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## **DBRS Assigns BBB Issuer Rating to First National Financial LP**

**Bloomberg: DBRS Assigns First National Financial LP BBB Issuer Rating**

**Industry Group: Financial Institutions**

**Sub-Industry: Non-Bank Financials**

DBRS has today assigned First National Financial LP (FNF or the Company) an Issuer Rating of BBB with a Stable trend. The rating and trend reflect FNF's status as Canada's largest non-bank mortgage originator and servicer (\$46 billion in mortgages under administration (MUA)), its strong asset quality profile, with all assets secured by real estate and a substantial portion insured, as well as its servicing capabilities.

Unlike most financial institutions, the Company funds most of its mortgage originations either through sales to institutional investors (73%) or off-balance sheet in securitization vehicles; on-balance sheet exposures are limited to a warehouse facility and a small portfolio of mortgage and loan investments, which are primarily multi-unit residential and commercial (MUR&C) bridge loans. The business model focuses on generating stable underlying cash flows from the servicing business (the Company retains servicing rights on virtually all originated mortgages) over the life of each loan.

While origination revenues have the potential to be more volatile depending on market conditions, the major costs of origination are variable (broker commissions), leading to less earnings volatility than would otherwise be the case. Efficiency is critical in the originating and servicing businesses, and FNF has gradually reduced operating expenses excluding broker commissions from 19 basis points (bps) of MUA in 2006 to 16 bps year-to-date.

While FNF is not exposed to credit risk on the majority of its MUA; it is exposed to credit risk on about \$900 million of assets, although there is security backing this exposure. The Company has been successful in the past in placing its originated mortgages with institutional investors or in securitization conduits, although there is a material level of funding concentration risk. However, earnings visibility is limited due to the nature of

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securitization accounting; revenues have the potential to be volatile depending on changes in assumptions, including discount rates, prepayment rates, credit loss estimates and spreads.

FNF is not regulated by the Office of the Superintendent of Financial Institutions (OSFI), resulting in funding and liquidity limitations as well as less stringent compliance requirements and oversight in a wide variety of areas including capital, liquidity and risk management.

FNF's pre-tax earnings have grown at a compound annual growth rate (CAGR) of 50% over the past 4.5 years, driven by CAGR in mortgages under administration of 37% and a 32% CAGR in placement fees and securitization gains over the same period. Profitability has been exceptional as measured by return on equity; if an assumed tax rate of 30% is used, FNF generated an average adjusted ROE of 57% over the past 4.5 years. The high level of profitability is largely a function of the fact that the business does not require much in the way of capital.

The pre-tax return on average MUA has improved from an average of 30 bps in the past five years to 37 bps points in the first three quarters of 2009. Spreads have already declined from the high levels achieved earlier in 2009; as a result, FNF's earnings are likely to come under pressure in 2010 relative to the very strong results achieved year to date in 2009. Credit losses will likely remain at an elevated level although they are expected to remain very low on an absolute basis.

#### Notes:

All figures are in Canadian dollars unless otherwise noted.

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The applicable methodology is the methodology for rating banks and banking organizations, which can be found on the DBRS website under methodologies. In applying this methodology, DBRS has allowed for the fact that the credit in question is not a bank. *Insight beyond the rating.*

This is a Corporate (Financial Institutions) rating.

The full report providing additional analytical detail is available by clicking on the link below or by contacting us at [info@dbrs.com](mailto:info@dbrs.com).

<u>Issuer</u>	<u>Debt Rated</u>	<u>Rating Action</u>	<u>Rating</u>	<u>Trend</u>
First National Financial LP	Issuer Rating	New Rating	BBB	Stable

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