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Program on Financial Stability

Improving our understanding and management of systemic risk.

Bank of Canada Establishes Series of Programs to Promote Market Liquidity

: **BY AIDAN LAWSON**
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Since the beginning of April, the Bank of Canada (BoC) has launched three market-liquidity programs. Two are new asset purchase programs, under which it will buy commercial paper and government bonds. The third is an activation of a standing repurchase agreement (repo) facility to get cash to market participants.

COMMERCIAL PAPER PURCHASE PROGRAM (CPPP)

The BoC announced its intent to directly purchase commercial paper under a new Commercial Paper Purchase Program (CPPP) on March 27, with purchases commencing on April 2. The BoC buys commercial paper (including asset-backed commercial paper) with up to a 3-month maturity on both the primary and secondary markets.

To be eligible, the commercial paper must be issued by Canadian businesses, municipalities, and provincial agencies through already-existing commercial paper programs. Issuers must have a minimum short-term credit rating of R-1 High/Mid/Low from DBRS Morningstar as of April 2, though the BoC can approve issuers that are downgraded after that date or are not rated by DBRS, so long as they have ratings from Fitch, Moody's, or S&P. The BoC limits individual purchases to 1.25 times the largest amount of Canadian dollar-denominated commercial paper that an issuer had outstanding on any day in the last year. The CPPP is expected to last for 12 months.

Purchases are made daily and priced at a fixed rate based on the 3-month Canadian overnight index swap (OIS) rate, which is the Canadian Overnight Repo Rate Average (see here, pp. 17). Pricing varies based on the credit risk of the issuer (see here). Aggregate results are published weekly by the BoC, but individual transaction data are not. As of April 8, the facility has purchased CAD$1.9 billion of commercial paper (see here).

The BoC has enlisted the help of Blackrock Financial Markets Advisory, TD Asset Management, and CIBC Mellon to act as advisor, asset manager and custodian, respectively.

SECONDARY MARKET BOND PURCHASE FACILITY

On April 1, the BoC launched a program to purchase at least CAD$5 billion in government bonds on the secondary market. These purchases are via reverse auction and conducted across the yield curve.

The BoC announced the program on March 27. So far, the BoC has conducted six auctions for a total of CAD$7.15 billion. It is planning on purchasing another CAD$500 million in 30-year government debt today (see here). The BoC releases details about the date and maturity of bonds it will purchase every two weeks. It announces more specific operational details closer to the date of each auction (see here).

CONTINGENT TERM REPO FACILITY (CTRF)

On April 3, the BoC activated the Contingent Term Repo Facility (CTRF). The CTRF is an unlimited emergency repo facility designed to counter severe liquidity stresses. It engages in one-month repurchase (repo) agreements with market participants that "demonstrate significant activity" in Canadian dollar money markets or fixed income markets. The BoC has considerably increased its presence in repo markets since the beginning of April, nearly doubling its repo activity from CAD$64.8 billion to CAD$110.7 billion as of April 8 (see here). This is the most the BoC has participated in the repo market, including at the height of the Global Financial Crisis.

All government and government-guaranteed bonds are eligible, as well as Canada Mortgage Bonds and National Housing Act (NHA) MBS, which are two types of mortgage bonds insured and guaranteed by the Canada Mortgage and Housing Corporation (see here, pp. 57). The CTRF began operation on April 6 and is open for a year. The CTRF is similar to the Bank of England's facility of the same name.

The Yale Program on Financial Stability has produced and will continue to update a spreadsheet to assist those contemplating market liquidity programs. The spreadsheet catalogs past and current examples of crisis-focused programs, identifies interesting program features, summarizes existing evaluations of programs, and shares general resources on the topic. This spreadsheet can be accessed here.

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