



Web site: www.cppib.ca

Backgrounder

CPP Investment Board investments in bank-sponsored ABCP

The CPP Investment Board is a long-term investor with a mandate to maximize returns without undue risk of loss and an objective of diversifying the portfolio. Current market conditions present good opportunities to purchase high-quality, bank-sponsored fixed income securities at an attractive yield to earn risk-adjusted returns. The opportunity stems from confusion in the marketplace between high-quality bank-sponsored ABCP and significantly lower-quality non bank-sponsored ABCP.

While **non bank-sponsored** ABCP has been frozen, is the subject of the Montreal Accord negotiations and has triggered calls for greater oversight and regulation, by contrast, **bank-sponsored** ABCP continues to add value for investors, subject to adjustments driven by market forces. While a lot of attention has been paid to the part of the ABCP market in Canada that is not working, there is a part of the ABCP market that has adapted and is working and delivering attractive yields to sophisticated investors.

Prior to the credit crunch in July and August, the CPP Investment Board had no exposure to any ABCP, and little corporate credit exposure at all within the total portfolio. In mid-September, we chose to begin investing in high-quality **bank-sponsored** ABCP that has global-style liquidity, full transparency, is not highly levered and is backed by mainly top-tier Canadian traditional assets – such as credit card receivables, equipment loans/leases, auto loans/leases, trade receivables and Canadian residential mortgages.

It is important to note that the CPP Investment Board has **no exposure to non bank-sponsored ABCP**, the highly-levered instruments that have experienced difficulty in recent months. We therefore are not a participant in the Montreal Accord. This is an important distinction.

As of mid-December we held approximately \$6 billion in bank-sponsored ABCP securities. This represents a small piece of the estimated total \$124 billion Canadian ABCP market (bank-sponsored and non bank-sponsored) and a small portion of the nominal fixed income assets in the \$121.3 billion CPP Fund.

Even though the ABCP instruments we have invested in are high-quality bank-sponsored securities we insisted on stringent preconditions before investing:

- **Global-style liquidity** was a precondition to our investment in bank-sponsored ABCP. We have only invested where this condition already existed or where banks have amended their structures to include this.
- **Full transparency** of the assets backing the ABCP and that these investments are over-collateralized.

- **Not highly-levered** structures as is the case in non bank-sponsored ABCP.
- **Traditional underlying assets** make up most of the bank-sponsored ABCP that we have invested in including auto-loans/leases, equipment loans/leases, Canadian residential mortgages and trade receivables.

Where these conditions did not exist, we did not invest.

At the same time, other investors were calling for the same conditions: greater transparency of underlying assets, the eradication of Canadian-style liquidity provisions in this part of the market, a move to global-style liquidity provisions and more attractive yields. The CPP Investment Board was one of the market participants that drove these changes and helped embed full transparency in these investment vehicles.

Given these changes, the CPP Investment Board is confident in the underlying value of our investments.

Frequently Asked Questions

1. What is ABCP?

Asset-backed commercial paper (ABCP) is a short-term investment vehicle. There are two types of ABCP with very different risk profiles – bank-sponsored and non bank-sponsored ABCP.

2. Why is the CPP Investment Board investing in the bank-sponsored ABCP market?

The confusion in the marketplace between bank-sponsored and non bank-sponsored ABCP has created an opportunity for us to purchase high-quality fixed income assets at an attractive yield.

We are only interested in high-quality bank-sponsored traditional-asset ABCP investments. We insist on global-style liquidity, as well as full transparency of the backing assets, reporting and disclosure.

Our unique characteristics, including our position as a long-term investor mean that we are well-positioned to act on short-term investment opportunities of this kind.

3. What is the difference between bank-sponsored ABCP and non bank-sponsored ABCP?

Bank-sponsored ABCP is an attractive investment vehicle. Non bank-sponsored ABCP is sponsored by third-party conduits operated by non-bank financial institutions, tends to be highly leveraged and backed by a mix of traditional and non-traditional assets. Non bank-sponsored ABCP is, for the most part, frozen in the marketplace.

CPP Investment Board is invested only in bank-sponsored ABCP where there is no leverage involved, it is over-collateralized with traditional assets and sponsored by Canadian chartered banks. It is important to note that the CPP

Investment Board has no exposure to non bank-sponsored ABCP and is therefore not a participant in the Montreal Accord.

4. Are these investments risky?

CPP Investment Board is confident in the underlying value of our investments. Our bank-sponsored ABCP contains high-quality assets, is over-collateralized and is sponsored by the major Canadian banks. This type of investment vehicle continues to add value for investors, subject to adjustments driven by market forces.

As a smart investor we were able to take advantage of current market conditions. Confusion in the marketplace between bank-sponsored and non bank-sponsored ABCP created an opportunity to invest in bank-sponsored ABCP to earn attractive yields for which we are earning attractive risk-adjusted returns.

5. Are you in the same position as the investors involved in the Montreal Accord?

No. The CPP Investment Board did not enter the market until mid-September, when we chose to invest in completely different instruments – non-levered bank-sponsored ABCP. Moreover, the CPP Investment Board insisted on strict preconditions before investing: global liquidity provisions, transparency of the backing assets, and traditional assets.

6. What is the difference between “global-style” and “Canadian-style” liquidity provisions?

Under global style liquidity provisions there are more stringent obligations on banks to back-stop these assets than is required under Canadian-style liquidity provisions. Many of the largest Canadian banks have moved away from Canadian-style liquidity provisions to global-style in most of their ABCP programs.

7. What do you mean by over-collateralized assets?

Over-collateralized assets are a credit enhancement by which an issuer pledges collateral in excess of what is needed to adequately cover the repayment of the securities, plus a reserve. The types of bank-sponsored ABCP that we invest in are all over-collateralized.

Dated: December 19, 2007