility resulting from the pandemic.

PSP's ratings are constrained by Canada's Country Ceiling, which reflects Fitch's assessment of the transfer and convertibility risks. On June 24, 2020, Fitch downgraded Canada's IDR to 'AA+' from 'AAA', but the Country Ceiling was affirmed at 'AAA'.

The Stable Outlook reflects Fitch's expectation that PSP will maintain exceptionally strong asset overcollateralization and liquidity over the Outlook Horizon and exhibit long-term investment performance consistent with its benchmarks and reference portfolio. The Outlook also reflects Fitch's expectation that PSP will continue to operate against the backdrop of a stable operating environment in terms of sovereign credit risk, country ceiling risk and the legal and regulatory environment.

The unsecured debt rating is equalized with the Long-Term IDR, reflecting PSP's predominantly unsecured funding profile and expectations for average recovery prospects in a stressed scenario.

The Short-Term IDR and CP rating of 'F1+' reflect the strongest intrinsic capacity for timely repayment of financial commitments and maintain the correspondence between Short- and Long-Term IDRs, as the 'F1+' IDR corresponds to a long-term IDR of 'AAA' under Fitch's criteria.

SUBSIDIARY AND AFFILIATED COMPANY

The ratings assigned to wholly-owned subsidiary PSP Capital Inc. are equalized with those of its parent to reflect the full guaranty provided to PSP Capital Inc. by PSP.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Positive rating action is not possible, given the ratings are already at the highest levels on the long- and short-term rating scales.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Factors that could, individually or collectively, lead to negative rating action/downgrade include a significant reduction in liquid assets, a material increase in leverage relative to historical averages and/or PSP's own stated leverage limits, including the recourse debt limit of 0.10x, a material change in risk appetite resulting in higher performance volatility and/or a material increase in proportion of less liquid investments, particularly in an attempt to improve the funded status of the plan, weak investment performance or increased single-name or industry concentrations, or an actual or reasonably expected change in the rule of law that has the effect of calling into question credit priority;

--The ratings are also sensitive to changes in the credit risk profile of Canada, to the extent that any such changes resulted in a reduction in Canada's Country Ceiling to a level below PSP's IDR;

--The unsecured debt rating is sensitive to changes in PSP's Long-Term IDR and would be expected to move in tandem;

--The Short-term IDR is primarily sensitive to changes in the long-term IDR and secondarily to changes in PSP's Funding, Liquidity and Coverage score;

--The CP rating is sensitive to changes in PSP's Short-Term IDR and would be expected to move in tandem.

SUBSIDIARY AND AFFILIATED COMPANY

The ratings of PSP Capital, Inc. are equalized with those of its parent and would be expected to move in tandem.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579

DATE OF RELEVANT COMMITTEE

26 May 2021

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING		
PSP Capital Inc.	LT IDR	AAA Rating Outlook Stable	New Rating
	ST IDR	F1+	New Rating
• senior unsecured	LT	AAA	New Rating
• senior unsecured	ST	F1+	New Rating
Public Sector Pension Investment Board	LT	AAA Rating Outlook Stable	New Rating

VIEW ADDITIONAL RATING DETAILS

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FITCH RATINGS ANALYSTS

Evgeny Konovalov
Director
Primary Rating Analyst
+1 212 612 7839
Fitch Ratings, Inc.
Hearst Tower 300 W. 57th Street New York, NY 10019

Dafina Dunmore
Senior Director
Secondary Rating Analyst
+1 312 368 3136

Johann Juan
Senior Director
Committee Chairperson
+1 312 368 3339

MEDIA CONTACTS

Sandro Scenga
New York
+1 212 908 0278
sandro.scenga@thefitchgroup.com

Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

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ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

PSP Capital Inc.	-
Public Sector Pension Investment Board	-

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Non-Bank Financial Institutions North America United States Canada

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