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Government of Canada announces additional support for credit markets

November 12, 2008

Justin Parappally

The Government of Canada has **introduced new measures** to provide liquidity to Canadian financial institutions. Earlier measures are described in **this post** of October 23.

Today, the Ministry of Finance advised that the mortgage-backed securities purchase program **announced previously** will be increased from \$25 billion to \$75 billion. \$12 billion in purchases have already been made from the first tranche of the purchase program, with an additional \$7 billion expected to be purchased in an auction taking place today. The final purchases from the first tranche are expected to take place on November 21.

Today's announcement also included a reduction in the base premium under the Canadian Lenders Assurance Facility (CLAF) of 25 basis points and a temporary waiver of the 25 basis point surcharge, which means that the lowest price for insurance under the facility will be 110 basis points rather than 160 basis points as **previously announced** on October 23. CLAF provides for government insurance for up to three years for certain borrowing by banks and other qualifying deposit-taking institutions. The reduction in pricing is an attempt to make the program more competitive with similar programs in other countries.

Consultations with Canadian financial institutions on the terms of the CLAF have been completed, and a term sheet for the program is expected to be released within a few days, which will include details of the commercial terms and application process. We understand that the Canadian program will be similar to the UK's Credit Guarantee Scheme. However, unlike the UK scheme, which appears to give government authorities some discretion in determining which entities are eligible and the amount of support to be provided, CLAF coverage will be available to any institution meeting the prescribed eligibility criteria and the maximum amount of coverage for each institution will be determined by formula.

As well, yesterday the Office of the Superintendent of Financial Institutions (OSFI), announced changes to the regulatory capital requirements for banks and other federally-regulated deposit-taking institutions. Debt covered by the CLAF can now be assigned the same risk weighting for regulatory capital purposes as Government of Canada debt during the term of the CLAF guarantee even if that term is less than the term to maturity of the debt. Similarly, debt covered by similar foreign programs can now be assigned the same risk weighting as the guaranteeing sovereign for the term of the foreign sovereign guarantee even if that term is less than the term to maturity of the debt. In addition, OSFI has raised the limit on qualifying preferred shares and “innovative instruments” as a component of Tier 1 capital from 30 percent to 40 percent. Since the current 15 percent limit on “innovative instruments” has been left unchanged, the effect of the change is to increase the amount of qualifying preferred shares that can be included in Tier 1 capital.

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