Fall 2023 Debt Management Strategy Consultations Summary

Regular conversations with market participants are an essential component of the Government's ongoing commitment to a well-functioning Government of Canada (GoC) securities market and an integral part of the debt management process. In September 2023, the Department of Finance and the Bank of Canada attended bilateral in-person meetings and received written comments from dealers, investors, and other relevant market participants. These consultations sought the views of market participants on the design and operation of the Government of Canada's domestic debt program for 2024-25. The Department of Finance and the Bank of Canada value the comments provided by market participants.

The views expressed below reflect those provided by market participants and will be taken into consideration when formulating the debt management strategy.

Overall Comments

Participants continue to view the GoC securities market as functioning well and that Canada has fared well during the market volatility events of the past year. While the makeup of GoC investors has not changed materially, several respondents did note an increase in retail interest at the shorter end of the yield curve as well as heightened domestic pension fund activity in the longer end. International interest remains strong for GoC securities, as is also the case for hedge funds.

The market has adjusted well to the Bank of Canada's absence from GoC auctions, with respondents being content with the increased supply of bonds and treasury bills. However, it was noted that the Bank's absence from recent auctions means bonds issued since the beginning of Quantitative Tightening (QT) are not available at the Bank's Securities Repo Operations (SRO).

Several market participants pointed out that Canada's transparency and consistency as an issuer has been somewhat lower over the past year, noting the unexpected cancellation of the Real Return Bond (RRB) program in particular. A solution suggested by several participants was that the government should communicate decisions better and with more lead time with the market and dealers also suggested that there would be benefit to additional investor relations activities.

Treasury Bills

The market has had no issue in absorbing the increased amount of treasury bills, where demand is especially strong due to the current yield environment, with some participants expressing that the bill supply could still grow further. Participants also expressed a desire for consistency in the bill stock's size, and for it not to decline too much in future years and as a result reduce its well-functioning as a sector.

Participants overwhelmingly expressed a desire for a 1-month treasury bill tenor to be introduced. Such a product would help support the well-functioning of Canada's money market as it transitions away from Bankers' Acceptances (BA) next year and towards other investment options. Most believed this 1-month tenor should be a temporary program, with clear stated objectives and sunset clauses, although some believed a 1-month bill could possibly become a permanent sector.

Bonds

A universal response from participants was the current mismatch between very strong demand for 30Y bonds and limited supply, both from Canada as well as provincial government issuers. Many respondents noted that even small trades in 30Y bonds can move markets somewhat and trying to trade larger positions can be challenging. Market participants therefore requested Canada to consider increasing the amount of 30Y bond issuance.

Conditions in the 2Y, 5Y and 10Y sectors are satisfactory in most participants' views. However, respondents highlighted that multiple "kinks" exist in the GoC yield curve and linked this in part to the Bank of Canada's large holdings of several ISINs. These bonds are difficult to source, expensive and problematic to price off of. A number of respondents believed that these issues could be alleviated by the introduction of a switch facility, where bonds of a similar maturity could be exchanged for those held by the Bank.

Market participants noted that the discontinuation of the 3Y sector has been well received.

The GoC futures market continues to progress. 5Y and 10Y futures remain liquid and are improving further, while use of 2Y futures is growing as well.

Several market participants raised the topic of RRBs. Beyond comments around the lack of advance warning ahead of last year's cancellation of the program, participants noted that there is strong demand for RRBs given it is the key asset available for hedging Canada-specific inflation risk and serves as an important curve to value Canadian pension liabilities. Many investors, including pension plans, have had to turn to imperfect inflation hedging assets such as US Treasury Inflation-Protected Securities (TIPS) and are therefore becoming more exposed to a change in correlation between US and Canadian CPI. While acknowledging that a resuscitated RRB program is very unlikely, many participants expressed that it would be welcome.

Bond Buybacks

Most participants recognised that use of the weekly Cash Management Buyback (CMBB) operations has been very low since these were re-introduced last year. In most respondents' view this lack of offers mainly comes down to a difference in value between what the market is willing to sell eligible bonds at and what price the Government is willing to pay. Bonds with remaining terms to maturity of two years or less are simply expensive to buy (partly exacerbated by the amounts of these bonds the Bank of Canada owns). Larger amounts of offers should appear again when this environment shifts and these bonds cheapen.

Environmental, Social and Governance (ESG) Securities

Market participants observed that Canada's existing green bond sees infrequent trading, although this is largely by design given the bond was always intended for buy and hold green investors. For the next green bond issuance, the majority of participants recommended that Canada open a new ISIN, rather than re-open the existing green bond, with different views on what an ideal tenor may be at this point. Syndication is still viewed as the optimal way to issue for this recently introduced program.

Broad support was given for Canada's ongoing consideration of one day adopting a Sustainable Bond Framework, seeing it as a natural next step from the Green Bond Framework.

Miscellaneous

Market participants are prepared for next year's transition to T+1 settlement for GoC bonds and treasury bills.