Summary of Comments—Government of Canada Debt Distribution Framework Review Consultations

The Government of Canada funds itself by selling Canadian-dollar-denominated debt securities through regular auctions at the Bank of Canada. A group of banks and investment dealers known as Government Securities Distributors (GSDs) participate in these auctions and disseminate the debt to other market participants. This Debt Distribution Framework (DDF) has been in place since 1998. A number of reviews have been done and minor enhancements were made to ensure the integrity of the auction process and to better support the debt management objectives of raising stable and low-cost funding while maintaining a well-functioning Government of Canada securities market.

The Department of Finance Canada and the Bank of Canada launched a consultation process in March 2018 to seek updated views on the current design and effectiveness of the DDF. Written feedback was received from 17 market participants, including GSDs (both primary dealers (PDs) and other non-PD GSDs) and institutional investors. This was followed up with on-site visits in Montréal and Toronto, as well as telephone conversations. The following is a summary of comments received during the consultation.

Key messages

Overall, nearly all respondents describe the Canadian primary and secondary markets for Government of Canada securities as competitive, functioning well and offering good liquidity. On balance, market participants commented that the DDF continues to appropriately balance the interests of the Government of Canada as an issuer of securities, GSDs and end investors. Therefore, the Government's long-held debt issuance objectives of raising stable, low-cost funding and maintaining a well-functioning Government of Canada securities market are being met.

Additional takeaways from the consultation are as follows:

Costs associated with primary and secondary Government of Canada market making activities have increased, but overall, they remain relatively balanced with benefits

While the benefits associated with primary dealing have remained more or less static, some costs have increased since the review in 2005. Cost increases have been driven primarily by regulatory capital, information technology and compliance changes. PDs highlighted that they have made some adjustments to their business models and market making activities in response to the changing external environment, in order to maintain profitability in the trading of government debt and to satisfy customer needs.

Unclear benefits from granting customers direct access to auctions

PDs do not support customers bidding directly at auctions, whereas customers expressed a preference for direct access. There are divergent opinions of the impact direct customer access would have on the government's debt issuance objectives.

Electronic trading in Canada is expected to grow

Market participants confirmed that electronic trading of Government of Canada securities in the secondary market is becoming more common. For the time being, electronic trading remains characterized by relatively small and medium-sized trades. While there has been growth in the proportion of large trades being conducted on some electronic platforms, they continue to be mainly transacted over the phone.

Most market participants view electronic trading as a positive development for reasons related to market transparency and trade execution. Some respondents caution that electronic platforms might not improve market liquidity, particularly in times of market stress when customer trades tend to be unidirectional, with ambiguous implications for the debt distribution framework.

Secondary trading requirements

When asked about the benefits of implementing additional requirements to support secondary market trading, the PDs and non-PD GSDs were in broad agreement that more stringent secondary market trading requirements are not needed to support the Government's objectives of stable, low-cost funding and well-functioning securities markets. While it was agreed that off-the-run Government of Canada securities are less liquid than benchmark bonds, participants largely agree that they should not be considered illiquid. Based on experience in countries that have secondary trading requirements, these requirements can, at times, lead to trading behaviours that do not support the Government's objectives.

Conclusion

Overall, consultation respondents described the Canadian primary and secondary markets for Government of Canada securities as competitive, well-functioning and offering good liquidity. Thus, if adjustments to the DDF are to be made, participants expressed the view that they should be minor. It was understood that primary and secondary market landscapes continue to evolve, and thus ongoing monitoring and regular consultations are needed to ensure the DDF continues to perform to the benefit of all participants and continues to meet the Government of Canada's debt-management objectives.