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Archived - Improving Access to Financing and Strengthening Canada's Financial System

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Highlights

- The Government's unprecedented actions to improve access to financing have significantly improved liquidity and credit conditions in Canada, assisting households and businesses across the country with their financing needs.
- Financial institutions now have ample funding to lend to creditworthy borrowers, and the Government's financial Crown corporations are continuing to play a strong role in providing support.
- To ensure access to financing as Canada's economy strengthens, the Government is continuing to provide broad-based financing support to lenders, as well as more direct support for particularly hard-hit areas of the financing market.
- Financing support of \$135 billion has been provided, all of it on a commercial basis to protect the taxpayer.
- Average effective interest rates paid by households and businesses are significantly below their level last year.

Improving Access to Financing

Canadians need access to affordable financing for their homes, cars and businesses. The level of interest rates and access to loans influence how Canadians invest and spend their money, which drives our economy and promotes job creation. Strong financial conditions are vital for a sustained recovery in Canada and elsewhere in

the world.

The Canadian financial system withstood the global financial crisis better than most. Indeed, the World Economic Forum's 2009–2010 *Global Competitiveness Report* ranked Canada as having the world's soundest banking system. This is the second year in a row that Canada has received this ranking.

The global crisis, however, made it difficult for Canadian banks and other lenders to obtain funds from international markets at reasonable costs. To soften the impact of this crisis, Canada's Economic Action Plan has taken measures to provide up to \$200 billion to support lending to Canadian households and businesses through the Extraordinary Financing Framework. All facilities under the Extraordinary Financing Framework are operational, and the measures that are described below and summarized in Table 2.13 have contributed significantly to improved credit conditions in Canada.

Table 2.13 Progress in Implementing Support for Financing			
	Financing Available	Elements in Place	Financing Provided Until Now
	(billions of dollars)		(billions of dollars)
Insured Mortgage Purchase Program	125	✓	66
New 10-year Canada Mortgage Bond	10	✓	9
Canadian Lenders Assurance Facility	N/A	✓	N/A
Canadian Life Insurers Assurance Facility	N/A	✓	N/A
Crown corporation new flexibilities, including Business Credit Availability Program	13	✓	8
Canadian Secured Credit Facility	12	✓	12
Bank of Canada	40	✓	40
	<hr/>		
Total	200		135

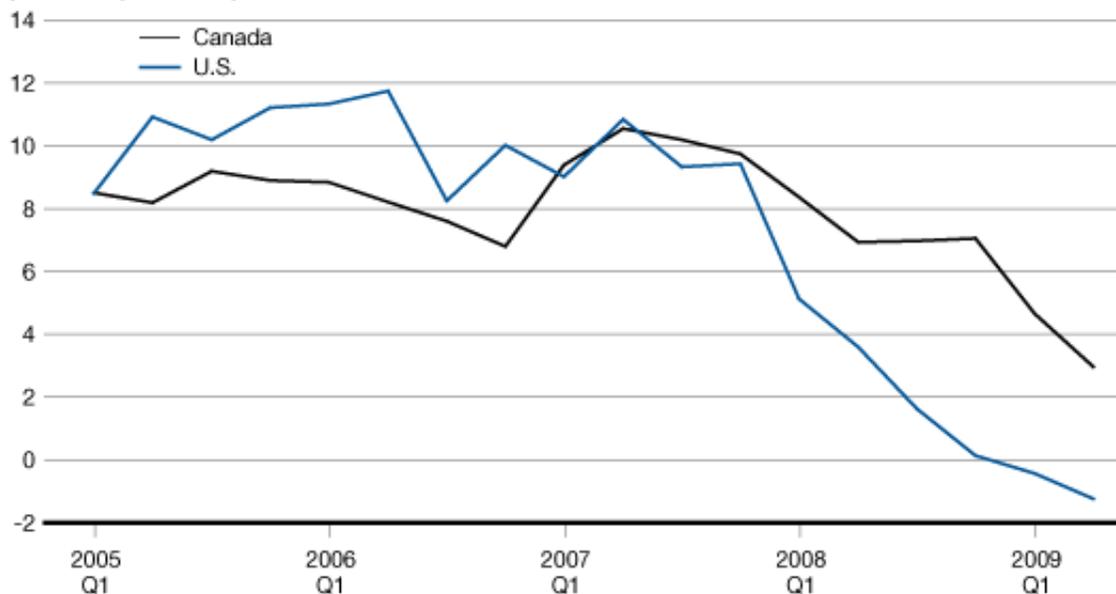
In total, the Government has provided \$135 billion in extraordinary support to improve access to financing for Canadian households and businesses, all of it on a commercial basis to protect taxpayers.

The Government's actions under the Extraordinary Financing Framework have contributed significantly to improved credit conditions. In Canada, total credit growth continues to be positive. This stands in contrast to the situation in other major economies such as the U.S., where total credit growth has slowed markedly (Chart 2.12).

Credit growth in Canada has slowed but remains higher than in the U.S. and other countries

Chart 2.12
Total Credit Growth

per cent, period to period at annual rates

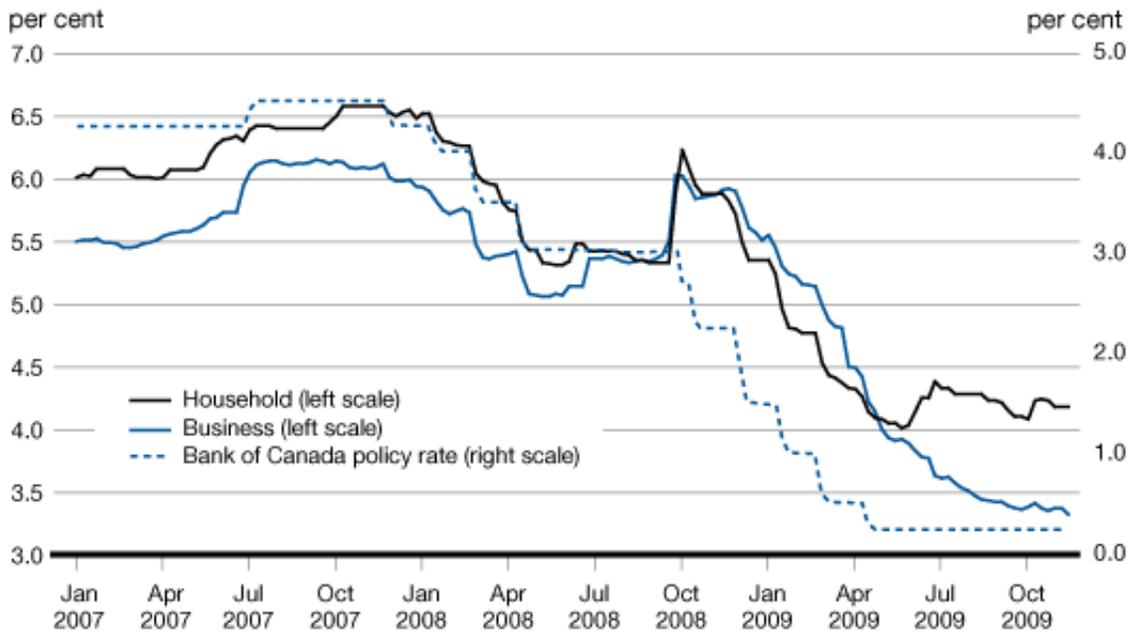


Sources: Bank of Canada; U.S. Federal Reserve Board.
Based on latest comparative data available.

In Canada, credit growth has been combined with significantly lower interest rates for borrowers. In response to the global financial crisis, the Bank of Canada reduced its policy rate by 425 basis points between July 2007 and April 2009 and has held it there since (Chart 2.13). The Government's measures to support access to financing have helped to alleviate market uncertainty and supported a dramatic reduction in interest rates. For example, a number of lenders have pointed to the Insured Mortgage Purchase Program as contributing to a significant decline in mortgage interest rates since October 2008. As a result, average effective interest rates for households and businesses, as estimated by the Bank of Canada, have fallen by over 200 basis points and about 270 basis points, respectively, since last fall.

Interest rates are lower

Chart 2.13
Effective Interest Rates and Policy Rate



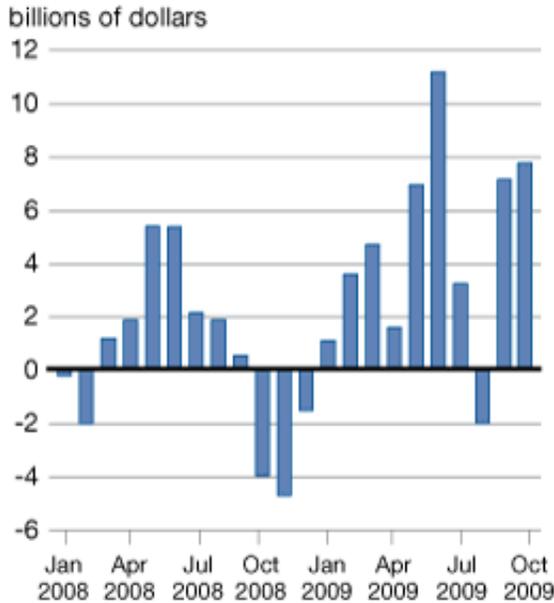
Source: Bank of Canada. Weekly data up to and including November 20, 2009.

Following extraordinary policy measures introduced by governments and central banks to support the financial system worldwide, financial market conditions have continued to improve significantly since the start of the year. Improved financial market conditions have led to a rebound in bond and equity issuances, following a retrenchment in these activities in late 2008 (Chart 2.14). Meanwhile, the difference between corporate and government bond rates has narrowed considerably.

Improvement in business lending conditions and financial market activity

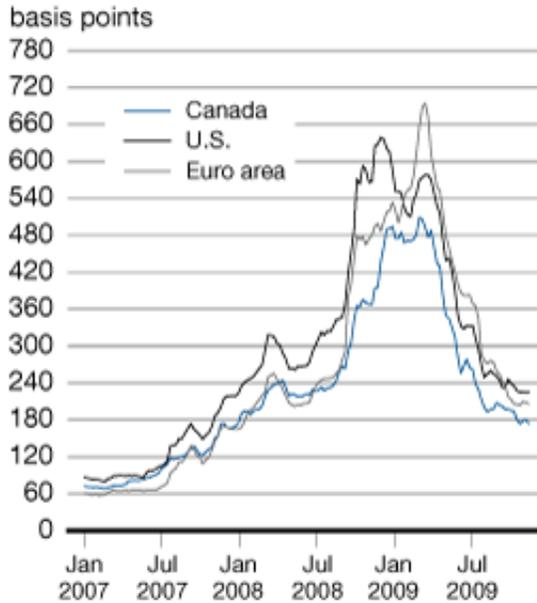
Chart 2.14

Net Funds Raised by Canadian Non-Financial Businesses Through Equities, Bonds and Short-Term Paper



Source: Bank of Canada.

Long-Term Corporate Spreads



Notes: The spreads are the difference between corporate and government yield of bonds with a maturity between 7 and 10 years. Weekly data up to and including November 20, 2009.

Source: Merrill Lynch.

As conditions have improved, demand for certain measures under the Extraordinary Financing Framework has decreased. For instance, lenders have not participated as aggressively in the Insured Mortgage Purchase Program, and the extraordinary liquidity provided by the Bank of Canada stood at about \$27 billion in mid-November, down from its peak of over \$40 billion in December 2008. Certain programs, however, continue to be an important source of liquidity should normal sources of funding become less available.

Reflecting improved conditions in funding markets, the Bank of Canada has begun to reduce or phase out its extraordinary liquidity facilities. The Canadian Lenders Assurance Facility and the Canadian Life Insurers Assurance Facility will expire on December 31, 2009. These facilities have not been used. Unlike the case in many other countries, Canadian deposit-taking institutions and life insurance companies have been successful in raising debt financing without the need for a government guarantee.

Direct Support for Small and Medium-Sized Business

The Government is continuing to work hard to help businesses find financing to fund growth and maintain jobs through the Business Credit Availability Program (www.fin.gc.ca/bcap). Since the Third Report to Canadians in September, Export Development Canada (EDC) and the Business Development Bank of Canada (BDC) have made further progress in providing loans and other forms of credit support under this program. As of the end of October, EDC and BDC reported total activity under the Business Credit Availability Program of about \$3.6

billion, assisting over 7,200 businesses. As illustrated in the tables below, the financial Crown corporations have provided assistance in regions all across the country and in all sectors of the economy, with a particular focus on small businesses. A sample of the success stories is found below. Program activity is expected to continue to increase.

Table 2.14 Business Credit Availability Program—Support by Region		
	Millions of Dollars	Number of Transactions
Western Canada	1,168	1,958
Central Canada	2,272	4,322
Atlantic Canada	147	953
Northern Canada	6	20
	<hr/>	
Total	3,594	7,253
Note: Totals may not add due to rounding.		

Table 2.15 Business Credit Availability Program—Support by Sector		
	Millions of Dollars	Number of Transactions
Manufacturing	943	2,547
Wholesale and retail	316	1,216
Construction and infrastructure	418	442
Business/non-business services	133	1,008
IT and telecom	31	158
Extractive and resources	839	360
Transport and storage	229	280
Real estate	394	245
Tourism	269	761

Other	21	236
Total	3,594	7,253

Notes: Totals may not add due to rounding. Further information on supplementary industry-specific support can be found in the section entitled "Supporting Industries and Communities."

Borrower Size (Sales)	Millions of Dollars	Number of Transactions
Less than \$25 million	1,422	7,084
\$25 million to \$250 million	776	149
Over \$250 million	1,395	20
Total	3,594	7,253

Note: Totals may not add due to rounding.

Canada's Economic Action Plan: Working for Canadians

Business Credit Availability Program

Success Stories

EDC provided \$35 million in financing towards a revolving credit facility for Calfrac Well Services of Calgary. Calfrac provides specialized oilfield services to exploration and production companies designed to increase the production of hydrocarbons from wells drilled throughout western Canada, the United States, Russia, Mexico and Argentina. The financing will support Calfrac's international expansion and general corporate purposes, in order to further establish Calfrac as a pre-eminent global oilfield service company.

EDC provided \$27 million in financing as part of a larger working capital facility for Montréal-based Kruger Inc., a major producer of publication papers, tissue, lumber and other wood products, corrugated cartons from recycled fibres, green and renewable energy, and wines and spirits. EDC worked in partnership with other

Canadian banks to add capacity to Kruger's credit facility as the credit crunch continues to constrain lending, in particular for companies in the pulp and paper sector.

BDC provided \$57 million, its largest contribution to date under this initiative, to support McMaster Innovation Park's new \$69-million research complex that will help boost the new economy in the Hamilton area. In collaboration with McMaster University, this 37-acre complex is evolving into a number of labs and research facilities focused mainly on new technology and higher-value products. The anchor tenant is Natural Resources Canada's CANMET Materials Technology Laboratory, one of the most recognized centres of research excellence of its kind in Canada.

BDC partnered with Peace Hills Trust, Canada's first and largest First Nations trust company, to provide financing for a \$12-million retail project in Duncan, British Columbia. Spearheading this venture is Property Development Group, a company that has developed commercial real estate throughout B.C. and has partnered successfully with numerous First Nations bands to create and support businesses on reserve lands. The project is located on the lands of the Cowichan Tribes, the single largest First Nation in B.C. with more than 3,800 members. The Duncan Village project is the most important corporate financing deal BDC has ever made with a First Nations financial institution and will contribute to the development and well-being of the local economy.

In addition to the support provided through the Business Credit Availability Program, the Government has provided extensive support to the forestry sector through other measures. For example, EDC and BDC have provided over \$12 billion in support to the forestry sector this year, an increase of almost 30 per cent over the same period last year. Since the release of the Economic Action Plan, the Government has also announced the creation of a \$1-billion program to support environmental improvements for the pulp and paper industry. Further information can be found in the forestry section in "Supporting Industries and Communities."

Support for Vehicle and Equipment Financing

The Canadian Secured Credit Facility is designed to support the financing of vehicles and equipment and to stimulate private lending to these sectors. Under the facility, the Government has committed to purchase up to \$12 billion of newly issued term asset-backed securities backed by loans and leases on vehicles and equipment and dealer floor plan (inventory financing) loans. There is evidence that the facility is having a positive impact on the availability and cost of financing for vehicles and equipment. The Government is also working, in conjunction with BDC, to identify prudent and effective means of providing financing support to smaller creditworthy finance and leasing companies that cannot directly access the Canadian Secured Credit Facility. The financing provided by these entities to consumers and businesses supplements the credit available from banks and other large financing providers, and will contribute to Canada's economic recovery.

Progress in implementing other initiatives under the Extraordinary Financing Framework can be found in Table 2.17.

Canada's Economic Action Plan: Working for Canadians

Recent Developments in Credit Conditions in Canada

Credit conditions in Canada continue to normalize towards pre-crisis levels. Total household credit growth remains strong and is showing signs of stabilization, after a deceleration from the cyclical peak observed around the start of the financial crisis. The three-month annualized growth rate of total household credit, as estimated by the Bank of Canada, stood at 7.5 per cent as of October 2009. The stabilization of household credit has been supported by increases in both consumer credit and residential mortgages.

The three-month annualized growth rate of total business credit, as estimated by the Bank of Canada, has decreased sharply from its peak of 10.8 per cent in May 2007 to 1.8 per cent as of October 2009. Nevertheless, there have been several signs that business credit is beginning to normalize. Spreads have narrowed significantly, leading to a resumption of activity in the bond and equity markets and providing businesses with a greater choice of whether to borrow on an intermediated basis through a financial institution, or non-intermediated basis by borrowing directly through financial markets. As a result, net issuance of bonds by non-financial corporations rebounded to over \$26 billion in the first ten months of 2009 after a decline of about \$2 billion in the fourth quarter of 2008. Another positive development in recent months has been the shift from shorter-term to longer-term business credit.

In the most recent Bank of Canada survey of senior loan officers at banks, conducted over the third quarter of 2009, survey respondents, by a narrow margin, reported that lending terms continue to tighten. However, the degree of tightening in lending conditions is the lowest since the onset of the global financial crisis. Tighter lending conditions were also less generalized among respondents than in previous quarters. In the Bank of Canada's most recent *Business Outlook Survey*, for the first time since the summer 2007 survey, the balance of opinion has fallen to below zero, suggesting that conditions have stabilized following several quarters of tightening conditions.

Average interest rates have continued to steadily decrease for both households and businesses. Over the past 12 months, the prime rate has fallen by 175 basis points and posted 5-year mortgage rates have dropped by about 140 basis points. The average effective household interest rate, estimated by the Bank of Canada, was 4.16 per cent in November compared to 5.47 per cent in December 2008. Similarly, the average effective business interest rate was 3.30 per cent in November compared to 5.75 per cent in December 2008.

Strengthening Canada's Financial System

Canada's financial system has shown exceptional stability throughout the crisis and has become a globally noted leader in best banking practices. The International Monetary Fund noted in March that while financial conditions in Canada have tightened, "strains are considerably less severe than in other major countries, and credit growth remains solid, both of which reflect a resilient financial system."^[2]

While the Extraordinary Financing Framework provided an immediate response to alleviate the impact of the global credit crunch in Canada, Canada's Economic Action Plan also contained initiatives to strengthen Canada's financial system and modernize the regulatory framework going forward. There has been further progress on these initiatives since the Third Report to Canadians in September.

Establishing a Canadian Securities Regulator

Since the last report, the Government has taken significant steps to move forward quickly with provinces and territories to establish a Canadian securities regulator that respects constitutional jurisdiction, regional interests and expertise.

On October 15, 2009, the Government announced the launch of the Advisory Committee of Participating Provinces and Territories. The Advisory Committee is responsible for providing advice to the Canadian Securities Transition Office to ensure that the views of participating provinces and territories are properly represented as work is undertaken to transition to a Canadian securities regulator. The Advisory Committee is comprised of a

member from each participating provincial and territorial government, which includes Ontario, Nova Scotia, New Brunswick, British Columbia, Prince Edward Island, Saskatchewan, Newfoundland and Labrador, the Northwest Territories, Yukon and Nunavut.

The Government also recently announced that it will seek the opinion of the Supreme Court of Canada, at such time as the draft legislation has been completed, as to whether Parliament has the constitutional authority to enact and implement a federal securities regulatory regime. The Government is mindful of the importance of having a definitive answer on the issue. An opinion from the Supreme Court of Canada will provide legal certainty to all provinces and territories, and market participants, and thus protect the integrity of a Canadian securities regulatory regime.

Federally Regulated Private Pension Plans

On October 27, 2009, the Government announced a series of measures to improve the legislative and regulatory framework respecting federally regulated private pension plans. These proposals were developed following extensive consultations led by Parliamentary Secretary Ted Menzies, which were conducted during the first half of the year. During the consultations, Canadians were invited to provide their views to the Government through written submissions or presentations at consultation sessions held across the country.

The proposed measures are divided into five main themes:

1. Enhanced protections for plan members.
2. Allowing sponsors to better manage their funding obligations.
3. Making it easier for participants to negotiate changes to their pension arrangements.
4. Improving the framework for defined contribution and negotiated contribution plans.
5. Modernizing the investment rules.

In addition, the Government is proposing a number of small, technical changes to the legislation to improve its operation.

Legislation and regulations to put these measures into effect will be introduced in the coming months, with the goal of having substantially all measures in force before the end of June 2010.

These proposals affect federally regulated pension plans, which constitute approximately 7 per cent of pension plans in Canada, representing 10 per cent of plan members. They build on previous actions by the Government to strengthen Canada's retirement income system. The Canada Pension Plan is being improved based on the recently concluded Triennial Review, and an important new savings vehicle, the Tax-Free Savings Account, has been put in place. Also, research on retirement income adequacy will be presented to Finance Ministers and Ministers responsible for pensions at the December Finance Ministers' Meeting in Whitehorse.

Code of Conduct for the Credit and Debit Card Industry in Canada

On November 19, 2009, the Government released for public consultation a proposed Code of Conduct for the Credit and Debit Card Industry in Canada. The proposed Code is intended to promote fair business practices and ensure merchants clearly understand the costs and benefits of accepting credit and debit cards. It would

also encourage choice and competition in the credit and debit market for the benefit of consumers and merchants. The objective is to have the Code finalized and in force as soon as feasible following the 60-day consultation period.

The credit card regulations released on September 30, 2009 complement the proposed Code in protecting credit card users by limiting business practices that are not beneficial to consumers and providing clear and timely information to Canadians about credit cards.

Progress in implementing other initiatives to strengthen the Canadian financial system can be found in Table 2.17.

Table 2.17 Improving Access to Financing and Strengthening Canada's Financial System			
	Total Financing Available	Authorities in Place	Financing Provided Until Now
	(billions of dollars)		(billions of dollars)
Insured Mortgage Purchase Program	Up to 125	Yes	66
Business Credit Availability Program, supported by expanded powers and additional capital for Export Development Canada/Business Development Bank of Canada	At least 5	Yes	3.6
Canada Small Business Financing Program	N/A	Yes	0.2
Canadian Secured Credit Facility	Up to 12	Yes	12
Canadian Lenders Assurance Facility	N/A	Yes	-
Canadian Life Insurers Assurance Facility	N/A	Yes	-
Modernization of Bank of Canada authorities	40	Yes	40
Canada Mortgage Bond	Up to 10	Yes	9
Advisory Committee on Financing	N/A	Yes	-
Canada Deposit Insurance Corporation authorities and mandate	N/A	Yes	-
Expanded powers for Minister	N/A	Yes	-
Recapitalization/equity investments in banks	N/A	Yes	-

Measures to protect consumers regarding credit cards	N/A	Yes	-
Canadian securities regulator	N/A	Yes	-
Measures to protect consumers regarding mortgage insurance	N/A	Yes	-
Consultations on leasing powers	N/A	Yes	-
National task force on financial literacy	N/A	Yes	-
Improving the legislative and regulatory framework for federally regulated pension plans	N/A	Yes	-

[2] International Monetary Fund, *2009 Article IV Mission to Canada: Concluding Statement* (March 9, 2009).

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