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TOUR DE TABLE ON THE IMPACT OF THE FINANCIAL CRISIS ON SMES AND SME FINANCING:

Intervention by Canada

WPSMEE TOUR DE TABLE ON THE IMPACT OF THE GLOBAL FINANCIAL CRISIS ON SME FINANCING *EVIDENCE ABOUT THE FINANCIAL CRISIS' IMPACT ON SME FINANCING*

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Canada's starting point going into this difficult period is better than most. The country has a sound financial system; strong household, corporate & government balance sheets; and a sound macroeconomic policy framework to guide decisions. Since the first quarter of 2004, banks' outstanding business loans in Canada have increased by 8.7% on an average annual quarterly growth basis. (This includes all loans to businesses, regardless of size). Moreover, in the third quarter of 2007, the cash position of chartered banks reached its lowest level since 1990 (low cash position means more funds are available for financial institutions to lend to businesses and consumers).

However, there is evidence that credit is tightening. There has been a slight decrease in the number of non-mortgage business loans extended in the second quarter of 2008. It may be too early to tell whether this decline is temporary or reflective of a trend. The cash position of banks has risen by 86 basis points since the third quarter of 2007. This is the largest increase since the first quarter of 1994 and suggests that chartered banks have reduced their lending activities. Credit conditions remain the main emphasis of comments related to the economic environment. Surveys of lenders and borrowers both point to tighter credit conditions. The Bank of Canada's Senior Loan Officers Survey shows that credit conditions have been tightening since mid-2007 and that, for the third quarter of 2008, the highest level of loan officers reported tighter lending conditions since 1999. This tightening is reflected in both pricing and non-pricing lending practices. The Canadian Federation of Independent Business (CFIB), which surveys business owners, also finds that credit conditions are tighter. In its latest weekly survey (Nov 6), the CFIB found that 25% of business owners reported worsening of bank credit (3% reported better access). This compares to 18% in September 2008 and 9% a year ago.

Policies to Ease the Financial Constraints on SMEs

The Government has taken action to ensure the borrowing needs of Canadian households and businesses continue to be well served by the financial system. Importantly, these actions have been taken on commercial terms and have not put Canadian taxpayers' money at risk.

Budget 2008 legislation modernized the authorities of the Bank of Canada to support the stability of the financial system. Consequently, the Bank has been able to widen the collateral it will accept and add more than $35 billion in liquidity to the Canadian financial system at a time when global credit markets have been severely stressed.

The Canada Mortgage Bond (CMB) program has been expanded, including a record $12.5-billion CMB issue in June and the introduction in November of a CMB with a 10-year maturity to allow the program to attract a broader pool of investors.

The Government is supporting the availability of longer-term credit in Canada by purchasing up to $75 billion in insured mortgage pools through Canada Mortgage and Housing Corporation under the Insured Mortgage Purchase Program (IMPP). This action will provide Canada's financial institutions with significant and stable access to longer-term funds that they can then make available to consumers, homebuyers and businesses in Canada. The IMPP will earn a modest rate of return for the Government with no additional risk to the taxpayer.

The Canadian Lenders Assurance Facility, launched in November, will ensure that Canada's financial system is not put at a competitive disadvantage by similar guarantee programs in other countries. The Facility will further help to secure access to term funding so that Canadian financial institutions can continue lending to consumers, homebuyers and businesses.

These measures are producing results. To date, $25 billion of insured mortgage pools have been purchased through the IMPP, and the remaining amount of up to $50 billion will be made available by the end of 2008–09, ensuring federally regulated financial institutions continue to have reliable funding. The net fiscal gain for the Government from the IMPP is projected to be approximately $1.1 billion in 2009–10.

The role of private sector financial institutions is to make loans to creditworthy people and businesses and to support capital markets. The Government is fulfilling its role by intervening with extraordinary measures when markets are profoundly disrupted so that private sector lenders can maintain access to the funds they need to keep lending, and by providing liquidity to capital markets in support of economic growth. Financial institutions have indicated that the IMPP and the Bank of Canada interest rate cuts were key to their decision to lower prime rates and mortgage rates.

While the private sector is and should remain the primary source of credit, the Government is also ensuring that the complementary forms of credit provided through its Crown agencies—Export Development Canada (EDC) and the Business Development Bank of Canada (BDC)—are available to counter the effects of the credit crunch. BDC and EDC have been responding to the needs of their clientele by maintaining and enhancing their existing suite of financing solutions. Recently the Government approved a $2-billion increase in the borrowing authority of EDC as well as a $1.8-billion increase in BDC's borrowing capacity, which enables them to offer additional flexibility to existing clients.

EDC is well positioned to continue to help Canadian companies grow internationally. It will facilitate nearly $80 billion in exports and investments from Canadian companies in 2008, including some $4 billion for the automotive sector. To help address emerging stresses and financial gaps in Canada's export sector, most notably in auto-related and other manufacturing enterprises, the Government is providing EDC with an additional $350 million in capital to support up to about $1.5 billion in increased credit capacity for those most affected by the financial crisis.

BDC is playing an active role in supporting the growth of Canadian small and medium-sized companies, with about $3 billion in new financing this year. The Government will provide BDC with an additional $350 million in capital so that it can increase its credit capacity by about $1.5 billion for term lending activities and a new time-limited facility providing guarantees to financial institutions for their lines of credit for viable small and medium-sized companies.

More information on Canada's policy responses can be found on the Bank of Canada website: http://www.bank-banque-canada.ca and the Department of Finance website: http://www.fin.gc.ca/ .