



ISSUER COMMENT

Caisse de dépôt et placement du Québec's Infrastructure Agreement with Québec Is Credit Negative

From [Credit Outlook](#)

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On 13 January, the Caisse de dépôt et placement du Québec (the Caisse, unrated), parent of [CDP Financial Inc.](#) (Aaa stable), announced that it will establish a new subsidiary to execute major public infrastructure projects for the Canadian [province of Québec](#) (Aa2 stable). The agreement is credit negative for the Caisse and for CDP, which depends on the Caisse for its credit quality, because it affirms the Caisse's strategy to increase investment in less-liquid infrastructure projects. We believe the agreement also risks increasing the Caisse's exposure to operational and reputational risks associated with provincial infrastructure projects.

Under the agreement, this new subsidiary, CDPQ Infra, will be responsible for the planning, financing, construction and operation of projects, while the province will be responsible for identifying projects of public interest. So far, Québec has identified two public transit system projects totaling CAD5 billion as priorities, and CDPQ Infra will begin project planning once the National Assembly of Québec passes the necessary changes to the Caisse's governing legislation. Although the Caisse's future exposure to these projects has yet to be determined, at CAD5 billion, their value represents only about 2% of depositors' net assets (assets placed on deposit with the Caisse by its institutional clients, as required by law).

Between 2009 and 2013, less liquid assets (including private equity, infrastructure, and real estate) as a proportion of depositors' net assets fell to 30% from 31% (see Exhibit 1). These investments align well with the long-term nature of the Caisse's operating model as an asset manager for Québec's public depositors. However, they tend to suffer from price opacity and additional risk measurement complexity because of a lack of market data. Relative to traditional asset classes, associated risk assessment is typically more complex and requires robust risk management oversight.

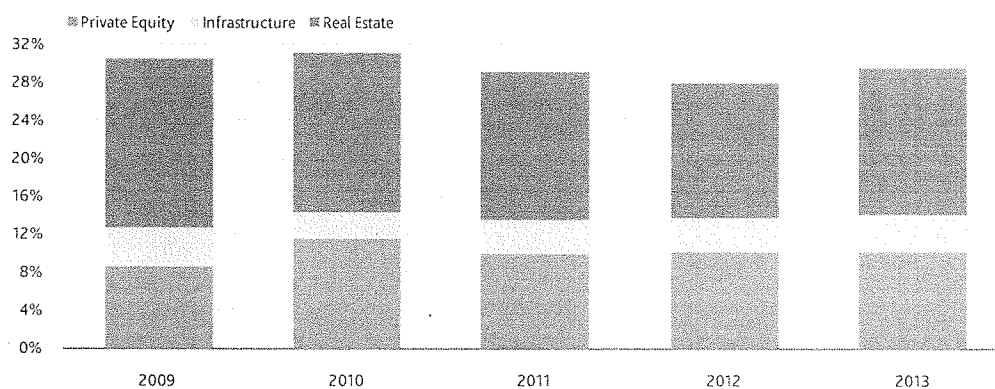
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EXHIBIT 1

Caisse de dépôt et placement du Québec's Alternative Assets as a Portion of Depositors' Net Assets

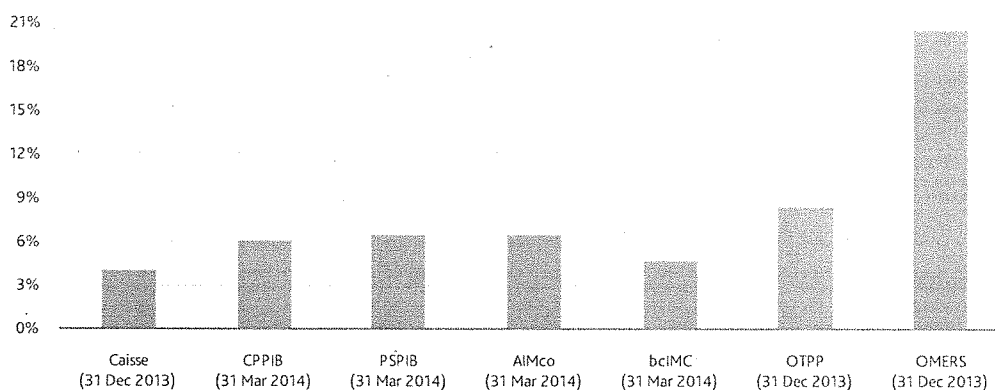


Source: Caisse de dépôt et placement du Québec

Infrastructure assets have become increasingly important in recent years among Canadian pension asset managers. However, the Caisse's exposure to infrastructure assets is the lowest among Canadian pension asset management organizations, as shown in Exhibit 2. This places it in a relatively better position to absorb the incremental liquidity risk associated with these assets. In addition, we expect that, as a result of the time it takes to develop such projects, it will take several years for any new investments to materially change the Caisse's portfolio mix.

EXHIBIT 2

Infrastructure Assets as a Portion of Canadian Pension Asset Managers' Investment Portfolio



Source: Company financial statements

The agreement reinforces the Caisse's dual mandate of generating returns for its depositors and contributing to the province's economic development. We believe this mandate can, at times, conflict, creating governance challenges. However, the Caisse will retain full control over whether it chooses to enter the projects. In addition, we also view the Caisse's natural strength in evaluating Québec investment opportunities as an offsetting factor.

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Although the province is responsible for identifying projects of public interest and has the right to select projects on the basis of optimal solutions provided by the Caisse, the Caisse will be responsible for the execution of the selected projects. The province could participate as an equity partner in projects, but will not have voting rights. As a result, the pension fund will have greater exposure to operational and reputational risks associated with the performance of public infrastructure projects, risks that would have otherwise rested with the provincial government.

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