

 **CANADA**

Canadian bonds: a vote of confidence by foreign investors

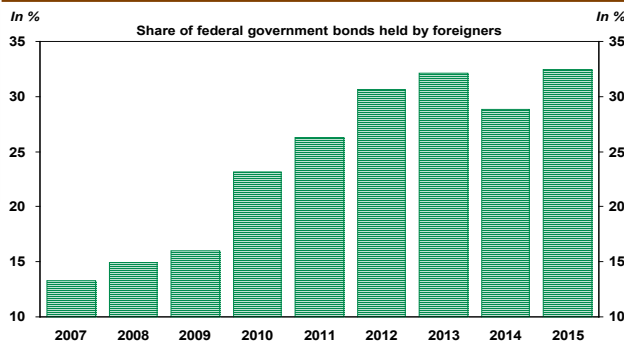
Official reserves of emerging countries have drawn much attention recently. In China, in particular, capital flight applies considerable pressure on the yuan and the central bank was compelled to sell some of its foreign exchange reserves to prevent a collapse of the currency. More than US\$350B of assets were sold by China in the second half of 2015, a considerable amount. The latest statistics suggest that the trend continued in the beginning of 2016. The central banks of several emerging countries have followed suit.

This has raised fears of a rise in bond yields in advanced countries, including the United States. U.S. bonds have indeed been the preferred instrument used by emerging countries to place their reserve accumulations in recent years. However, Canada was also vulnerable. In recent years, foreign interest for Canadian bonds has increased. Foreigners owned less than 15% of Canadian federal bonds in 2007. This proportion has more than doubled to 32% last year.

However, in both the United States and Canada, the rise in yields that some were apprehending did not occur. The Canadian 10-year bond yield rather reached a low of 0.91% on February 11. The latest data on international transactions in securities indicate that in aggregate, foreigners have not lost confidence in Canadian bonds. Other categories of investors have indeed absorbed Canadian assets freed by emerging countries. For example, net purchases of U.S., British and European investors have more than compensated for the net sales of emerging countries in the fourth quarter. This confirms that Canada, which enjoys a AAA status, continues to attract a clientele of developed-country investors, especially those with long-term horizons and who value high-quality assets.

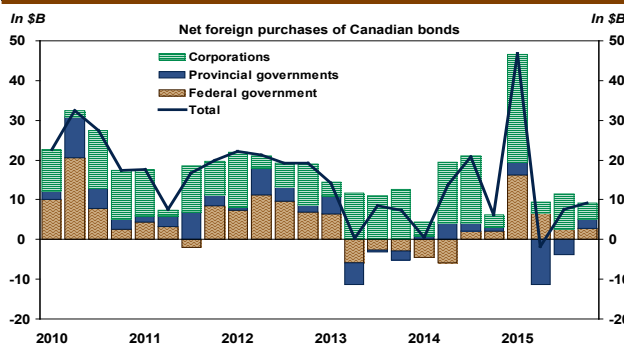
Implications: Despite reserve liquidation, and despite the upcoming federal government deficits that will apply some upward pressure on the supply of Canadian bonds, the

The share of Canadian federal bonds held by foreigners has increased



Sources: Statistics Canada and Desjardins, Economic Studies

Net foreign investment flows in Canadian bonds remain positive



Sources: Statistics Canada and Desjardins, Economic Studies

confidence of foreign investors with regards to Canadian debt is far from being shaken. This should prevent a sharp escalation of the government's borrowing costs.

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