

Banking on a Better System: Lessons from Canada

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Outline

- Presentation will focus on three key questions:
 - (1) How did Canadian banks perform during the crisis?
 - (2) Why did they do so well?
 - (3) What can be done to make the system even stronger?



How Did Canadian Banks Perform?

- Short answer: Extremely well compared to their foreign counterparts
- Long answer:
 - (1) Fewer loan losses and less need for provisioning [\[Chart 1\]](#)
 - (2) (Relatively) strong profits and a reasonable return on equity [\[Chart 2\]](#)
 - (3) Less need for official liquidity support and no public bailouts [\[Chart 3\]](#)

How Did Canadian Banks Perform? (cont'd)

- (4) Lower short-term interest rate spreads and easier market access [\[Chart 4\]](#)
- (5) Solid growth in consumer credit and residential mortgages [\[Chart 5\]](#)



Why Did Canadian Banks Do So Well?

- Ten reasons for their relatively strong performance:
 - (1) Prudent lending practices from risk-based supervision and natural conservatism
 - (2) A stronger housing sector [\[Charts 6\]](#)
 - (3) Less reliance on wholesale financing and securitization
 - (4) A single national regulator for most deposit-taking institutions
 - (5) Close co-operation among government agencies and departments



Why Did Canadian Banks Do So Well? (cont'd)

- (6) High capital ratios and heavier reliance on equity capital
[\[Chart 7\]](#)
- (7) A strict limit on bank leverage and inclusion of most off-balance activities [\[Chart 8\]](#)
- (8) Mortgage insurance and prudent underwriting standards [\[Chart 9\]](#)
- (9) An effective deposit insurance system
- (10) Mechanism for the quick and orderly resolution of any problem institutions

Why Did Canadian Banks Do So Well? (cont'd)

- Advantages of a principles-based system vs. a rules-based system
- The importance of good supervision vs. regulation

What Can Be Done to Make the System Even Stronger?

- Ambitious international agenda for financial sector reform under the auspices of the G20 and FSB
- Priority areas for ourselves and others:
 - (1) More and higher quality capital
 - (2) Strict limit on leverage
 - (3) Measures to reduce pro-cyclicality
 - (4) Higher and more effective liquidity requirements
 - (5) Continuous core financial markets
 - (6) Better market infrastructure and CCP for repos and OTC derivatives
 - (7) Coherent contingency and resolution plans for SIFIs



What Can Be Done to Make the System Even Stronger? (cont'd)

- This list is not exhaustive -- other issues are also important (improved compensation schemes, enhanced transparency and consistent accounting rules, closer scrutiny of CRAs and hedge funds,...)
- International co-operation and consistency are critical
- Significant challenges but promising progress has been made on many fronts



BANK OF CANADA
BANQUE DU CANADA

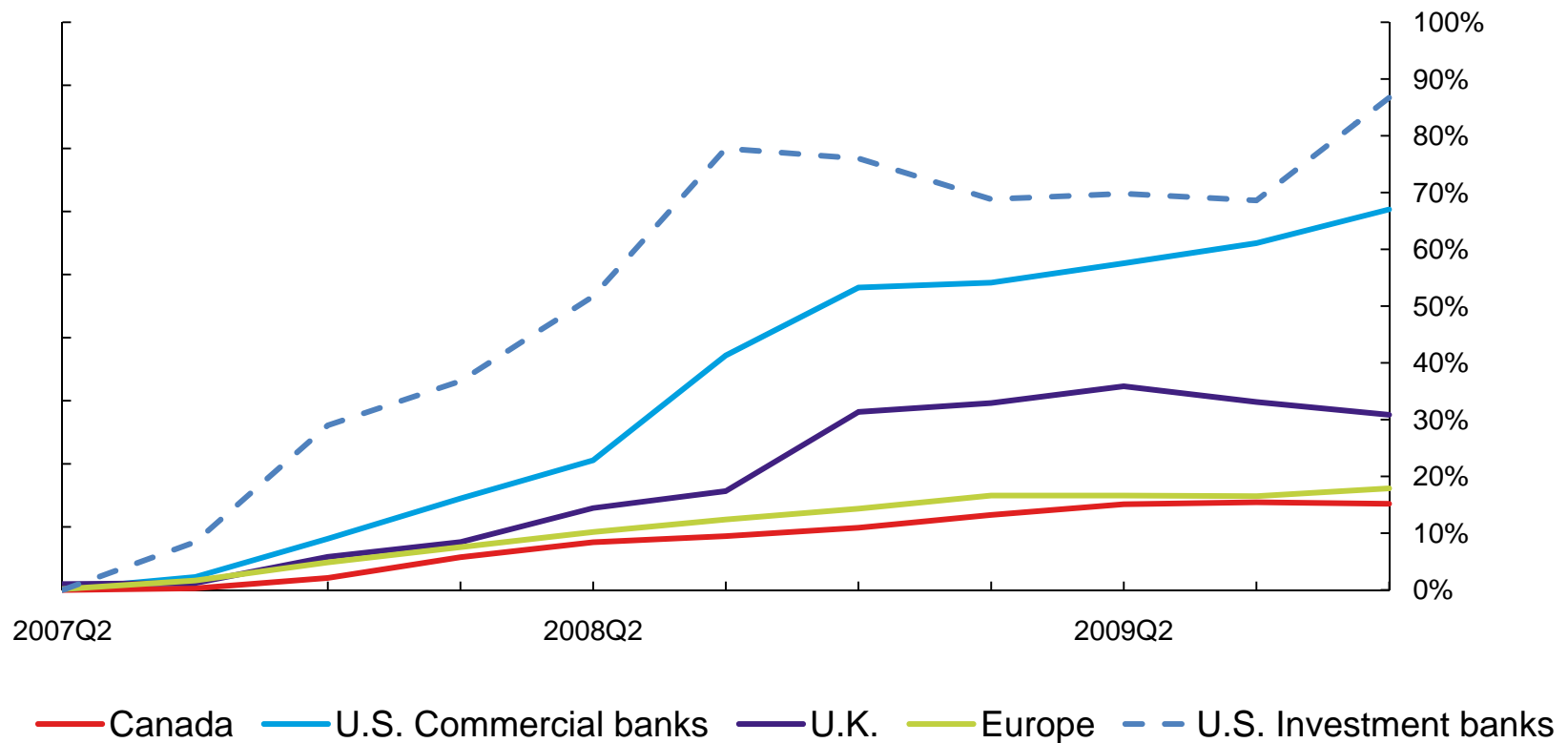
CELEBRATING 75 YEARS
CÉLÉBRONS 75 ANS





Loan losses at banks

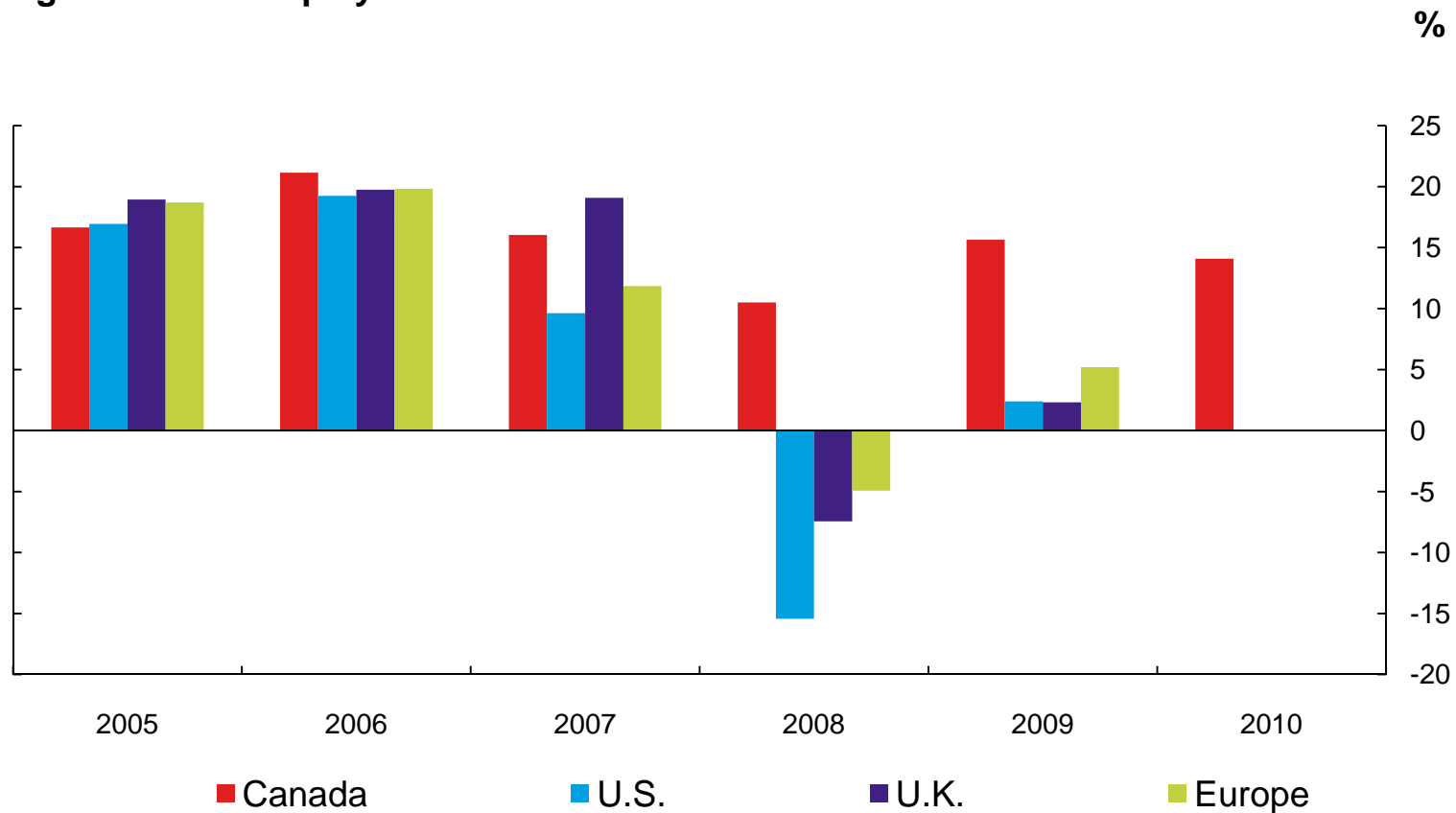
Cumulative Writedowns as a % of Total Shareholders' Equity



Source: Bloomberg

Rate of return at major banks

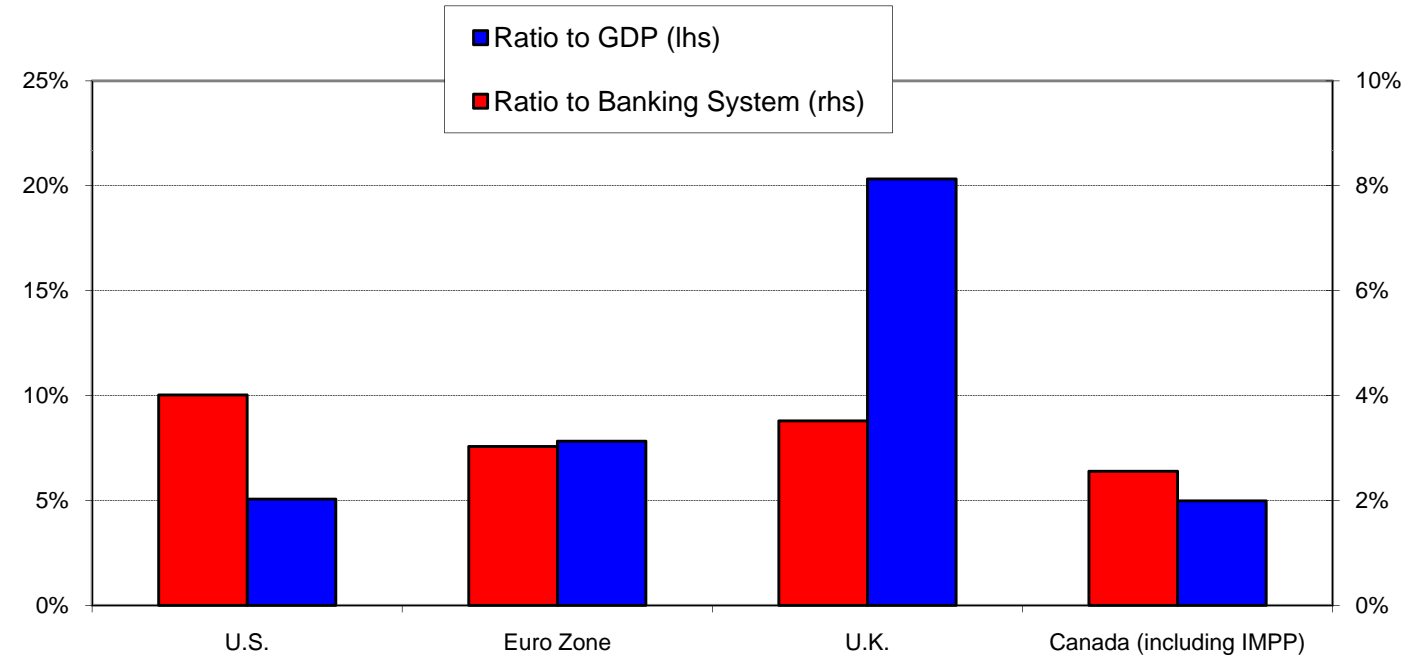
Average Return on Equity



Source: Bloomberg

Liquidity support across countries

Total public sector liquidity extension



Note: Liquidity extension refers to central banks' liquidity provision operations, as well as foreign currency swaps with other central banks, but excludes outright securities purchases.

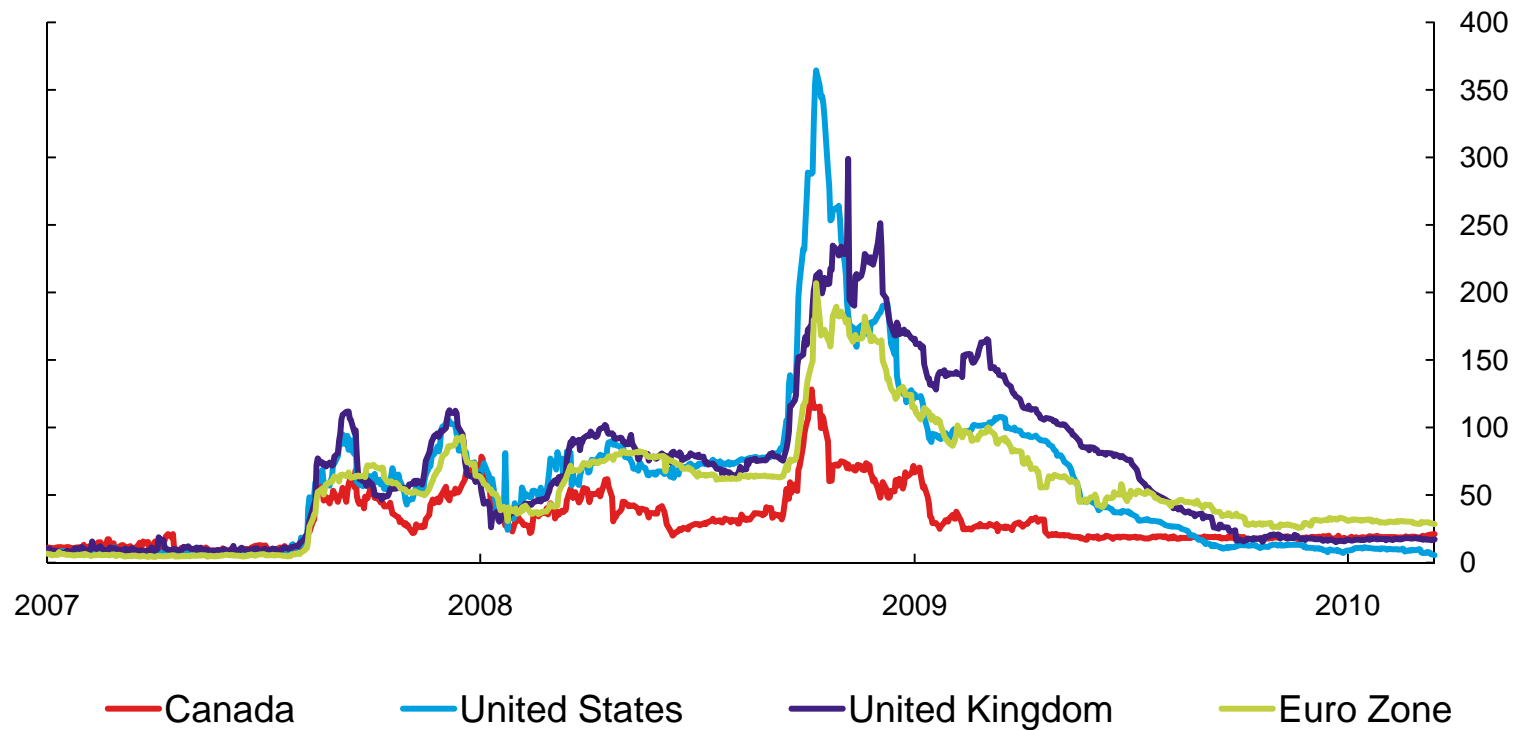
IMPP: Insured Mortgage Purchase Program provides for government purchases of insured mortgage pools.



Short-term interest rate spreads

3-month LIBOR*-OIS Spreads

Basis points



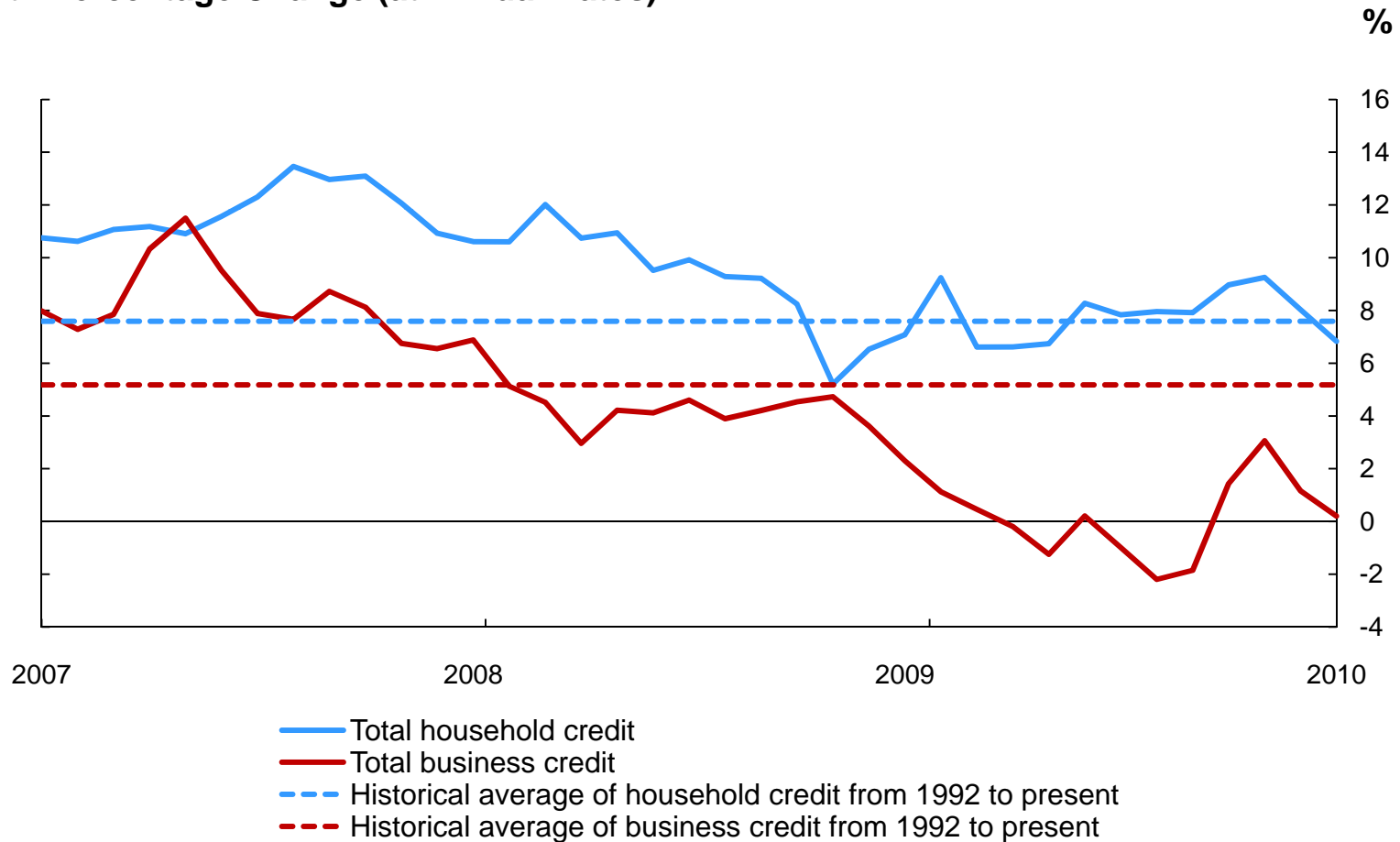
* For the United States and the United Kingdom, LIBOR; for the Euro area, EURIBOR; and for Canada, CDOR

Source: Bloomberg



Credit growth in Canada

3-month Percentage Change (at Annual Rates)

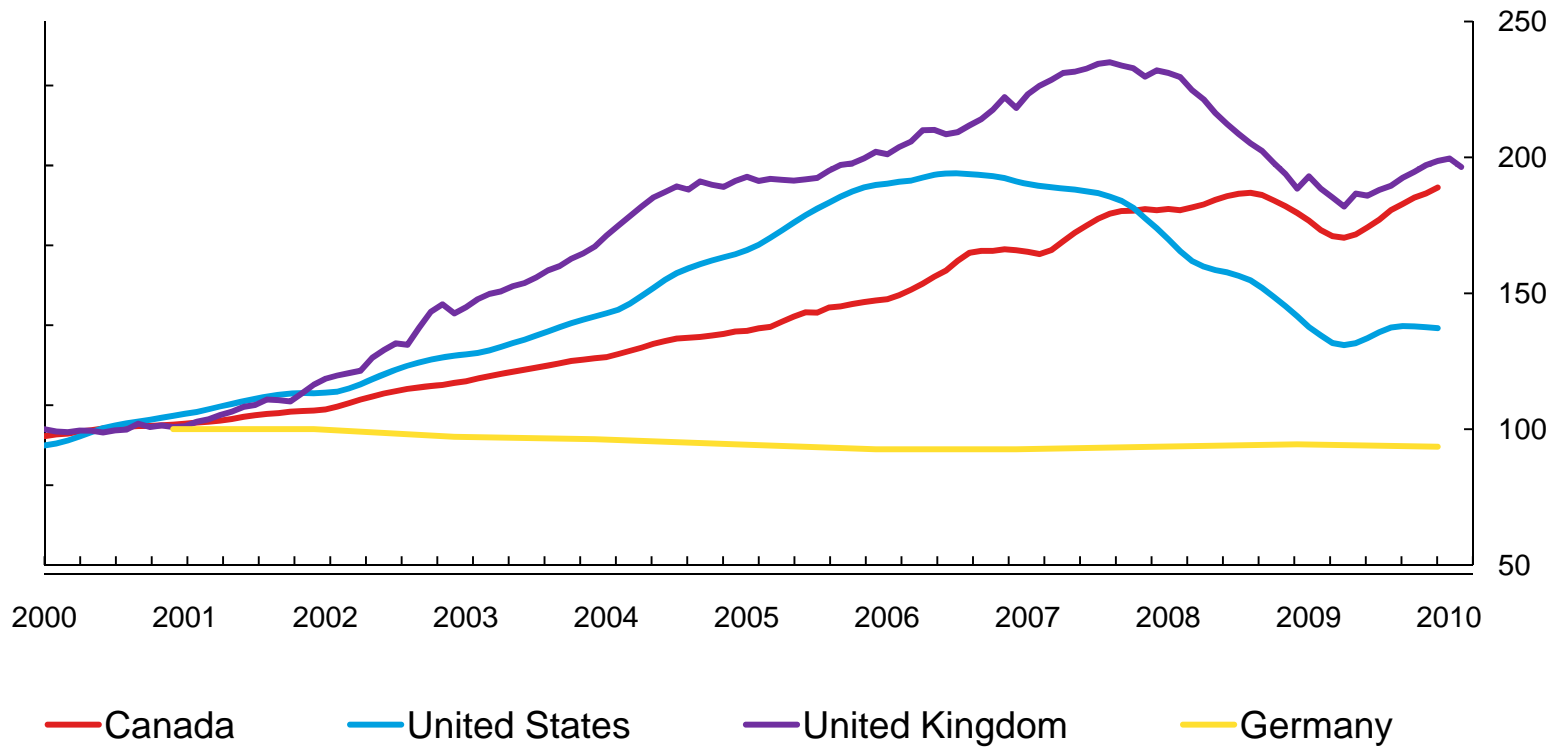


Source: Bank of Canada



Housing Prices

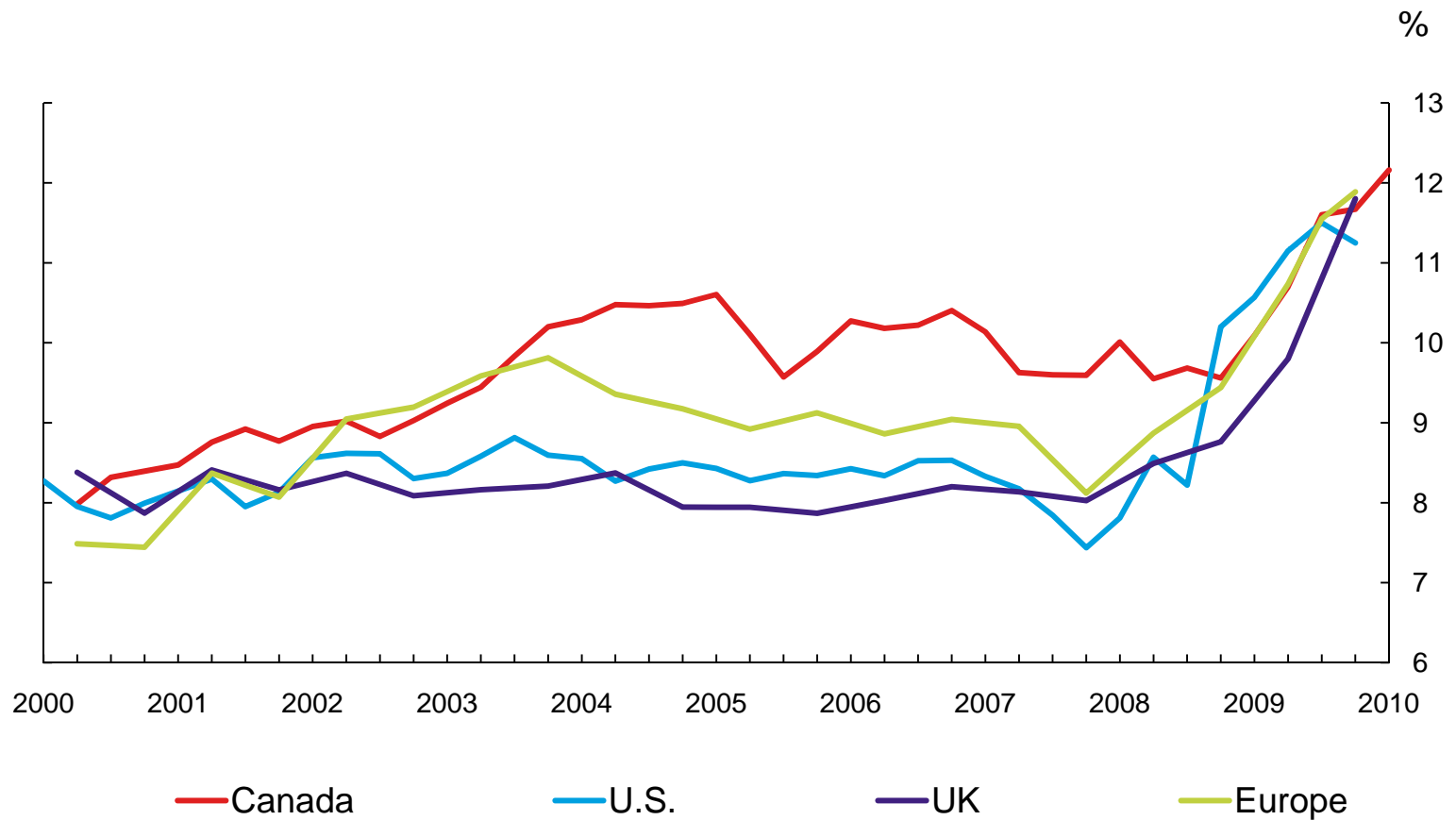
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Source: Teranet-National Bank for Canada; Global Insight for United states and United Kingdom; and National Sources for Germany



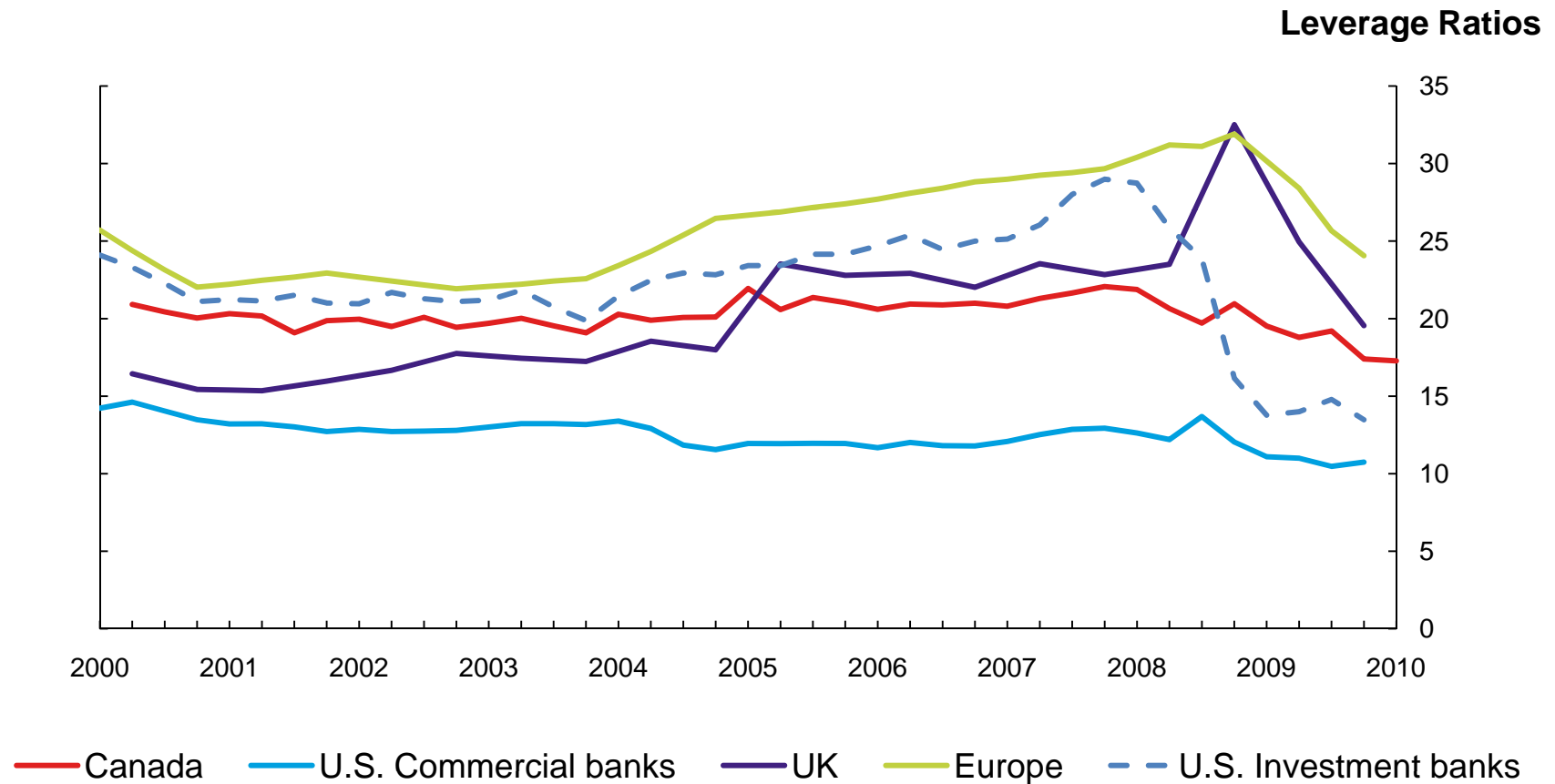
Higher capital ratios in Canada



Source: Bloomberg



Bank leverage ratios



Source: Bloomberg



Healthier mortgage market in Canada

Mortgage Arrears as a Percentage of Outstandings

